Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Wednesday, July 3, 2019

The Global Markets Monitor will be on holiday for the remainder of the week and will resume service on Monday, July 8.

- **UK yields, rate cut bets surge on Carney trade warning, dismal June data (link)**
- **Analysts lowering their US Treasury yield forecasts (link)**
- **EU leaders agree nominations for top EU posts (link)**
- **Japan plans to restrict exports to Korea on a widening range of goods (link)**
- **Special Feature: EM Capital Flows Monitor (attached)**

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

Weak data and easing expectations lift markets

Bond yields are dropping and equities are inching higher as expectations for monetary easing are bolstered around the globe. The UK became the latest major economy to experience a disappointing PMI reading, adding fuel to a Gilt rally triggered by a gloomy speech yesterday on trade and no-deal Brexit risks by BoE Gov. Carney. The sizeable moves in UK yields (-14 bps since Monday's close) have spilled over to US and euro area bond markets, where recent gains have also been linked to the nomination of Christine Lagarde to helm the ECB, who analysts see as likely to continue Draghi's dovish policies. In the US, the Trump administration indicated it will nominate two candidates for Fed governor seen as likely to advocate lower interest rates. US markets will be closed for the holiday tomorrow, but investors will be scrutinizing this Friday's jobs numbers, which will be a critical data point for the FOMC as it decides whether to cut interest rates later in July, as is expected. Light trading conditions due to the shortened holiday week could set up significant volatility if the print defies expectations: the last payroll print to come on the Friday immediately after July 4th (in 2013) surprised to the upside and triggered a 24 bps surge in 10-year yields.

Key Global Financial Indicators

Last updated: 7/3/19 8:02 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
S&P 500		2973	0.3	2	8	10	19
Eurostoxx 50		3535	0.8	3	7	4	18
Nikkei 225		21638	-0.5	3	6	-1	8
MSCI EM		43	-0.3	2	5	1	11
Yields and Spreads				bps			
US 10y Yield		1.95	-5.0	-9	-12	-88	-73
Germany 10y Yield		-0.38	-1.6	-8	-18	-68	-63
EMBIG Sovereign Spread		341	0	-3	-43	-27	-73
FX / Commodities / Volatility				%			
EM FX vs. USD, (+) = appreciation		63.0	0.1	0	2	-2	1
Dollar index, (+) = $ appreciation		96.7	0.0	1	0	2	1
Brent Crude Oil ($/barrel)		63.1	1.1	-5	3	-19	17
VIX Index (%, change in pp)		13.0	0.1	-3	-6	-3	-12

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

United States

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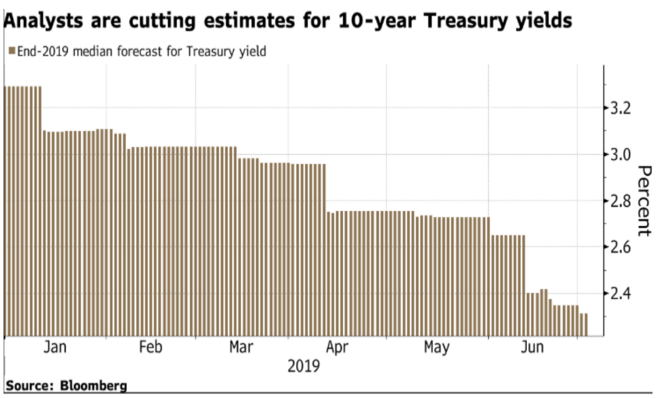
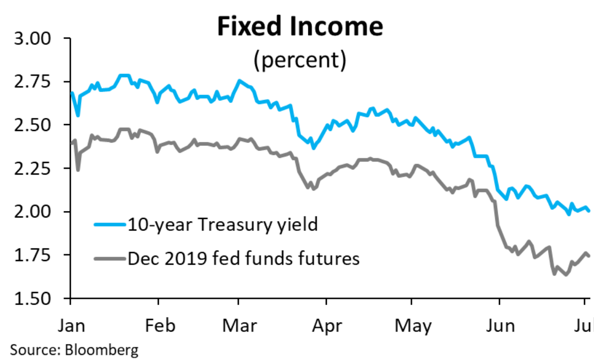
US stocks ended somewhat higher Tuesday. Stocks dipped initially as the trade war focus abruptly changed focus from China to Europe. The US government advised it will add $4 bn in proposed tariffs on the EU on the top of the list of $21 bn in tariffs published in April to address a long-running dispute about subsidies for Airbus. Investors also **bought safe haven** assets such as Treasuries and gold.

This morning, **ADP reported that private payrolls increased by just 102k in June versus market expectations of a 140k gain**. There was little initial market reaction to the release.

Ten-year yields fell 5 bps yesterday to 1.97%, reportedly driven in part by large movements in UK gilts. Traders are still pricing in ~75 bp of rate cuts by the December FOMC meeting. Tomorrow is a national holiday, so Friday trading will likely be muted. Still, Friday will bring the release of the US payrolls report—the last one the FOMC will see before its meeting at the end of the month where it is widely expected to initiate an easing cycle. The last time a payrolls report fell on July 5, in 2013, the 10-year yield rose 23.6 bps as the jobs print beat forecasts, lifting the 2y-10y curve spread by more than 20 bps on the day.

Sell-side analysts have been **lowering their forecasts of Treasury yields** for year-end, reflecting slowing global growth, dimming investor sentiment from trade and geopolitical tensions, and Fed signaling that rate cuts are in the offing,. Goldman Sachs and JP Morgan have recently cut their forecast for end-2019 10-year Treasury yields to 1.75%, in the case of Goldman reflecting a 105 bp revision down from their previous end-2019 forecast made in mid-June. Some analysts (BMO, BofA) are also noting significant further downside to 10-year yields to clients, with BMO analysts saying yields could "easily" go below 1% in the next 12-18 months.





The US is once again **approaching a debt ceiling deadline**. Short-term rates are reacting: Yields on 3-month bills maturing on October 3rd are trading higher than later maturities. There were $38 bn of 3-month bills sold Monday, some 8 bps higher than the previous week's sale.

Home prices increased nationally by 3.6% y/y in May according to CoreLogic. Coastal states were absent from the states with the fastest gains. CoreLogic expects house prices to rise 5.6% by May 2020.

Chubb advised it would **no longer insure nor invest in coal-related firms** in a move to address climate change. This will be the first such move by a US insurer and follows similar moves by European firms. Bloomberg reports that over one-third of global reinsurers have now restricted their coal coverage. And Norway's sovereign wealth fund last month said it would divest $13 bn in fossil fuel investment holdings. Unfriend Coal advised in a report last year severe weather and fires caused global losses of $337 bn in 2017, with insured losses of $144 bn.

Europe

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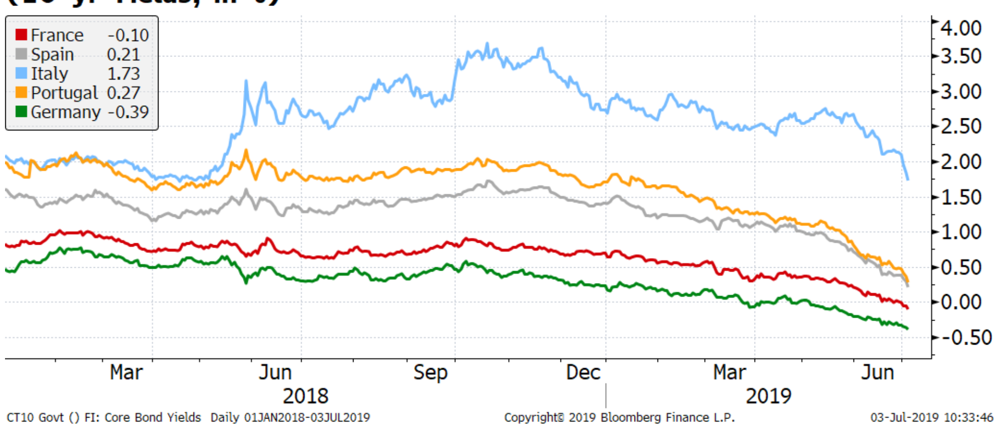
European stocks gain across countries and sectors. EuroStoxx 600 (+0.8%), DAX (0.7%), and CAC 40 (+0.7%). Bank equities (+0.6%) are performing largely in line with main indices.

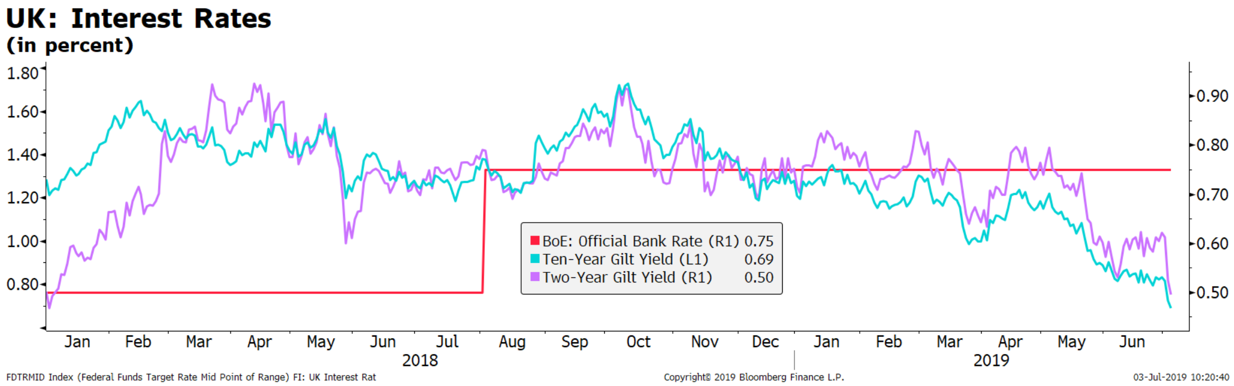
European leaders agreed yesterday the nominations for key posts in the EU. Ursula von de Leyen is being considered as new president of the European Commission, Christine Lagarde as president of the ECB, Charles Michel as president of the European Council, and Josep Borrell as the EU's foreign policy chief. The nominations are still awaiting confirmation.

Ten-year Eurozone sovereign yields declined about 4-11 bps this morning. German bonds at -0.39% (-4 bps); French at -0.09% (-4 bps); Italian at 1.73% (-11 bps); Spanish at 0.21% (-7 bps); and Portuguese at 0.27% (-9 bps). Market contacts attribute the drop in yields to the nomination of Christine Lagarde to head the ECB, whose recent comments on the health of the world economy have been interpreted as dovish.

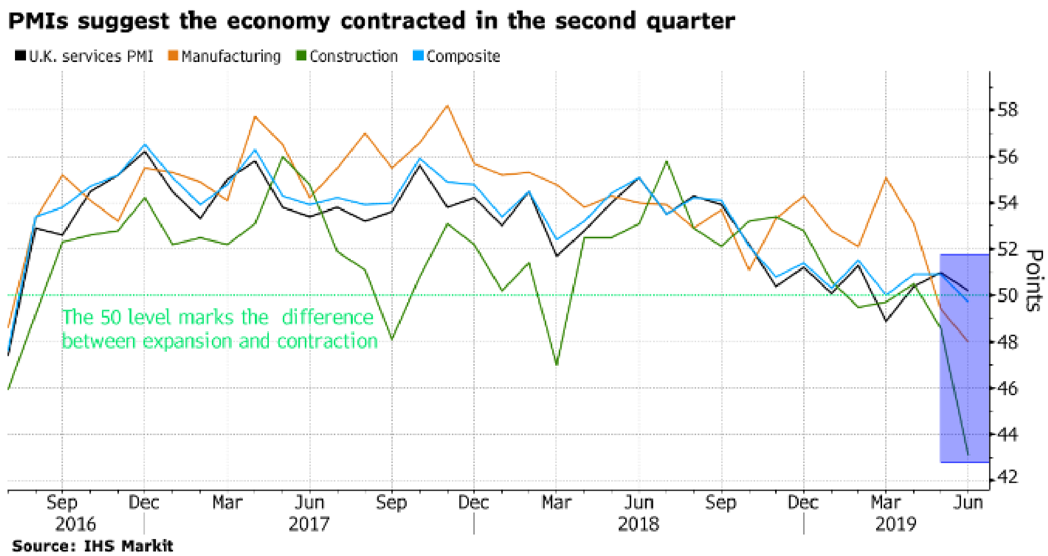
Selected Government Bond Yields
(10-yr Yields, in %)



Gilt yields dropped 9 bps in yesterday's session are down a further 3-4 bps across tenors today. The move, which takes the 10-year yield down to 0.69% and the 2-year to 0.50%, seems to have been propitiated by worse-than-expected UK macro data as well as by a speech by governor Carney which markets interpreted as dovish.



UK PMI indicators disappointed in June, pointing to a second-quarter contraction for the British economy amidst Brexit uncertainty. The Composite Index (at indices for Construction (at 49.7) and the gauges for Construction (at 43) and Manufacturing (at 48) were all in contraction territory, with the construction subindex particularly weak.



According to the European Banking Authority, the EU's largest banks need to raise capital levels by a weighted average of about 24% to comply with the full Basel III implementation by 2027 (so-called Basel IV by the industry). The EBA estimates that large banks in the EU have a capital shortfall of €135 bn. The shortfall is €900 mn for medium-sized banks and €100 mn for small banks. EBA will publish a full report of its finding in July.

Table 2 Capital ratios and shortfalls (EUR bn)

	CET1 capital			T1 capital			TC capital		
	Current Ratio	Revised Ratio	Shortfall (EUR bn)	Current Ratio	Revised Ratio	Shortfall (EUR bn)	Current Ratio	Revised Ratio	Shortfall (EUR bn)
All banks	**14.4%**	**11.5%**	**91.1**	**15.3%**	**12.3%**	**127.5**	**17.9%**	**14.3%**	**135.1**
Large	14.2%	11.4%	91.0	15.2%	12.2%	126.8	17.8%	14.2%	134.1
of which G-SII	12.7%	9.9%	53.5	13.8%	10.8%	69.0	16.2%	12.7%	82.8
of which O-SII	15.4%	12.5%	33.6	16.3%	13.2%	51.5	19.2%	15.6%	43.8
Medium	17.4%	15.2%	0.1	17.6%	15.4%	0.8	19.0%	16.6%	0.9
Small	17.0%	16.0%	0.0	17.2%	16.1%	0.0	18.3%	17.1%	0.1

Other Mature Markets back to top

Japan

Equities (-0.6%) declined with cyclicals underperforming defensives. Energy was the biggest underperformer due to oil price weakness. Electronics also lagged on reports that Japan may expand its export restrictions against Korea. Separately, the Bank of Japan made changes to its bond purchases, lowering purchases of longer dated bonds while increasing buying in the one-to-three year range. The adjustment was made in response to a flattening yield curve. In line with the risk-off sentiment, **the yen strengthened 0.2%, while 10-year JGB yields fell 1bps to -0.16%.**

Emerging Markets back to top

It's been a relatively quiet session in EM with major market across regions mixed but most trading in narrow ranges. Asian equities (-0.3%) fell on net with Korea (-1.2%) underperforming. Reports that Japan may consider expanding export restrictions to Korea beyond raw and intermediate goods used in the production of displays and semiconductors weighed on stocks. Additionally, the Korean government also lowered its GDP projections. Chinese equities (Shanghai -0.9%; Shenzhen -1.2%), particularly tech, also lagged on negative headlines regarding Huawei and services PMI data. Asian currencies were mostly stable, but the Korean won depreciated 0.4%. **In EMEA**, major bourses are higher by 0.1-0.4%, with the exception of Turkey, down 0.5%. Regional currencies are little changed with the only notable move being a 0.6% appreciation of the Ukrainian hryvnia vs the dollar. **In Latin America,** the Mexican peso outperformed appreciating by 0.4% against the dollar on the back of President Trump's positive comments on Mexico's immigration measures. The Brazilian real reversed an intraday decline as latest developments on the pension bill point to increased chances of a full floor vote before July 19.

Key Emerging Market Financial Indicators

Last updated: 7/3/19 8:09 AM	Level Last 12m	Level index	Change 1 Day	Change 7 Days	Change 30 Days	Change 12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		43.31	-0.3	2	5	1	11
MSCI Frontier Equities		29.87	0.3	2	4	5	14
EMBIG Sovereign Spread (in bps)		341	0	-3	-43	-27	-73
EM FX vs. USD		62.93	0.0	0	2	-3	1
Major EM FX vs. USD					%, (+) = EM currency appreciation		
China Renminbi		6.88	-0.1	0	0	-3	0
Indonesian Rupiah		14120	0.1	0	1	2	2
Indian Rupee		68.90	0.1	0	1	0	1
Argentine Peso		42.17	0.5	1	6	-33	-11
Brazil Real		3.86	-0.4	0	1	1	0
Mexican Peso		19.01	0.2	1	4	2	3
Russian Ruble		63.63	-0.5	-1	3	-1	9
South African Rand		14.12	-0.1	1	2	-3	2
Turkish Lira		5.64	0.3	2	3	-17	-6
EM FX volatility		7.86	0.0	-0.4	-0.7	-1.8	-1.9

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

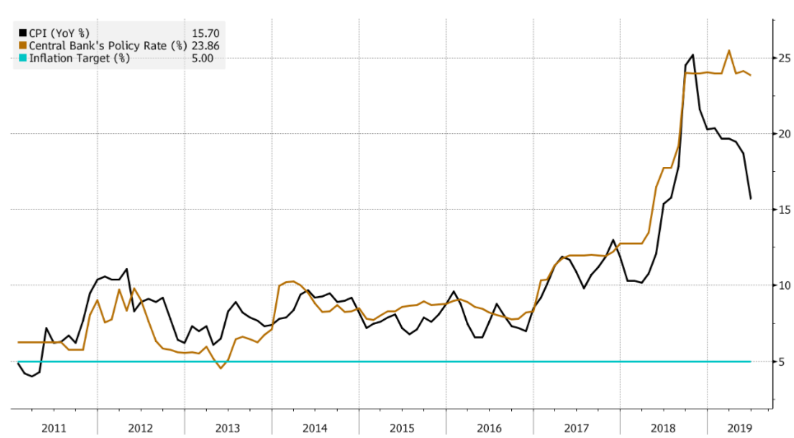
China

Chinese equities (Shanghai -0.9%; Shenzhen -1.2%) declined on negative news on Huawei and disappointing services PMI numbers. Notably, the tech dominated Chinext Index dropped -1.7%. According to Reuters, a senior US official told enforcement staff in the Commerce Department that Huawei should still be treated as blacklisted when dealing with approvals to sell to the Chinese firm. This was despite US President Trump stating during the G20 meeting over the weekend that US companies are allowed to sell products that do not affect national security to Huawei. Separately, the Caixin services PMI fell to a four-month low of 52.0 in June from 52.7 in May, missing expectations for stabilization at 52.6. Notably, new export orders placed with Chinese services firms contracted for the first time in nine months in June due to subdued global demand and tariffs. **The onshore and offshore RMB were stable.**

Turkey

Inflation declined faster than expected in June to 15.72% y/y, contributing to firming expectations of near-term easing. For comparison, the May CPI figure was 18.71%, down from over 25% in late 2018. The drop was largely due to a decline in food prices and base effects. The gap between inflation and the policy rate is now at multi-year wide levels (about 800 bps). This gap, along with a more stable lira and lower risk of US sanctions, has led some analysts to call for a 25-bps rate cut for as early as the central bank's July 25 meeting. The lira has appreciated 2.5% since the start of Q3, but it's little changed against the dollar today.

Gap Between Inflation, Rates at Its Widest

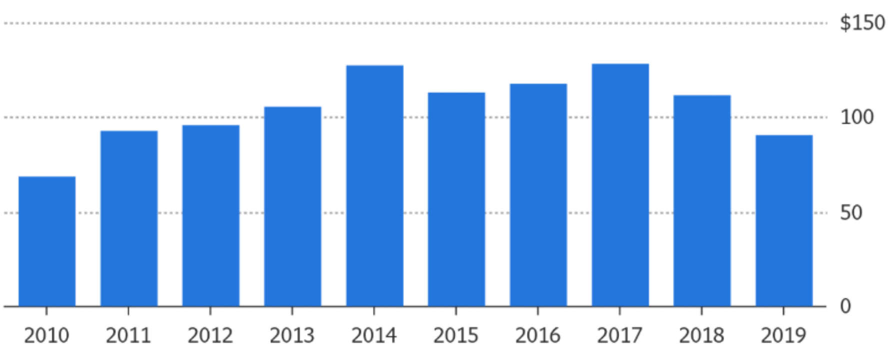


Latin America

About $91 bn of offshore and local notes were syndicated over the first six months of this year, in Latin America down 19% from a year earlier and the least since 2010, according to data compiled by Bloomberg. Santander – the region's top underwriter – believes there will be pickup in issuance in the second half given the dovish monetary policy outlook in advanced economies, with volumes ending close to 2018 levels of $163 bn. June was the region's busiest month with $22 bn issued. Peru tapped the offshore market with a $2.5 bn sale of dollar and sol-denominated notes, paying its lowest yields on record for international issues. Argentinian issuers are also making a comeback recently. Last week, YPF priced $500 mn of notes at below 9% and this week Pampa Energia priced $300 mn at a 9.4% yield. Argentina in total priced over $1 bn in the first six months of the year, after selling more than $20 bn in the first half of 2018.

Latin American Lull

Sales of global, local bonds in the first half fall to a near decade low



Source: Bloomberg

Bloomberg

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Global Financial Indicators

Benchmark	Level		Change				
7/3/19 8:02 AM	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		2973	0.3	2	8	10	19
Europe		3535	0.8	3	7	4	18
Japan		21638	-0.5	3	6	-1	8
China		3015	-0.9	1	4	8	21
Asia Ex Japan		71	0.0	3	7	0	11
Emerging Markets		43	-0.3	2	5	1	11
Interest Rates					basis points		
US 10y Yield		1.95	-5.0	-9	-12	-88	-73
Germany 10y Yield		-0.38	-1.6	-8	-18	-68	-63
Japan 10y Yield		-0.15	-0.4	-1	-6	-18	-15
UK 10y Yield		0.69	-3.2	-14	-17	-55	-59
Credit Spreads					basis points		
US Investment Grade		118	1.0	-9	-13	8	-29
US High Yield		437	4.4	-10	-46	76	-84
Europe IG		49	-0.7	-6	-21	-24	-38
Europe HY		242	-3.1	-22	-65	-78	-111
EMBIG Sovereign Spread		341	0.0	-3	-43	-27	-73
Exchange Rates					%		
USD/Majors		96.71	0.0	1	0	2	1
EUR/USD		1.13	0.1	-1	0	-3	-2
USD/JPY		107.7	0.2	0	0	3	2
EM/USD		63.0	0.1	0	2	-2	1
Commodities					%		
Brent Crude Oil ($/barrel)		63	1.1	-5	3	-19	17
Industrials Metals (index)		111	-0.1	-2	0	-13	1
Agriculture (index)		41	0.7	-3	-2	-6	-2
Implied Volatility					%		
VIX Index (%, change in pp)		13.0	0.1	-3.2	-5.8	-3.1	-12.4
10y Treasury Volatility Index		4.4	0.0	-0.7	-1.3	0.5	-0.2
Global FX Volatility		6.3	0.0	-0.6	-0.6	-1.8	-2.7
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		244	-11.4	-32	-64	-122	-172
Italy		209	-12.1	-36	-68	-26	-42
Portugal		67	-6.3	-11	-29	-77	-81
Spain		60	-5.8	-9	-29	-40	-57

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

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Emerging Market Financial Indicators

Last updated:	Exchange Rates							Local Currency Bond Yields (GBI EM)						
7/3/2019	Level		Change (in %)					Level		Change (in basis points)				
8:10 AM	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	-0.1	0.0	0	-3	0		3.3	-1.2	0	-5	-29	5
Indonesia		14120	0.1	0.4	1	2	2		7.4	-0.9	-12	-66	-60	-74
India		69	0.1	0.4	1	0	1		6.9	-3.3	-2	-22	-111	-50
Philippines		51	0.0	0.7	1	4	3		4.8	-1.3	-11	-24	-107	-146
Thailand		31	0.0	0.5	2	8	6		2.2	-6.4	-8	-33	-50	-46
Malaysia		4.14	0.1	0.3	1	-2	0		3.6	-0.9	-3	-17	-60	-48
Argentina		42	0.5	0.5	6	-33	-11		28.9	20.3	46	-458	983	594
Brazil		3.86	-0.4	-0.5	1	1	0		6.8	3.4	-11	-81	-289	-130
Chile		680	-0.1	0.1	3	-3	2		3.4	-2.6	-4	-44	-149	-111
Colombia		3211	-0.1	-0.6	5	-9	1		5.6	-12.0	-10	-52	-76	-87
Mexico		19.01	0.2	0.6	4	2	3		7.5	-6.1	-25	-66	-27	-124
Peru		3.3	-0.1	0.3	2	0	2		4.8	-3.4	0	-41	-86	-94
Uruguay		35	-0.1	0.1	0	-10	-8		10.5	3.3	0	-79		-26
Hungary		286	0.2	-0.4	1	-2	-2		1.5	-4.5	-4	-29	-120	-67
Poland		3.76	0.0	-0.3	1	0	-1		2.0	-0.9	4	-17	-58	-24
Romania		4.2	0.0	-1.0	0	-5	-3		4.1	-2.0	12	-9	-71	-15
Russia		63.6	-0.5	-1.0	3	-1	9		7.3	1.1	-3	-44	-24	-116
South Africa		14.1	-0.1	0.8	2	-3	2		9.3	0.9	-14	-14	-19	-34
Turkey		5.64	0.3	2.4	3	-17	-6		16.4	-11.2	-37	-369	-62	-46
US (DXY; 5y UST)		96.7	0.0	0.5	0	2	1		1.73	-1.2	-6	-10	-99	-78

	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		3015	-0.9	1	4	8	21		179	-1	3	-2	-13	-15
Indonesia		6363	-0.3	1	2	13	3		186	0	5	-32	-35	-50
India		39839	0.1	1	-1	13	10		144	0	-7	-13	-16	-52
Philippines		8093	0.0	1	0	11	8		76	-3	5	-27	-58	-45
Malaysia		1690	-0.1	1	2	1	0		120	-6	-4	-12	-49	-42
Argentina		41793	0.7	4	24	54	38		805	-3	-73	-207	220	-10
Brazil		100605	-0.7	1	4	37	14		232	0	-2	-36	-95	-41
Chile		5010	-1.1	-2	0	-5	-2		134	0	3	-12	-12	-32
Colombia		1544	-0.3	-1	4	-1	16		177	-1	-5	-36	-19	-51
Mexico		43442	0.0	-1	1	-8	4		327	0	-9	-6	44	-27
Peru		20729	0.0	1	4	5	7		124	2	1	-26	-45	-44
Hungary		40881	0.3	2	-1	13	4		93	2	22	-35	-53	-55
Poland		60618	0.1	1	5	7	5		40	0	14	-35	-35	-45
Romania		8829	0.6	2	3	11	20		189	6	8	-29	13	-32
Russia		2822	0.4	2	3	23	19		200	-3	-3	-31	-10	-52
South Africa		58111	0.0	-1	3	1	10		280	-1	-6	-49	-42	-85
Turkey		99709	-0.5	5	10	3	9		468	4	-17	-85	46	39
Ukraine		548	-0.1	0	-3	16	-2		518	-1	1	-147	-89	-269
EM total		43	-0.3	2	5	1	11		341	0	-3	-43	-27	-73

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