



- **ECB surprises with 50 bps rate hike** ([link](#))
- **Resignation of Italian PM Draghi hits markets** ([link](#))
- **Russian gas supplies resume** ([link](#))
- **Euro area consumer confidence falls to all time low** ([link](#))
- **Markets still predict terminal Fed rate around 3.50% despite inflation surprises** ([link](#))
- **Indonesia in spotlight as central bank stays dovish amidst rising risks** ([link](#))
- **Ukraine devalues currency by 25%** ([link](#))

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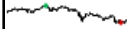
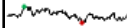
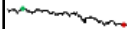
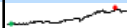


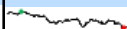



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## Markets grapple with multiple challenges

The ECB surprised markets with a 50 bps rate hike, with most expecting a 25 bps move. This is the first ECB rate hike since 2011. It also announced a new Transmission Protection Instrument (TPI) designed to alleviate stresses in local bond markets. European stocks fell 0.5% on the news, dragging US equity index futures prices lower. Euro area and US government bond yields pushed higher and the euro appreciated. Earlier, the resignation of Italian PM Draghi pushed local government bond spreads higher and introduced yet another major source of uncertainty to a euro area already reeling from the war in Ukraine, the prospect of natural gas shortages and stubbornly high inflation. However, the resumption of Nordstream 1 gas supplies from Russia was a major relief for investor sentiment. The Bank of Japan stayed on hold as expected while highlighting growth and inflation risks. Central banks in Indonesia, Turkey and Ukraine also stayed on hold but South Africa is expected to hike by 50 bps later today.

Key Global Financial Indicators

Last updated: 7/21/22 8:09 AM	Level		Change from Market Close				YTD	Since 23-Feb-22
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		
<b>Equities</b>			%				%	
S&P 500		3960	0.6	4	5	-9	-17	-6
Eurostoxx 50		3584	0.0	6	3	-11	-17	-10
Nikkei 225		27803	0.4	5	6	1	-3	5
MSCI EM		39	-0.4	2	-2	-26	-19	-17
<b>Yields and Spreads</b>			bps					
US 10y Yield		3.05	2.6	9	-22	176	154	106
Germany 10y Yield		1.29	3.0	11	-48	168	146	106
EMBIG Sovereign Spread		557	-15	-26	57	201	190	145
<b>FX / Commodities / Volatility</b>			%					
EM FX vs. USD, (+) = appreciation		50.0	-0.6	2	-4	-11	-5	-6
Dollar index, (+) = \$ appreciation		107.1	0.0	-1	3	15	12	11
Brent Crude Oil (\$/barrel)		102.6	-4.1	3	-11	42	32	6
VIX Index (% change in pp)		24.0	0.2	-2	-6	6	7	-7

Colors denote **tightening**/**easing** financial conditions for observations greater than  $\pm 1.5$  standard deviations. Data source: Bloomberg.

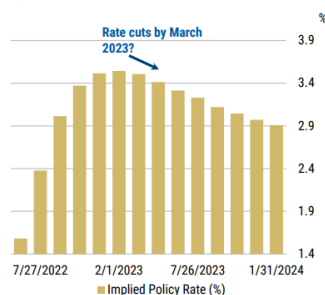
## Mature Markets

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### United States

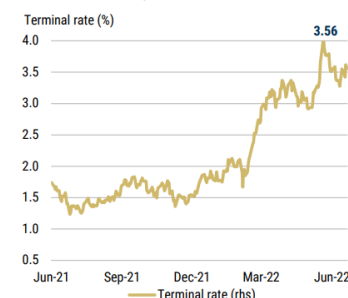
**Markets still expect a terminal Fed Funds rate around 3.50% next year despite each successive CPI print being worse than expected.** Recession fears have even driven interest rate futures markets to predict rate cuts in the first half of 2023. Such an outcome is likely only if inflation declines sharply to 2–3%, which nobody expects, or if the Fed pivots to fighting recession despite inflation remaining high by historical standards. The latter is only possible if inflation falls below the 8–9% currently prevailing to a more *acceptable* 4–5% range. The great danger for markets is that if inflation remains stuck at recent levels, the Fed will have no choice but to keep hiking rates despite the negative impact on the economy.

Exhibit 14: Market-implied path for fed funds rate in the next eighteen months



Source: Bloomberg, Morgan Stanley Research

Exhibit 15: Market-implied terminal rate over the last 12m

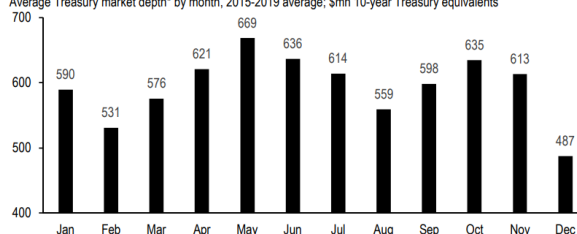


Source: Bloomberg, Morgan Stanley Research

**The Treasury market has experienced high volatility this year, and investors are bracing for further volatility going into August, which is usually a month with very low market liquidity.** Uncertainty about Fed interest rate policy and the pace of tightening has driven Treasury volatility to historically high levels. Market liquidity has worsened when volatility spikes higher. Next week's FOMC meeting on July 27 will be more important than traditional summer meetings as the Fed delivers another big rate hike and markets look for clues about how a potentially slowing economy will alter the trajectory of future Fed rate moves. The inverted yield curve is a symptom of worries about recession that is keeping a lid on long rates, but another bout of volatility could push rates much higher than their current levels. However, most contacts do not expect the 10-year Treasury yield to rise much above the 2022 peak close to 3.50% seen on June 14.

Exhibit 6: Seasonally, liquidity tends to weaken further in August, and given these dynamics, the Treasury market could be susceptible to continued sharp swings

Average Treasury market depth\* by month, 2015-2019 average; \$mn 10-year Treasury equivalents



Source: BrokerTec, J.P. Morgan

\* Market depth is the sum of the three bids and offers by queue position, averaged between 8:30 and 10:30am daily, using 2-, 5-, 10-, and 30-year Treasuries

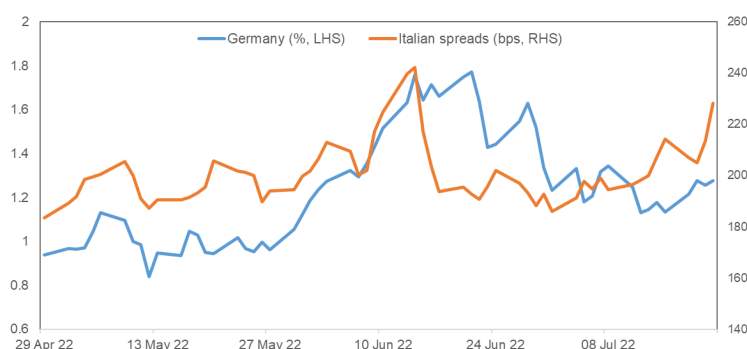
### Euro Area

**The ECB surprised markets with a 50 bps rate hike, with most expecting a 25 bps move although the larger move was very much part of the discussion prior to the meeting due to numerous leaks.** This is the first ECB rate hike since 2011. It also announced a new Transmission Protection Instrument (TPI) designed to alleviate stresses in local bond markets, with more details expected at the press conference later today. What drew the most attention was the statement that the TPI would not be limited

on ex ante basis, suggesting that the mechanism could be more powerful than originally envisaged. Italian equities initially fell by over 2% and banking stocks underperformed after PM Draghi announced that he will resign, although some losses were retraced in later trading.

**10-yr Italian spreads to bunds jumped 13 bps to 225 bps after PM Draghi resigned.** Analysts think early elections are likely, probably in October. Draghi's government will remain in place as a caretaker until then, with the next steps set to be agreed upon by the President and both houses of parliament later today. Analysts fear that the annual budget will be delayed, complicating the finalizing of economic reports required for EU recovery fund financing.

Europe: 10Y bund yield (%) and Italy-Germany 10-yr spreads (bps)



Source: Bloomberg and IMF calculations

**European natural gas prices eased (1-month ahead Dutch natural gas was down 6% to €146/MWh) as gas flows via Nord Stream 1 (NS1) were resumed after the scheduled maintenance came to an end this morning.** Gas flows reached 40% of pipeline capacity, according to Bloomberg reports, similar to levels seen prior to the scheduled maintenance. Concern remains over future gas supplies with the focus on increasing gas storage to 80% by November. EU gas storage is currently at 65%.

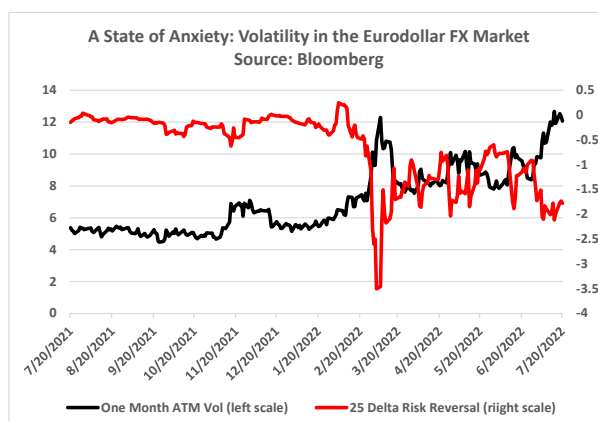
**Amid gas supply uncertainty, the EU yesterday shared proposals for natural gas consumption in member states to be reduced by 15% from August to March 2023, to ensure that a total gas cut-off from Russia is manageable.** The proposed measures are voluntary but also enables the EC to impose a mandatory reduction, if required. The proposal is set to be discussed on July 26.

**On the data front, preliminary July euro area consumer confidence fell to its lowest level since the survey started in 1985 (-27 vs expected -24.9 from -23.8).** Consumer sentiment deterioration was broad based across sub-components, with consumer particularly pessimistic regarding their ability to save and conduct large purchases over the next year.

### Foreign Exchange Markets

**Volatility in the eurodollar currency market has reached very high levels as market participants parse the rhetoric from the latest ECB press conference and uncertainty about Russian gas supplies remains front and center.** Short term (one month) at-the-money FX volatility is close to levels last seen during the first days of the Russian invasion of Ukraine. Overnight volatility hit 25% per annum. Worries over a potential cutoff or even a sharp reduction in Russian gas imports on the euro area economy has come to overshadow questions about the ECB's monetary policy. However, the FX options market is not as dislocated than the spot compared to the peak of volatility seen in February. The out of the money (25 delta) risk reversal, which involves buying euro calls in preference to dollar puts remains in favor of the dollar with a negative number, but the move is not as extreme as it was in February. Contacts speculate

that investors are less interested in cheap insurance against a major depreciation in the euro because they expect a resolution of some kind.



## Emerging Markets

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**EMEA equities were mixed while currencies generally weakened.** Equities in **Hungary** gained (+1.6%) while the Hungarian forint weakened against the euro (-0.8%) after Hungary left its one-week deposit rate unchanged at 9.75%, as expected. The **South African** rand weakened (-0.3%) against the dollar ahead of the monetary policy decision later today, where the central bank is expected to increase the repo rate by 50bps to 5.25%. **The Turkish lira (-0.4%) weakened for the fourth consecutive day** ahead of the central bank meeting where policy rates were left unchanged at 14%, despite headline inflation reaching 78.6% in June. **Asian equities were mixed, -0.2% on net, while currencies weakened.** LATAM markets were also mostly lower. The US and Canada have initiated dispute settlement consultations under the USMCA trade deal with Mexico over the latter's energy policy, which aims at nationalizing Mexico's energy sector.

## Emerging Market Bond Issuance

**EMs' net financing requirements look manageable despite low issuance and market challenges .** As per a JP Morgan report, 2022 bond issuances by EMs in the external markets (\$159 bn in 1H2022) has been less than half of the 2021 levels, with issuance by high yield or non-rated (HY/NR) countries even worse (less than 1/3 of 2021 volumes). Maturities, on the other hand, are on the rise and estimated at \$131 bn and \$268 bn in 2022 and 2023, respectively. However, 60–65% these maturities comprise of higher rated investment grade (IG) bonds, and originate in regions like Asia that have both access to international markets and sizable domestic bond markets.

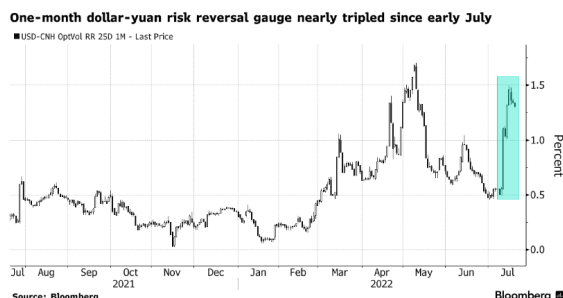
EM Corporate Bond Maturities: by Region and Top 3 Countries within (bn. USD)

	Overall		HY/NR		Local bonds	
	2022	2023	2022	2023	Outstanding	2021 supply
<b>Asia</b>	<b>95.8</b>	<b>182.4</b>	<b>28.4</b>	<b>46.9</b>	<b>9800</b>	<b>2556</b>
China	65.3	115.8	20.5	33.1	8049	2135
Korea	12.3	26.5	0.1	0.5	686	202
Hong Kong	5.1	10.2	2.7	1.5	36	9
<b>Emerging Europe</b>	<b>13</b>	<b>26.4</b>	<b>10.2</b>	<b>21.6</b>	<b>276</b>	<b>50</b>
Russia	4.8	13.8	4.8	13.8	149	28
Turkey	4.6	5.6	4.4	5.6	7	1
Czech Republic	0.3	1	0	0	12	1
<b>LatAm</b>	<b>15.6</b>	<b>30.6</b>	<b>10.8</b>	<b>20.1</b>	<b>262</b>	<b>55</b>
Mexico	5	7.7	2.3	5.7	64	8
Brazil	3.9	8.2	3.9	8	155	43
Chile	1.2	2.6	0	0	9	1
<b>Middle East &amp; Africa</b>	<b>6.9</b>	<b>28.9</b>	<b>4.2</b>	<b>7.7</b>	<b>185</b>	<b>29</b>
UAE	1.2	11.1	0.4	0.4	1	0
Saudi Arabia	0	3	0	0.5	30	6
Qatar	0.2	2.8	0	0.1	1	-

Sources: J.P. Morgan, Bloomberg Finance L.P., Bond Radar. As of June 30, 2022. Note: 2022 maturities for rest of the year.

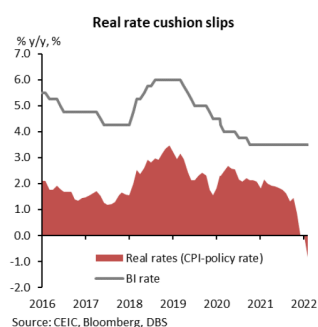
## China

**China's sovereign wealth fund is merging its private equity, infrastructure investments arm with its main operations.** China Investment Corp., a Beijing-based fund managing \$1.2 tn in assets, reportedly aims at boosting efficiency after a talent exodus and as offshore investing grows more complex, according to Bloomberg. Separately, China's holdings of the US Treasuries fell -\$21 bn to below \$1 tn in May. Meanwhile, the year-long probe into the rideshare company Didi ended with a fine exceeding 8 bn yuan (\$1.2 bn). The company's chairman and president were fined 1 mn yuan (\$148 k) each. Equities slipped (Shanghai: -1%, Shenzhen: -0.8%). 10-year yields were little changed. Renminbi weakened onshore -0.1%. One-month US dollar-yuan risk reversals have nearly tripled since start-July amid depreciative yuan pressures as investors use the FX options market to hedge against the risk of further yuan weakening.



## Indonesia

**Bank Indonesia (BI) kept its 7-day reverse repo rate unchanged at 3.5% as expected.** BI noted that core inflation remains manageable amid a global slowdown. However, policy normalization is still considered to be underway, the bank will continue bond sales to absorb liquidity and money market rates will be allowed to increase. BI estimated hiked reserve requirements to have mopped up 219 tn rupiah (\$15 bn) of liquidity since March 2022. The bank downgraded its current account forecast for 2022 (-0.5% to +0.3% of GDP, previous: -0.5% to 1.3%) but left growth (4.5–5.3%) and inflation (2–4%) projections unchanged. BI will also intervene in the FX market to stabilize the rupiah amid growing outflows from emerging markets. The cushion of real rates has turned negative as compared to the comfortable positive buffer at the start of the year, DBS highlighted. The rupiah may remain between 15,000 to 15,500 per US dollar, its weakest in more than two years, due to accelerated capital outflows and as a dovish BI lags its peers, Morgan Stanley noted.

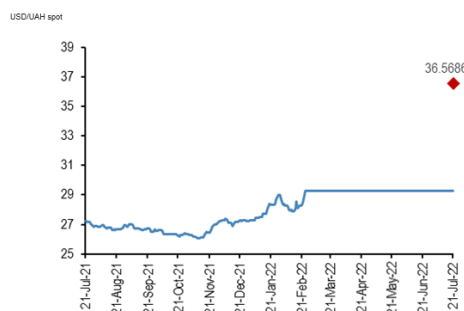


## Ukraine

**The central bank of Ukraine devalued the hryvnia exchange rate against the dollar by 25% pointing to a fundamental shift in the parameters of Ukraine's economy as well as US dollar strength.** The Hryvnia was devalued and fixed to 36.5686 per dollar, from 29.25—the level it was fixed at since Russia invaded Ukraine. **The central bank also left its key rate unchanged at 25%. JPMorgan analysts expect the devaluation to ease pressure on FX reserves.**

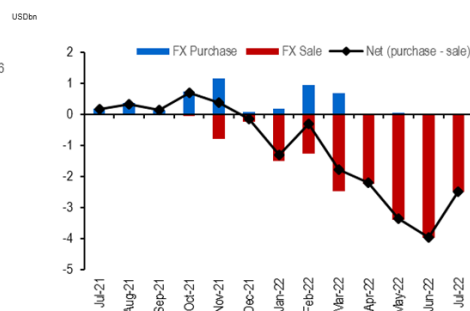
Yesterday, the group of governments in the Paris Club agreed to allow the suspension of Ukraine's debt service starting next month until the end of 2023, with an option to extend the suspension by another year. The FT reports that government lenders also encouraged private debtors to follow suit, while Ukraine said it would invite holders of Ukraine's eurobonds to allow similar terms.

Exhibit 1: Official USD/UAH level to be set at a level of 36.5686



Source: J.P. Morgan, NBU.

Exhibit 2: FX sales have seen a notable increase in recent months



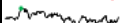











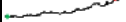




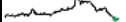



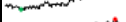






Source: J.P. Morgan, NBU. Note: Jul-22 date is of 15-Jul-22

*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

7/21/22 8:10 AM	Level		Change				YTD	Since 23-Feb-22
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		
Equities			%				%	%
United States		3962	0.6	5	5	-9	-17	-6
Europe		3584	0.0	6	3	-11	-17	-10
Japan		27803	0.4	5	6	1	-3	5
China		4236	-1.1	-2	-1	-18	-14	-8
Asia Ex Japan		68	-0.6	1	-2	-25	-18	-14
Emerging Markets		39	-0.4	2	-2	-26	-19	-17
Interest Rates			basis points					
US 10y Yield		3.05	2.6	9	-22	176	154	106
Germany 10y Yield		1.29	3.0	11	-48	168	146	106
Japan 10y Yield		0.24	-1.0	0	0	22	17	4
UK 10y Yield		2.19	5.5	9	-46	159	122	72
Credit Spreads			basis points					
US Investment Grade		171	0.0	-5	5	78	59	28
US High Yield		515	-4.2	-53	-4	182	177	108
Europe IG		111	0.1	-14	4	63	63	39
Europe HY		553	1.5	-66	16	314	311	201
Exchange Rates			%					
USD/Majors		107.10	0.0	-1	3	15	12	11
EUR/USD		1.02	0.2	2	-3	-13	-10	-10
USD/JPY		138.8	0.4	0	2	26	21	21
EM/USD		50.0	-0.6	2	-4	-11	-5	-6
Commodities			%					
Brent Crude Oil (\$/barrel)		103	-4.1	3	-8	54	37	15
Industrials Metals (index)		145	-0.9	4	-15	-6	-16	-22
Agriculture (index)		63	-1.4	0	-14	9	4	-10
Implied Volatility			%					
VIX Index (% change in pp)		24.0	0.2	-2.4	-6.2	6.1	6.8	-7.0
US 10y Swaption Volatility		120.6	3.1	-19.4	-13.1	42.8	41.5	26.3
Global FX Volatility		11.2	0.0	-1.1	0.1	4.3	3.7	3.7
EA Sovereign Spreads			10-Year spread vs. Germany (bps)					
Greece		230	9.5	-2	13	122	79	-10
Italy		226	12.5	19	33	118	91	55
Portugal		116	2.1	-3	12	51	52	24
Spain		125	1.8	9	16	58	50	21

Colors denote **tightening**/**easing** financial conditions for observations greater than  $\pm 1.5$  standard deviations. Data source: Bloomberg.

## Emerging Market Financial Indicators

Last updated: 7/21/2022 8:12 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)								
	Level		Change (in %)					Since 23-Feb-22	Level		Change (in basis points)				YTD	Since 23-Feb-22
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD		Last 12m	Latest	1 Day	7 Days	30 Days	12 M		
	vs. USD		(+)= EM appreciation						% p.a.							
China		6.77	-0.2	-0.2	-1	-4	-6	-7		2.8	-1.0	-3	-5	-18	-1	-2
Indonesia		15037	-0.3	-0.1	-1	-3	-5	-5		7.5	2.6	14	0	118	111	100
India		80	0.0	-0.1	-2	-7	-7	-7		6.3	0.0	0	9	75	0	
Philippines		56	-0.1	-0.4	-4	-11	-10	-9		5.7	0.0	0	0	173	118	68
Thailand		37	-0.6	-0.9	-4	-11	-10	-13		2.7	1.5	10	-13	107	83	45
Malaysia		4.46	-0.1	-0.3	-1	-5	-7	-6		4.0	-1.5	-1	-27	94	45	37
Argentina		129	-0.2	-1.2	-5	-26	-21	-17		68.7	74.0	156	705	2454	1810	2070
Brazil		5.47	0.1	-0.8	-6	-5	2	-8		13.9	37.3	69	120	458	323	239
Chile		926	0.0	8.8	-5	-18	-8	-15		7.0	0.0	2	58	290	153	104
Colombia		4342	-0.6	3.8	-6	-12	-6	-10		9.8	0.0	21	110	419	343	196
Mexico		20.54	0.1	1.3	-2	-2	0	-1		8.9	-3.3	-1	-18	207	135	103
Peru		3.9	-0.4	1.7	-4	2	3	-4		8.6	0.4	22	82	293	266	256
Uruguay		42	0.2	-1.5	-4	5	6	1		11.6	0.0	51	78	373	288	345
Hungary		392	-0.2	3.3	-4	-22	-17	-18		8.7	12.0	-12	37	616	417	387
Poland		4.67	0.4	3.0	-6	-17	-14	-13		6.0	-15.0	-26	-139	451	250	213
Romania		4.8	0.2	1.8	-3	-14	-10	-10		9.0	-2.5	-8	-17	600	419	386
Russia		58.0	-5.5	2.7	-5	28	30	41		8.7	4.0	37	36	143	-11	-252
South Africa		17.2	-0.1	-0.1	-7	-15	-7	-12		9.2	-9.0	-17	45	200	174	158
Turkey		17.69	-0.5	-1.4	-2	-52	-25	-22		17.4	-10.0	-148	-233	-6	-689	-499
US (DXY; 5y UST)		107	0.0	-1.3	3	15	12	11		3.18	2.1	12	-18	245	192	128

	Equity Markets							Bond Spreads on USD Debt (EMBIG)								
	Level		Change (in %)					Since 23-Feb-22	Level		Change (in basis points)				YTD	Since 23-Feb-22
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD		Last 12m	Latest	7 Days	30 Days	12 M	YTD		
									basis points							
China		4236	-1.1	-2	-1	-18	-14	-8		207	-4	15	-6	4	-1	
Indonesia		6864	-0.2	3	-2	12	4	-1		222	-12	22	33	57	37	
India		55682	0.5	4	7	5	-4	-3		204	-11	31	50	72	50	
Philippines		6256	-0.3	0	1	-5	-12	-15		157	-24	12	37	56	20	
Thailand		1546	0.5	1	-1	0	-7	-9		0	0	0	0	0	0	
Malaysia		1450	0.9	2	1	-5	-7	-9		144	0	19	6	27	11	
Argentina		106949	-0.2	5	24	62	28	17		2779	42	562	1188	1099	1042	
Brazil		98287	0.0	0	-1	-22	-6	-12		343	-42	-1	59	32	12	
Chile		5147	-0.3	0	1	20	19	18		183	-10	10	29	43	9	
Colombia		1303	1.7	-1	-10	5	-8	-14		425	-36	39	153	77	33	
Mexico		47132	-0.3	-1	-2	-6	-12	-8		441	-30	13	83	109	71	
Peru		18645	1.0	2	-5	-1	-12	-20		210	-8	8	44	60	20	
Hungary		41714	1.4	6	2	-13	-18	-13		244	7	3	95	120	91	
Poland		53193	-1.0	3	-2	-21	-23	-15		26	13	-74	-14	-6	10	
Romania		12164	0.6	2	-2	2	-7	-8		346	-4	32	148	153	114	
Russia		2050	-1.2	-1	-13	-45	-46	-34		3411	-577	938	3228	3234	2897	
South Africa		67605	-0.1	4	1	2	-8	-10		501	-67	43	151	146	112	
Turkey		2526	0.0	5	-2	87	36	25		717	-80	47	235	139	154	
Ukraine		519	0.0	0	0	-1	-1	0		7005	-365	3128	6488	6246	5532	
EM total		39	0.1	2	-2	-26	-19	-17		463	-31	34	93	77	5	

Colors denote **tightening**/easing financial conditions for observations greater than  $\pm 1.5$  standard deviations. Data source: Bloomberg.

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