GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

TUESDAY, JUNE 2, 2020

- **Investors frontrunning of Fed asset purchases in corporate bond ETFs are helping drive record inflows** (link)
- **US risky assets powered ahead in May as reopening measures spread across most states** (link)
- **ECB GC members may oppose increase in QE on Thursday** (link)
- **RBA leaves its current policy settings unchanged, holding the cash rate at 25 bps** (link)
- **PBC introduces new tools to support MSE lending** (link)
- **Moody's downgrades India's sovereign rating to one level above junk with a negative outlook** (link)
- **Special Feature: ESG Monitor (attached)**

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

Market sentiment improves as US-China tensions take a back seat

European bourses and US equity futures gained as investors focused on positive signs of stimulus and the re-opening of the global economy. Markets appeared to shrug off US-China tensions and social unrest in the US, with the VIX trading at levels not seen since late February. European markets also seemed to brush off speculation that ECB Governing Council members may oppose an increase in the ECB's Pandemic Emergency Purchase Program in June and prefer to wait till September. Southern European sovereign spreads narrowed and crossover high-yield spreads tightened 20 bps to 393 this morning, the lowest mark since March 6. The dollar weakened for the fourth consecutive trading session while US Treasury yields were marginally higher. Oil prices gained on better risk sentiment and as the OPEC is expected to extend production curbs already agreed. Emerging markets also benefited, with most currencies appreciating to the dollar and domestic equities gaining.

Key Global Financial Indicators

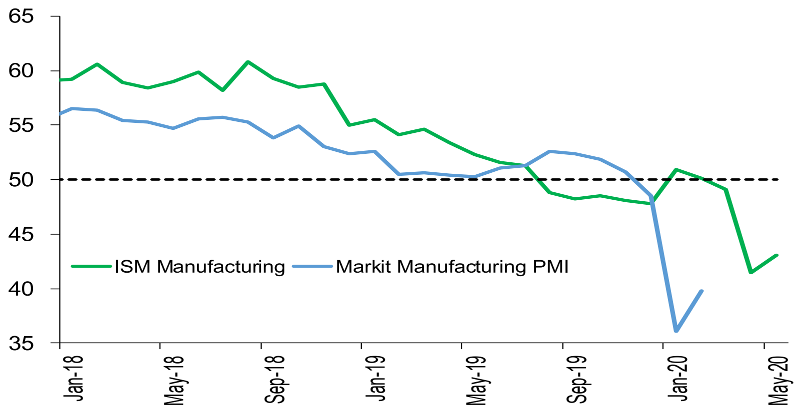
Last updated: 6/2/20 8:19 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		3056	0.4	3	8	11	-5
Eurostoxx 50		3156	0.7	5	8	-4	-16
Nikkei 225		22326	0.8	5	14	8	-6
MSCI EM		38	0.3	1	7	-7	-16
Yields and Spreads			bps				
US 10y Yield		0.68	0.7	-1	7	-144	-124
Germany 10y Yield		-0.41	3.5	2	18	-21	-22
EMBIG Sovereign Spread		513	-3	-20	-93	133	220
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		54.9	0.2	2	4	-11	-11
Dollar index, (+) = $ appreciation		98.2	-0.2	-2	-1	0	2
Brent Crude Oil ($/barrel)		39.2	0.8	8	48	-39	-41
VIX Index (%, change in pp)		27.6	1.9	0	-10	9	14

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

United States

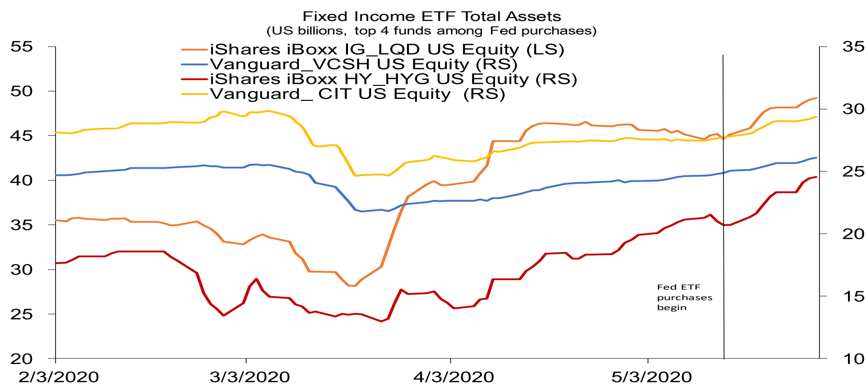
back to top

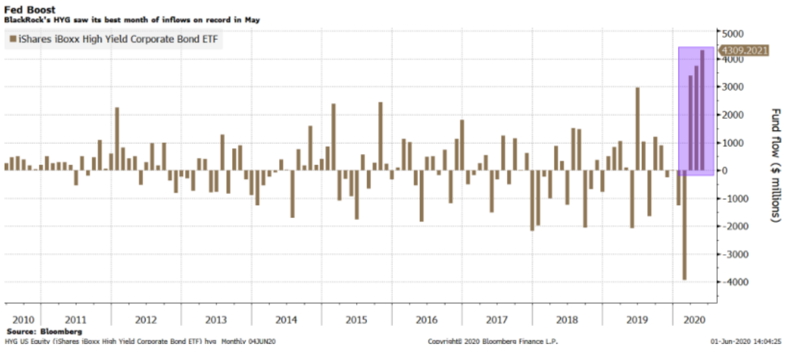
Markets shrugged off a volatile weekend and US equities managed to crawl higher to extend their rally from last week. The S&P 500 was up 0.4%, while the Treasury curve steepened as long-dated bonds sold off, with the 30-year yield up 5 basis points. Domestic tensions exploded over the weekend with widespread protests and intermittent rioting. US-China tensions remained elevated after China's state-owned agricultural companies halted purchases of some American products, casting doubt on the Phase 1 trade agreement. **Manufacturing surveys for May largely met expectations, with a modest recovery to still subdued levels.** The ISM index stabilized at 43.1, up from 41.5, with the survey committee chair noting that "demand remains uncertain."



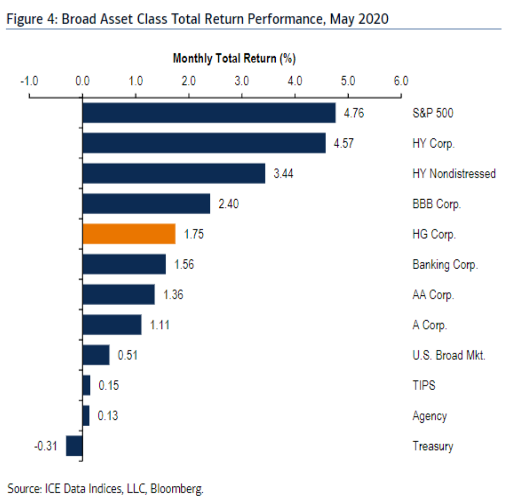
Source: Bloomberg

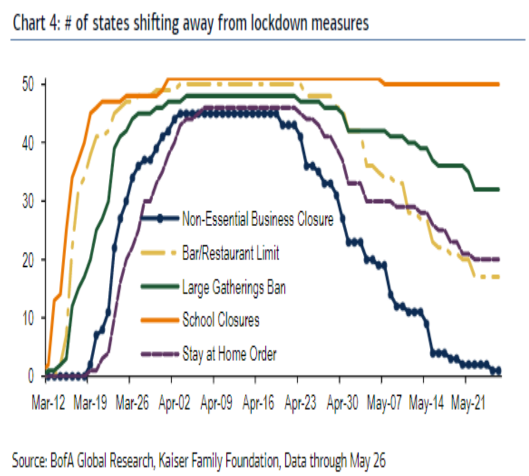
Investors are reportedly frontrunning Fed asset purchases of corporate bond ETFs, helping drive record inflows. Inflows to fixed income ETFs rose to $27 bn in May (as compiled by Bloomberg), helping boost total assets at several prominent funds to all time highs, particularly those that were involved with the Fed's Secondary Market Corporate Credit Facility (SMCCF) that began in mid-May. Notably, private inflows far outpaced the relatively modest amount bought by the Federal Reserve, which totaled about $3 bn through the end of the month, as investors may have tried to both front run the purchases and benefit from the program's continued support. Among others, the iShares iBoxx High Yield Fund, which was in the top 5 for Fed purchases with about 8% of the total through May 19th, had a record $4.3 billion of inflows in May, surpassing the previous records in March and April following the Fed's original annoucement. Five funds accounted for about 75% of purchases under the SMCCF. Despite the modest amounts purchased under the SMCCF, the program's availability seems to have had the desired effect, with **high-yield bond spreads narrowing 110 basis points in May to their lowest level since March 10**.





Markets powered ahead in May as reopening measures spread across most states. Risk-on sentiment largely resumed in May, as equities and high-yield credit posted the largest returns amid a broad-based rally in US asset classes. Investors may be overlooking the scale of the economic damage and further downside risks, but reopening measures across most states and a sense that the worst is over provided a tailwind in May. Reopening has unsurprisingly been a difference maker for consumer spending, with BofA analysts highlighting that for states furthest along in reopening, spending at restaurants has recovered to 70% of February levels, compared to 55% for the other end of the spectrum. On the corporate side, supportive monetary and fiscal measures helped drive a record pace of investment grade bond issuance year to date at over $1 trillion, while high-yield issuance in May 2020 was the largest May on record, and the busiest month since 2013.





Europe

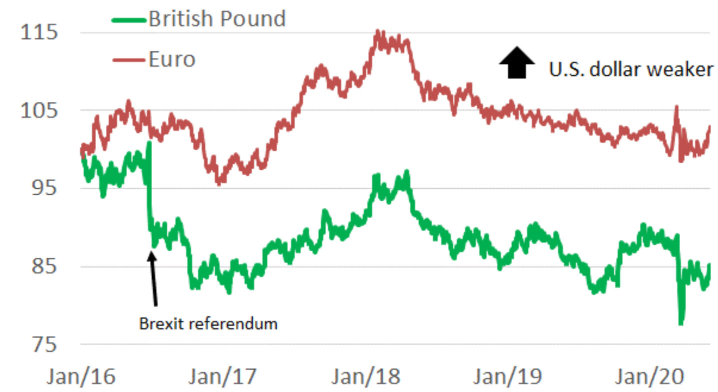
back to top

Euro area

European equities (+2.3%) rose, with strong gains in bank stocks (+4%), and **the euro (+0.3% to $1.12) appreciated**. **Crossover high-yield spreads continued to tighten**, falling 20 bps to 393. Investment-grade CDS spreads traded 1 bps lower at 69 bps. European markets appeared to brush off speculation that **many ECB Governing Council members reportedly oppose an increase in the ECB's Pandemic Emergency Purchase Program in June** and prefer to wait till September. In contrast, analyst have been expecting the ECB to increase its PEPP program by €500 bn on Thursday. Similar to credit spreads,

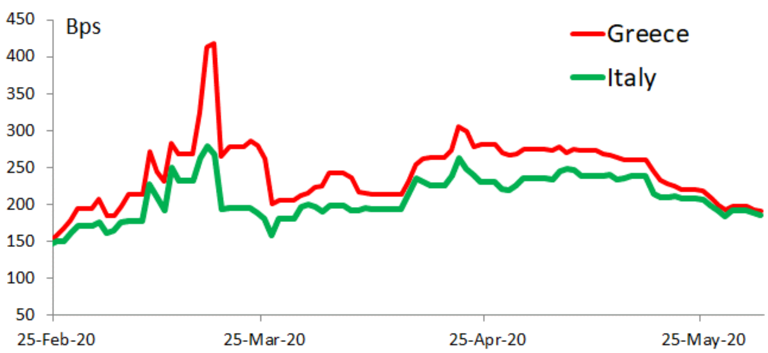
Southern European sovereign spreads also tightened. 10-year Italian spreads fell 3 bps to 187 bps, and Spanish 10-year spreads tightened 2 bps.

Euro and British pound against U.S. dollar (Jan 2016: 100)



Source: Bloomberg and IMF

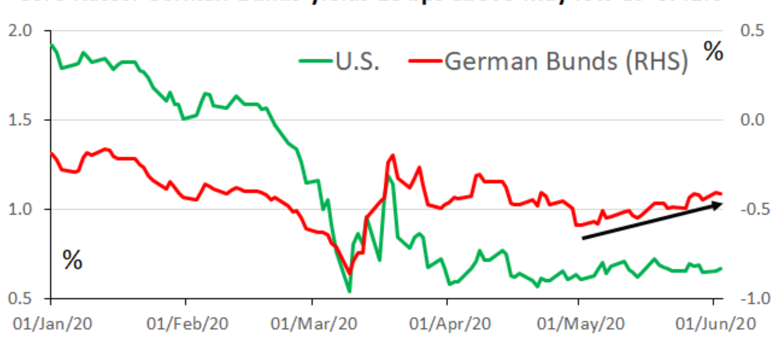
Euro area: 10-year spread over German bunds (bps)



Source: Bloomberg and IMF staff

German 10-year bund yields were little changed today, trading in a tight range around -0.4% after trading 18 bps higher in May. **German Chancellor Merkel is hosting a call with members of her government to discuss a round of post-pandemic stimulus**. Analysts expect the package to be in the range of €50-100 bn.

Core Rates: German Bunds yields 18 bps above May low at -0.41%



Source: Bloomberg and IMF staff

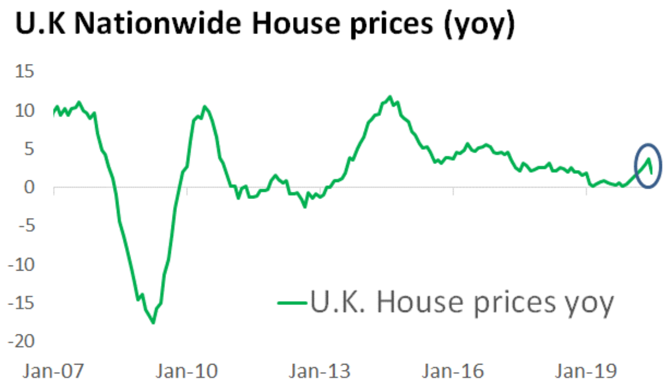
Citi calculates that **Italy's government could have a cash deficit of ~€200 bn, or 12.5% of GDP in 2020**. The state sector cash deficit totaled €76 bn in the Mar-May three-month period (4.2% of GDP), compared to €24 bn in the same period of 2019.

The French government cuts its 2020 GDP forecast to -11% from -8% ahead of a budget review and is expected to announce further stimulus in coming weeks ahead of a supplementary budget update later in June.

United Kingdom

The British pound (+0.6%) outperformed on reports that the U.K. government is showing some willingness to compromise in Brexit negotiations. The U.K. could reportedly shift its position on fisheries and "level playing field" trade rules. **PM Boris Johnson intends to hold high-level talks with European Commission President von der Leyen at the end of June** after the European Council summit on 19 June. Equities (+1%) also rose, albeit lagging other European stock markets.

U.K. house prices (collected by the Nationwide Building Society) fell 1.7% mom in May (fall of 1% mom expected), the sharpest monthly fall since 2009. U.K. house prices still rose 1.8% yoy in May (2.8% expected from 3.7% in April).



Source: Nationwide Building Society, Bloomberg and IMF

Other Mature Markets

back to top

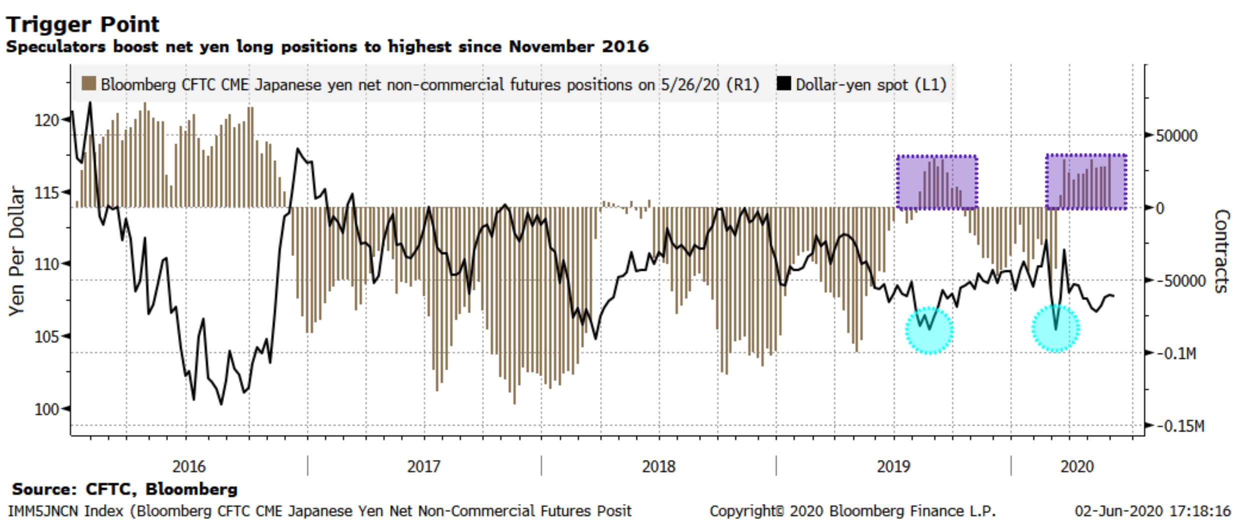
Australia

RBA left its current policy settings unchanged, holding the cash rate and the 3-year government bond yield target at 25 bps. RBA Governor Lowe noted that the depth of the downturn could be less than expected and that the "substantial, coordinated and unprecedented easing of fiscal and monetary policy in Australia is helping the economy". Meanwhile, the central bank reduced its bond buying in May. **The Australian dollar appreciated 0.9% on the day**, outperforming other G10 currencies with a number of market analysts expecting the AUD to reach as high as USD0.70/AUD in the coming days. That said, BoP data indicated that overseas investors sold a record amount of Australian government bonds in 1Q, totaling AUD 30.2 bn, the biggest since 1988. By Bloomberg's estimate, total foreign ownership of ACGBs fell from 57.7% in December to 51.9%, the least since 2004.

Japan

The yen were little changed on the day though net long yen positions by speculators reached the highest level since November 2016. Data from CFTC indicated a build-up of net long positions, which reached levels similar to those seen last year. Market contacts noted that a sudden reversal of these positions could subject the yen to a sharp depreciation, in a replay of last year's rapid reversal that took the yen spot rate from around ¥105/dollar to beyond ¥110/dollar within weeks. The yen spot rate is currently at ¥107.70/dollar, little changed since mid-May.

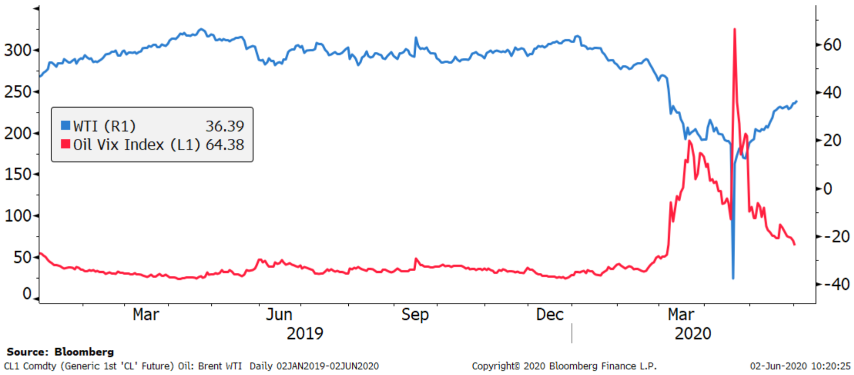
Tax revenue in April fell 29.4%, yoy its biggest monthly drop since August 2009. Market contacts noted that this sharp revenue contraction raised the prospect of further government debt issuance. **PM Abe indicated on Monday that the government will submit a second budget to parliament early next week to fund a new, $1.1 tn stimulus package** to blunt the impact of the pandemic. JGB yields were mostly steady after a 10-year auction, with market focus now shifting to the 30-year auction on Thursday



Oil Markets

Oil prices gained 2% to 3% as OPEC is expected to extend production curbs already agreed. Brent (+2.8%) traded at $39/barrel and WTI (+2.4%) at $36/barrel ahead of an OPEC announcement at the conclusion of its summit on Tuesday. Reportedly, Saudi Arabia would be in favor of maintaining the production cuts at least until there is more clarity on the impact of the Covid-19 pandemic on global oil demand.

Oil Markets: Selected Indicators
($ price/barrel, Vol. index)



Emerging Markets

back to top

The reopening of economies lifted risk appetite while US-China tension took a backseat. **Asian equities posted broad-based gains and currencies mostly strengthened** against the dollar. The Indonesia rupiah outperformed, gaining 1.3% on the day and reached its strongest level in more than 11 weeks, as the market reopened following Monday's holiday. Other Asian currencies also gained, with the Malaysian ringgit (+0.96%), the Thai baht (+0.4%) and the Singapore dollar (+0.4%) all up on the day. **EMEA equities gained for a second day**, led by South Africa (+2.4%), Russia (+1.0%); Turkey (+1.0%); and Hungary (+1.1%). Currencies were fairly stable, with an appreciation trend as the US dollar weakened globally. The Czech koruna (+0.9%), the Polish zloty (+0.7%), and the Russian ruble (+0.6%) strengthened the most. **Latin American equity markets were higher on Monday.** Equities in Argentina (5.8%), Mexico (2.4%), Colombia (1.9%), Brazil (1.4%), Chile (1.1%) and Peru (1.0%) advanced.

Key Emerging Market Financial Indicators

Last updated:	Level		Change				
6/2/20 8:24 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		38.60	1.5	6	9	-5	-14
MSCI Frontier Equities		23.58	-0.5	2	7	-18	-22
EMBIG Sovereign Spread (in bps)		504	-7	-17	-102	124	211
EM FX vs. USD		54.90	0.2	2	4	-11	-11
Major EM FX vs. USD				%, (+) = EM currency appreciation			
China Renminbi		7.14	0.0	0	-1	-3	-2
Indonesian Rupiah		14610	0.7	1	5	-1	-5
Indian Rupee		75.55	0.1	1	-1	-8	-6
Argentine Peso		68.53	-0.1	-1	-3	-35	-13
Brazil Real		5.34	0.0	2	3	-27	-25
Mexican Peso		22.00	0.8	2	12	-10	-14
Russian Ruble		69.66	0.7	3	8	-6	-11
South African Rand		17.45	0.6	1	8	-17	-20
Turkish Lira		6.81	0.2	0	3	-14	-13
EM FX volatility		10.94	0.9	-0.1	-0.9	2.4	4.3

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

China

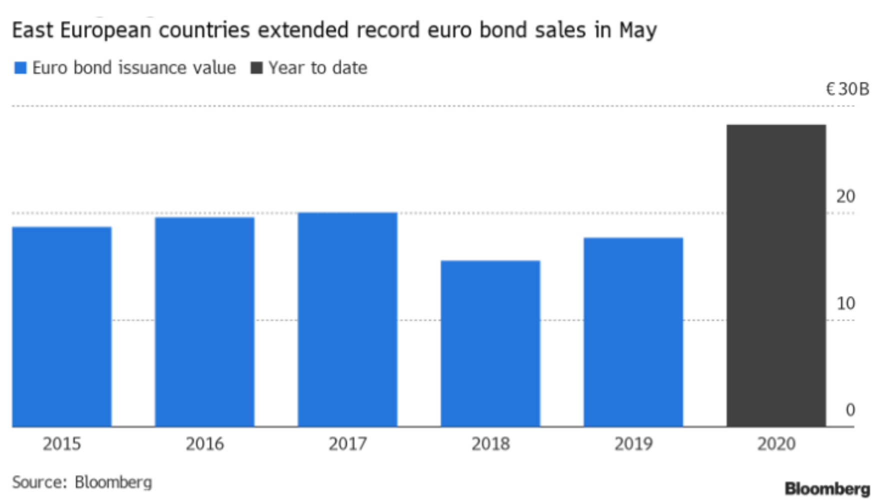
PBC introduced new tools to support MSE lending – an SME loan extension program and an SPV to support SME lending. The PBC and CBIRC (the securities and insurance regulator) jointly stated that SME loans scheduled to mature this year are allowed to be extended through March 31, 2021, as long as borrowers promise to keep employment stable. Roughly RMB 7 tn of SME loans are eligible for the program. Meanwhile, the PBC will use RMB 400bn of its relending quota to purchase SME loans via an SPV on a quarterly basis from qualified banks. Banks need to buy back these loans after a year, at zero interest; credit risks still reside with the loan originator if the loans go sour. The PBC estimates that this program can increase SME lending by about RMB 1 tn. The RMB gained against the dollar, with both the onshore CNY and the offshore CNY roughly 0.3% stronger.

India

Moody's downgraded India's sovereign rating to one level above junk with a negative outlook. The ratings agency lowered India's rating from Baa2 to Baa3, the last rung of the investment grade, in line with S&P and Fitch, though the latter two have maintained a "stable" outlook on India. Moody's cited macro fragilities developed before the pandemic, including prolonged slowdown, high fiscal deficit and elevated public debt as deciding factors behind its ratings decision. Moreover, the negative outlook "reflects dominant, mutually-reinforcing, downside risks from deeper stresses in the economy," and strains to the financial system "could exacerbate the erosion in India's fiscal position". Specifically, Moody's expect growth in FY2021 to contract by 4%, yoy, while public debt is expected to reach 84% of GDP. The Indian rupee appreciated 0.3% against the dollar overnight. Government bond yields fell across the yield curve, led by the short end, which fell by as much 3 bps.

EMEA Primary Issuance

Recent data show how **Central and Eastern European countries have successfully raised close to €30 bn in international markets year-to-date**, as they borrow to tackle the pandemic. According to Bloomberg, more deals are in the pipeline, including Hungary's debut green bond.

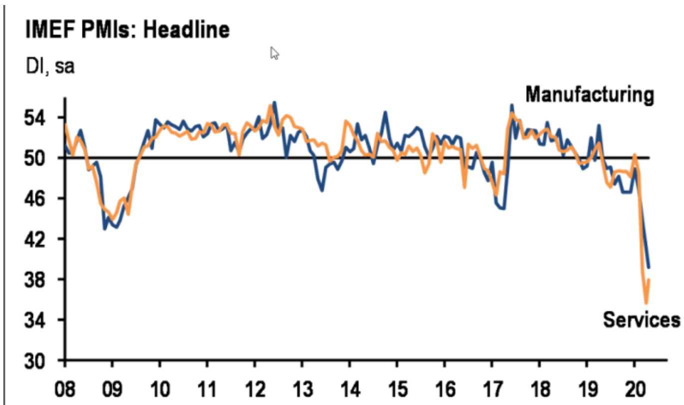


Czech Republic

Czech GDP contracted at a 2.0% clip in 2020Q1, from a 2.0% expansion in 2019Q4. The new data start to uncover the widespread damage from the pandemic. Separately, the Czech Banking Association reported that about 345,000 loan deferment requests had been filed with Czech banks, amounting to about $421 mn worth of debt. Nonetheless, **equities in Prague gained 0.5% today – largely in line with regional peers** – while the Czech koruna strengthened 1.0% to the US dollar.

Mexico

The Mexican peso strengthened (+0.7%) on Monday, supported by overall dollar weakness, amid the release of PMI data for May. The manufacturing PMI dropped to a new low of 39.2 in May from 41 in April. All subcomponents declined during the month, with production, in particular down 1.5 pts to 27.1. The services PMI did better than expected, however, rising from 35.6 to 38 in May (vs. 36.9 expected). The increase was driven by a jump in both the output and new orders gauges. Mexican stocks had strong gains, with the MEXBOL index advancing 2.4%, supported by the outperformance of industrials (+5.4%) and materials (+3.4%).

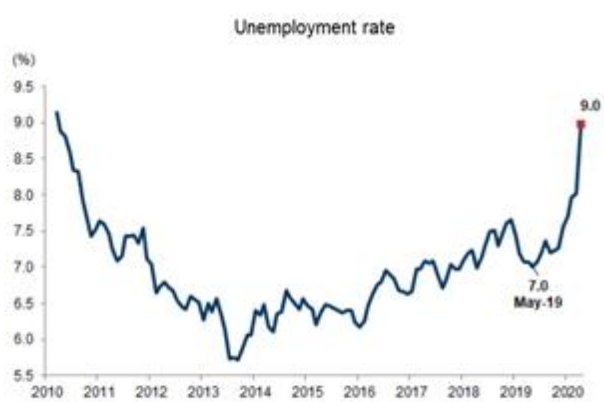


Source: IMEF and J.P. Morgan.

Chile

The Chilean peso appreciated 1.6% to the dollar yesterday, despite a bigger than expected drop in April's GDP data and a jump in unemployment. The monthly indicator of economic activity (IMACEC), a measure of GDP, decreased to 14.1% yoy in April (vs. -11% yoy expected). This is the second month of negative growth, following a 3.5% yoy decline in March. The three-month moving average unemployment rate was 9.0% in April, which is the highest in the last 10 years.

Source: Goldman Sachs Economics Research



Source: Goldman Sachs Economics Research

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Global Financial Indicators

Last updated: 6/2/20 8:20 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		3056	0.4	3	8	11	-5
Europe		3156	0.7	5	8	-4	-16
Japan		22326	0.8	5	14	8	-6
China		2915	2.2	3	2	1	-4
Asia Ex Japan		66	1.9	5	7	0	-10
Emerging Markets		38	0.3	1	7	-7	-16
Interest Rates					basis points		
US 10y Yield		0.68	0.7	-1	7	-144	-124
Germany 10y Yield		-0.41	3.5	2	18	-21	-22
Japan 10y Yield		0.01	0.9	0	3	11	2
UK 10y Yield		0.22	2.7	1	-2	-66	-60
Credit Spreads					basis points		
US Investment Grade		170	0.6	-8	-28	39	73
US High Yield		640	0.4	-24	-122	157	247
Europe IG		69	-1.5	-5	-18	-2	25
Europe HY		393	-20.3	-54	-130	86	185
EMBIG Sovereign Spread		513	-3.0	-20	-93	133	220
Exchange Rates					%		
USD/Majors		98.16	-0.2	-2	-1	0	2
EUR/USD		1.12	0.4	2	2	-1	0
USD/JPY		108.3	0.1	-1	-1	0	0
EM/USD		54.9	0.2	2	4	-11	-11
Commodities					%		
Brent Crude Oil ($/barrel)		39	0.8	8	48	-39	-41
Industrials Metals (index)		99	0.3	2	6	-11	-13
Agriculture (index)		35	0.4	0	0	-16	-16
Implied Volatility					%		
VIX Index (%, change in pp)		27.6	1.9	-0.4	-9.5	8.9	13.9
10y Treasury Volatility Index		4.7	-0.3	0.0	0.0	-0.9	0.6
Global FX Volatility		7.9	0.0	-0.1	-1.3	1.1	1.9
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		191	-0.8	-18	-84	-120	26
Italy		185	-4.1	-13	-50	-102	25
Portugal		90	-1.9	-22	-51	-12	27
Spain		95	-3.0	-11	-36	3	30

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

back to top

Emerging Market Financial Indicators

Last updated:	Exchange Rates							Local Currency Bond Yields (GBI EM)						
6/2/2020	Level		Change (in %)					Level		Change (in basis points)				
8:23 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		7.14	0.0	0.0	-1	-3	-2		2.7	0.7	13	34	-62	-44
Indonesia		14610	0.7	0.7	5	-1	-5		7.4	-2.2	-9	-50	-69	31
India		76	0.1	0.5	-1	-8	-6		6.1	1.0	0	-19	-114	-79
Philippines		50	0.6	1.0	1	3	1		4.3	-8.6	-12	-59	-78	0
Thailand		32	0.4	0.9	2	-1	-6		1.4	-2.4	8	-2	-113	-23
Malaysia		4.32	0.7	1.0	0	-3	-5		2.8	-0.6	-2	-8	-105	-60
Argentina		69	-0.1	-0.5	-3	-35	-13		45.2	-9.5	-144	644	1163	-1736
Brazil		5.34	0.0	2.0	3	-27	-25		5.4	-2.7	-39	-55	-229	-81
Chile		806	0.2	-0.1	4	-12	-7		2.4	-4.5	11	-37	-143	-91
Colombia		3731	-0.8	1.2	5	-10	-12		5.4	12.4	4	-105	-85	-60
Mexico		22.00	0.8	2.5	12	-10	-14		6.3	-1.5	-7	-42	-175	-67
Peru		3.4	0.3	0.0	-2	-2	-3		4.3	2.8	7	-37	-87	-23
Uruguay		43	0.0	0.1	-2	-19	-14		10.4	-8.2	-23	-170	-86	-51
Hungary		311	0.5	3.6	4	-7	-5		1.6	-12.8	-6	-6	-35	37
Poland		3.98	0.7	3.7	4	-4	-5		0.7	0.1	-31	-32	-150	-115
Romania		4.4	0.2	1.9	1	-3	-2		3.8	-12.0	-29	-42	-46	-24
Russia		69.7	0.7	2.9	8	-6	-11		5.3	0.2	6	-52	-242	-80
South Africa		17.5	0.6	1.1	8	-17	-20		9.8	1.0	-11	-106	39	30
Turkey		6.81	0.2	0.0	3	-14	-13		11.3	15.8	1	47	-964	-38
US (DXY; 5y UST)		98	-0.2	-1.7	-1	0	2		0.31	0.5	-3	-4	-160	-138

	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		2921	0.2	3	2	1	-4		238	-3	-4	-17	57	62
Indonesia		4848	2.0	7	3	-22	-23		273	-4	-12	-71	60	117
India		33826	1.6	11	0	-15	-18		264	6	-8	-65	107	139
Philippines		6025	1.6	10	6	-24	-23		161	-3	-7	-26	63	95
Malaysia		1508	1.2	5	7	-9	-5		196	-8	-38	-89	64	84
Argentina		40017	5.8	-2	22	18	-4		2624	-12	-142	-940	1634	855
Brazil		88620	1.4	3	10	-9	-23		379	-5	-2	-37	111	164
Chile		3686	1.0	-1	-7	-26	-21		222	-3	-1	-60	76	89
Colombia		1117	1.9	4	-2	-25	-33		286	-3	1	-103	72	123
Mexico		36981	2.4	3	1	-13	-15		519	-7	-18	-143	188	227
Peru		15743	1.0	2	7	-21	-23		189	-1	-4	-64	40	82
Hungary		36078	0.6	2	3	-12	-22		184	-2	-26	-28	61	98
Poland		48656	0.0	2	6	-16	-16		65	-12	-23	-74	-7	47
Romania		8801	1.1	1	10	4	-12		316	-8	-24	-47	98	142
Russia		2777	1.0	1	5	4	-9		200	-5	-7	-74	-28	69
South Africa		52419	2.9	4	4	-6	-8		564	-7	11	-121	235	244
Turkey		107631	0.3	4	6	19	-6		620	-11	-1	-66	72	219
Ukraine		500	0.0	0	0	-11	-2		707	-18	-14	-166	49	287
EM total		39	1.5	6	9	-5	-14		504	-7	-17	-102	124	211

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

back to top