GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

THURSDAY, JUNE 30, 2022

- **US Treasury yields fall as softer economic data adds to growth worries** (link)
- **US high yield corporate default rates are projected to rise and drive spreads wider** (link)
- **Swedish central bank hikes 50 bps and signals further tightening ahead** (link)
- **Weaker economic data releases in the UK raises recession fears** (link)
- **Chinese PMIs return to expansionary levels in June as virus situation improves** (link)
- **Special Feature: Emerging Markets Local Currency Bond Holdings Monitor** (attached)

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Concerns around growth and inflation trade-off dampens risk appetite

Core sovereign bond yields and global equity markets are declining as investors weigh ongoing growth concerns against recent central bank communications. Major European equity indices and US futures are down over 1.5% this morning as worries over inflation and recession risks returned to dominate the narrative and have ultimately reduced risk sentiment. At the ECB forum in Sintra, statements from key central banks reiterated the commitment to combating inflation but noted tighter financial conditions may be needed to slow demand growth. Uncertainty over the global growth outlook, alongside a recent mixed bag of data releases, has pushed US Treasury yields down 10 to 15 bps across maturities and German bund yields have declined 15 to 20 bps across the curve over the past day. Breakeven inflation rates drove the move lower in rates yesterday and oil prices also continued to slip as OPEC ratified the planned supply increase for August at its meeting this morning. Although Asian equities mostly closed lower across the region overnight, Chinese equities were the notable outperformer and gained over 1% following some improving PMI data and further re-opening optimism.

Key Global Financial Indicators

Last updated: 6/30/22 8:06 AM	Level Last 12m	Latest	Change from Market Close 1 Day	7 Days	30 Days	12 M	YTD	Since 23-Feb-22
Equities					%		%	
S&P 500		3819	-0.1	2	-8	-11	-20	-10
Eurostoxx 50		3420	-2.7	0	-10	-16	-20	-14
Nikkei 225		26393	-1.5	1	-4	-8	-8	0
MSCI EM		40	-0.4	2	-6	-27	-18	-15
Yields and Spreads					bps			
US 10y Yield		3.04	-5.4	-5	30	157	153	104
Germany 10y Yield		1.40	-12.4	-3	34	160	157	117
EMBIG Sovereign Spread		535	13	26	81	197	168	122
FX / Commodities / Volatility					%			
EM FX vs. USD, (+) = appreciation		51.3	-0.5	-1	-3	-10	-2	-3
Dollar index, (+) = $ appreciation		105.5	0.4	1	4	14	10	10
Brent Crude Oil ($/barrel)		115.5	-0.7	5	-6	54	48	19
VIX Index (%, change in pp)		30.0	1.9	1	4	14	13	-1

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

Mature Markets

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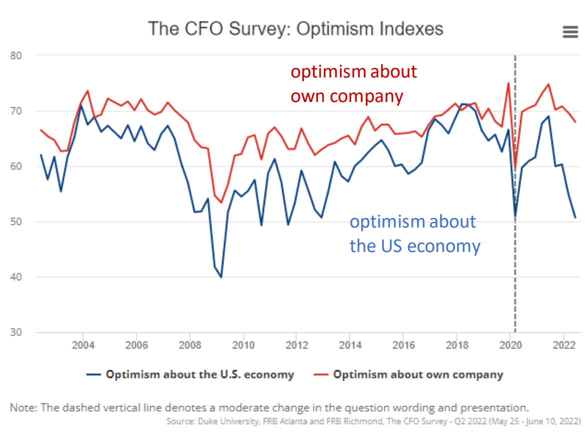
United States

US equities were little changed, as the S&P 500 closed down -0.1% after fluctuating between gains and losses throughout the trading session. Downward revisions of 1Q consumer spending and GDP spurred growth concerns. Cyclical shares, such as the energy, industrial and financial sectors, underperformed. **US Treasury yields declined by 5–8 bps across tenors, with 10-year yields down 8 bps to 3.1%.** Fed Chair Powell spoke at the ECB forum in Sintra, reiterating that the US economy is in strong shape and should be able to withstand tighter monetary policy. He also commented that markets are "pretty well-aligned" with what the Fed is thinking regarding rate hike expectations. Markets are pricing in 68 bps of hikes by July and an additional 56 bps by September.

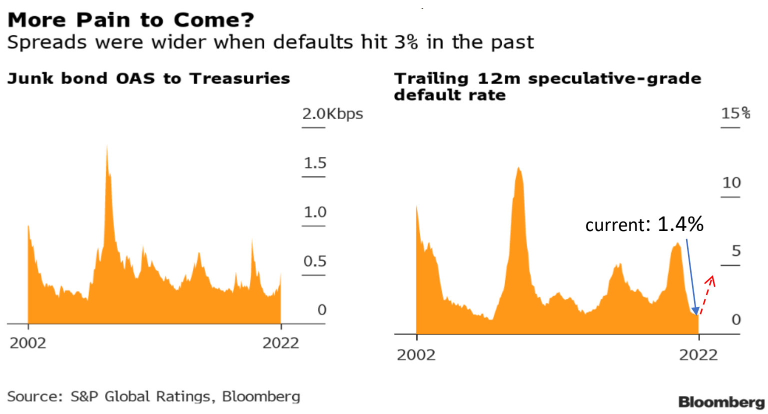
In data releases this morning, US inflation data came in slightly lower than expected, with the PCE deflator rising 0.6% m/m (vs. 0.7% expected) and 6.3% y/y (vs. 6.4%) in May. The core deflator was up 0.3% m/m (vs. 0.4%) and 4.7% y/y (vs. 4.8%). Personal spending was weaker than expected (0.2% vs. 0.4% expected). Weekly initial jobless claims dropped to 231k from 233k (revised up from 229k) and were slightly worse than expected (consensus 229k); continuing claims recorded 1328k versus expected 1318k. There was limited market reaction following these releases.

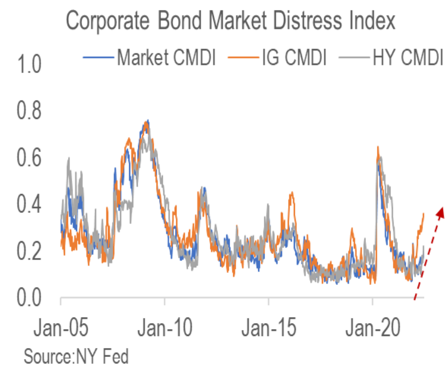
Yesterday, Q1 US consumer spending was revised down from 3.1% to 1.8%, causing a downward revision of Q1 US GDP from -1.5% to -1.6%. Spending on both services and goods was revised lower. In addition, following weak consumer confidence data, the US CFO survey conducted by Duke University and the Fed shows **that CFOs' optimism about the economy has declined**, with the CFO Optimism index dropping to 50.7 this quarter from 54.8 last quarter (scale from 0 to 100). According to JP Morgan analysts, one year ahead recession probabilities calculated from economic data, the slope of the yield curve, and risk assets (the S&P 500 and high-grade credit spread) show that recession risk has risen.



Source:Duke University, FRB Atlanta and FRB Richmond, The CFO Survey

S&P Global Ratings estimates that the US HY corporate default rates will hit 3% by the end of this year, presaging additional spread widening. According to data from S&P and Bloomberg, over the past 20 years, spreads tend to be wider than the current level (520 bps) when default rates rise above 3%. In early 2016, spreads spiked above 800 bps as default rates hit 3% from 1.8% the prior year. Separately, **the NY Fed launched the Corporate Bond Market Distress Index (CMDI) as an aggregate measure to gauge market functioning in primary and secondary corporate bond markets**. The index is made up of seven underlying sub-indices, including trading and issuance volume, prices on both traded and non-traded bonds, and market liquidity. The index identifies past market distress periods and reflects recent worsening trends driven by global uncertainty and monetary policy tightening.





Euro area

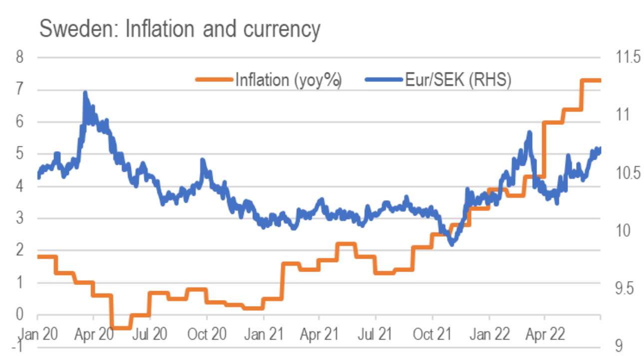
European equities fell (Stoxx 600 Europe index -1.4%) with all sectors trading in the red. **Sovereign yields fell (10y bund -10 bps to 1.42%), while Southern spreads edged higher (10y Italian spreads +3 bps to 191 bps). The euro was little changed.**

The ECB will discuss a proposal next week to request banks to take a more prudent approach to dividend and share buyback plans, according to the head of the ECB supervisory board Enria. Enria said that the request would be for banks to use a more adverse scenario—including potentially a gas embargo or a recession—when calculating their capital trajectories. **European gas prices continue to trend higher amid energy supply uncertainty** (Dutch natural gas prices 1-m ahead +5% to €145/MWH).

This morning, France's preliminary June inflation data increased to 6.5% y/y, the highest level since the introduction of the euro. The increase was in line with expectations, up from 5.8% y/y in May. This follows on data earlier this week that showed a notable upside surprise in preliminary data for Spain (10.0% y/y vs expected 8.7%) and an unexpected easing in Germany (8.2% y/y vs expected 8.8% from +8.7%). Euro area preliminary inflation for June is due on Friday, with consensus expecting inflation to increase to 8.5% y/y from 8.1%. **At the ECB's conference in Sintra, ECB President Lagarde said that the low inflation era prior to the pandemic is not likely to return, and that central banks have to adjust to higher expectations for price growth.** Money markets have continued to price in a lower ECB policy rate at the end of this year (-10bps to 0.93%), with roughly 29 bps of tightening priced in for the July meeting.

Sweden

The krona was initially little changed against the euro but depreciated in later trade after the Riksbank increased its policy rate by 50 bps to 0.75%, in line with expectations. With inflation expected to remain above 7% for the rest of 2022, the central bank's executive board forecast further tightening and sees the policy rate at close to 2% at the start of 2023, according to the press statement. The Riksbank's asset holdings will also be reduced as at faster pace than announced in April. **ING analysts caution that the short-term outlook for the krona is troubled by an unstable risk environment, including its pending entry into NATO.**

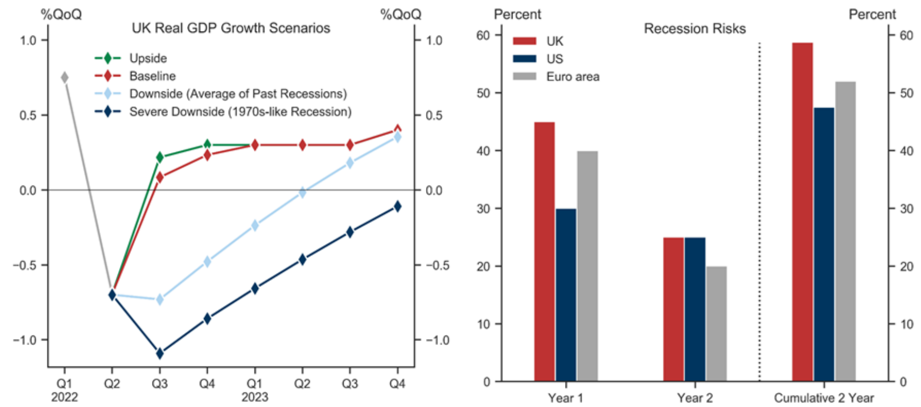


Source: Bloomberg and IMF calculations

United Kingdom

The pound weakened marginally (-0.1%) this morning after data continue to point to weakening economic activity. UK house price growth eased to 10.7% y/y in June, from 11.2% in May, according to the Nationwide House Price Index, while UK business confidence in June fell to the lowest level seen since March 2020 (28 from 38), according to Lloyd's business barometer. Real disposable income fell by 0.2% in Q1, according to the Office for National Statistics. Goldman Sachs analysts now see GDP growth at -0.7% in Q2 and +0.1% in Q3, with a 45% probability that the UK falls into a recession in the next year. **While analysts caution a clear recession would see less rapid monetary tightening, they continue to expect 50 bps hikes in both August and September, and 25 bps hikes in November and December.** Markets are pricing in roughly 155 bps of tightening by the end of the year, with roughly 40 bps of tightening priced in for the next BoE monetary policy meeting in August.

Exhibit 4: Growth Scenarios and Recession Risks

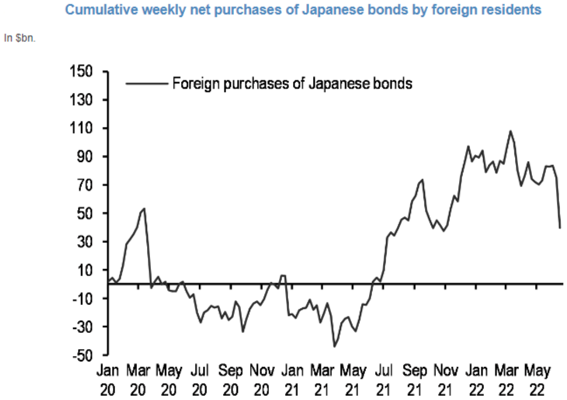


Source: Goldman Sachs Global Investment Research

Japan

Equities slumped -1.2%. Industrial production unexpectedly dived -7.2% m/m in May (consensus: -0.3%, previous: -1.5%), largely due to supply bottlenecks and weakened demand amid China lockdowns. Separately, **Japan's three largest banks will reportedly raise mortgage rates next month.** MUFG Bank and SMBC will raise headline rates by 5 bps to 3.69%. Mizuho will hike 15 bps to 3.15%, FNN reports. **The yen gained +0.3%, 10-year yields were little changed.** The BOJ announced unchanged planned bond purchases for July-September. According to JP Morgan, foreign investor selling and increased macro hedge fund shorts likely spurred recent upward yield pressures.

Cumulative weekly net purchases of Japanese bonds by foreign residents



Source: MoF, J.P. Morgan.

Emerging Markets

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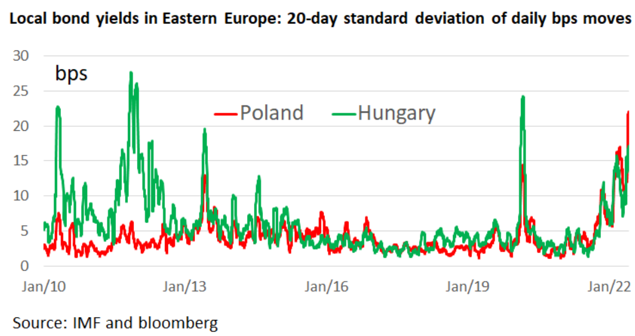
In **Latin America,** the **Chilean peso** underperformed all EMFX declining by 1.6% yesterday amid continued weakness in copper prices. The recent announcement of $5 bn in FX sales from the Treasury had limited impact. Over the last month copper has declined by 15% and the Chilean peso depreciated by close to 12%. The **Brazilian real** outperformed all EMFX gaining 1.7% on the day. The positive reaction was likely a relief rally following the finalization of the latest social spending bill after several iterations.

Asian equities slipped -1.1% on net. Mainland China rallied (Shanghai: +1.1%, Shenzhen: +1.4%) on travel optimism and improved PMI readings while other markets slipped. The Philippines lost -2.3%, South Korea fell -1.9%. Asian currencies were mixed, and 10-year yields mostly fell. Bond yields in **Sri Lanka** surged +24 bps. Consumer price inflation hit 55% y/y in June (survey: 44%). The country will continue virtual IMF talks to reach a staff-level Extended Fund Facility agreement soon, following *significant progress* and *constructive and productive* discussions in late June, according to the IMF statement.

In EMEA, Equities and currencies traded lower in line with broader markets. Shares recorded large declines in Russia (-5%), the Czech Republic (-2%), Poland (-1.8%) and Hungary (-1.3%). As expected, Hungary aligned its one-week deposit rate to its base rate with a hike of 50 bps, leaving both rates at 7.75%. Hungary's PPI rose 2.6% m/m in May (from 2.9% in April) with the PPI index up 32% y/y. **Local yields in Central and Eastern Europe generally traded lower as interest rate markets remain extremely volatile.** Ukraine said that a deal with Russia to end Russia's blockade of Ukraine' seaports and grain exports remains distant.

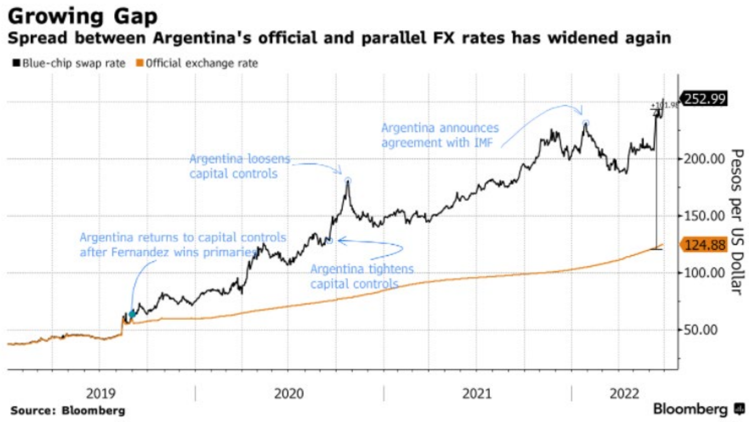


China

China PMIs turned expansionary in June as COVID measures eased. Non-manufacturing PMI surged to 54.7 (previous: 47.8) well above expectations, manufacturing PMI firmed as well to 50.2 (previous: 49.6). China Logistics Information Center, a PMI co-publisher, noted that China's economy bottomed out in June, with recovery already entrenched although an imbalanced supply-demand recovery warranted continued attention. Separately, the **Peoples' Bank of China (PBOC) reiterated its pledge to provide additional monetary support.** In a statement published after the quarterly meeting of its monetary policy committee on Wednesday, the PBOC emphasized goals to stabilize employment and prices and provided further signals it will focus on boosting credit growth, Bloomberg reports, **Equities rallied (Shanghai: +1.1%, Shenzhen: +1.4%)** and the renminbi and 10-year yields were little changed.

Argentina

The government raised about $2 bn in local instruments, enough to roll over all its bonds maturing by the end of the month. The sale was seen as a barometer of market sentiment after a selloff in peso securities in recent weeks. Some analysts highlighted that the ministry rolled less than 50% of the debt service when excluding the central bank's direct help and even lower when considering indirect support. **Despite the rollover, the parallel peso rate has continued its climb higher this week.** Bloomberg noted several analysts citing the need to increase the monetary base to meet peso financing needs, a drop in agricultural exports, and an increase in energy imports are all creating significant devaluation pressures.



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Global Financial Indicators

Last updated:	Level		Change					Since
6/30/22 8:06 AM	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
Equities					%		%	%
United States		3801	-0.1	0	-8	-12	-20	-10
Europe		3420	-2.7	0	-10	-16	-20	-14
Japan		26393	-1.5	1	-4	-8	-8	0
China		4485	1.4	3	10	-14	-9	-3
Asia Ex Japan		69	-0.4	2	-3	-26	-16	-12
Emerging Markets		40	-0.4	2	-6	-27	-18	-15
Interest Rates					basis points			
US 10y Yield		3.04	-5.4	-5	30	157	153	104
Germany 10y Yield		1.40	-12.4	-3	34	160	157	117
Japan 10y Yield		0.23	-0.5	-1	-1	17	16	3
UK 10y Yield		2.33	-5.5	1	34	161	136	85
Credit Spreads					basis points			
US Investment Grade		176	1.1	4	22	88	64	33
US High Yield		573	10.5	28	128	261	235	166
Europe IG		121	3.7	8	34	74	73	50
Europe HY		593	10.9	34	155	361	351	241
Exchange Rates					%			
USD/Majors		105.50	0.4	1	4	14	10	10
EUR/USD		1.04	-0.5	-1	-3	-12	-9	-8
USD/JPY		136.3	-0.2	1	6	23	18	18
EM/USD		51.3	-0.5	-1	-3	-10	-2	-3
Commodities					%			
Brent Crude Oil ($/barrel)		116	-0.7	5	0	68	53	27
Industrials Metals (index)		156	-2.7	-3	-16	0	-10	-17
Agriculture (index)		70	-0.5	1	-7	21	15	-1
Implied Volatility					%			
VIX Index (%, change in pp)		30.0	1.9	1.0	3.8	14.2	12.8	-1.0
US 10y Swaption Volatility		123.9	0.1	2.9	17.3	56.4	44.9	29.6
Global FX Volatility		10.9	0.0	-0.3	1.3	4.2	3.5	3.4
EA Sovereign Spreads					10-Year spread vs. Germany (bps)			
Greece		228	12.4	-7	-18	124	76	-12
Italy		192	3.4	-4	-8	89	57	20
Portugal		108	1.9	1	-6	48	43	16
Spain		108	0.7	-1	-2	46	34	5

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

Emerging Market Financial Indicators

Last updated: 6/30/2022 8:10 AM	Exchange Rates								Local Currency Bond Yields (GBI EM)							
	Level		Change (in %)					Since	Level		Change (in basis points)					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
		vs. USD	(+) = EM appreciation							% p.a.						
China		6.70	0.0	-0.1	0	-4	-5	-6		2.9	-5.1	3	6	-27	7	6
Indonesia		14898	-0.3	-0.4	-2	-3	-4	-4		7.2	-5.5	-19	19	63	84	72
India		79	0.0	-0.8	-2	-6	-6	-6		6.3	0.0	0	9	75	0	
Philippines		55	0.2	-0.5	-5	-11	-7	-7		5.7	0.0	0	20	155	118	68
Thailand		35	-0.4	0.4	-3	-9	-6	-9		2.9	-4.0	14	-7	110	104	67
Malaysia		4.41	-0.2	-0.1	-1	-6	-6	-5		4.3	3.1	7	8	99	68	60
Argentina		125	-0.1	-0.9	-4	-23	-18	-14		60.0	11.0	-179	401	1466	941	1202
Brazil		5.22	-0.7	0.4	-9	-5	7	-4		12.5	-52.0	-6	14	328	180	97
Chile		925	-1.4	-3.9	-10	-21	-8	-15		6.4	0.0	23	32	220	99	50
Colombia		4116	-0.5	-2.3	-4	-8	-1	-5		9.0	0.0	9	81	318	263	116
Mexico		20.19	-0.3	-0.8	-3	-1	2	0		9.0	0.0	22	53	200	148	116
Peru		3.8	-0.3	-1.8	-3	3	6	-1		7.7	0.2	6	21	240	184	174
Uruguay		40	-0.8	0.7	1	10	13	7		10.6	0.0	-15	35	273	188	245
Hungary		382	-1.2	-0.6	-3	-22	-15	-16		7.9	-25.0	20	86	516	335	305
Poland		4.51	-0.8	-0.9	-5	-15	-11	-10		6.6	-28.8	-5	22	480	302	265
Romania		4.8	-0.6	-1.3	-3	-13	-9	-8		8.7	-7.9	-29	99	594	391	358
Russia		53.9	-3.7	0.9	16	36	39	51		8.1	-10.0	-15	-1	74	-67	-308
South Africa		16.4	-0.8	-2.5	-4	-13	-3	-8		9.0	10.0	40	62	168	160	144
Turkey		16.67	-0.2	4.1	-2	-48	-20	-17		19.3	-5.0	-34	-347	193	-501	-311
US (DXY; 5y UST)		105	0.3	1.0	4	14	10	10		3.08	-6.5	-7	36	219	182	118

	Equity Markets								Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)					Since	Level		Change (in basis points)				Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22	Last 12m	Latest	7 Days	30 Days	12 M	YTD	23-Feb-22
									basis points						
China		4485	1.4	3	10	-14	-9	-3		198	5	-15	-5	-5	-10
Indonesia		6912	-0.4	-1	-3	15	5	0		210	6	10	37	45	25
India		53019	0.0	1	-4	1	-9	-7		194	21	14	47	62	40
Philippines		6155	-2.3	1	-8	-12	-14	-16		156	12	14	57	55	19
Thailand		1568	-1.1	1	-6	-2	-5	-8		0	0	0	0	0	0
Malaysia		1444	-0.5	1	-7	-6	-8	-9		133	3	3	10	16	0
Argentina		88131	-0.1	3	-5	41	6	-4		2374	106	458	800	694	637
Brazil		99622	-1.0	0	-11	-21	-5	-11		365	19	59	111	54	34
Chile		5010	0.1	-1	-6	16	16	14		183	8	22	42	43	9
Colombia		1347	-2.5	-2	-16	8	-5	-11		456	44	103	207	108	64
Mexico		48062	-0.8	2	-7	-4	-10	-6		461	29	93	122	129	91
Peru		18675	-0.7	-2	-10	-1	-12	-20		213	11	38	53	63	23
Hungary		39577	-0.8	0	0	-16	-22	-17		229	-8	7	95	105	76
Poland		53614	-2.0	3	-7	-19	-23	-15		87	-12	70	53	55	71
Romania		12400	-1.0	1	-1	4	-5	-6		337	12	82	158	144	105
Russia		2257	-5.1	-6	-4	-41	-40	-27		3411	-577	938	3228	3234	2897
South Africa		66672	-1.6	2	-8	1	-10	-11		490	26	109	170	135	101
Turkey		2396	-0.2	-6	-6	77	29	19		685	36	89	223	107	122
Ukraine		519	0.0	0	0	-2	-1	0		4827	814	1584	4337	4068	3354
EM total		40	-1.2	2	-6	-27	-18	-15		458	22	67	101	71	0

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

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