GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

TUESDAY, JUNE 20, 2023

- **Chinese banks cut loan prime rates by 10bps, less than expected** (link)
- **GS analysts expect disinflation in the US slower than the one priced-in by markets** (link)
- **ECB officials differ on September rate hike prospects** (link)
- **Bank of England launches NBFI stress test exercise** (link)
- **Zambian Eurobond prices edge higher on reports of official restructuring offer** (link)
- **Chile's central bank holds key interest rate unchanged at 11.25%** (link)

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Market rally encounters headwinds

With uncertainty around future central bank policy actions, possible economic headwinds and concerns of extended bullish positioning, equity markets have begun to lose steam. European equities are set to decline for a second straight day, and US equity futures point to a lower opening after falling modestly on Friday. ECB officials have been offering differing views on the outlook for future policy action. While markets expect a very high chance of an additional hike in July, the path beyond is uncertain. Some members have continued to emphasize the persistence of inflation, especially core, while others have highlighted a wait-and-see approach. The outlook for the Fed also remains up in the air, with markets implying roughly a 75% chance of a hike in July and continue to price in much less additional hikes than what the dots imply.

Key Global Financial Indicators

Last updated: 6/20/23 8:00 AM	Level		Change from Market Close					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
Equities					%		%	
S&P 500		4410	-0.4	3	5	20	15	4
Eurostoxx 50		4355	-0.2	0	-1	25	15	10
Nikkei 225		33389	0.1	1	8	27	28	26
MSCI EM		41	-0.3	3	5	3	8	-14
Yields and Spreads					bps			
US 10y Yield		3.75	-1.2	-6	8	52	-13	176
Germany 10y Yield		2.44	-7.7	2	1	69	-13	221
EMBIG Sovereign Spread		445	-5	-11	-43	-58	-7	32
FX / Commodities / Volatility					%			
EM FX vs. USD, (+) = appreciation		49.9	-0.1	0	0	-3	0	-6
Dollar index, (+) = $ appreciation		102.4	-0.1	-1	-1	-2	-1	7
Brent Crude Oil ($/barrel)		76.7	0.7	3	1	-33	-11	-21
VIX Index (%, change in pp)		14.4	0.2	-1	-2	-17	-7	-17

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

Markets await the release of the UK inflation rate on Wednesday and the BoE's policy rate decision on Thursday, with surveys indicating a 25-bp hike. Other expected policy rate decisions include Hungary on Tuesday (surveys showing unchanged policy rate), Czech Republic and Brazil on Wednesday (both unchanged); Indonesia, Mexico, Egypt, and the Philippines (all unchanged) as well as Switzerland (+25 bp) on Thursday. A large hike is expected for Turkey on Thursday from the current 8%; the range of estimates for the new rate is from 14% to 40%, with the median surveyed expectation at 20%.

Mature Markets

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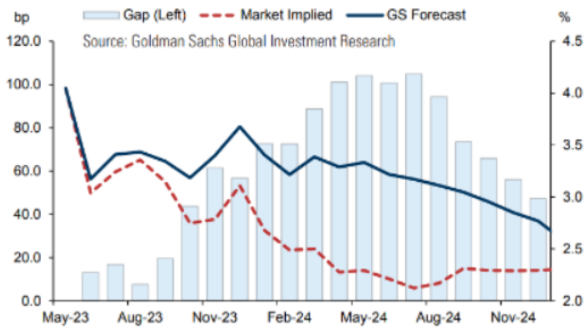
United States

On Friday, the S&P 500 fell by 0.4%, with losses driven mostly by the Information Technology and Communication Services sectors (-0.8% and -.1.0%, correspondingly). US Treasury yields rose by 4-5 bp across the yield curve, driven predominantly by real yields. The US Dollar appreciated 0.2% versus major currencies.

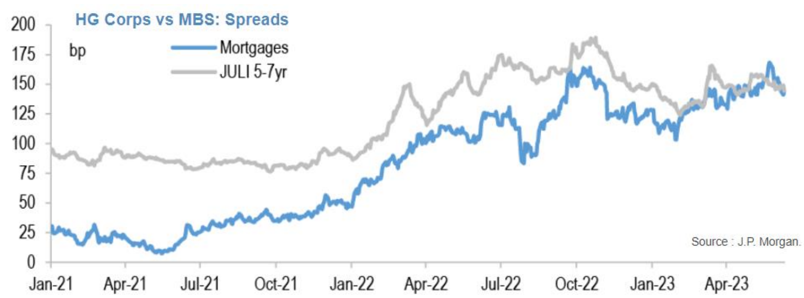
Goldman Sachs analysts warn that disinflation in the US will happen at a much slower rate than markets are pricing in (see chart below). Some market participants expect that a drop in growth rates and a downward pressure on commodity prices will contribute to a fast disinflation. However, GS analysts see limited ability for those factors to bring inflation down as there is potential for "delayed-onset inflation" (in sectors like health care) and various second-round effects keeping inflation at elevated levels. The gap between GS projections and market-implied figures increases up to 1 percentage point by the mid-2024.

Exhibit 1: Markets appear considerably more optimistic than we are about the pace of inflation normalization

Inflation, forecast and market-implied

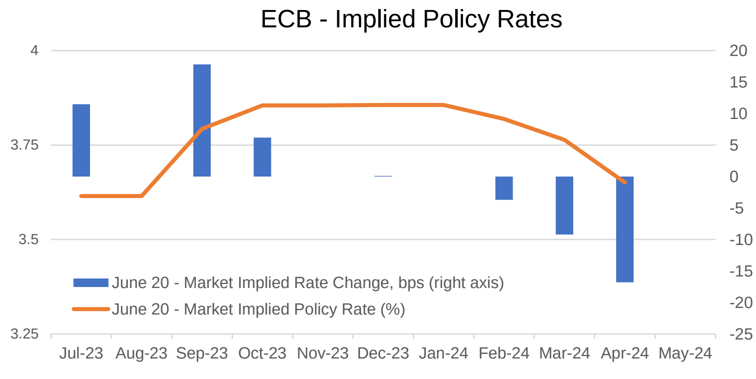


The spreads of Mortgage-Backed Securities (MBS) continue rising relative to other asset classes. The chart below shows MBS spread versus the spread of Investment-Grade bonds of equivalent duration (5-7 years): the spread difference has shrunk from ~70-80 bp one year ago to virtually zero now. Initially, the rise of MBS spreads was driven by the Fed's sales of MBS during Quantitative Tightening. Recently, contributing factors included also a higher expected prepayment risk for underlying mortgages once the Fed starts cutting rates, as well as the risk of cash-out refinancing for borrowers with low loan-to-value ratios if home prices start appreciating again.



Euro Area

European markets are mixed, on a quiet trading morning. The equity market (Stoxx Europe 600) is down 0.4%, with banking stocks are losing 0.3%. The euro was strengthening marginally 0.1% vs. the dollar to 1.09. German 10y bund yields were down 4 bp to 2.47%, and Italian spreads were down 2 bp to 158 bp.

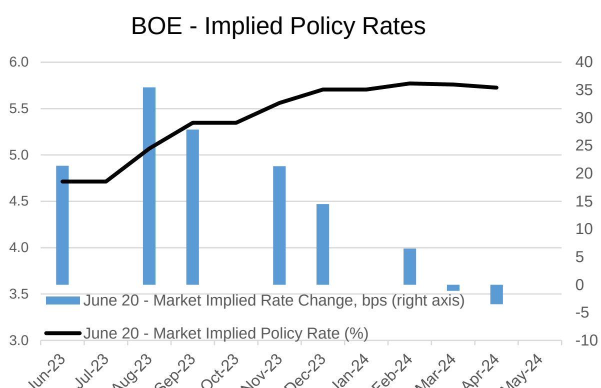


Source: Bloomberg WIRP and IMF

ECB officials are voicing different views about the ECB's September rate decision after ECB president Lagarde indicated in the ECB decision press conference last week that the General Council (GC) would 'very likely' increase the deposit rate in July. After some hawkish commentary by others late last week, ECB Board member Isabel Schnabel said that officials should "err on the side of doing too much rather than too little" as risks to inflation are tilted on the upside. On Friday, Belgian governor Wunsch said that the ECB will have to keep raising interest rates even after September if core inflation does not slow down sustainably by then. Since then, on the dovish side, ECB Chief Economist Philip Lane, French governor Villeroy de Galhau, Lithuanian governor Simkus and Salk governor Kazimir emphasized that "September will be decided in September" (Lane), and pointed out that there will be an important amount of data between now and then, and a full scale forecasting round from ECB staff before the decision is due. This morning, Finnish governor Rehn pointed out that while headline inflation is slowing, core inflation is falling only gradually and that a pullback in that measure was a prerequisite for pausing rate hikes. He said that in uncertain times, it is essential to focus on incoming data and that monetary policy has become "as much art as science". Markets are pricing in a 90% probability of a 25 bp hike in July, and 72% for September, with a terminal rate currently seen at 3.85%.

United Kingdom

UK markets are focused on the May inflation print (due tomorrow) and the MPC meeting on Thursday. Consensus sees headline inflation easing to 8.4% y/y (from 8.7%) and core inflation easing to 6.7%y/y (from 6.8%). After recent inflation and pay data surprised on the upside – markets have priced in more BoE tightening with roughly five additional 25bp hikes priced in to take the terminal rate to around 5.75%. Some think that the BoE could even hike by 50bp on Thursday. Yesterday, 2y gilt yields went shortly over 5% (4.98% today) for the first time since 2008. Today, yields on 10y gilts were down 10 bp to 4.39%, while the UK equity market (FTSE 100) was flat, and the British pound was weakening 0.2% vs the dollar.

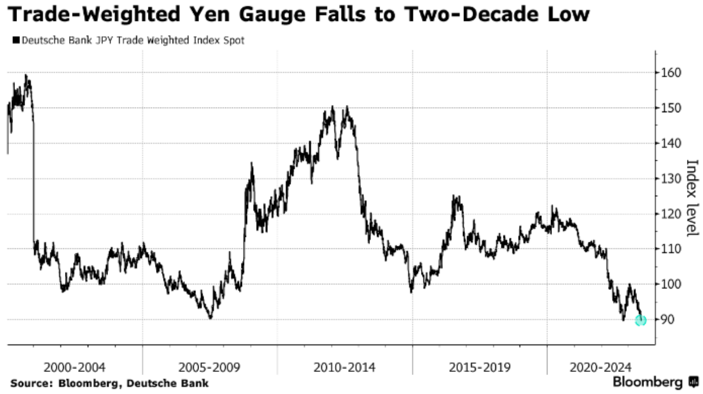


Source: Bloomberg WIRP and IMF

Yesterday, the Bank of England (BoE) announced that it has kicked off its first ever stress tests of the NBFI (non-bank financial institutions) sector. This exercise was announced earlier, after the turmoil caused by the "mini budget" last September. The tests will examine how firms would react to a severe stress to global financial markets and how this could threaten the UK's financial stability. It will cover hedge funds, pension funds, insurers, clearing houses, and other financial firms. A full report is expected next year.

Japan

Japanese stocks declined 0.3%, as insurance stocks dragged the market lower on the news that the Financial Services Agency (FSA) will probe the firms on suspicion of colluding to fix premiums. Separately, Reuters reported on Monday the FSA asked the nation's banks about their exposure to geopolitical risk from China and requested their plans in the event that tensions between China and the West escalate. **The yen appreciated 0.2%.** Japan authorities welcomed the country's removal from United States' FX watchlist. Separately, Deutsche Bank AG's trade-weighted yen gauge, a measure of yen's strength against global trading peers, fell to a record low. **Yields on 10Y bonds declined -0.9bp.**



Australia

The Reserve Bank of Australia (RBA) board was considering a pause at the June meeting. RBA minutes revealed that the arguments were "finely balanced" between a pause and a hike, with the board eventually concluding that the case to hike was a stronger one. Separately, RBA Deputy Governor Bullock said on Tuesday that Australia's jobless rate needs to rise to around 4.5% from the current 3.6%, along with an economy growing at a "below-trend pace", for inflation to return to the RBA's 2-3% target range. Australian equities rose 0.9%. and the Australian dollar weakened by 0.7%.

Emerging Markets

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Asian equities declined -0.7%. Hong Kong stocks slumped 1.8%, amid less than expected China rate cuts. Thailand fell 1.2%, with Maybank analysts noting that political concerns continue to weigh on investors' appetite. Asian currencies were mixed. The Taiwanese dollar declined by 0.3%, followed by Indian rupee -0.2%. The Thai baht and Philippine peso saw gains (+0.3%). 10-year bond yields were little changed. Hong Kong dollar one month rate (1-month Hibor) rose to its highest since 2007 to 5.1%. **EMEA equities generally traded weaker, except in Turkey**. Currencies were little changed. Local rates in Eastern Europe followed euro area rates lower. The National Bank of Hungary (NBH) is expected to keep its base rate unchanged at 13.0% but focus remains on the overnight rate, currently at 17%. Most contacts expect the NBH to cut the overnight rate 100 bp to 16% but some have a strong conviction that too much easing is priced into the swaps curve given still high inflation. **Latin American assets were mixed on Monday.** Stocks gained in Brazil (0.93%), Chile (0.25%) and Mexico (0.16%), while Peru and Colombia equity markets lost 0.07% and 0.39%, respectively. Currencies depreciated in Colombia (-0.34%), Peru (-0.20%) and Chile (-0.08%), while the Brazilian real (0.97%) and the Mexican peso (0.04%) strengthened against the US dollar.

Emerging Market Bond and Equity Flows

Emerging Markets bond outflows eased (-$30mn, from -$338mn the prior week), as outflows from hard currency bond dropped (-$87mn, from -$445mn) while local currency funds had inflows for a second week (+$57mn, from +$107mn). ETF inflows increased (+$389mn, from +$237mn) and non-ETFs outflows decreased (-$419mn, from -$574mn). Meanwhile, EM equity funds saw inflows (+$296mn, from -$18mn). Year-to-date flows currently stand at -$1.0bn and +$38bn for bonds and equities, respectively.

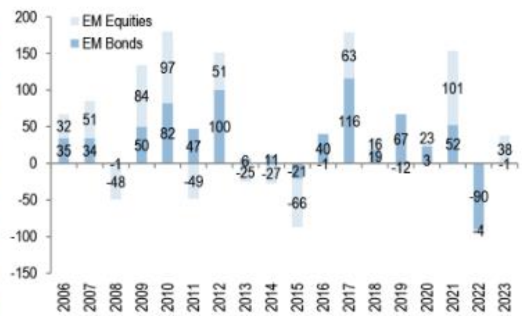
Figure 1: Weekly cross-asset flows

USD billion

	Asset	8w flows (8w ago → current)	This wk	YTD
Fund Flows	**EM Bonds and Equities**		0.3	37.0
	EM Bonds		0.0	-1.0
	Hard Ccy		-0.1	-2.1
	Local Ccy^		0.1	1.0
	o.w. EM ex-China		0.1	2.9
	o.w. China		-0.1	-2.7
	EM Equities		0.3	38.0
	US HG		6.3	137.2
	US HY		0.2	-4.4
	Global Equities		25.6	-10.2
	EM Bond and Equity ETFs		1.4	31.2
	EM Bond ETFs		0.4	0.4
	EM Equity ETFs		1.1	30.8
	Non-resident EM flows*		4.0	33.0

Figure 2: EM bond and equity fund flows

USD billion

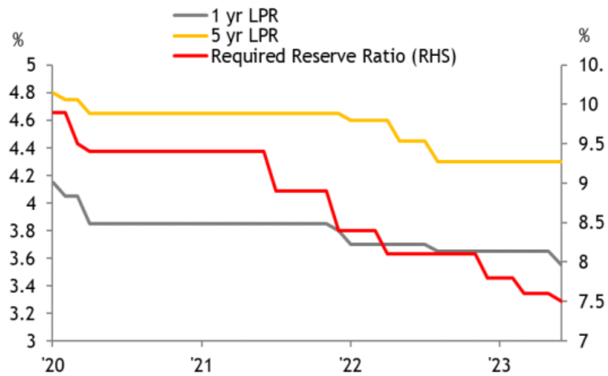


*High frequency non-resident EM portfolio flow data where available. ^Local ccy split is retail only. All charts and data in this report: J.P. Morgan, EPFR Global, Bloomberg Finance L.P.

China

Chinese banks reduced one-year and five-year loan prime rates by 10bp for the first time since August 2022. This was largely an expected move, following People's Bank of China (PBoC) cuts to the medium-term lending facility and 7-day reverse repo last week, as the authorities sought to shore up the slowing economy. However, market expectations were for a bigger reduction in the five-year loan prime rate to support the property sector. Citibank analysts are expecting more policy easing efforts ahead and highlighted the July Politburo meeting as a window for more comprehensive measures. PBOC also added the most liquidity since end-March via reverse repos, injecting a net of 180bn yuan ($25.1bn), Bloomberg estimated. Separately, **President Xi stated that progress had been made on United States-China ties** following his meeting with United States Secretary of State Antony Blinken's visit to China. He further added that China will not challenge or replace the United States and sought for the same in return. Chinese stocks fell (-0.2%). Renminbi weakened (offshore -0.2%, onshore -0.1%). 10Y bond yields fell 2bp.

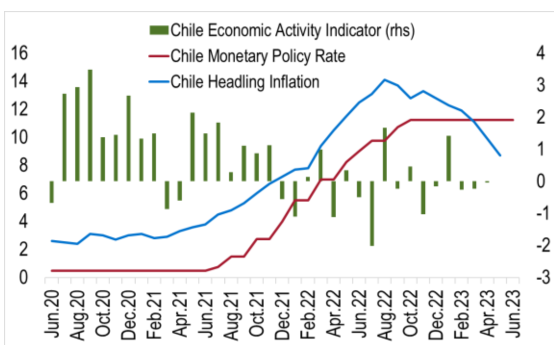
Fig 1: 1 and 5-year LPRs Cut By 10bps For First Time Since Aug 2022



Source: PBOC, CEIC, Maybank

Chile

Chile's central bank held its key interest rate unchanged at 11.25% as the market expected. However, the vote was surprisingly split. Three board members voted for keeping the rate unchanged while the other two voted for a 50bp reduction. Policymakers signaled that a monetary easing cycle was imminent due to stagnant growth. The central bank dropped its previous guidance of waiting for an inflation slowdown and stated that the economy was moving in the right direction. The decision comes as economic activity remained unchanged in April,

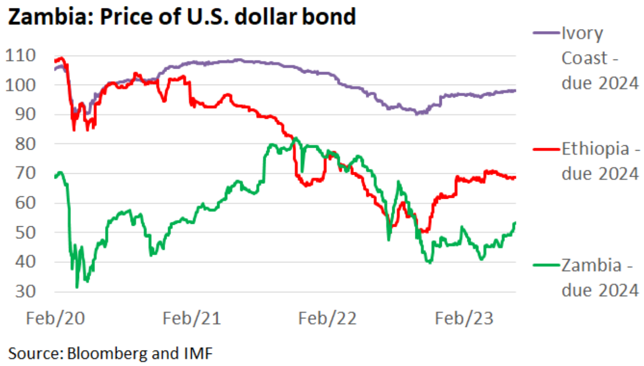


Source: Bloomberg and IMF staff

and inflation slowed to 8.7% in May. The prospect of declining inflation has fueled speculation of easing in countries like Chile, Peru, and Brazil, while Mexico is expected to cut rates later in the year. Two-year Chilean swap rates have fallen by 93 bp in the past month alone.

Zambia

Eurobond prices rose 1-2 points on reports that official creditors have made "significant progress" and could even be close to making a restructuring offer. A Bloomberg article cites an official at the Paris Club. Creditors will reportedly make an announcement during the summit for a New Global Financing Pact in Paris June 22-23.



Turkey

The Turkish lira was little changed today as central bank of Turkey is expected to hike its policy rate 11.5 percentage points on Thursday, from 8.5% to 20%. JP Morgan even expects a policy rate hike to 25%, along with forward guidance suggesting smaller rate hikes if needed, and has a year-end policy rate forecast of 30%, with risks to the upside.

This monitor is prepared under the guidance of Jason Wu (Assistant Director), Charles Cohen (Deputy Division Chief), Nassira Abbas (Deputy Division Chief), and Antonio Garcia-Pascual (Deputy Division Chief). Fabio Cortes (Senior Economist), Reinout De Bock (Senior Economist-London Representative), Sanjay Hazarika (Senior Financial Sector Expert), Esti Kemp (Financial Sector Expert-London Representative), Johannes S Kramer (New York Representative), Aurelie Martin (Senior Economist-London Representative), Tom Piontek (Senior Financial Sector Expert) and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Yingyuan Chen (Financial Sector Expert), Deepali Gautam (Research Officer), Shoko Ikarashi (Externally Financed Appointee), Phakawa Jeasakul (IMF Resident Representative in Hong Kong SAR), Harrison Kraus (Research Assistant), Yiran Li (Research Assistant), Kleopatra Nikolaou (Senior Financial Sector Expert), Natalia Novikova (IMF Resident Representative in Singapore), Mustafa Oguz Caylan (Research Officer), Silvia Ramirez (Senior Financial Sector Expert), Patrick Schneider (Financial Sector Expert), Ying Xu (Economist), Dmitry Yakovlev (Senior Research Officer), and Akihiko Yokoyama (Senior Financial Sector Expert). Javier Chang (Senior Administrative Assistant), Dalila Mujevic (Staff Assistant), and Srujana Sammeta (Staff Assistant) are responsible for the word processing and production of this monitor.

Global Financial Indicators

6/20/23 8:00 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		4410	-0.4	2	5	20	15
Europe		4355	-0.2	0	-1	25	15
Japan		33389	0.1	1	8	27	28
China		3924	-0.2	2	-1	-9	1
Asia Ex Japan		69	-0.2	3	4	2	7
Emerging Markets		41	-0.3	3	5	3	8
Interest Rates					basis points		
US 10y Yield		3.75	-1.2	-6	8	52	-13
Germany 10y Yield		2.44	-7.7	2	1	69	-13
Japan 10y Yield		0.39	-0.7	-3	-1	15	-3
UK 10y Yield		4.34	-15.1	-9	35	174	67
Credit Spreads					basis points		
US Investment Grade		155	-2.4	-8	-19	-13	-3
US High Yield		446	-5.6	-16	-68	-81	-34
Exchange Rates					%		
USD/Majors		102.45	-0.1	-1	-1	-2	-1
EUR/USD		1.09	0.1	1	1	4	2
USD/JPY		141.4	-0.4	1	2	5	8
EM/USD		49.9	-0.1	0	0	-3	0
Commodities					%		
Brent Crude Oil ($/barrel)		76.7	0.7	3	2	-20	-8
Industrials Metals (index)		146	-2.0	2	0	-14	-12
Agriculture (index)		71	-1.1	6	10	-6	3
Implied Volatility					%		
VIX Index (%, change in pp)		14.4	0.2	-0.6	-2.4	-16.7	-7.3
US 10y Swaption Volatility		96.0	0.0	-11.5	-24.1	-36.8	-29.7
Global FX Volatility		8.1	0.0	0.1	-0.6	-3.3	-2.6
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		131	0.3	2	-29	-97	-75
Italy		160	-0.3	-3	-24	-35	-54
Portugal		64	-0.1	-3	-15	-41	-37
Spain		92	-0.4	-2	-13	-17	-17

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

Emerging Market Financial Indicators

Last updated: 6/20/2023 8:01 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		7.18	-0.2	-0.2	-2	-7	-4		2.8	-4.0	5	-3	-14	-31
Indonesia		15005	-0.1	-0.9	-1	-1	4		6.3	0.9	5	-10	-116	-60
India		82	-0.2	0.3	1	-5	1		7.5	0.1	5	28	(33.2)	0
Philippines		56	0.3	0.7	0	-3	0		5.9	0.0	0	6	26	-9
Thailand		35	0.0	-0.2	-1	2	0		2.8	0.5	12	15	-7	20
Malaysia		4.64	-0.2	-0.5	-2	-5	-5		3.8	2.7	7	3	-54	-26
Argentina		249	-0.4	-1.8	-7	-51	-29		111.9	-0.1	94	774	5029	2369
Brazil		4.79	-0.2	1.6	4	8	10		11.3	5.6	-14	-67	-135	-127
Chile		795	-0.1	1.5	0	11	7		5.0	0.0	5	-30	-134	-31
Colombia		4166	-0.3	0.4	9	-2	16		7.9	-5.5	-13	-56	-106	-184
Mexico		17.11	-0.1	0.7	5	18	14		8.3	0.0	-4	-14	-74	-42
Peru		3.6	-0.2	0.4	1	2	5		7.0	-0.1	-18	-36	-71	-98
Uruguay		38	0.0	1.4	2	5	5		9.9	0.0	0	-12	-93	-79
Hungary		341	0.3	0.5	1	11	9		7.6	-7.0	22	-38	-80	-199
Poland		4.07	0.1	2.1	2	9	8		5.3	-5.0	10	-16	-229	-85
Romania		4.5	0.1	1.3	1	4	2		6.6	-2.3	-9	-31	-253	-113
Russia		84.3	-0.3	-0.2	-5	-34	-12							
South Africa		18.2	-0.2	2.2	5	-12	-7		9.9	-1.0	7	-23	109	73
Turkey		23.57	0.2	0.3	-16	-26	-21		17.5	-7.0	-53	767	-213	769
US (DXY; 5y UST)		102	-0.1	-1.1	-1	-2	-1		3.97	-1.8	-3	23	62	-4

	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	7 Days	30 Days	12 M	YTD
								basis points					
China		3924	-0.2	2	-1	-9	1		185	-3	-12	-8	8
Indonesia		6660	-0.4	-1	-1	-5	-3		140	-7	-1	-64	0
India		63328	0.3	0	3	21	4		131	-5	-27	-43	-11
Philippines		6449	0.0	-1	-3	3	-2		111	-7	-4	-41	14
Thailand		1538	-1.2	-2	1	-2	-8		0	0	0	0	0
Malaysia		1388	0.1	1	-3	-5	-7		92	-3	-8	-33	-8
Argentina		409417	4.5	7	21	370	103		2376	-20	-208	174	171
Brazil		119858	0.9	2	8	20	9		250	-5	-21	-96	-24
Chile		5754	0.3	1	2	13	9		129	-3	-3	-45	-3
Colombia		1174	-0.4	-1	4	-19	-9		361	-7	-56	-24	-11
Mexico		54931	0.2	1	1	15	13		377	-19	-31	-52	-4
Peru		22568	-0.1	2	4	16	6		167	-7	-15	-35	-13
Hungary		49480	-0.2	-1	6	25	13		221	-9	-2	-20	-1
Poland		67271	-0.1	3	4	27	17		136	-2	0	31	63
Romania		12292	-0.5	2	0	0	5		235	-12	-16	-79	-21
South Africa		76992	-1.3	1	-2	16	5		401	-6	-52	-67	34
Turkey		5284	0.3	-3	17	108	-4		468	-23	-148	-212	28
Ukraine		507	0.0	0	0	-2	-2		4553	-508	-749	742	474
EM total		41	-0.8	3	5	3	8		390	-8	-38	-43	14

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

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