Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Friday, July 12, 2019

- **Global volume of negative yielding debt is at historical highs (link)**
- **US Treasuries sell off on higher-than-expected CPI print (link)**
- **ECB minutes show "broad agreement" for further easing (link)**
- **Bank of Thailand announces measures to curb baht appreciation (link)**
- **Brazilian pension reform passes its first legislative test (link)**
- **Serbian central bank unexpectedly cuts policy rate by 25 bps to 2.75% (link)**

US | Europe | Other Mature | Emerging Markets | Market Tables

Global equities grind higher amid summer trading conditions

Price action was limited overnight in the wake of this week's testimony from Fed Chair Powell and the release of the minutes from the latest policy meetings at the Fed and the ECB. In the US, the consensus expectation has firmed that the Fed will deliver a cut in policy rates at its upcoming July 31 meeting. Fed watchers have shifted their focus to the probability of additional easing after the July meeting amid a broader global slowdown. Trade negotiations and the looming debt ceiling will also likely remain topics for US market participants through the summer. In Europe, yesterday's ECB minutes confirmed the broad-based support within the governing council for easing in the months of to come. While 10-year European government yields have risen fairly notably this week, many ascribe the price action largely to positioning and the recent heavy duration supply. In emerging markets, hard currency bond funds continue to see robust inflows, while outflows continue from EM-dedicated equity funds.

Key Global Financial Indicators

Last updated: 7/12/19 8:32 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
S&P 500		3000	0.2	0	4	7	20
Eurostoxx 50		3500	0.1	-1	3	2	17
Nikkei 225		21686	0.2	0	3	-2	8
MSCI EM		43	0.3	-1	3	-2	10
Yields and Spreads				bps			
US 10y Yield		2.13	7.6	10	1	-71	-55
Germany 10y Yield		-0.21	1.8	16	3	-56	-45
EMBIG Sovereign Spread		334	2	0	-24	-12	-80
FX / Commodities / Volatility				%			
EM FX vs. USD, (+) = appreciation		63.1	-0.1	0	2	-3	1
Dollar index, (+) = $ appreciation		97.0	-0.1	0	0	2	1
Brent Crude Oil ($/barrel)		66.8	0.5	4	11	-10	24
VIX Index (%, change in pp)		12.7	-0.3	-1	-3	0	-13

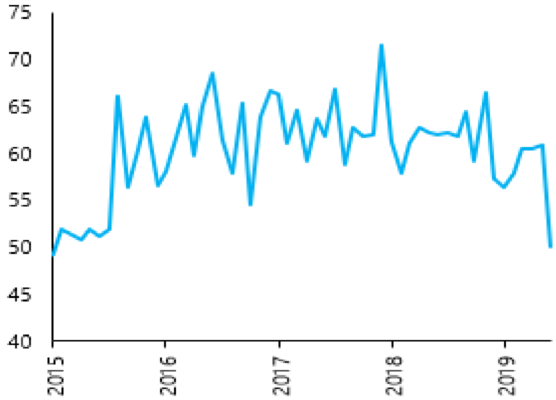
Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

United States

back to top

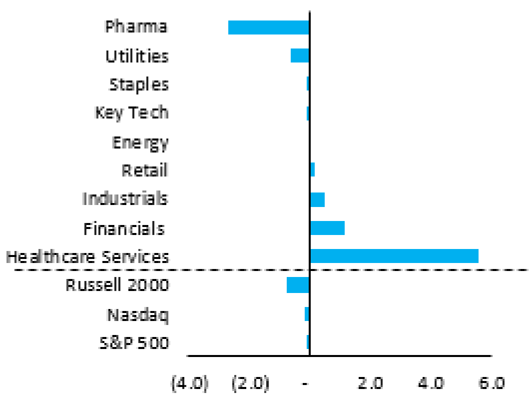
Stronger-than-expected inflation prints on Thursday led to a sell-off in the rates, with 10-year Treasury yields rising by 8 bps (to 2.14%) and 2-year yields rising by 3 bps (to 1.86%). The longer-end Treasuries were also impacted by a weak 30-year bond auction. The bid-to-cover ratio, at 2.13x, was reportedly the lowest of the past decade. Analysts also indicated that the take-up at Thursday's auction was particularly poor among indirect bidders, a class of investors that includes pensions and mutual funds. Their share of 50% was the lowest since February 2015, and well below the 60.8% they took at the prior auction in May. While the S&P 500 was broadly unchanged on Thursday, there was significant sectoral deviation after the Trump administration withdrew a rule that would kill drug rebates. The healthcare services sub-segment was up 5.5%, which was partially offset by the 2%+ decline in the biotech and drug-makers indices.

% of 30-yr sale taken by indirect bidders



Source: Bloomberg

Performance on 11th June: Key US (Sub) Indices

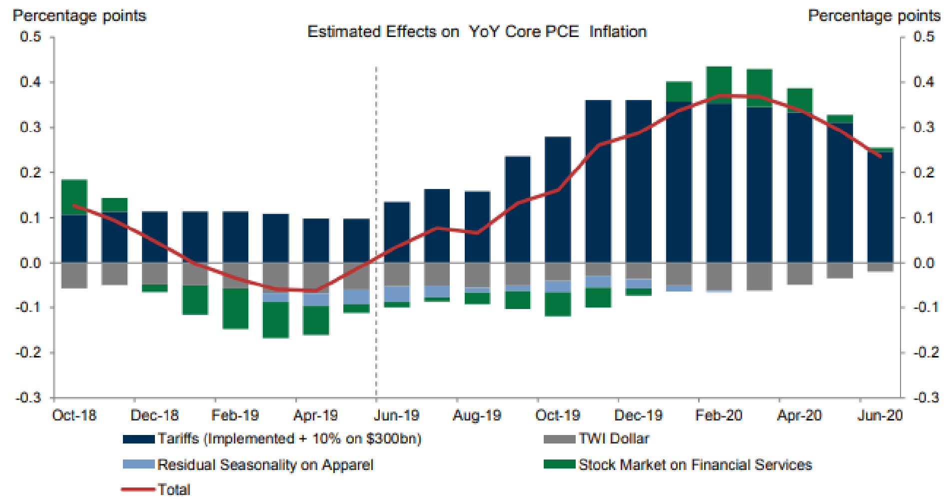


Source: Bloomberg

Chair Powell testified that the central bank has room to ease as the tie between the inflation and jobless rates has weakened. He also stressed that the U.S. economy is "in a very good place." That said, the central bank wants "to use our tools to keep it there," and offset weakness stemming from a global slump in manufacturing and business confidence linked to trade tensions. NY Fed President Williams said that arguments for easing have strengthened, while the Atlanta and Richmond Fed presidents said a July cut may not be warranted. The yield curve steepened across tenors, continuing the trend this week, though remains flatter versus historical levels.

Market analysts highlight that the inflation impulse from tariffs, the dollar and the stock market is likely to rise. GS economists find that a significant portion of the core PCE shortfall (relative to the 2.25% pace in 2006-07) is concentrated in medical categories. Outside of medical and cyclical categories, the analysts estimated that the current 0.1 ppt boost from tariffs roughly offsets the drags from past dollar appreciation, residual seasonality in apparel, and the January decline in financial services prices partially due to the Q4 stock market selloff. However, analysts expect these four forces to become more inflationary over the next year with a peak combined boost of nearly 0.4pp in March. **5-year TIPS inflation breakeven rates rose by 3 bps today, extending the increase this week to 8 bps.**

Exhibit 4: The Inflation Impulse from Tariffs, the Dollar, the Stock Market and Apparel Residual Seasonality Is Likely to Rise



Source: Goldman Sachs Global Investment Research

Note: assumes a 10% tariff on $300bn of remaining imports from China, a flat dollar & historically average equity gain

This morning, headline PPI for the June for the US was reported at 1.7% y/y, ahead of consensus expectations of 1.6% and compares with the 1.8% print in May. Core PPI at 2.3% y/y also surpassed expectations of 2.1% y/y. The yield on 2-year notes rose 1 bp immediately following the release.

Europe

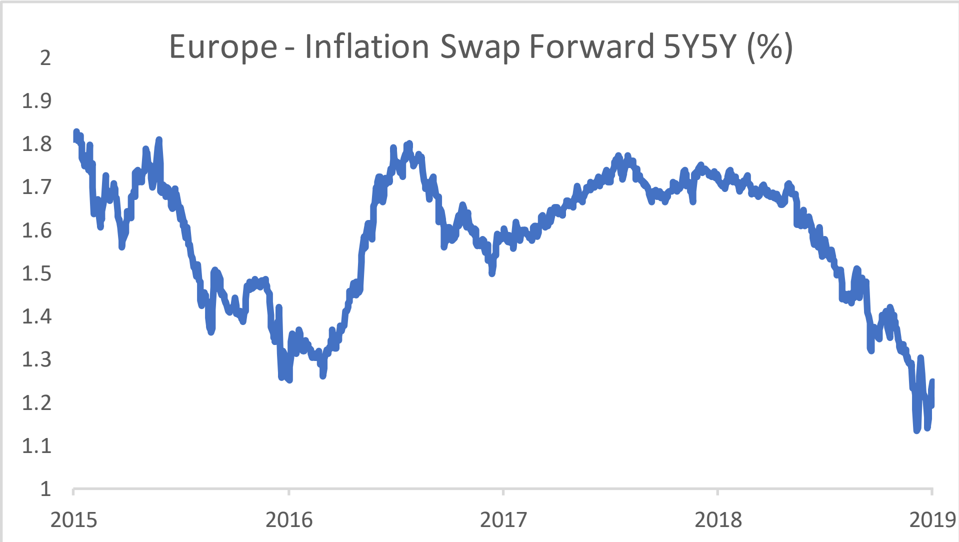
back to top

Europe

Sovereign yields were mixed this morning. Italy and UK saw a slight drop in borrowing costs while Spanish and Portuguese 10-years were 3 to 4 bps higher. Bund yields were little changed and continue to trade at the highest levels since mid-June. **Equities were moderately higher across the continent.** The Euro Stoxx 600 was up by 0.2% with banks (+0.7%) outperforming. Deutsche Bank (+1.7%) rose for the third consecutive day as investors continue to mull the likely effects of the bank's restructuring. On the data front, industrial production in the euro area beat expectations. The May print saw seasonally adjusted growth of 0.9% m-o-m compared to expectations of 0.2%.

The probability of a no-deal Brexit has increased recently according to the Bank of England. In its latest Financial Stability Report, the bank said that such a scenario would entail "material risks of economic disruption" as well as increased market volatility. During the subsequent press conference, governor Carney said that no deal would constitute a "major economic shock", despite extensive preparations by policymakers and banks' sizeable buffers. Apart from Brexit, the report flagged global trade as the other key risk to financial stability.

Minutes from last month's ECB meeting showed "broad agreement" that the bank needed to be ready to ease monetary policy further. In terms of instrument, the minutes provided support for using continued forward guidance, resuming net asset purchases, as well as decreasing policy rates further. The minutes also took note of market developments, including the recent fall in sovereign yields as well as the "trend decline" in five-year, five-year inflation swaps. The latter reached a low of 1.14% last month but has edged higher since and is currently trading at 1.25%.



Source: Bloomberg

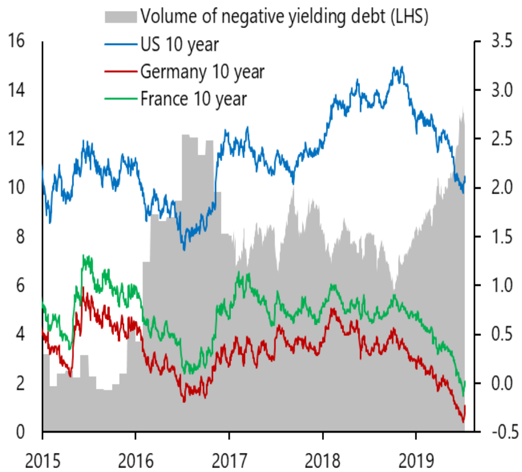
Irish finance minister Donohoe approved a request from the country's central bank to activate a systemic risk buffer for banks. The buffer represents an additional tool for the central bank which has described it as a measure to add resilience against tail risks. Separately, Donohoe told reporters that the prospect of a disorderly Brexit is now a "significant risk".

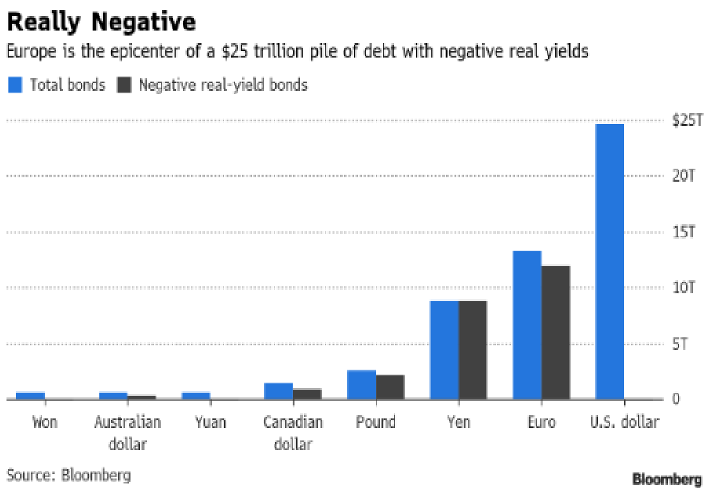
Other Mature Markets

back to top

Mature credit markets

Notwithstanding the recent pick up in global yields, the global volume of negative yielding debt (in the Bloomberg Barclays Global Agg Index) remains at historical highs touching $13tn recently. Bloomberg analysis also highlights that once adjusted for inflation, the global volume of negative *real* yielding debt increases to more than $25tn. The majority of this negative debt is housed in Europe.





Japan

Equities (-0.1%) were little changed on average volumes. Financials outperformed on rising bond yields and a steepening yield curve. **10-year JGB yields rose 2bps to -0.13% and the yen appreciated a modest 0.2%**.

Emerging Markets

back to top

Emerging markets experienced a mixed session. Asian equities were little changed on net. China and India (+0.4%) outperformed, while Southeast Asian bourses traded lower as weak Q2 GDP data from trade bellwether Singapore signaled a further slowdown in regional trade and growth momentum. Regional currencies were stable except the baht (-0.8%) on the BoT announcing measures to curb inflows and the Korean won (-0.5%) as Korea called for an international probe of Japanese claims that it allowed sensitive material to be exported to North Korea. Stocks in EMEA were mixed this morning. Hungary (+0.5%) and Poland (+0.2%) edged higher while Russia and Turkey (both -0.6%) saw losses. Currencies in the region were mostly flat against the dollar although Turkey (-0.6%) and Russia (-0.4%) saw some weakness. Latin American equity markets were mixed yesterday but mainly traded in narrow ranges. Local currencies were mostly stronger, and the Chilean peso outperformed (+0.7%). 10-year government bond yields were mixed as well.

Key Emerging Market Financial Indicators

Last updated:	Level		Change				
7/12/19 8:34 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		42.82	0.3	-1	3	-2	10
MSCI Frontier Equities		30.37	-0.1	1	1	5	16
EMBIG Sovereign Spread (in bps)		334	2	0	-24	-12	-80
EM FX vs. USD		63.07	-0.2	0	2	-3	1
Major EM FX vs. USD					%, (+) = EM currency appreciation		
China Renminbi		6.88	-0.2	0	1	-3	0
Indonesian Rupiah		14008	0.4	1	2	3	3
Indian Rupee		68.68	-0.3	0	1	0	2
Argentine Peso		41.72	0.3	0	7	-34	-10
Brazil Real		3.75	0.0	2	3	3	3
Mexican Peso		19.06	0.1	0	1	0	3
Russian Ruble		63.08	-0.4	1	3	-1	10
South African Rand		13.97	0.0	1	6	-5	3
Turkish Lira		5.72	-0.8	-2	2	-15	-8
EM FX volatility		7.28	0.0	-0.3	-1.1	-2.8	-2.5

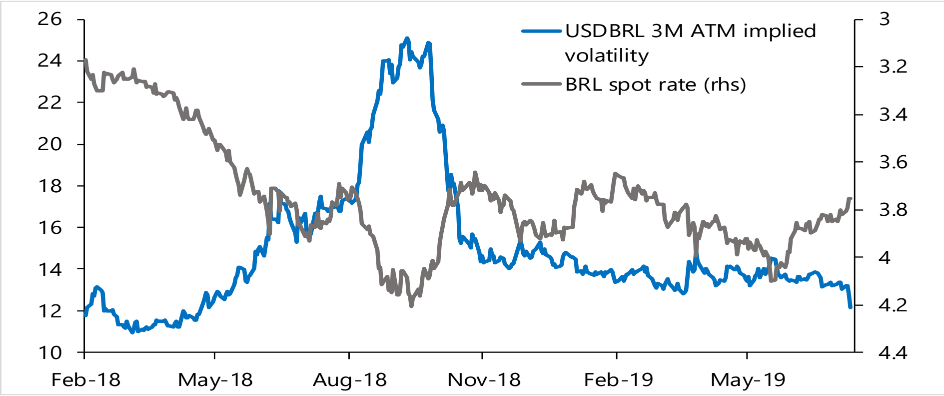
Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

Thailand

The Bank of Thailand (BOT) announced measures to "enhance surveillance of short-term capital flows" which analysts believe is intended to curb the baht's appreciation. The measures include reducing limits on non-resident baht accounts and increasing reporting requirements for non-resident's holding of debt securities issued in Thailand. The BoT had expressed concerns in its latest MPC statement over the recent baht appreciation in the context of weak growth momentum. Analysts viewed today's measures a relatively benign and probably of limited effectiveness beyond the short term. The baht depreciated 0.8% on the day, but remains Asia's best performing currency this year with an appreciation of 5.5% against the dollar.

Brazil

Brazil's pension reform passed its first vote in the Lower House late on Wednesday, with 379 votes to 131 against, a wider-than-expected majority. By raising the retirement age to 65 for men and 62 for women, the bill aims to save $250 bn in 10 years. The bill faces a second Lower House vote before moving to the Senate. Legislators and experts expected the bill to be passed around September. Despite the promising news on pension reform, Brazilian domestic equities edged up lower yesterday and the real was unchanged. However, **real implied volatility fell 4.6% yesterday, indicating increasing certainty from investors.**



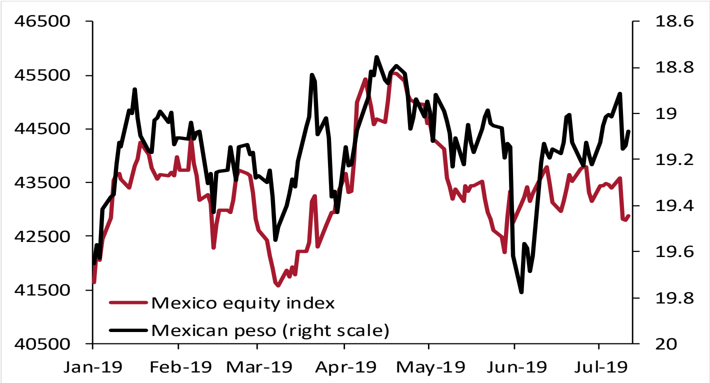
Source: Bloomberg

Serbia

The central bank unexpectedly cut interest rates yesterday by 25 bps. Almost all analysts had expected the bank to keep rates at 3% but the bank took advantage of declining inflation and a stronger currency. In its statement, the bank said that inflation will continue to move within the 1.5-4.5% target band and likely towards the lower end. The bank has recently been attempting to reduce the pace of dinar appreciation with purchases of foreign currency. According to Bloomberg, the bank bought €1 bn between last month's rate decision and July 9.

Mexico

Mexico's central bank published the minutes of the June 27 meeting yesterday. At the meeting, the board decided to keep the policy rate unchanged at 8.25%. Deputy Governor Gerardo Esquivel dissented, preferring a 25 bp rate cut. He mentioned several reasons such as improving inflation, monetary easing in advanced economies and economic slowdown. The committee agreed that the economy still faces the risk of uncertainty in inflation and emphasized the importance of preventing Pemex from experiencing further credit downgrades. Analysts commented that they expect Banxico to stay on hold for the near future. Market reaction to the minutes was muted, with both domestic equity and the peso closing slightly higher.



Source: Bloomberg

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Global Financial Indicators

Last updated: 7/12/19 8:33 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities			%				%
United States		3000	0.2	0	4	7	20
Europe		3500	0.1	-1	3	2	17
Japan		21686	0.2	0	3	-2	8
China		2931	0.4	-3	1	3	18
Asia Ex Japan		69	0.0	-2	3	-4	9
Emerging Markets		43	0.3	-1	3	-2	10
Interest Rates			basis points				
US 10y Yield		2.13	7.6	10	1	-71	-55
Germany 10y Yield		-0.21	1.8	16	3	-56	-45
Japan 10y Yield		-0.11	2.1	4	0	-15	-12
UK 10y Yield		0.84	0.1	10	-3	-45	-44
Credit Spreads			basis points				
US Investment Grade		118	0.4	0	-12	12	-29
US High Yield		428	0.6	0	-20	75	-93
Europe IG		49	0.3	-1	-12	-17	-38
Europe HY		246	1.0	2	-27	-52	-107
EMBIG Sovereign Spread		334	2.0	0	-24	-12	-80
Exchange Rates			%				
USD/Majors		97.00	-0.1	0	0	2	1
EUR/USD		1.13	0.0	0	0	-4	-2
USD/JPY		108.3	0.2	0	0	4	1
EM/USD		63.1	-0.1	0	2	-3	1
Commodities			%				
Brent Crude Oil ($/barrel)		67	0.5	4	11	-10	24
Industrials Metals (index)		113	0.2	2	2	-7	4
Agriculture (index)		41	-0.2	1	0	-3	0
Implied Volatility			%				
VIX Index (%, change in pp)		12.7	-0.3	-0.6	-3.2	0.1	-12.8
10y Treasury Volatility Index		4.4	0.1	0.0	-0.3	0.7	-0.2
Global FX Volatility		6.1	0.0	-0.1	-0.7	-2.0	-2.9
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		255	6.5	4	-44	-96	-160
Italy		193	0.6	-18	-74	-34	-57
Portugal		83	3.6	3	-6	-56	-65
Spain		75	5.0	6	-6	-18	-42

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

Data source: Bloomberg.

back to top

Emerging Market Financial Indicators

Last updated: 7/12/2019 8:36 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)						
	Level		Change (in %)					Level		Change (in basis points)				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
		vs. USD	(+) = EM appreciation						% p.a.					
China		6.88	-0.2	0.2	1	-3	0		3.2	-0.7	1	-7	-33	2
Indonesia		14008	0.4	0.5	2	3	3		7.2	-12.1	-9	-59	-46	-91
India		69	-0.3	-0.4	1	0	2		6.7	-3.0	-20	-47	-140	-76
Philippines		51	0.3	0.2	2	5	3		4.7	1.3	-7	-30	-115	-157
Thailand		31	-0.5	-0.4	1	7	5		2.1	-2.1	-3	-28	-59	-53
Malaysia		4.11	0.1	0.5	1	-2	0		3.6	-1.0	1	-10	-48	-48
Argentina		42	0.3	0.2	7	-34	-10		29.4	8.7	28	-151	988	643
Brazil		3.75	0.0	1.8	3	3	3		6.6	-0.1	-13	-60	-302	-153
Chile		681	0.1	0.4	2	-5	2		3.3	0.4	-1	-10	-153	-114
Colombia		3200	0.2	0.1	2	-10	2		5.7	6.7	18	-15	-69	-78
Mexico		19.06	0.1	-0.3	1	0	3		7.7	3.8	31	-6	-8	-101
Peru		3.3	-0.1	0.2	1	0	3		4.7	1.3	-5	-30	-84	-101
Uruguay		35	0.1	0.0	1	-11	-8		10.4	-5.7	-2	-69		-31
Hungary		290	0.0	-0.3	-2	-4	-3		1.6	6.0	16	-22	-95	-65
Poland		3.80	-0.1	-0.2	-1	-2	-2		2.0	4.1	2	-15	-59	-28
Romania		4.2	-0.1	0.0	-1	-5	-4		4.0	-4.0	-1	-11	-60	-23
Russia		63.1	-0.4	1.2	3	-1	10		7.2	-1.7	-5	-33	-21	-125
South Africa		14.0	0.0	1.5	6	-5	3		9.1	-5.9	-1	-25	-17	-46
Turkey		5.72	-0.8	-1.6	2	-15	-8		17.1	-13.3	92	-201	-144	19
US (DXY; 5y UST)		97.0	-0.1	-0.3	0	2	1		1.88	-1.1	5	1	-87	-63

	Equity Markets							Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)					Level		Change (in basis points)				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
								basis points						
China		2931	0.4	-3	1	3	18		177	0	0	-3	-16	-17
Indonesia		6373	-0.7	0	2	8	3		171	5	-6	-21	-33	-65
India		38736	-0.2	-2	-3	6	7		135	-4	-8	-19	-32	-61
Philippines		8142	-0.2	0	1	11	9		66	4	-1	-16	-58	-55
Malaysia		1669	-0.6	-1	1	-2	-1		115	0	-2	-16	-42	-47
Argentina		42856	0.1	3	5	60	41		790	1	3	-61	216	-25
Brazil		105146	-0.6	3	7	39	20		212	0	-14	-30	-83	-61
Chile		5075	0.0	0	0	-4	-1		129	-1	-2	-5	-11	-37
Colombia		1601	0.0	2	6	4	21		169	0	-6	-20	-14	-59
Mexico		42882	0.2	-1	-2	-12	3		326	-1	5	-5	57	-28
Peru		20699	-0.3	-1	1	5	7		109	0	-9	-21	-45	-59
Hungary		40757	0.0	-1	0	15	4		82	1	2	-16	-51	-66
Poland		60435	0.1	0	3	7	5		33	7	7	-20	-39	-52
Romania		9095	0.8	1	6	15	23		180	-4	-6	-9	16	-41
Russia		2770	-0.7	-2	1	19	17		193	5	-4	-17	-4	-59
South Africa		57412	0.2	0	-2	1	9		272	3	-8	-48	-22	-93
Turkey		97860	-1.5	-2	6	9	7		495	10	29	-30	42	66
Ukraine		543	0.3	-1	-2	10	-3		513	-1	-3	-65	-53	-274
EM total		43	0.3	-1	3	-2	10		334	2	0	-24	-12	-80

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