GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

FRIDAY, JULY 1, 2022

- **US equities, Treasuries, and credit all post sharp losses for first half of the year** (link)
- **Canadian government bond yields fall off recent highs as growth worries mount** (link)
- **Euro area headline inflation higher but core inflation below expectations** (link)
- **ECB to start reinvestment flexibility from PEPP redemptions** (link)
- **Colombian central bank accelerates tightening pace with 150 bp policy rate hike** (link)
- **India raises taxes on energy exports and gold imports to reduce pressure on rupee** (link)

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Global risk assets struggle to gain traction amidst growth worries

Global risk assets are facing a challenging backdrop to start the second half of the year with central banks stepping up action on inflation, which has stoked concerns around the growth outlook and the potential for a soft landing. US equities pulled back yesterday as signs of weakening consumption fueled recession fears and has investors contemplating whether the economy may already be feeling the effects of tighter financial conditions. Growing risk aversion has sustained the pressure on core sovereign bond yields with 10-year US Treasury and German bund yields both back down to early-June levels below 3% and 1.3%, respectively. European bourses and US stock futures are trading slightly lower this morning, and Asian equities posted losses across the region in response to the weaker global risk sentiment. Commodity prices have also remained volatile with metals prices slipping further amid unease around slowing demand. Emerging market currencies are depreciating on the back of some softer PMI readings in EMEA and EM Asia ex-China, while in Latin America the Colombian central bank delivered its largest policy rate increase in over two decades in the face of inflation that remains well above the target range.

Key Global Financial Indicators

Last updated: 7/1/22 8:04 AM	Level		Change from Market Close					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
Equities				%			%	
S&P 500		3785	-0.9	0	-8	-12	-21	-10
Eurostoxx 50		3439	-0.5	-3	-9	-16	-20	-13
Nikkei 225		25936	-1.7	-2	-7	-10	-10	-2
MSCI EM		40	-0.5	1	-5	-27	-18	-16
Yields and Spreads				bps				
US 10y Yield		2.94	-7.4	-19	3	148	143	95
Germany 10y Yield		1.30	-3.5	-14	11	150	148	107
EMBIG Sovereign Spread		542	7	32	88	203	175	129
FX / Commodities / Volatility				%				
EM FX vs. USD, (+) = appreciation		51.1	-1.0	-1	-3	-10	-3	-4
Dollar index, (+) = $ appreciation		105.2	0.5	1	3	14	10	9
Brent Crude Oil ($/barrel)		112.1	2.8	-1	-4	48	44	16
VIX Index (%, change in pp)		28.8	0.1	2	3	13	12	-2

Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

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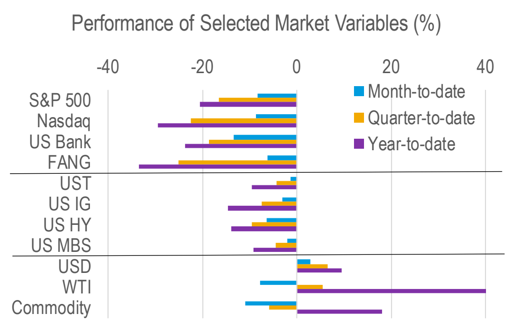
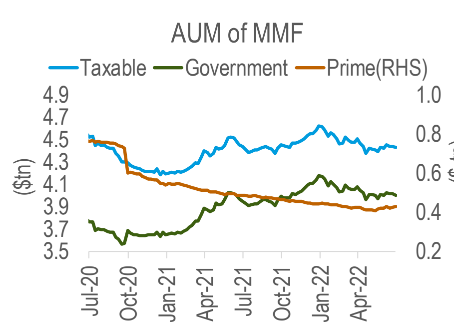
United States

US equities fell, and US Treasury yields dropped as a slowdown in consumer spending, and weaker Chicago PMI data (fell to 56.0 from 60.3) fueled growth concerns. Meanwhile, the Atlanta Fed updated its GDPNow forecast and suggested that 2Q US GDP will retract by 1%. **US equity and bond markets posted sharp losses for the first half of the year. The S&P 500 is down 21% year-to-date,** the worst first-half since 1970. Despite recent sharp yields declines (10-year Treasury yields fell by 50 bps from a recent peak of 3.5%), **US bond indices also posted negative returns** as Treasury yields went higher (10-year: +19 bps in June, 83 bps year-to-date), as well as credit spreads, especially **HY spreads widening sharply** in June. The US Treasury index has fallen 9.6% this year. According to Bloomberg, the worst annual loss for the Treasury index was -3.6% in 2009, and there have been only five annual declines since 1973. Oil posted its first monthly drop this year (-7.8% in June).

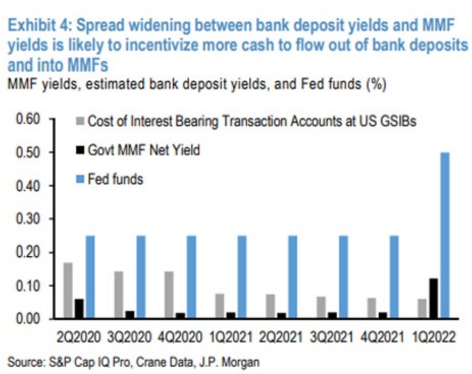


Source:Bloomberg

The Fed's Overnight Reserve Repo balances increased to $2.33 trillion on Thursday, surpassing the previous record level of $2.28 trillion. Meanwhile, money market fund (MMF) assets outstanding (as of June 29) remain steady, increasing by $3 bn this month (Prime +$6 bn, Government $-3 bn). **Both BAML and JP Morgan analysts expect MMF AUM to increase as yields become more attractive compared to bank deposit rates**. The right chart shows bank deposit rates and market rate sensitive MMF yields have diverged already, and the spread between those two rates is likely to continue to widen in the latter half of the year, leading to outflows from bank deposits and inflows to MMFs. With a strong preference for shorter duration assets alongside a reduction in T-bill issuances, MMFs are likely to deploy money into the RRP facility, leading RRP balances to remain high.



source:Bloooberg



Canada

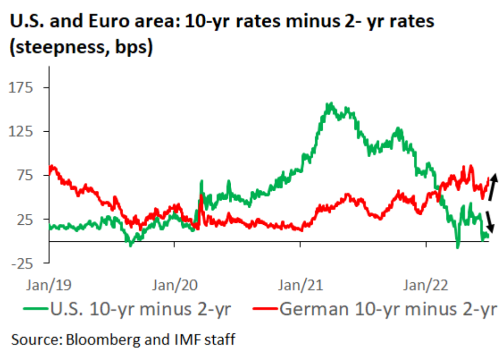
Canadian government bond yields fell 5–10 bps across the curve as global growth concerns intensifying. **According to Statistic Canada, real GDP is projected to decrease 0.2% m/m in May following an expansion of 0.3% in April and 0.7% in March**. **Analysts think a weak economic forecast**

is unlikely to deter the Bank of Canada from aggressive tightening as the CPI data recently showed the largest increase in three decades (7.7% y/y in May). Ten-year yields have declined the last few weeks after reaching a decade-high of 3.66% earlier in June, as a fall in oil prices and ongoing recession fears have weighed on market sentiment. However, markets are still pricing in more than a 90% probability of a 75 bps hike at the July meeting.

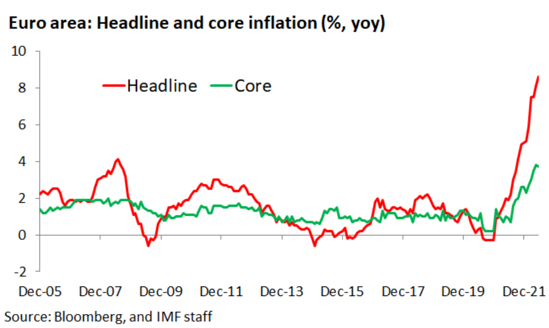
Euro area

The euro (-0.2%) edged lower and equities and bund yields were little changed after euro area headline inflation surprised to the upside, but core inflation was lower than expected. Final euro area PMI data confirmed that the euro area is still in expansionary territory, but new orders and business expectations fell.

The German yield curve remains relatively steep as the yield curve has flattened in the US. This divergence has created quite some chatter among contacts as yield curves tend to flatten into a tightening cycle when growth is slowing. Some contacts argue that some banks and insurers could be driving flows but other believe this is not very convincing.



Euro area headline inflation rose to 8.6% y/y (8.5% expected) in June from 8.1% in May, but core inflation was lower than expected at 3.7% y/y (3.9% expected). Analysts link the drop in euro area core inflation to fiscal measures in Germany (such as the €9 euro ticket for public transportation this summer). **Contacts believe that upside risks to inflation remain, especially given upside surprises to inflation in Italy and Spain this week.** Headline inflation in Italy unexpectedly rose to 8.5% y/y (7.9% y/y expected) and was up 1.2% m/m in June.



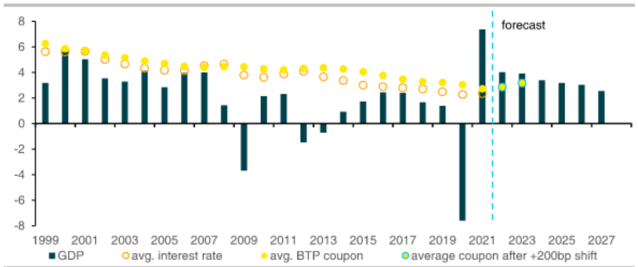
Italian spreads (-2 bps to 191 bps) are tighter as ECB starts flexibility in the reinvestment of its PEPP redemptions today. According to ECB sources, the ECB plans to use the proceeds from maturing debt purchased from so-called donor countries in its PEPP holdings to buy bonds from recipient countries—including Greece, Italy, Spain, and Portugal. **The central bank has reportedly split the euro area's 19**

countries into three groups based on the size and speed of an increase in spreads over German government bunds. Donors reportedly include Germany, France, and the Netherlands. Recipients are considered riskier, while neutrals act as a buffer.

Analysts at Commerzbank argue that Italy can afford higher yields but warn that investor sentiment will be key as Italy will have to attract new investors again in 2022 when PEPP reinvestment flows slow down, and political risks increase. The bank finds that Italian rates will stay below nominal GDP growth even under a yield shift of 200 bps.

Italian rates to stay below nominal GDP growth even under 200bp yield shift

Italy: Nominal GDP growth rate, average interest rate on Italian debt and average coupon on Italian BTPs, incl. projection under 200bp parallell yield curve shift, in %

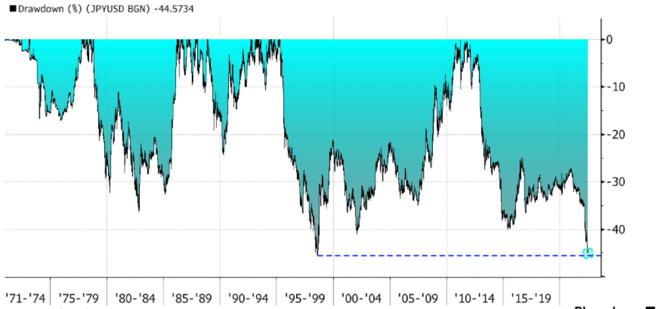


Source: Bloomberg, Commerzbank Research

Japan

Equities slumped -1.4%. Large manufacturer confidence fell below expectations in Q2. Tankan survey results showed +9 (consensus: +13, previous: +14) reflecting deteriorated terms of trade. Non-manufacturers' confidence improved to +13 (previous: +9). Also, **Tokyo inflation, excluding food, firmed to 2.1% y/y in June** (previous: 1.9%). Higher inflation was driven by tightened supply constraints and a durable goods price surge amid yen depreciation, according to JP Morgan. Government oil subsidies for wholesale companies likely offset gasoline and heating oil inflation by 0.2%, Citi estimated. Separately, **Japan's GPIF returned +5.4% for fiscal year 2021.** Foreign equities (+18.5%) and a weakened yen were the main contributors to strong performance. The fund, however, posted its first quarterly loss in two years in January-March 2022 (-1.1%) due to declines in global stock and bond markets.

Yen just a hair's breadth away from its worst drawdown ever



Source: Bloomberg

Emerging Markets

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In **Latin America**, the Brazilian real, the Peruvian Sol and the Colombian Peso all declined yesterday by ~1% largely on the back of weaker commodity prices and poor risk sentiment globally. The **Colombian** peso failed to benefit from the announcement of a new finance minister (Ocampo) that is widely known to the markets. Additionally, the Colombian central bank raised rates by 150 bps to 7.5% after the local market close, in line with market expectations and with a unanimous decision from the Board (below chart).

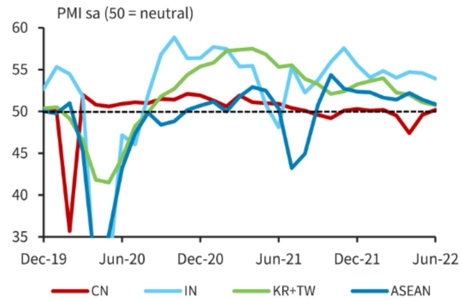
Table 1. Central bank of Colombia recent monetary policy decision

Date	30-Sep-21	29-Oct-21	17-Dec-22	26-Jan-22	31-Mar-22	29-Apr-22	30-Jun-22
Previous rate	1.75%	2.00%	2.50%	3.00%	4.00%	5.00%	6.00%
Decision (size of hike)	0.25%	0.50%	0.50%	1.00%	1.00%	1.00%	1.50%
New rate	**2.00%**	**2.50%**	**3.00%**	**4.00%**	**5.00%**	**6.00%**	**7.50%**
Vote for 150bp hike					2	3	7
Vote for 100bp hike				5	5	4	
Vote for 75bp hike			3	2			
Vote for 50bp hike	3	5	4				
Votes for 25bp hike	4	2					

Source: BanRep

Asian equities slipped -0.9% on net. Taiwan, Province of China fell -3.3%, Indonesia lost -1.7%, Sri Lanka gained +1.5%. **Asian currencies mostly weakened.** Thai baht depreciated -0.8%. **Indian rupee** weakened -0.1%. The currency depreciated to a new record of 79 per US dollar (-6% YTD) as equity outflows by foreign investors reached $28 bn by end June. On Friday, the government increased levies on gasoline and diesel exports and raised gold import duties to 12.5% following a surge of gold imports in May and June. Banks were reporting dollar shortages as investors and companies rushed to swap the rupee for other assets or to pay for imports, Bloomberg reported. **Regional manufacturing PMIs declined modestly in June but remained expansionary.** Export orders slowed across all economies except Thailand (+1.6 pts). Barclay's forecasts regional manufacturing will face continued uncertainty and price pressure drags but will land softly as the growth driver shifts to services.

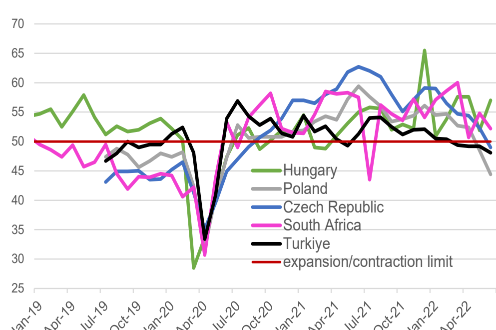
. Manufacturing PMIs ex-China moderated in June



Source: S&P Global Markit, Barclays Research

Equity markets were generally up in EMEA, while currencies were weakening. Stock indices were gaining across the board, except in the Czech Republic (-1%). Central and Eastern European currencies were weaker against the euro. The Polish zloty was down 0.4% (to 4.7/euro) as data releases showed high inflation and a larger than expected manufacturing contraction. Yields on local bonds in central and eastern Europe, which have shown extreme volatility over the last month, were down again. PMI data releases imply that activity is slowing everywhere in EMEA, except in Hungary, with activity remaining in expansion territory in June only in Hungary and South Africa.

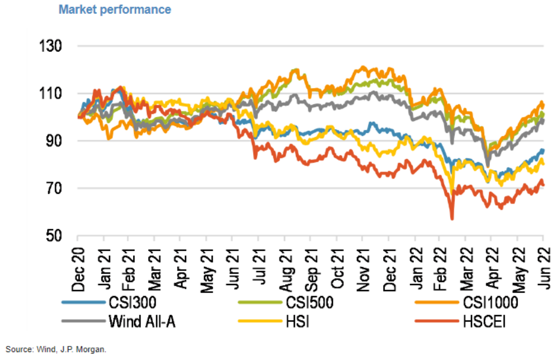
EMEA: Manufacturing PMIs



Source: Bloomberg and IMF

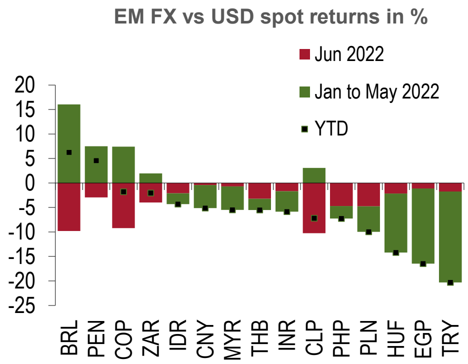
China

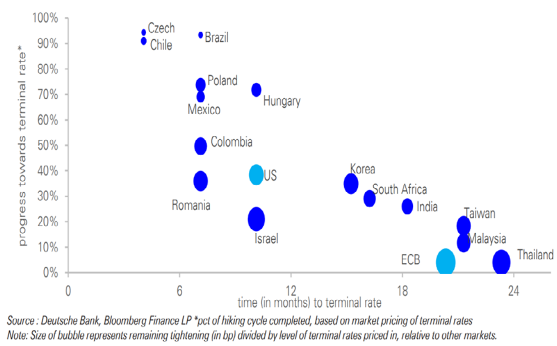
China's government will raise an additional 300 bn yuan ($44.8 bn) for infrastructure projects. The Wednesday State Council decision will replenish funds for major projects to expand effective investment, drive employment, and facilitate consumption, while not over-stimulating the economy, state-owned Xinhua reported. Separately, **Caixin manufacturing PMI rose more than expected to 51.7 in May** (consensus: 50.2, previous: 48.1), alongside official readings released yesterday. **Equities slipped mildly (Shanghai: -0.3%, Shenzhen: -0.2%)**. China's recurring current account surplus, room for stimulus, and lower financing costs amid contained inflation make China equities a compelling investment case, JP Morgan notes. **Renminbi weakened (onshore: -0.1%, offshore: -0.3%), 10-year yields were little changed.**



Latin American Currency Performance

Market sentiment soured in June after a notable outperformance earlier in 2022 (left chart). The appeal of high interest rate differentials started to decline as advanced economy central banks became more hawkish and some central banks in Latin America signaled that their tightening cycles are approaching the end. Additionally, the decline in industrial metals amid global growth concerns was felt in key exporters like Chile where the peso had its worst month in more than a decade. Finally, political developments have also played a role including the negative market reaction to the election outcome in Colombia and increased concerns about fiscal risks in Brazil ahead of the October election.





Source: Bloomberg

This monitor is prepared under the guidance of Ranjit Singh (Assistant Director), Nassira Abbas (Deputy Division Chief), Charles Cohen (Deputy Division Chief), and Antonio Garcia-Pascual (Deputy Division Chief). Fabio Cortes (Senior Economist), Reinout De Bock (Economist-London Representative), Sanjay Hazarika (Senior Financial Sector Expert), Esti Kemp (Financial Sector Expert-London Representative), Tom Piontek (Financial Sector Expert) and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Yingyuan Chen (Financial Sector Expert), Mohamed Diaby (Economist, EP), Dimitris Drakopoulos (Senior Financial Sector Expert), Deepali Gautam (Research Officer), Frank Hespeler (Senior Financial Sector Expert), Shoko Ikarashi (Externally Financed Appointee), Phakawa Jeasakul (IMF Resident Representative in Hong Kong SAR), Johannes S Kramer (New York Representative), Aurelie Martin (Senior Economist- London Representative), Kleopatra Nikolaou (Senior Financial Sector Expert), Natalia Novikova (IMF Resident Representative in Singapore), Patrick Schneider (Financial Sector Expert), Dmitry Yakovlev (Senior Research Officer), Akihiko Yokoyama (Senior Financial Sector Expert), and Xingmi Zheng (Research Assistant). Javier Chang (Senior Administrative Assistant) Olga Lefebvre (Staff Assistant), and Srujana Sammeta (Staff Assistant) are responsible for the word processing and production of this monitor.

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Global Financial Indicators

Last updated: 7/1/22 8:06 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD	Since 23-Feb-22
Equities					%		%	%
United States		3778	-0.9	-3	-8	-13	-21	-11
Europe		3439	-0.5	-3	-9	-16	-20	-13
Japan		25936	-1.7	-2	-7	-10	-10	-2
China		4467	-0.4	2	9	-12	-10	-3
Asia Ex Japan		69	-0.2	1	-3	-26	-16	-13
Emerging Markets		40	-0.5	1	-5	-27	-18	-16
Interest Rates					basis points			
US 10y Yield		2.94	-7.4	-19	3	148	143	95
Germany 10y Yield		1.30	-3.5	-14	11	150	148	107
Japan 10y Yield		0.23	-0.5	0	-1	18	16	3
UK 10y Yield		2.16	-6.7	-14	1	143	119	68
Credit Spreads					basis points			
US Investment Grade		180	1.8	11	29	93	68	37
US High Yield		596	11.1	67	167	288	258	189
Europe IG		119	0.1	9	29	73	71	47
Europe HY		580	0.6	47	134	351	339	229
Exchange Rates					%			
USD/Majors		105.17	0.5	1	3	14	10	9
EUR/USD		1.04	-0.5	-1	-2	-12	-8	-8
USD/JPY		135.3	-0.3	0	4	21	18	18
EM/USD		51.1	-1.0	-1	-3	-10	-3	-4
Commodities					%			
Brent Crude Oil ($/barrel)		112	2.8	3	-1	62	50	23
Industrials Metals (index)		151	-2.9	-4	-18	-2	-13	-19
Agriculture (index)		68	0.0	-1	-8	19	13	-2
Implied Volatility					%			
VIX Index (%, change in pp)		28.8	0.1	1.6	3.1	13.3	11.6	-2.2
US 10y Swaption Volatility		127.9	-0.2	8.1	19.3	60.7	48.9	33.6
Global FX Volatility		11.1	0.0	0.2	1.4	4.3	3.7	3.6
EA Sovereign Spreads					10-Year spread vs. Germany (bps)			
Greece		224	-3.7	-9	-23	121	73	-16
Italy		189	-4.2	-13	-13	88	54	17
Portugal		107	-1.1	-1	-8	49	43	15
Spain		107	-1.8	-4	-5	47	33	4

Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

Emerging Market Financial Indicators

Last updated: 7/1/2022 8:08 AM	Exchange Rates								Local Currency Bond Yields (GBI EM)							
	Level		Change (in %)					Since	Level		Change (in basis points)					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
		vs. USD	(+) = EM appreciation							% p.a.						
China		6.70	0.0	-0.2	0	-3	-5	-6		2.9	0.6	0	7	-27	8	6
Indonesia		14938	-0.3	-0.6	-2	-3	-5	-4		7.3	4.4	-7	22	68	88	77
India		79	-0.1	-0.9	-2	-6	-6	-6		6.3	0.0	0	9	75	0	
Philippines		55	-0.2	-0.2	-5	-11	-7	-7		5.7	0.0	0	20	155	118	68
Thailand		36	-0.8	-0.4	-4	-10	-6	-9		2.8	-8.0	6	-16	102	96	59
Malaysia		4.41	0.0	-0.1	-1	-6	-5	-5		4.2	-4.1	3	0	95	63	56
Argentina		125	-0.1	-0.9	-4	-24	-18	-14		60.1	12.3	56	398	1467	954	1214
Brazil		5.29	-0.6	-0.9	-9	-5	5	-5		12.7	-26.6	-5	17	336	197	113
Chile		918	0.7	-1.5	-10	-20	-7	-14		6.4	0.0	6	26	208	96	47
Colombia		4155	-0.9	-1.1	-9	-10	-2	-6		9.0	0.0	-3	64	310	260	113
Mexico		20.25	-0.6	-1.9	-3	-1	1	0		8.9	0.0	6	29	179	137	105
Peru		3.8	-1.0	-1.7	-3	1	5	-2		7.8	-0.3	3	22	235	185	175
Uruguay		40	-0.6	-0.2	0	10	12	6		10.6	1.1	-14	36	274	189	246
Hungary		384	-1.6	-1.0	-3	-23	-16	-17		7.9	-3.0	-1	82	507	334	304
Poland		4.52	-0.8	-1.7	-5	-16	-11	-10		6.3	-36.0	-51	-11	449	272	235
Romania		4.7	-0.4	-1.1	-2	-12	-8	-8		8.7	-0.4	-6	98	595	390	357
Russia		55.1	-1.7	-1.2	15	33	36	48		8.1	0.0	-13	-5	83	-67	-308
South Africa		16.4	-0.9	-3.8	-5	-12	-3	-8		9.0	-5.0	22	53	157	157	141
Turkey		16.75	-0.3	1.1	-2	-48	-21	-17		19.4	6.0	-16	-313	184	-495	-305
US (DXY; 5y UST)		105	0.5	1.0	3	14	10	9		2.93	-10.7	-25	2	204	167	103

	Equity Markets								Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)					Since	Level		Change (in basis points)				Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22	Last 12m	Latest	7 Days	30 Days	12 M	YTD	23-Feb-22
										basis points					
China		4467	-0.4	2	9	-12	-10	-3		199	3	-14	-4	-4	-9
Indonesia		6794	-1.7	-4	-5	13	3	-2		216	9	16	42	51	31
India		52908	-0.2	0	-5	1	-9	-8		193	13	13	51	61	39
Philippines		6165	0.2	-1	-9	-12	-13	-16		164	17	22	61	63	27
Thailand		1573	0.3	0	-5	0	-5	-7							
Malaysia		1450	0.4	1	-6	-5	-8	-9		129	-1	-1	6	12	-4
Argentina		88450	0.4	6	-3	43	6	-3		2430	142	514	851	750	693
Brazil		98542	-1.1	0	-12	-22	-6	-12		368	20	62	109	57	37
Chile		4950	-1.2	0	-7	14	15	13		179	6	18	37	39	5
Colombia		1323	-1.8	-1	-18	5	-6	-12		444	26	91	193	96	52
Mexico		47524	-1.1	2	-8	-6	-11	-7		457	24	89	115	125	87
Peru		18389	-1.5	-1	-11	-2	-13	-21		207	9	32	47	57	17
Hungary		39446	0.5	0	-3	-18	-22	-17		238	6	16	102	114	85
Poland		53526	-0.1	1	-6	-20	-23	-15		92	12	75	57	60	76
Romania		12388	0.8	0	-1	4	-5	-6		347	27	92	166	154	114
Russia		2227	1.0	-7	-6	-42	-41	-28		3411	-577	938	3228	3234	2897
South Africa		66116	-0.2	0	-7	-1	-10	-12		523	73	142	200	168	134
Turkey		2433	1.1	-5	-5	77	31	21		713	74	117	249	135	150
Ukraine		519	0.0	0	0	-2	-1	0		5086	831	1843	4596	4327	3613
EM total		40	-0.8	1	-5	-27	-18	-16		461	26	70	105	75	3

Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

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