GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

TUESDAY, JULY 7, 2020

- **Consumer worries about US COVID crisis on the rise** (link)
- **Argentina offers improved deal to bondholders** (link)
- **Ecuador nears deal on defaulted debt** (link)
- **UK to introduce more stimulus measures** (link)
- **Dollar weakens as global risk sentiment improves** (link)
- **US high yield sector delivers strongest quarter in 11 years** (link)
- **Bank of Israel to start corporate bond purchases** (link)

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Markets Take a Break After Extended Rally

Most global markets are lower today as the rally of the past week runs out of steam. US equity futures point to a negative session, while European stocks are down 1% and Japanese stocks lost nearly 0.5%. Weak economic data in the euro area weighed on sentiment, while the latest polling data from the US showed that consumers have become more pessimistic about the economic impact of COVID-19. However, there were some bright spots as the rally in China entered its sixth day, while Argentina and Ecuador appeared to make progress in their debt negotiations. Markets are entering the third quarter of 2020 after a very strong Q2, with the S&P 500 delivering its best Q2 return since 1998. The economic rebound in countries like the US and China has been much stronger than expected. However, with the corporate earnings season about to begin and the virus continuing its spread across the globe, the prospects for the months ahead remain very uncertain.

Key Global Financial Indicators

Last updated: 7/7/20 8:10 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		3180	1.6	6	0	6	-2
Eurostoxx 50		3318	-0.9	3	-2	-6	-11
Nikkei 225		22615	-0.4	1	-1	4	-4
MSCI EM		43	4.3	8	5	1	-4
Yields and Spreads					bps		
US 10y Yield		0.68	0.0	2	-22	-136	-124
Germany 10y Yield		-0.42	0.8	3	-15	-6	-24
EMBIG Sovereign Spread		456	0	-18	-5	122	163
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		54.8	-0.4	1	-3	-13	-11
Dollar index, (+) = $ appreciation		96.9	0.2	0	0	0	1
Brent Crude Oil ($/barrel)		43.0	-0.3	4	2	-33	-35
VIX Index (%, change in pp)		28.4	0.5	-3	4	15	15

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

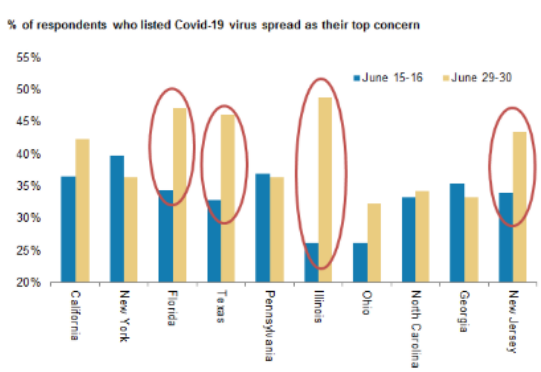
COVID-19 continues to dominate the headlines as the crisis intensifies in countries such as Brazil, India, Russia and the US. Markets are playing close attention to the evolving policy debate in the US Congress as the existing relief measures approach their terminal dates. Enhanced unemployment benefits are scheduled to end on July 31, and the Paycheck Protection Program ends on August 8. An alliance appears to be forming between the administration and Congressional Democrats to press for another aid package against Republican senators who are more reluctant to increase spending. The outcome of the debate will have a big impact not just in the US but throughout the global financial system. It is a very quiet week on the data front. The US calendar has only jobless claims on Thursday and PPI on Friday. In the euro area, French industrial production also comes out on Friday, while Japan publishes PPI on Thursday. India will publish its industrial production report on Friday.

United States back to top

Monday saw a continuation of the recent rally which has extended into its fifth day. For the S&P 500, this was longest rally since December, and the Nasdaq hit yet another record, pushing its annual gain to over 16%. The Nasdaq and China's CSI 300 are among a handful of major equity indexes to post major gains in 2020 while a sea of red extends over the rest of the market. However, post-holiday trading volumes were very light in the US as many remained on vacation. Sentiment was boosted by the Shanghai index's biggest one-day rally since 2015 (+5.67%) as a front page editorial in state-run media called for investors to be bullish. The rally in China pushed stocks higher across most of the globe. Treasury yields were slightly higher, and the dollar weakened.

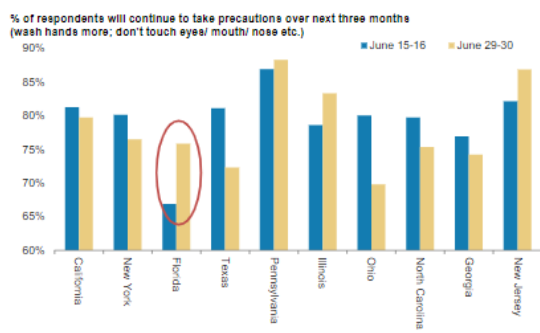
Rising worries about COVID-19 could put the recent market recovery at risk as the rapidly accelerating pace of new infections dominates news headlines. The data show that consumers in most hot spot states were more worried about the virus in the June-29-30 survey than they were in the earlier June 15-16 survey. With the US recording its first 50K+ day of new cases on July 1 and with new case counts well above 40K on most days, consumer sentiment may decline even further. High frequency mobility data from cell phone users support this finding, as mobility has begun to trend downwards in the sunbelt states such as Florida, Alabama, Texas, Arizona and especially Florida. The ten largest hot zones including California make account for 35% of national spending on service, and preliminary data show that rising risk aversion drives spending on services lower.

Exhibit 4: % of respondents who listed Covid-19 virus spread as their top concern



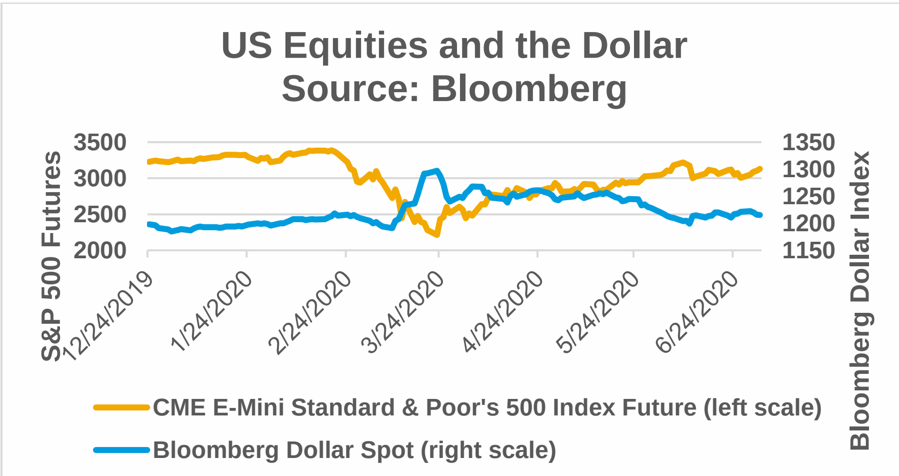
Source: AlphaWise, Morgan Stanley Research

Exhibit 5: % of respondents will continue to take precautions over next three months

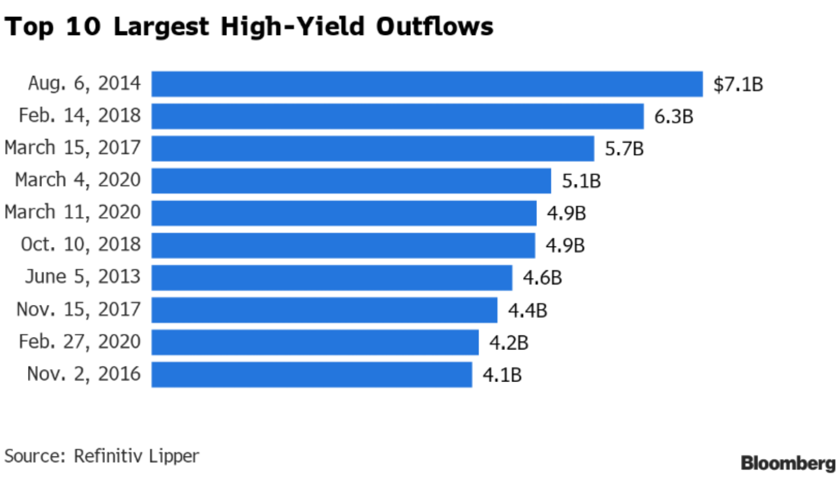


Source: AlphaWise, Morgan Stanley Research

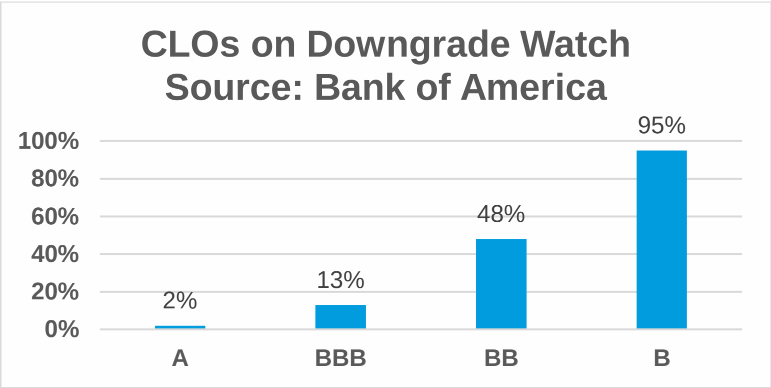
Growing market optimism that the COVID-19 crisis will eventually be contained has pushed risk assets such as stocks higher since the market low on March 23. This trend has been associated with a weakening of the dollar, as sentiment improves in other parts of the global financial system and markets in other parts of the world follow US markets higher. This has lent support to euro area and emerging markets as dollar funding costs have fallen and investors have cautiously begun to reverse their earlier outflows. Nevertheless, markets remain hostage to COVID-19 as the crises intensifies around many parts of the globe.



High yield (HY) bond funds could face weekly outflows as high as $5 bn as investors take profits after the HY sector delivered its strongest return in almost 11 years, according to analysis by JP Morgan. The HY sector delivered a Q2 return of 10.2%, the strongest quarterly return since the 14.2% gained in September 2009. The average bond yield for the sector has fallen to 6.77% after spiking as high as 11.69% on March 23rd. The rebound of confidence in the HY sector resulted in a record monthly issuance volume of $58 bn in June. According to some analysts, many high credit risk companies have done better than expected as the economy has recovered more quickly than originally expected. However, others are worried that the growing virus counts are harbingers of hard times for the economy in the weeks ahead as more states reimpose shutdowns and the progress made in the last few months is reversed. A renewed slowdown in the economy could pose severe problems for companies in the HY sector.



The collateralized loan obligation (CLO market is coming under increasing downgrade pressure from the rating agencies. Bank of America estimates that 22% of all tranches are on downgrade watch across the credit spectrum from S&P and Moody's. Last week, S&P alone placed 156 CLO tranches on downgrade watch. Moody's has also put 1% of AA-rated CLOs on watch for a downgrade.



Moody's and S&P have also begun to complete the reviews of bonds previously on downgrade watch. The number of actual downgrades after the reviews were completed appear to be lower than analysts had originally expected, which may account for the recent stabilization in CLO credit spreads. In other CLO news, last week's partial rollback of Dodd-Frank rules will allow CLO managers to invest up to 5% of their assets in high yields bonds, which is a positive because it expands their investment horizons but is also a negative for risk because bonds are subordinate to loans in the credit hierarchy.

Table 2: Bonds where reviews were completed and they were either downgraded or affirmed by Moody's/S&P

			Ratings Affirmed			Ratings Downgraded		
Rating	# of cusips	% rating affirmed	WARF	OC	CCC	WARF	OC	CCC
AA	1	100%	3,796	126%	12%			
A	7	43%	3,566	119%	13%	3,544	118%	12%
BBB	34	56%	3,411	111%	13%	3,517	111%	10%
BB	41	10%	3,567	105%	14%	3,528	105%	12%
B	20	0%				3,589	102%	13%

Source: BofA Global Research, Moody's, S&P, Intex, Bloomberg

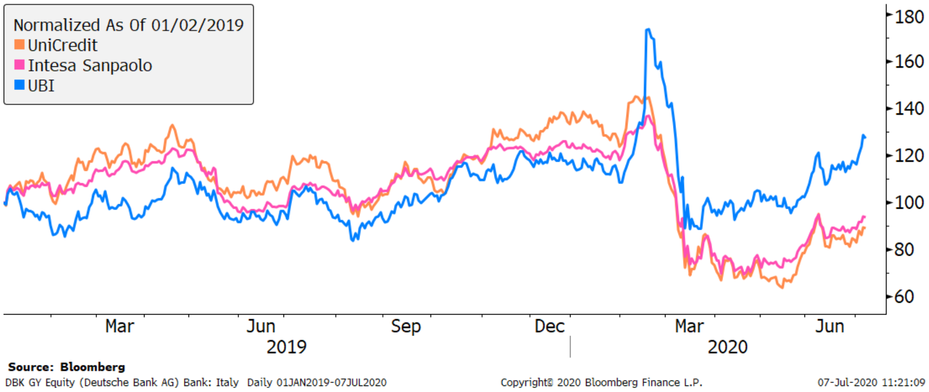
Europe back to top

Equities were down 1% in most European bourses as new outbreaks are reported and economic data show the extent of the damage. German Industrial Production contracted 19.3% (y/y) in May, compared to -16.9% expected. The bad data release adds to the damage from the April lockdowns, when IP contracted around 25%. In Italy, retail sales contracted by 10.5% (y/y), vs. -17% forecasted and compared to -26.3% in April. Sovereign yields were flat.

Bank stocks (-1.1%) performed broadly in line with market indices. Equities of Italian lenders Unicredit (-0.6%) and Intesa (-0.5%) outperformed peers. Unicredit is expected to sell two portfolios of non-performing loans valued at €800 mn and €700 mn to other local banks. Intesa, in turn, is proceeding with its bid on UBI (-1.3%), as it aims to increase its relative weight against other large European competitors.

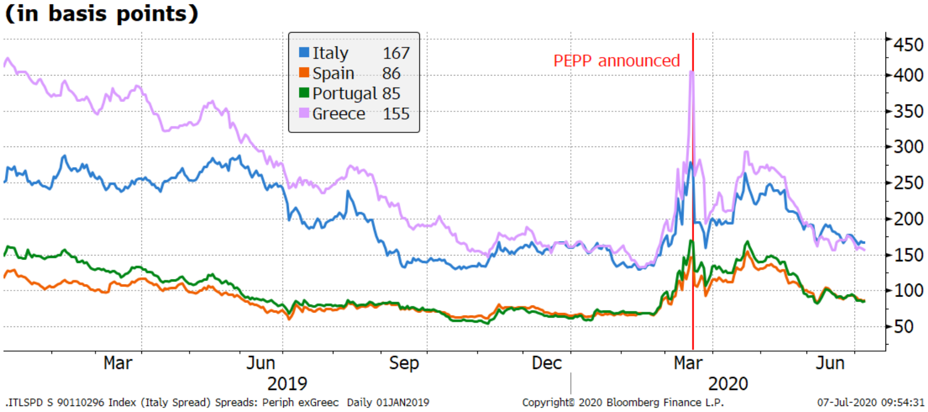
Notably, **the volume of put options on Intesa traded in Milan jumped to over 3,000 contracts today**, compared to about 700 contracts on average over the previous 20 days, Bloomberg reported.

Equity Performance: Italian Banks
(euro per share)



The ECB slowed down the pace of its PEPP purchases to €20 bn for the week ending July 3rd, from a weekly average of about €27 bn through May-June. Analysts at Jefferies note that PEPP purchases have resulted in negative net supply of eurozone's sovereign paper in the second half of 2020, and that a further slowdown of purchases could lead to a widening of spreads.

Selected European Sovereign Spreads to 10yr Bunds
(in basis points)



UK banks are reportedly discussing an industry-wide approach to possible state-guaranteed loans. The talks presumably involve private lenders as well as the state-owned British Business Bank – according to local [newspapers](#) – and are aimed at agreeing on a common approach for tackling the expected defaults under the government schemes BBLS (Bounce Back Loan Scheme) and CBILS (Coronavirus Business Interruption Loan Scheme). Industry estimates place such defaults at 40% to 80% of all bounce-back loans. It is also estimated that about 10% to 15% of the BBLS loans are fraudulent applications.

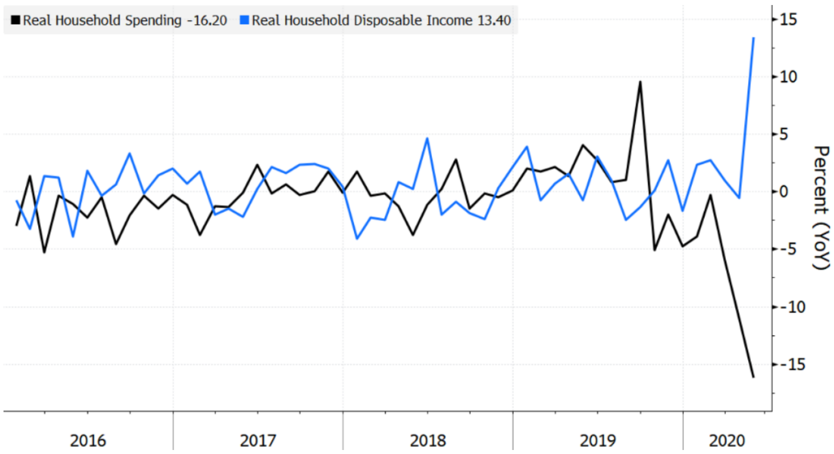
Feature	CBILS	BBLS
Target Audience	SMEs with a turnover of less than £45m	Low level early stage micro businesses and SMEs (no specific turnover criteria)
Type of finance	• term loans • overdrafts • invoice finance • asset finance	• Term loans only
Finance provided	• Maximum value of facility - £5m • Minimum for term loans and overdrafts is £50,001. • Lenders delivering asset or invoice finance only will be able to provide finance at less than £50,001.	• Maximum value of facility - £50k • Businesses can apply for between £2,000 up to 25% of their turnover
Lenders	Over 40 accredited lenders including our sister company GC Business Finance	Over 15 accredited lenders
Interest rate and fees set by lender	Interest rate and fees set by lenders and will vary per lender	Government set interest rate at 2.5% per annum. No lender levied fees

UK Chancellor Rishi Sunak is expected to delivery his "Summer Economic Update" on Wednesday, potentially announcing new measures to stimulate the economy worth up to 1.5% of GDP. Market contacts suggest that the focus of the package would be the housing market, through an immediate Stamp Duty holiday for 6 months and an increase of the zero-duty threshold from the current £125k to as high as £500k. Other measures discussed could include £3 bn sterling for green spending, consumption vouchers for hard-hit sectors worth up to £30 bn as well as VAT cuts for hospitality sectors. The UK's fiscal stimulus measures to date are estimated at around 5.5-6.0% of GDP.

Other Mature Markets back to top

Japan

Household spending in May declined more than expected, pointing to a weak economic rebound. Real household expenditure fell 16.2% y/y—a record decline—in May, after a 11.1% y/y reduction in April. The consensus forecast expected a 11.8% decline y/y in May. Household spending remained under pressure despite the rise in real disposable income by 13.4% y/y on the back of the government ¥100,000 relief paychecks. The pandemic has given a hard hit to jobs and incomes, with real cash earnings falling 2.1% y/y, larger than the consensus forecast (0.8% y/y decline). The lifting of coronavirus containment measures in May appeared to support spending. According to supplementary data in the household survey, real household expenditure fell just 1.7% y/y in the week ended May 31 after a sharp drop of 26.4% y/y in the week ended May 3. Equities fell (NIKKEI: -0.4%) and the yen depreciated (-0.3%). JGB yields declined (10-year: -0.4 bp; 30-year: -0.9 bp) after strong appetite at a 30-year auction.

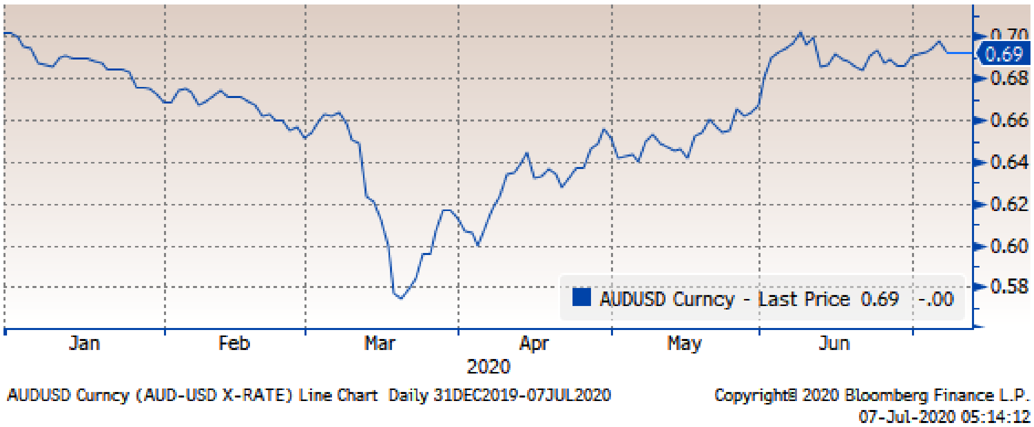


Source: Bloomberg, with data sourced from Ministry of Internal Affairs and Communications.

Australia

The Reserve Bank of Australia (RBA) kept the benchmark rate and the yield control unchanged as expected. The cash rate and the 3-year government bond yield target were maintained at 0.25%. The RBA reiterated its pledge to scale up its bond purchase program as needed. Given that the yields are at its target, the RBA has not purchased government bonds for some time, with total purchases to date amounting to about 50 billion Australian dollars. The RBA continues to maintain ample liquidity in the financial system; banks are expected to further draw on the Term Funding Facility in the coming months. The RBA expects a bumpy economic recovery and highlighted the uncertainty on consumer and business confidence. Meanwhile, Melbourne is facing a second-wave outbreak. The nation's second largest city re-introduced a 6-week lockdown. Australian dollar depreciated (-0.6%) today after a strong gain in recent months; equities were little changed.

Australian Dollar (USD per AUD)



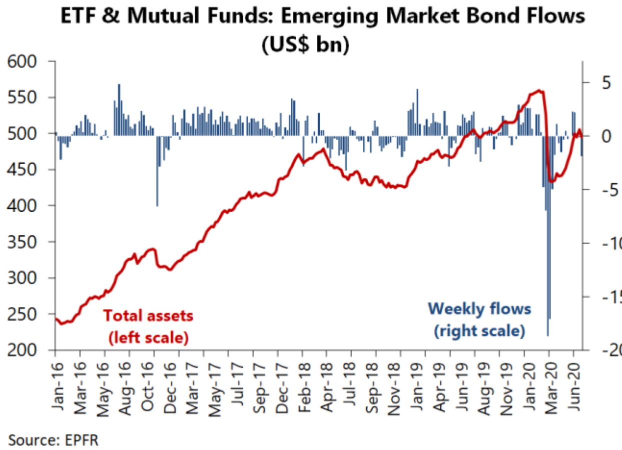
Source: Bloomberg.

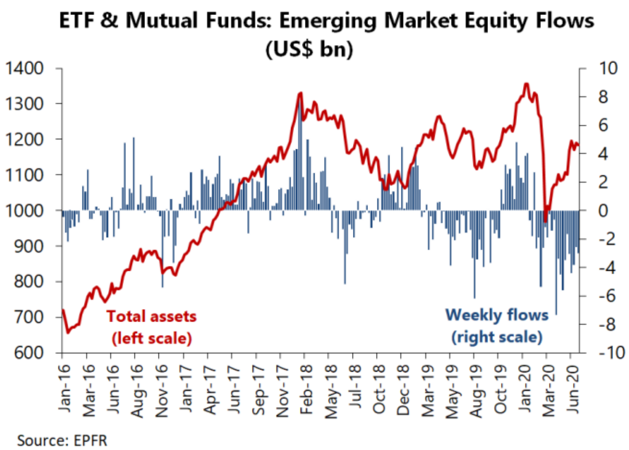
Emerging Markets back to top

Equities were mixed while currencies were generally weaker. The central bank of Nigeria devalued the naira by 360 to 380/dollar, although the parallel market rate is at 462. Bank Indonesia committed to purchase $40 billion of bonds, including $27.4 billion in private placements, at the benchmark 7-day reverse repurchase rate. The one-off agreement to purchase government bonds is to help fund the budget deficit, which is projected at 6.3% of GDP. The Hong Kong Monetary Authority continued selling local currency—about $925 million on July 6—to defend the peg. The USD/HKD option prices pointed to the near-term stability of the currency. Malaysia cut rates by 25 bps to 1.75% as expected.

Emerging Market Fund Flows

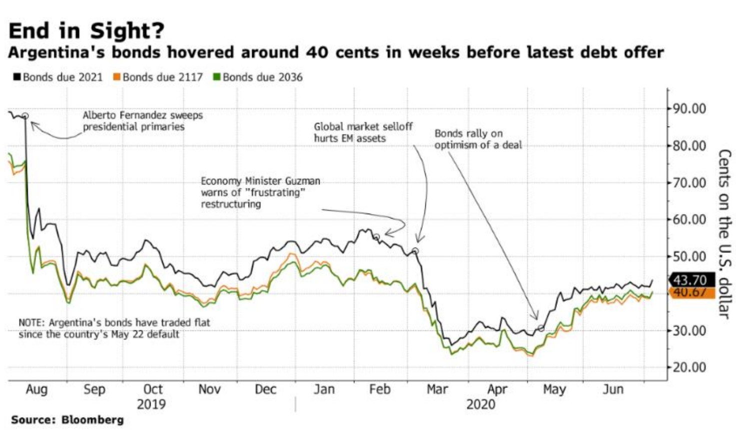
Emerging market bond and equity flows were negative last week. Equity outflows were $3.0 bn and bond outflows were $2.0 bn. This was the 20th consecutive weeks of equity outflows from emerging markets. The series of negative equity flows started in mid-February when the COVID-19 crisis began to worsen. Since then, the total equity outflows have now reached to $61.3 bn. Last week`s bond outflow was the largest since the beginning of April.





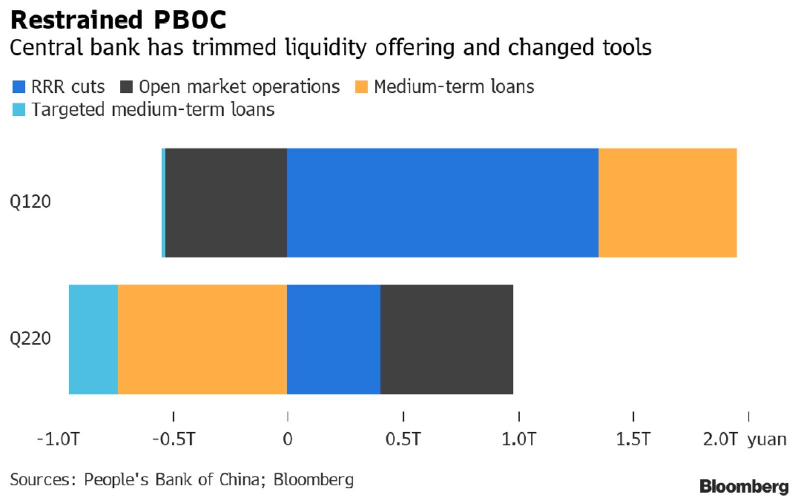
Argentina

The government made an improved offer to bondholders to resolve the country's May 22 default on $65 bn of debt, the ninth in its history. Local bonds rallied on the news, with Argentina's $2.6 bn century bonds appreciating to 40 cents on the dollar, up nearly 2% from the previous day. Press reports indicated that the offer amounted to debt relief of $31.5 bn compared to $44.8 bn in the original offer, or 53 cents on the dollar compared to the earlier offer of 40 cents. Some investors groups expressed appreciation for the government's flexibility but said more would be required. A number of opposition leaders were also reported to have come out in favor of the new offer.



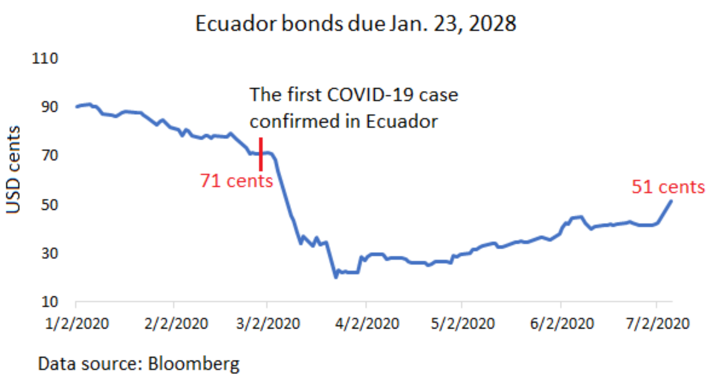
China

The People's Bank of China (PBOC) is tightening liquidity as the economy recovers. The central bank injected a net 28.7 bn RMB of funds between April and June, a sharp decline from the 1.4 tn RMB during the first three months. The policy shift highlighted the PBOC's determination to safeguard financial stability. Concurrently, the PBOC is trying to curb the growth of structured deposits to limit risks to financial stability, some firms are trying to take advantage of arbitrage opportunities to borrow money cheaply and invest in higher yielding structured deposits offered by banks, creating the risk of liquidity mismatches and valuation problems.



Ecuador

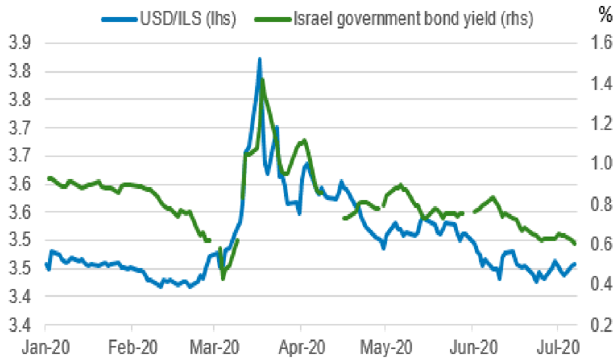
Ecuador has reached a preliminary deal with several major bondholders to restructure $17.4 bn in outstanding debt. Press reports described it as a "deal in principle." The government plans to exchange several bonds maturing between 2022 and 2030 for three new notes due in 10, 15 and 20 years, decreasing the average coupon rate to 5.3%, according to Bloomberg. Local bonds rallied sharply on the news, with the benchmark 2028 bond up to 51 cents on Monday from 42 cents on Friday. A number of fund management companies said they would support the offer. The deal provides debt relief of $10 bn over the next decade with an additional $ 6bn from 2025 to 2020.



Israel

The Bank of Israel (BOI) kept its policy rate unchanged at 0.1%, as expected, but introduced new credit easing measures. These new tools include corporate bond purchases in the amount of 15bn shekel (1.1% of GDP), renewal of the SME loan support facility without a lending cap and use of banks mortgage portfolios as collateral. The corporate bond QE will only apply to vanilla bonds with A- or higher rating. The measures come on top of the existing government bonds QE program of 50bn shekel (3.8% of GDP). The Israeli shekel weakened by 1% and local bond yields declined by 5bps after the announcement. Market contacts expect further stimulus measures from the BOI, primarily through the increase of the QE programs. The economy faces the risk of the second wave, while the deflation deepened to 1.6% y-o-y in May.

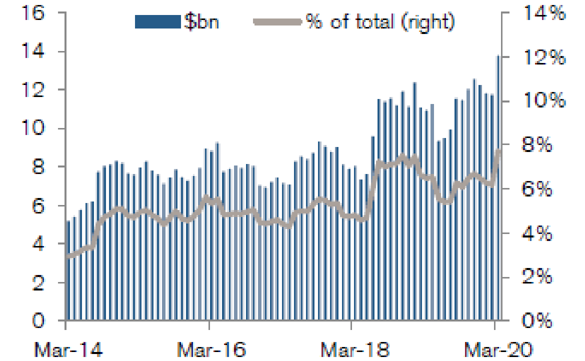
Israel: exchange rate and local 10-year bond



Source: Bloomberg, IMF

Figure 24: Israel

Non-residents' holdings in local currency government bonds



Source: Central Bank, Credit Suisse

List of GMM Contributors

Global Markets Analysis Division, MCM Department

Anna Ilyina
Division Chief

Will Kerry
Deputy Division Chief

Evan Papageorgiou
Deputy Division Chief

Sergei Antoshin
Senior Economist

John Caparusso
Senior Financial Sector Expert

Sally Chen
Senior Economist

Yingyuan Chen
Financial Sector Expert

Han Teng Chua
Economic Analyst

Fabio Cortés
Senior Economist

Reinout De Bock
Economist

Dimitris Drakopoulos
Financial Sector Expert

Mohamed Jaber
Senior Financial Sector Expert

Phakawa Jeasakul
Senior Economist

Sanjay Hazarika
Senior Financial Sector Expert

Frank Hespeler
Senior Financial Sector Expert

Rohit Goel
Financial Sector Expert

Henry Hoyle
Financial Sector Expert

Dmitri Petrov
Financial Sector Expert

Thomas Piontek
Financial Sector Expert

Patrick Schneider
Research Officer

Jochen Schmittmann
Senior Economist

Can Sever
Economist (Economist Program)

Juan Solé
Senior Economist

Jeffrey Williams
Senior Financial Sector Expert

Akihiko Yokoyama
Senior Financial Sector Expert

Piyusha Khot
Research Assistant

Xingmi Zheng
Research Assistant

Global Financial Indicators

Last updated: 7/7/20 8:19 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		3180	1.6	6	0	6	-2
Europe		3317	-1.0	3	-2	-6	-11
Japan		22615	-0.4	1	-1	4	-4
China		3345	0.4	12	14	11	10
Asia Ex Japan		75	5.0	9	8	8	2
Emerging Markets		43	4.3	8	5	1	-4
Interest Rates					basis points		
US 10y Yield		0.67	-0.3	2	-22	-136	-124
Germany 10y Yield		-0.43	0.5	3	-15	-6	-24
Japan 10y Yield		0.05	0.5	2	0	20	6
UK 10y Yield		0.19	-0.9	2	-16	-55	-63
Credit Spreads					basis points		
US Investment Grade		142	1.0	-8	-4	23	45
US High Yield		615	1.4	-31	63	186	222
Europe IG		62	0.9	-5	1	11	18
Europe HY		364	8.0	-19	24	117	158
EMBIG Sovereign Spread		457	1.0	-17	-4	123	164
Exchange Rates					%		
USD/Majors		96.92	0.2	0	0	0	1
EUR/USD		1.13	-0.2	0	0	1	1
USD/JPY		107.7	-0.3	0	1	1	1
EM/USD		54.8	-0.3	1	-2	-13	-11
Commodities					%		
Brent Crude Oil ($/barrel)		43	-0.3	4	2	-33	-35
Industrials Metals (index)		106	-0.5	2	4	-5	-8
Agriculture (index)		36	-0.5	3	0	-13	-14
Implied Volatility					%		
VIX Index (%, change in pp)		28.1	0.2	-3.6	3.6	14.9	14.4
10y Treasury Volatility Index		61.6	0.1	-2.7	-11.6	-1.9	-0.4
Global FX Volatility		7.7	0.0	-0.5	0.1	1.6	1.7
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		154	-4.1	-13	-10	-97	-12
Italy		166	-0.9	-5	-3	-45	6
Portugal		84	-0.5	-9	3	4	21
Spain		86	-0.1	-7	2	17	20

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: 7/7/2020 8:21 AM	Exchange Rates: Level		Change (in %)					Local Currency Bond Yields (GBI EM): 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		7.02	-0.1	0.6	1	-2	-1		3.0	8.6	10	14	-16	-10
Indonesia		14440	0.3	-1.2	-4	-2	-4		7.2	-3.9	-4	-7	-8	9
India		75	-0.3	0.8	1	-8	-5		6.0	-0.3	-5	-11	-82	-88
Philippines		50	-0.3	0.6	1	4	2		4.1	0.3	1	-11	-66	-23
Thailand		31	-0.4	-1.0	1	-1	-5		1.5	0.0	6	-6	-67	-15
Malaysia		4.28	0.0	0.2	0	-3	-4		2.7	-0.7	-11	-17	-88	-63
Argentina		71	-0.3	-0.6	-2	-41	-15		44.7	41.0	-54	-204	1536	-1793
Brazil		5.38	-0.4	1.6	-10	-29	-25		5.2	-1.3	-7	-12	-158	-106
Chile		798	0.5	2.7	-4	-14	-6		2.6	-8.2	4	-16	-77	-70
Colombia		3637	0.4	3.3	-1	-11	-10		5.3	-4.1	-34	-14	-39	-69
Mexico		22.59	-1.0	1.8	-5	-16	-16		5.9	-2.2	-15	-56	-158	-107
Peru		3.5	-0.1	-0.4	-3	-7	-7		4.4	3.4	8	5	-31	-9
Uruguay		43	-0.7	-2.2	-1	-18	-13		9.8	-15.8	-32	-30	-63	-106
Hungary		313	-0.6	0.7	-3	-8	-6		1.6	3.3	9	-11	14	41
Poland		3.96	-0.2	0.0	-1	-4	-4		0.8	2.0	-4	-12	-116	-106
Romania		4.3	-0.2	0.5	0	-2	0		3.7	1.0	3	-9	-32	-29
Russia		71.7	0.1	-0.7	-5	-11	-14		5.6	-1.1	25	19	-159	-49
South Africa		17.1	-0.6	1.5	-2	-17	-18		10.4	12.4	36	53	120	87
Turkey		6.87	-0.1	-0.2	-1	-16	-13		11.1	5.6	62	40	-532	-64
US (DXY; 5y UST)		97	0.2	-0.5	0	0	1		0.30	-0.2	1	-16	-153	-139

	Equity Markets: Level		Change (in %)					Bond Spreads on USD Debt (EMBIG): 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		3345	0.4	12	14	11	10		226	0	-2	-6	49	50
Indonesia		4987	0.0	2	1	-22	-21		257	2	-7	12	80	101
India		36675	0.5	5	7	-7	-11		243	-1	-2	-5	109	118
Philippines		6267	-1.0	1	-3	-23	-20		160	1	-3	20	93	94
Malaysia		1567	-0.6	4	1	-7	-1		186	2	-4	12	69	74
Argentina		43340	9.0	8	-4	4	4		2389	-10	-105	-150	1602	620
Brazil		98937	2.2	3	5	-5	-14		362	6	-12	31	136	147
Chile		4284	2.0	8	6	-16	-8		203	1	-9	8	72	70
Colombia		1129	0.4	2	-6	-28	-32		276	2	-15	10	101	113
Mexico		37885	-0.2	0	-3	-13	-13		505	4	-22	32	184	213
Peru		16976	1.7	2	-2	-19	-17		175	0	-7	8	57	68
Hungary		35687	-2.2	0	-6	-13	-23		167	-3	-10	7	87	81
Poland		51113	-0.7	3	-1	-16	-12		42	-4	-7	-10	16	24
Romania		8540	-0.6	-1	-3	-5	-14		276	-4	-16	-8	95	103
Russia		2827	-0.3	2	1	0	-7		213	3	-4	24	16	82
South Africa		54835	0.0	1	0	-5	-4		523	9	-11	47	243	203
Turkey		118830	0.3	2	8	19	4		590	10	-2	50	124	189
Ukraine		499	0.0	0	0	-9	-2		640	10	0	60	124	220
EM total		43	-1.3	8	5	1	-4		457	1	-17	-4	123	164

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

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