



Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Monday, July 8, 2019

- **A strong June US jobs report leads to a sharp rise in rates ([link](#))**
- **Deutsche Bank announces a radical restructuring plan ([link](#))**
- **Turkish President unexpectedly removes central bank governor ([link](#))**
- **Emerging market dollar issuance in 1H2019 is second highest on record ([link](#))**
- **Burgeoning Japan-Korea trade tension weighs on Asian assets ([link](#))**








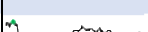
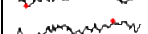


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Stronger than expected US data roils markets

US fixed income markets sold off on Friday as stronger than expected non-farm payroll data led investors to price in a potentially less dovish Fed. US rates rose on the news led by the front end of the curve, with the yield on 2-year and 10-year Treasuries up by 9 bps and 7 bps, respectively. The importance of the June NPF report was accentuated by the fact that it was the last one to be issued before the July 30 FOMC meeting, with all eyes now set on the Fed Chairman's testimony to Congress on Wednesday. While markets continue to expect a full 25 bps rate cut in July, the probability of a 50 bps rate cut has now dropped to less than 1%. Approximately three 25 bps rates cuts are currently priced in over the next 12 months. The US dollar appreciated by about 0.5% against major currencies on the news, while the reaction of equity markets was generally muted. In emerging markets, Turkish assets sold off and the lira dropped by close to 2% following the sudden dismissal of the central bank's governor as investors fretted about its potential impact on near-term interest rates and, more generally, on the monetary authority's independence. Lastly, Deutsche Bank unveiled a radical restructuring plan that was mostly in line with analysts' expectations, as reflected by the market's generally muted reaction to the news.

Amongst the data releases anticipated this week, US headline CPI for June (Thursday) is expected to moderate to 1.6% y/y from 1.8% in May, while core CPI is expected to remain unchanged at 2.0% y/y. Initial jobless claims (Thursday) are also expected to remain unchanged at 221k, though NFIB small business optimism (Tuesday) is expected to decline marginally. Among key central bank releases, Bank of Canada (Wednesday), Israel (Monday), Malaysia (Tuesday), Peru (Thursday) are expected to keep rates unchanged. Japan's PPI print (Tuesday) for June is expected to moderate to 0.4% y/y from 0.7% in May. Industrial production in the UK (Wednesday) is expected to rise to 1.3% y/y from -1.0% in May.

Key Global Financial Indicators

Last updated: 7/8/19 8:58 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		2990	-0.2	2	4	8	19
Eurostoxx 50		3520	-0.2	1	4	2	17
Nikkei 225		21534	-1.0	-1	3	-1	8
MSCI EM		43	-0.8	0	4	-1	10
Yields and Spreads			bps				
US 10y Yield		2.02	8.4	0	-6	-80	-66
Germany 10y Yield		-0.37	-1.1	-2	-12	-67	-62
EMBIG Sovereign Spread		337	3	-1	-26	-19	-77
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		62.9	0.1	0	2	-3	1
Dollar index, (+) = \$ appreciation		97.3	0.0	1	1	4	1
Brent Crude Oil (\$/barrel)		64.2	0.0	-1	1	-17	19
VIX Index (% change in pp)		13.9	0.6	-1	-2	1	-12

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

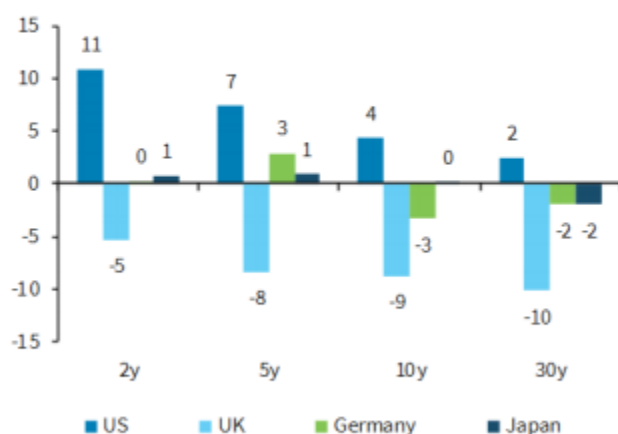
United States

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US rates increased sharply on Friday driven by the stronger than expected jobs report, while equity markets remained unchanged. US 2-year and 10-year yields rose by 10 and 8 bps respectively on Friday, underperforming their safe haven counterparts. Correspondingly, the yield curve flattened with 3m10s curve declining by around 10 bps, and 2s10s declining by 7bps last week. The US dollar also appreciated by 0.5% against the major trading peers on Friday. The Trump administration said trade talks with China are starting again as Beijing reiterated that it would be essential for the US to remove all existing tariffs for a deal to be reached.

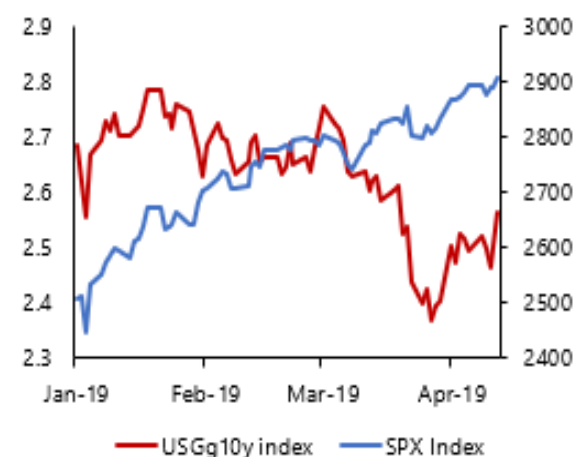
FIGURE 1

US Treasury yields rose sharply, led by the front end
Changes over the last week, yields, bp



Note: Used generics where current is not available. Source: Bloomberg, Barclays Research

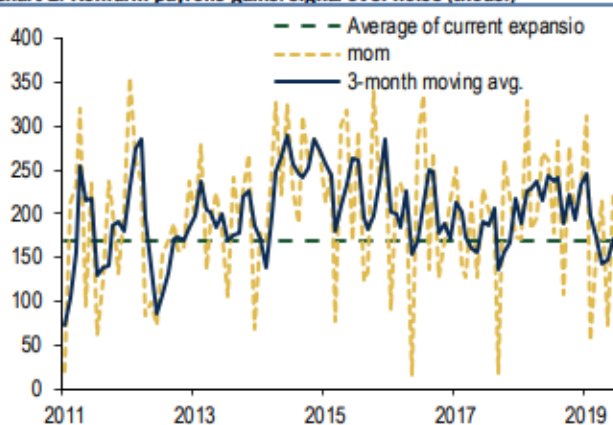
Performance: US equities and 10-yr yields



Source: Bloomberg

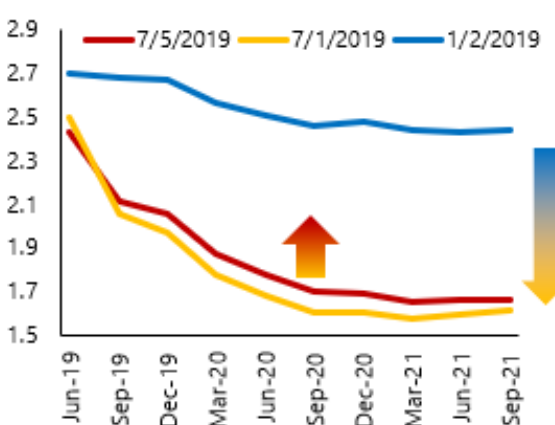
The June jobs report produced mixed signals, with payrolls rebounding from a paltry May print and annual wage growth stagnating at their previous level. Nonfarm payrolls surprised sharply to the upside in June, recovering to a solid 224k print (vs a consensus of 160k) which followed a soft 72k in May. On a 3-month moving average basis, job gains are averaging 171k, in line with the 169k average during the current expansion. The annual pace of wage growth remained unchanged at 3.1% y/y for a second consecutive month. The unemployment rate ticked up a tenth to 3.7% in June reflecting an increase in the participation rate to 62.9%. **The Eurodollar rates reacted accordingly, with Mar-2020 forward rates rising by almost 9 bps last week. However, despite the move, markets continue to price-in a full 25 bps rate cut in July, while the probability of a 50 bps rate cut has declined.**

Chart 2: Nonfarm payrolls gains: signal over noise (thous.)



Source: BofA Merrill Lynch Global Research, BLS

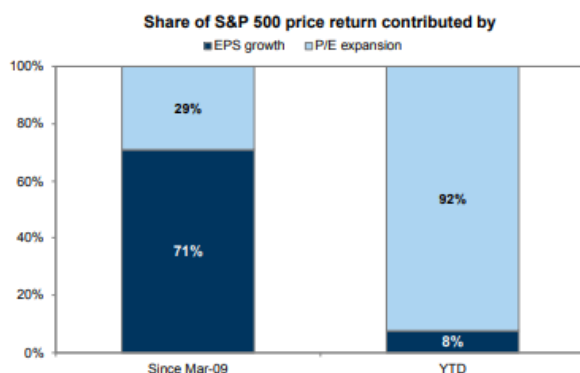
Eurodollar future rates



Source: Bloomberg

Goldman analysts highlight that more than 90% of the 19% YTD rally in the S&P 500 index has been driven by valuation expansion as the forward P/E multiple expanded from 14x to 17x. The lower interest rates have benefitted equity valuations, while it has been partially offset by a worsening of the growth outlook along with a rise in uncertainty. The GS US Current Activity Indicator slipped to 1.3% on average during 2Q 2019, compared with a recent high of 4.1% in early 2018. The fall in bond yields and rise in equity valuations is also consistent with prior rate cutting cycles, as per the analysts.

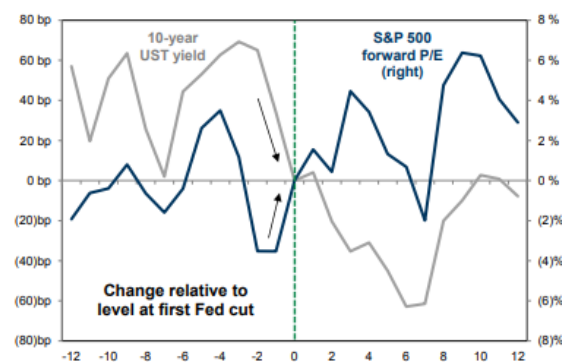
Exhibit 2: Most of YTD price return driven by valuation expansion as of June 28, 2019



Source: FactSet, Goldman Sachs Global Investment Research

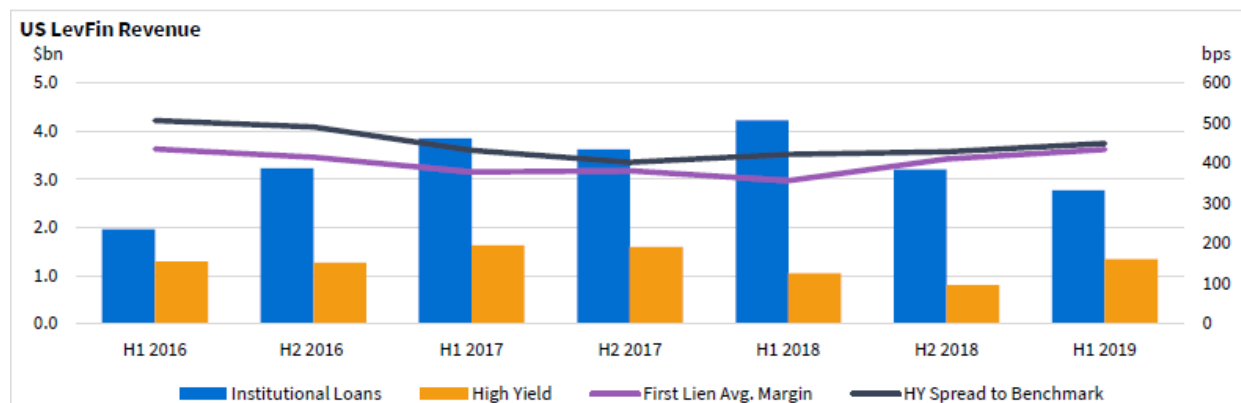
Exhibit 6: Path of S&P 500 P/E multiples and interest rates around Fed cuts

median of 7 episodes since 1984



Source: Compustat, FRB, Goldman Sachs Global Investment Research

Dealogic data suggests that the net revenue from US leveraged finance shrank to \$4.1bn in H1 2019, down by 23% on H1 2018. The decline in revenue generated by banks was driven by a subdued leveraged loans market which saw activity falling from 910 deals in H1 2018 to 411 deals in H1 2019. The subdued US LevFin market also coincided with a weaker number of CLOs hitting the market which was at its lowest in terms of volume and activity since H1 2016 (\$22.4bn via 54 deals). Year-on-year CLO issuances declined from \$140.6bn via 272 deals during H1 2018 to \$82.8bn via 169 deals in H1 2019. However, the High Yield segment performed solidly during H1 2019 with volume and revenue jumping by 24% and 19% respectively from H1 2018.

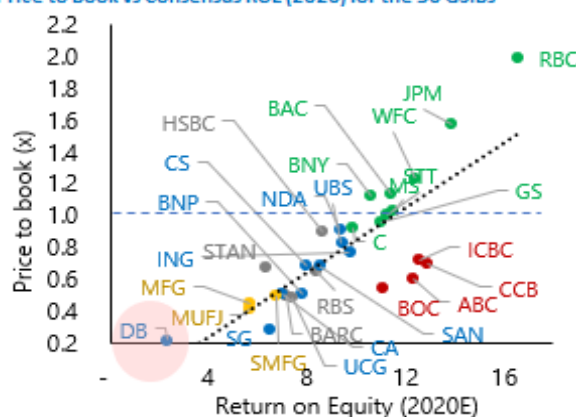


Europe

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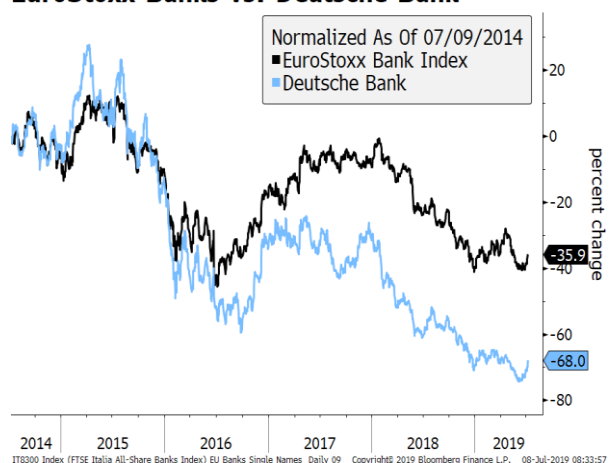
The main news in Europe came from Deutsche Bank as management prepares to undergo a massive restructuring, curbing its ambition to become an industry leader in the region. The bank will terminate its loss-making equity business, shrink its bond and rates trading operations, while cutting its 91K workforce by a fifth. In addition, it will create a “capital release unit” (a.k.a. bad bank) with €74 bn in assets, equivalent to €288 bn of leverage exposure (21-23% of Group balance sheet) that it intends to wind down. The restructuring will cost about €3 bn upfront and €7.4 bn by 2022 but should not require any additional capital. Analysts highlighted that these restructuring charges (c12% of tangible equity) were heavier than anticipated, but spread out over 4 years. It is notable that within the 30 GSIBs, Deutsche Bank has the lowest projected 2020 return on equity (at 2.3 percent), which is also reflected in the stocks trading at distressed valuations of 0.2x price to book. DB stock is up over 20% from this year's low but up 4% year-to-date, compared to a 6% gain for the EuroStoxx bank sub-index. Over a 5-year horizon, however, DB shares are down nearly 70%, compared to declines of 35% for the EuroStoxx banks. Despite the scale and scope of the restructuring plan, market reaction to the news has been fairly subdued so far (stock down about 1% on the day) as investors seem to be concerned about management's ability to implement these plans without any additional capital injections. Analysts have also expressed doubts about management's medium-term revenue and cost-cutting projections, which some have deemed as potentially ambitious.

Price to Book vs Consensus ROE (2020) for the 30 GSIBs



Source: Bloomberg

EuroStoxx Banks vs. Deutsche Bank

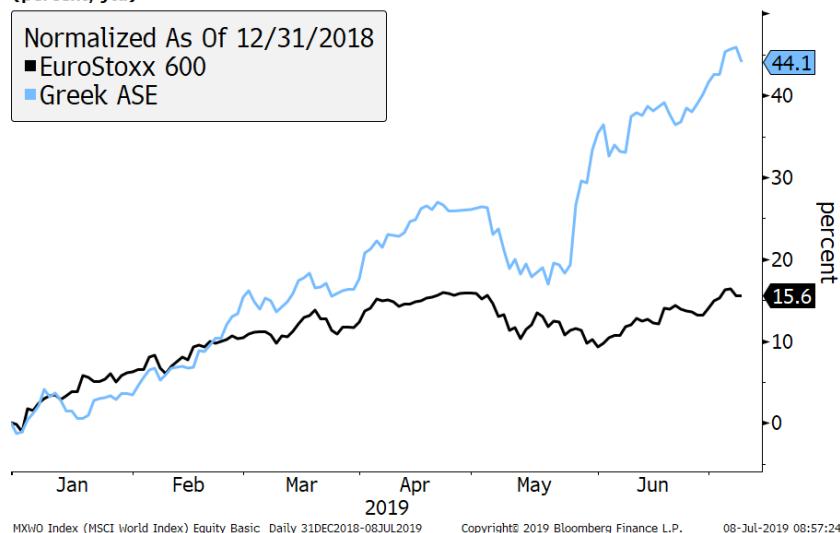


Greece

The New Democracy (ND) center-right party has won the snap elections, as expected, establishing the first outright parliamentary majority since 2010. The ND will have 158 seats, including the 50-seat bonus for the winner, compared to the outgoing Syriza's 86 seats. The party's leader, Kyriakos Mitsotakis, will look to implement a pro-business agenda to boost investment, which includes selling state assets, lowering taxes and trying to get fiscal concessions from Brussels to boost growth. The prospects of a more market-friendly government have been largely priced in, as seen by the massive outperformance of the Greek ASE index (+44% ytd), but the index is down -1.2% today.

Greek Stocks

(percent, ytd)



Other Mature Markets

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Japan

Equities declined while the yen strengthened after a strong U.S. jobs report muddled the outlook for near-term Fed rate cuts. The Topix's fell 0.9%, partially reversing the 2.7% gain last week while the yen gained 0.1% against the dollar. **Burgeoning trade tension between Korea and Japan is also**

weighing on investor sentiment, with stricter checks on exports of semiconductor materials that are considered vital to the tech industry in Korea. The stricter control took effect last Thursday and requires Japanese exporters to obtain a separate license each time they want to sell the restricted materials to South Korea; such tightened controls could introduce sizable delays in the production process. Meanwhile, Bloomberg reported that Japan is also considering removing South Korea from a list of trusted export markets, a move that could affect a broader set of products.






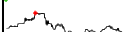

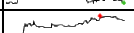




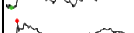

On the data front, **Japan's machinery orders fell for the first time since January**. Core machinery orders in May fell 7.8%, m/m, its biggest decline in eight months, and far exceeded expectations for a 3.8% drop. The decline is casting doubt on the strength of capital investment over the coming months, underscoring challenges amid moderating global economic growth.

Emerging Markets

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EM assets were mostly lower with negative idiosyncratic stories in Turkey and Asia. Asian equities suffered broad-based losses as regional trade tensions weighed on investor sentiment. Chinese and Korean bourses bore the brunt of the losses (Shanghai: -2.6%; Kospi: -2.2%) as technology stocks underperformed. Shares of Korea's semiconductor makers were under pressure. Samsung Electronics lost about KRW 16 tn (\$13 bn) in market value this month after Japan curbed exports of materials that are crucial for the production of memory chips to Korea. Local news reported that the Seoul Metropolitan Government will provide emergency funds to domestic companies affected by Japan's export restrictions. Meanwhile, Asian currencies weakened against the dollar, as last week's robust U.S. jobs report supported the dollar and weighed on regional currencies. The Korean won underperformed (-1.0%) while the onshore CNY outperformed, gaining 0.2% to CNY 6.88/dollar. **In EMEA**, equity indices are mixed with Russia and Turkey (both down near 1%) underperforming against other bourses. The Turkish lira is the outlier in an otherwise calm currency market, depreciating 1.6% against the dollar after President Erdogan unexpectedly removed the central bank governor. **Latin American equity markets** were mostly higher last Friday. Argentina saw the biggest gains as the Merval went up 1%, followed by Colombia equity index (+0.8%). local currencies were mostly weaker but mainly traded in narrow ranges.

Key Emerging Market Financial Indicators

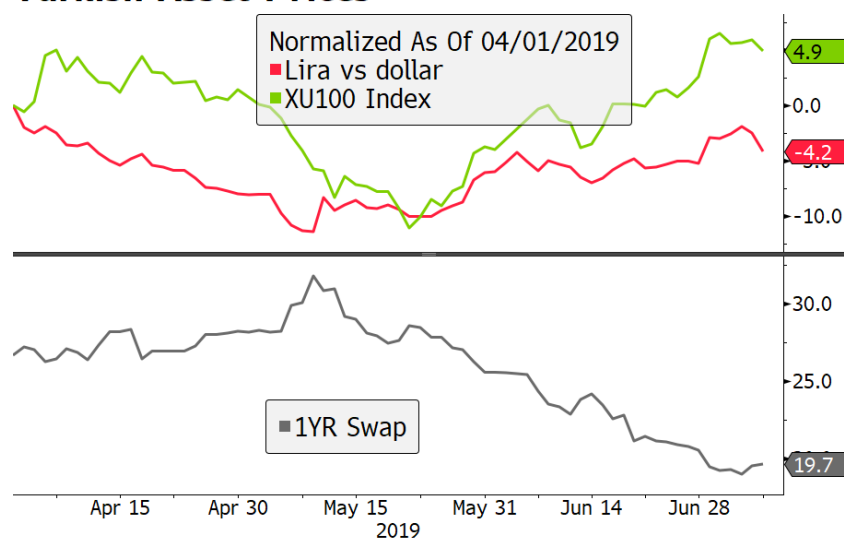
Last updated: 7/8/19 8:55 AM	Level		Change				YTD
	Last 12m	index	1 Day	7 Days	30 Days	12 M	
Major EM Benchmarks			%				%
MSCI EM Equities		42.93	-0.7	0	4	-1	10
MSCI Frontier Equities		29.99	0.0	2	2	4	15
EMBIG Sovereign Spread (in bps)		337	3	-1	-26	-19	-77
EM FX vs. USD		62.92	0.0	0	2	-3	1
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.88	0.2	0	1	-4	0
Indonesian Rupiah		14108	-0.2	0	1	2	2
Indian Rupee		68.66	-0.3	0	1	0	2
Argentine Peso		41.82	0.0	2	7	-33	-10
Brazil Real		3.80	0.5	1	2	2	2
Mexican Peso		18.92	0.5	1	2	1	4
Russian Ruble		63.67	0.2	-1	2	-2	9
South African Rand		14.13	0.3	0	5	-5	2
Turkish Lira		5.72	-1.6	-1	1	-17	-8
EM FX volatility		7.73	1.4	-0.3	-1.0	-1.7	-2.0

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

Turkey

Local assets are down sharply after President Erdogan used a presidential decree to oust the central bank governor. The move suggests market fears of a further erosion of central bank independence and the risk of premature easing under the new governor Murat Uysal. Indeed, some contacts noted that the governor's dismissal a year before his term expired was down to his refusal to implement early rate cuts. The one-year swap rate is up some 70 bps over the last two sessions, the lira has depreciated nearly 2% against the dollar, and the BIST index is underperforming on the day.

Turkish Asset Prices



EM Issuance

Emerging market fixed-rate dollar issuance totaled \$132.0 bn in 2019, reaching the second highest 1H on record. Dollar issuance during 2019Q2 was dominated by corporate issuers, while only \$17.6 bn was placed by sovereigns, with the majority of the latter coming in June. From a regional perspective, Asia was the largest EM corporate issuer, accounting for around \$79.1 bn. As in the first quarter of 2019, issuers in Latin America continued to return to the market following the lack of supply in the middle of last year.

EM Fund Flows

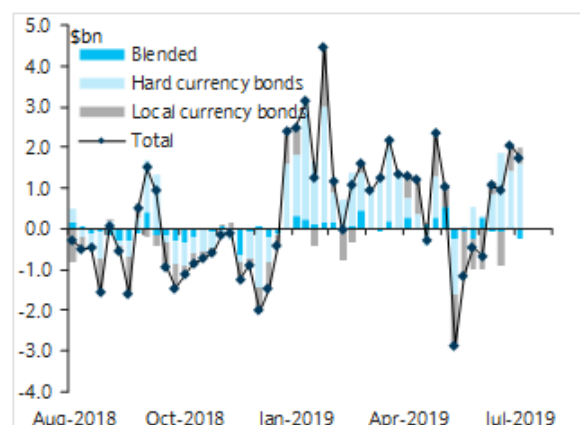
EM bond funds continued to benefit from inflows last week, while EM dedicated equity funds suffered small outflows. According to research reports, the current environment of dovish central banks and globally depressed yields have helped the flow of capital into emerging market. For EM bond funds, these positive push factors appear to more than offset concerns about EM growth prospects. However, these concerns seemed to have a non-trivial effect on flows into EM equity funds.

Figure 2: Flows into dedicated EM Equity funds



Source: EPFR Global, Barclays Research

Figure 3: Flows into dedicated EM bond funds



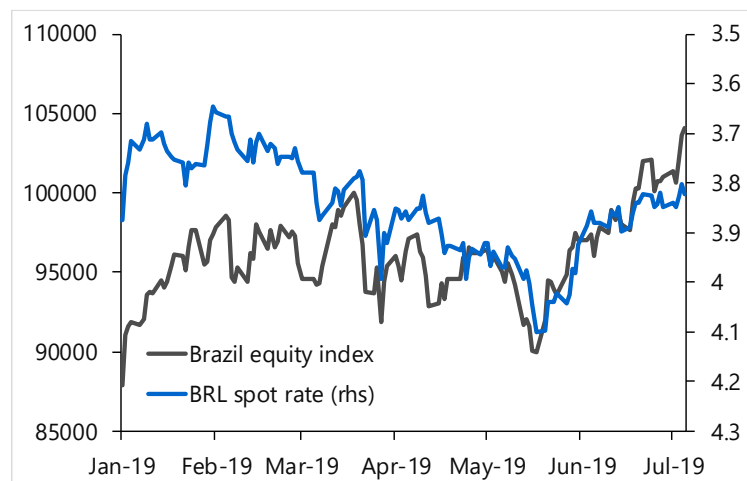
Source: EPFR Global, Barclays Research

China

China's foreign-currency reserves rose for a second month amid potential capital inflows and positive valuation effects. FX reserves rose from \$3.101 tn in May to \$3.119 tn, its highest level in more than a year, exceeding expectations. Analysts noted that the value of reserves was likely boosted by stronger currencies against the dollar and higher asset prices. The RMB outperformed their Asian peers on the day, with the onshore CNY gaining 0.2% to CNY 6.88/dollar and the offshore CNH gained 0.1% to CNH6.89/dollar.

Brazil

The social security reform bill cleared another important step last Thursday after being approved by a special commission. This was the final step to be cleared for the bill to now move to the lower house for voting. To pass, it requires the approval by a qualified majority (308 of 513 congressmen) in two rounds of votes. Market reaction was optimistic, with domestic equity finishing 1.6% higher and the real appreciating 0.7% against the dollar.



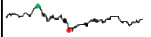






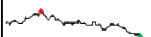





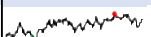















Source: Bloomberg

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Global Financial Indicators

Last updated: 7/8/19 8:59 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		2990	-0.2	2	4	8	19
Europe		3520	-0.2	1	4	2	17
Japan		21534	-1.0	-1	3	-1	8
China		2933	-2.6	-4	4	7	18
Asia Ex Japan		70	-0.8	0	5	-2	10
Emerging Markets		43	-0.8	0	4	-1	10
Interest Rates			basis points				
US 10y Yield		2.02	8.4	0	-6	-80	-66
Germany 10y Yield		-0.37	-1.1	-2	-12	-67	-62
Japan 10y Yield		-0.15	1.0	0	-3	-18	-15
UK 10y Yield		0.70	-3.5	-11	-11	-56	-57
Credit Spreads			basis points				
US Investment Grade		119	0.7	2	-9	10	-28
US High Yield		430	1.7	-2	-23	68	-91
Europe IG		51	0.8	0	-10	-17	-36
Europe HY		249	4.8	1	-20	-53	-103
EMBIG Sovereign Spread		337	3.0	-1	-26	-19	-77
Exchange Rates			%				
USD/Majors		97.28	0.0	1	1	4	1
EUR/USD		1.12	0.0	-1	-1	-4	-2
USD/JPY		108.6	-0.1	0	0	2	1
EM/USD		62.9	0.1	0	2	-3	1
Commodities			%				
Brent Crude Oil (\$/barrel)		64	0.0	-1	1	-17	19
Industrials Metals (index)		112	0.5	-1	2	-10	2
Agriculture (index)		41	0.2	-1	1	-8	-1
Implied Volatility			%				
VIX Index (% change in pp)		13.9	0.6	-1.2	-2.4	0.5	-11.5
10y Treasury Volatility Index		4.4	0.2	-0.3	-0.3	0.7	-0.2
Global FX Volatility		6.2	0.1	-0.3	-0.7	-1.4	-2.8
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		247	-4.0	-18	-61	-121	-169
Italy		210	-1.1	-23	-52	-32	-40
Portugal		81	1.5	4	-7	-70	-67
Spain		77	8.4	8	-4	-25	-40

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: 7/8/2019 8:56 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	-0.4	1	-4	0		3.2	0.3	-7	-6	-31	1	
Indonesia		14108	-0.2	0.0	1	2	2		7.3	-3.3	-16	-78	-66	-86	
India		69	-0.3	0.4	1	0	2		6.8	-5.9	-16	-34	-126	-63	
Philippines		51	-0.3	-0.5	2	4	2		4.7	-7.0	-14	-33	-118	-15	
Thailand		31	-0.4	-0.5	2	8	6		2.1	0.1	-12	-30	-54	-50	
Malaysia		4.14	-0.1	-0.1	1	-3	0		3.6	0.2	-3	-12	-55	-49	
Argentina		42	0.0	1.6	7	-33	-10		29.3	16.1	62	-326	1026	630	
Brazil		3.80	0.5	1.0	2	2	2		6.8	2.6	-11	-78	-307	-138	
Chile		681	0.3	-0.3	2	-4	2		3.4	3.3	2	-39	-147	-110	
Colombia		3210	-0.4	0.0	3	-10	1		5.7	9.7	-12	-39	-72	-86	
Mexico		18.92	0.5	1.1	2	1	4		7.5	4.7	-13	-60	-29	-126	
Peru		3.3	0.0	0.1	2	0	2		4.7	-2.7	-11	-41	-86	-99	
Uruguay		35	-0.2	0.0	0	-11	-8		10.4	1.0	-5	-67		-28	
Hungary		289	-0.2	-1.0	-2	-5	-3		1.5	5.8	-18	-31	-115	-75	
Poland		3.79	0.0	-0.8	-1	-3	-1		2.0	1.3	-9	-13	-62	-29	
Romania		4.2	0.0	-0.3	-1	-6	-3		4.0	1.0	-5	-10	-72	-21	
Russia		63.7	0.2	-1.1	2	-2	9		7.2	0.5	-6	-39	-24	-119	
South Africa		14.1	0.3	0.0	5	-5	2		9.2	4.0	-2	-30	-11	-41	
Turkey		5.72	-1.6	-1.2	1	-17	-8		16.4	23.5	-54	-378	-116	-50	
US (DXY; 5y UST)		97.3	0.0	1.2	1	4	1		1.82	-0.8	3	-3	-90	-69	
	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		2933	-2.6	-4	4	7	18		177	0	-4	-6	-17	-17	
Indonesia		6352	-0.3	0	2	12	3		181	4	-5	-13	-41	-55	
India		38721	-2.0	-2	-2	9	7		134	-9	-14	-22	-34	-62	
Philippines		8052	-0.8	0	1	12	8		72	5	-6	-10	-62	-49	
Malaysia		1678	-0.3	0	2	1	-1		116	-1	-12	-16	-53	-46	
Argentina		41756	0.9	0	17	51	38		794	7	-18	-154	229	-21	
Brazil		104090	0.4	3	6	39	18		228	2	-1	-19	-80	-45	
Chile		5076	0.4	0	3	-4	-1		132	1	-1	-8	-12	-34	
Colombia		1579	0.8	2	5	1	19		174	-1	-1	-22	-8	-54	
Mexico		43405	-0.1	1	0	-11	4		322	1	-4	-19	46	-32	
Peru		20882	0.2	1	3	5	8		119	1	-3	-15	-48	-49	
Hungary		40920	-0.2	1	-1	14	5		86	6	-2	-14	-60	-62	
Poland		60629	0.0	1	3	7	5		32	6	-5	-31	-45	-53	
Romania		8912	-0.6	1	4	14	21		181	-5	-2	-15	7	-40	
Russia		2817	-0.6	1	3	20	19		198	1	-1	-15	-8	-54	
South Africa		57672	0.1	-1	-1	1	9		281	1	5	-44	-31	-84	
Turkey		98860	-0.8	-1	5	0	8		485	19	29	-50	84	56	
Ukraine		545	-0.4	-1	-2	11	-3		519	3	17	-67	-63	-268	
EM total		43	-0.7	0	4	-1	10		337	3	-1	-26	-19	-77	

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