



- **U.S. yield curve flattens on perceived hawkish shift in FOMC** ([link](#))
- **U.S. Fed's reverse repo facility sees record usage** ([link](#))
- **Bank of Japan announces new program for climate change** ([link](#))
- **Banks warn about growth impact of Basel 3 rules** ([link](#))

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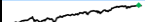
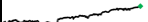





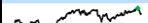



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U.S. curve flattens as investors digest FOMC decision

Markets are calm at the start of the inaugural Juneteenth holiday. U.S. 30-yr yields dropped sharply yesterday as contacts argue that the Fed's interpretation of the average inflation targeting framework may be less tolerant of an inflation overshoot than previously anticipated. The Brazilian real outperformed after the central bank signaled further tightening but most currencies are weaker against the U.S. dollar since this week's FOMC meeting.

Key Global Financial Indicators

Last updated: 6/18/21 1:10 PM	Level		Change from Market Close				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
S&P 500		4222	0.0	0	2	36	12
Eurostoxx 50		4123	-0.8	0	3	27	16
Nikkei 225		28964	-0.2	0	2	29	6
MSCI EM		55	0.6	-2	2	37	6
Yields and Spreads			bps				
US 10y Yield		1.48	-2.0	3	-15	78	57
Germany 10y Yield		-0.20	-0.8	7	-10	20	37
EMBIG Sovereign Spread		334	6	2	3	-134	-16
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		57.2	0.1	-1	-1	5	-1
Dollar index, (+) = \$ appreciation		91.9	0.0	2	2	-6	2
Brent Crude Oil (\$/barrel)		72.5	-0.8	0	5	75	40
VIX Index (% change in pp)		19.5	1.7	4	-2	-13	-3

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

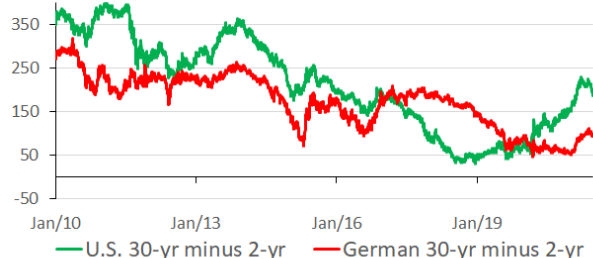
Mature Markets

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United States

U.S. yields are trading in a 1-2 bps range this morning after 30-yr yields closed 11 bps lower and the U.S. yield curve flattened yesterday. The SPX index was little changed yesterday while the tech-heavy NASDAQ closed 1% higher. The U.S. dollar, as measured by the DXY index, is now 1.5% higher compared to pre-FOMC.

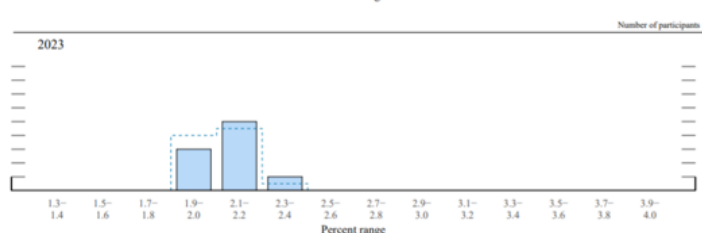
**U.S. and Euro area: 30-yr rates minus 2-yr rates
(steepness, bps)**



Source: Bloomberg and IMF staff

Contacts note that the Fed's interpretation of the average inflation targeting framework may be more flexible and less tolerant of an inflation overshoot than anticipated. As such, some observers note that markets may have pulled forward expectations for the hiking cycle as well as for the business cycle peak in response to the more hawkish than expected FOMC. In support of this view, contacts point to the June SEP itself, which shows an earlier start to the hiking cycle but no change to the terminal rate. In addition, contacts cite downside risks to a prolonged business expansion, including a slowdown in China, a potential negative U.S. fiscal impulse as the unemployment benefits expire (and if a significant infrastructure package is not passed), and small business scarring from the pandemic.

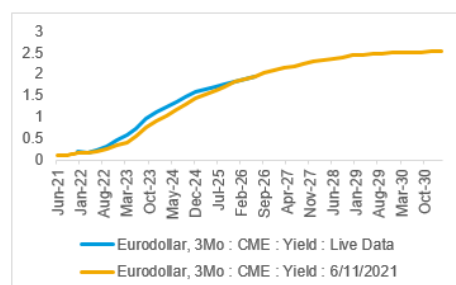
United States: Distribution of FOMC participants' June vs March projections for 2023 PCE inflation



Source: Federal Reserve

Markets have priced in more Fed tightening in 2023-24. The Sept 2023 - June 2024 eurodollar futures contract yields rose up to 5 bps yesterday. Similarly, the 1y1y forward OIS contract rate has risen by 8 bps since the FOMC decision. Price action in Eurodollars, forward OIS, and TIPs have reflected a hawkish interpretation to this week's FOMC. **TIPs inflation breakevens are lower, resulting in higher real rates.** The 5y5y TIPs breakeven rate, a measure of longer-dated inflation expectations, has declined by 8 bps on net since the FOMC event.

United States: Eurodollar futures contract yields reflect earlier FOMC hikes

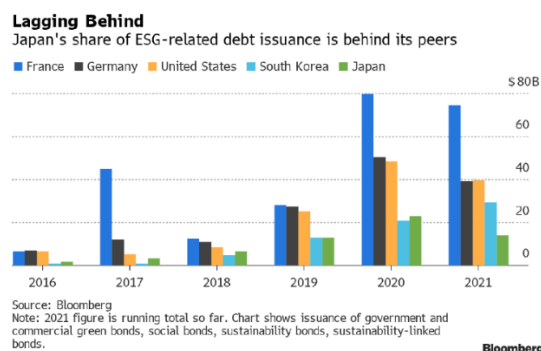


Source: Bloomberg, IMF

The Fed's reverse repo facility surged to a record of \$756 bn after the FOMC increased the RRP rate on the facility from 0 to 5 bps as part of a technical adjustment to interest rates to help keep its key overnight benchmark interest rate from falling too low. The NY Fed said there will be no change to planned open market operations on the new Juneteenth federal holiday today.

Japan

The Bank of Japan (BOJ) kept policy rates unchanged as expected. The policy balance rate and the 10-year JGB yield target were left at -0.1% and 0%, respectively. The BOJ also extended its COVID-related lending measures by six months to March 2022. Governor Kuroda said that in-person consumption will pick up along with vaccination. Japanese yen appreciated (+0.1%). Equities declined (NIKKEI: -0.2%). Long-end JGB yields dropped (10-year: -0.5 bp; 30-year: -0.7 bp). **Furthermore, the BOJ announced a new financing program for climate change, which is expected to start operating within the year.** The new program will provide funds for bank lending to climate friendly businesses. Analysts noted that Japan's green finance lags behind its peers. Headline CPI fell 0.1% y/y in May, while CPI excluding fresh food edged up 0.1%. Both showed stronger than expected inflationary pressures, underpinned by rising energy prices.

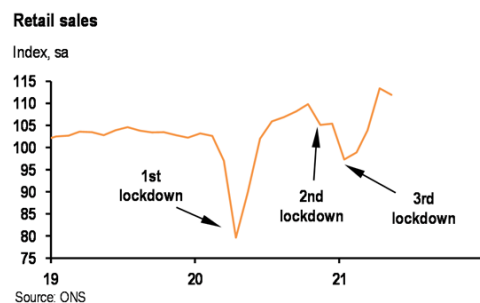


Europe

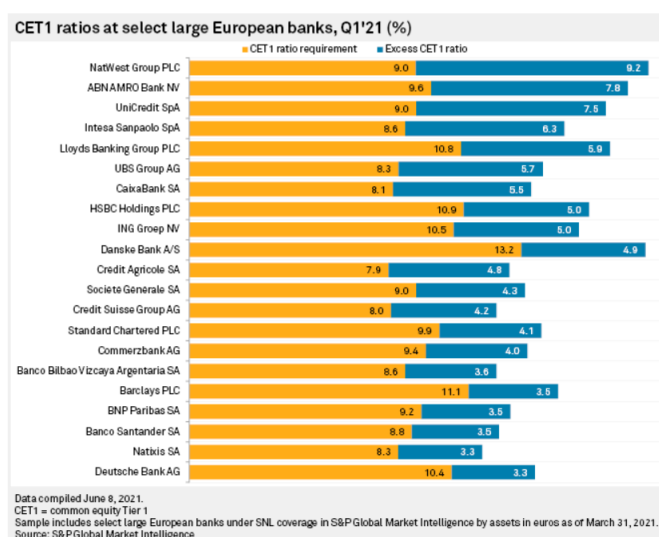
European equity trades seem to be taking a breather to digest the Fed's new forecast and direction. Trading has been mixed through the session but in tight ranges for core markets: DAX (-0.2%), CAC 40 (+0.3%). On the other hand, Spain and Italy are seeing a larger correction: Italy's Titans 30 (-0.6%), and Spanish Ibex (-0.4%). **Bank stocks (-1.1%) are also underperforming, as the prospects for a steeper yield curve in the US have faded somewhat.** In fact, compared to March 2021, the US yield curve has flattened.

Sovereign yields traded flat today as investors reassess the balance between reflation trades and the Fed's commitment to targeting average inflation. Several contacts report on the unwinding of reflation trades at the long end of the US yield curve by fast money accounts as the reason for lower yields yesterday. German 10-year yields at -0.20% (-1 bps); French OATs are at 0.15% (flat); Italian at 0.83% (+1 bps); and Spanish at 0.43% (flat).

UK retail sales (including autos) dropped in May, printing at -1.4% m/m vs +1.5% expected. On an annual basis, retail sales came in at +24.6% (incl. autos) and +21.7% (excl. autos). **UK financial assets have traded in line with European peers, thus seemingly shrugging off the data release.** FTSE 250 flat; UK 10-yr yields at 0.76% (-1 bp); sterling at \$1.39 (-0.1%). Separately, Chancellor Sunak has ruled out an extension of business support despite delayed reopening.



Top executives at BNP and Deutsche Bank warn that forthcoming Basel 3 rules risk hampering banks' ability to fund the recovery. The new Basel 3 rules come into force on Jan 1, 2023, and the European Banking Authority has estimated that European global systemically important entities would face a 23% increase in their minimum Tier 1 requirements. **Bank top executives have called on regulators to consider the current economic situation before the new rules are implemented, also noting that many have capital levels well above the requirements.**



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Latin American equities closed lower yesterday. Argentina underperformed as the equity index fell 1.7%, followed by Brazil (-0.9%) and Mexico (-0.7%). The Brazilian real (+0.9%) outperformed after the central bank signaled further hikes, while the Chilean peso and the Colombian peso depreciated 1.5% and 1.0%, respectively. 10-year government bond yields were little changed. **Asian equities were mixed, gaining 0.4 on net.** Share prices gained in Hong Kong SAR (+0.8%) while falling in Indonesia (-1.0%) and India (-0.6%). Asian currencies were also mixed. The Indian rupee appreciated (+0.2%), while Korean won depreciated (+0.2%). **Long-end government bond yields generally dropped, led by China (10-year: -2.8 bps) and Philippines (20-year: -5.1 bps), following yesterday's decline in U.S. treasury yields (10-year: -7.1 bps).** In Thailand, the baht was little changed after the government finalized plans to re-open Phuket on July 1, allowing fully vaccinated tourists to visit the island with no quarantine. **India's 10-yr government bond yield increased 18 bps in the past week as market participants have split opinions on the monetary policy direction following an increase in inflation in May.** The Reserve Bank of India purchased 345.8 bn rupee (\$4.7 bn) of government bonds at a scheduled G-SAP auction on Thursday, larger than a planned amount (300 bn rupee). **EMEA currencies reversed some of yesterday's weakness.** The largest moves were for the Turkish lira (+0.4%), the Polish zloty (+0.3%), and the Czech

koruna (+0.3%). In equities, performance was mixed but contained. The Czech Republic (-0.5%) and Hungary (-0.5%) saw the largest losses while stocks advanced the most in UAE (-0.8%) and Poland (0.2%).

EM sovereigns issued \$4 bn this week, led by Kenya (\$1 bn due 2034) and sukuk bonds of Turkey (\$2.5 bn due 2026). Morgan Stanley points out that Turkey has now issued a total of \$6 bn worth of Eurobonds in 2020 and expects another \$2-3 bn of issuance is likely.

Peru

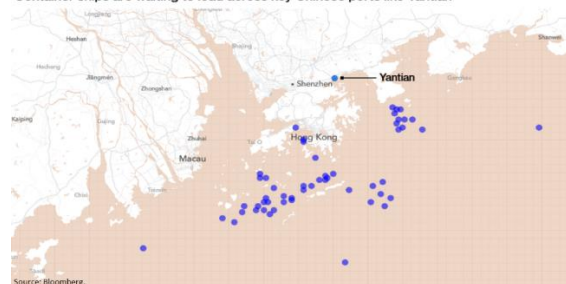
Peru's Electoral Board stated on Thursday that it is still checking contested votes from the presidential election held on June 6 to declare results. The official vote count has been completed on June 15 and showed Castillo lead Fujimori by 44,058 ballots (Castillo had 50.125% of the votes, and Fujimori had 49.875%). According to press reports, Fujimori said yesterday that her party had challenged the validity of as many as 250,000 votes cast at 900 voting tables in mostly impoverished rural areas. **The National Elections Jury said that it would declare a winner after reviewing all the voting records that have been contested and ruling on requests to have votes annulled.** Electoral experts expect that the process could take days or even weeks.

China

Disruptions at one of China's main ports could disrupt global trade. Yantian Port, located in Shenzhen, announced in late May that it would not accept new export containers due to a local COVID-19 outbreak. Yantian Port said today that it expects to be back to normal by end-June. **Some analysts viewed that it could take few months to clear the cargo backlog in southern China, which would be worse than the Suez Canal blockage in March.** Maersk, the largest cargo carrier globally, said that the situation is worrying. Based on the vessel data (see chart below, with blue dots representing ships), there are 139 container vessels are anchored off the coast of China, about 50% more than the average. Analysts expected to see a further rise in freight costs. **Equities gained (CSI 300: +0.1%). The RMB was little changed.**

Waiting for Cargo

Container ships are waiting to load across key Chinese ports like Yantian



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Global Financial Indicators

Last updated: 6/18/21 1:13 PM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		4220	0.0	-1	2	35	12
Europe		4124	-0.8	0	3	27	16
Japan		28964	-0.2	0	2	29	6
China		3525	0.0	-2	1	19	1
Asia Ex Japan		93	0.8	-1	2	36	4
Emerging Markets		55	0.6	-2	2	37	6
Interest Rates			basis points				
US 10y Yield		1.49	-1.7	4	-15	78	57
Germany 10y Yield		-0.20	-0.6	7	-10	21	37
Japan 10y Yield		0.06	-0.4	2	-3	4	4
UK 10y Yield		0.77	-0.8	6	-10	54	57
Credit Spreads			basis points				
US Investment Grade		89	-0.3	-2	-5	-60	-6
US High Yield		325	1.8	-3	-16	-268	-55
Europe IG		48	0.2	1	-4	-19	0
Europe HY		234	0.1	3	-22	-150	-8
Exchange Rates			%				
USD/Majors		91.94	0.1	2	2	-6	2
EUR/USD		1.19	-0.1	-2	-3	6	-3
USD/JPY		110.2	0.0	0	1	3	7
EM/USD		57.2	0.0	-2	-1	5	-1
Commodities			%				
Brent Crude Oil (\$/barrel)		72	-0.9	0	5	74	40
Industrials Metals (index)		150	-0.2	-6	-7	46	13
Agriculture (index)		54	2.1	-8	-8	55	13
Implied Volatility			%				
VIX Index (% change in pp)		19.6	1.8	3.9	-1.8	-13.4	-3.2
US 10y Swaption Volatility		67.2	0.0	3.3	-4.4	1.5	3.9
Global FX Volatility		6.8	0.0	0.4	-0.4	-1.9	-1.2
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		101	2.6	-1	-18	-68	-19
Italy		106	4.3	4	-15	-73	-6
Portugal		63	3.0	0	-7	-27	3
Spain		65	2.5	2	-6	-28	3

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

Emerging Market Financial Indicators

Last updated: 18/06/2021 1:15 PM	Exchange Rates						YTD	Local Currency Bond Yields (GBI EM)						
	Level		Change (in %)					Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
	vs. USD		(+) = EM appreciation					% p.a.						
China		6.44	0.1	-0.6	0	10	1		3.3	0.7	3	5	33	-1
Indonesia		14375	-0.1	-1.3	-1	-2	-2		6.3	0.7	2	-16	-101	25
India		74	0.3	-1.1	-1	3	-1		6.4	0.9	8	7	25	41
Philippines		48	-0.1	-1.5	-1	4	-1		4.3	-1.5	0	0	20	68
Thailand		31	-0.1	-1.2	0	-1	-5		1.8	0.4	-1	2	35	52
Malaysia		4.14	0.0	-0.7	0	3	-3		3.3	1.1	2	1	43	73
Argentina		95	0.0	-0.3	-1	-27	-12		44.9	-49.9	-68	-100	-305	-1125
Brazil		5.01	0.0	2.2	5	7	4		8.3	12.8	16	3	308	273
Chile		738	-1.5	-2.3	-3	8	-4		4.2	1.0	7	42	155	142
Colombia		3730	-1.3	-3.6	-1	1	-8		6.6	-4.1	-2	-19	83	149
Mexico		20.46	-0.2	-2.9	-3	11	-3		6.7	0.9	11	-13	53	112
Peru		3.9	-0.3	-0.6	-5	-11	-8		5.3	0.4	30	44	94	172
Uruguay		44	-0.1	-0.5	1	-3	-3		7.9	4.2	-1	34	-224	61
Hungary		299	0.0	-3.7	-4	3	-1		2.3	2.2	6	-12	59	78
Poland		3.82	0.1	-2.8	-3	4	-2		1.2	5.0	3	-10	28	60
Romania		4.1	-0.1	-1.9	-3	4	-4		2.7	3.0	1	2	-99	0
Russia		72.3	0.0	-0.4	2	-3	2		6.9	-3.4	-3	15	163	122
South Africa		14.1	-0.2	-3.0	-1	24	4		9.7	8.2	22	-24	-61	2
Turkey		8.71	0.2	-3.6	-4	-21	-15		17.8	7.4	-9	13	728	466
US (DXY; 5y UST)		92	0.1	1.5	2	-6	2		0.87	-1.0	13	5	54	51

	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		Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
								basis points						
China		5102	0.0	-3	-1	24	-2		199	0	-2	-9	30	-9
Indonesia		6007	-1.0	-1	4	22	0		158	0	-9	-25	-5	-29
India		52344	0.0	0	4	51	10		141	-2	-5	-22	-101	-10
Philippines		6851	-0.5	-1	11	8	-4		83	0	-9	-17	13	-22
Malaysia		1589	1.2	1	2	5	-2		113	0	-2	-3	9	3
Argentina		66440	0.0	-3	18	75	30		1459	0	19	8	-570	91
Brazil		128057	0.0	-2	4	33	8		253	0	0	-16	58	3
Chile		4330	0.0	0	4	9	4		126	0	-6	-16	-14	-18
Colombia		1249	0.0	-1	-2	10	-13		207	0	-4	-15	44	2
Mexico		50203	0.0	-1	1	33	14		348	0	-9	-34	55	-12
Peru		18696	0.0	-6	-14	10	-10		133	0	-4	-3	22	1
Hungary		48339	-0.9	-1	5	29	15		65	0	-6	-15	-42	-31
Poland		66005	0.3	0	4	31	16		-22	0	-4	-11	-54	-21
Romania		11660	0.0	1	0	34	19		183	9	-3	2	-100	-20
Russia		3786	-0.9	-1	3	39	15		159	0	-5	-3	19	-7
South Africa		66181	-0.6	-2	-2	23	11		357	0	-4	-35	25	-23
Turkey		1403	-0.8	-4	-4	25	-5		421	0	-5	-47	34	-24
Ukraine		531	0.0	0	0	6	6		479	0	12	-21	127	-12
EM total		55	-0.4	-2	2	37	6		421	0	17	-10	97	128

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

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