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- Cyclical stocks lead US rally ([link](#))
- ECB to end pandemic QE in 2022 according to survey ([link](#))
- China continues crackdown on crypto mining ([link](#))
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Markets trade higher after last week's slump

Most European markets were higher after last week's losses and US index futures also pointed to a positive start to the day. Asian markets began the week sharply lower, but sentiment began to turn as the European session got underway. Nevertheless, the Fed's hawkish pivot on Wednesday still looms over markets and the outlook remains uncertain. The US 30-year long bond yield fell below 2% for a while, a level not seen since February. Fed Chair Powell is to testify before Congress tomorrow and markets will be watching closely. Meanwhile, China's crackdown on crypto mining has pushed Bitcoin down by 10%. FX markets are holding steady but the VIX and other volatility measures have crept higher in recent days. Most commodity markets are lower in early trading.

Key Global Financial Indicators

Last updated: 6/21/21 8:03 AM	Level		Change from Market Close				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
S&P 500		4166	-1.3	-2	0	34	11
Eurostoxx 50		4095	0.3	-1	2	25	15
Nikkei 225		28011	-3.3	-4	-1	25	2
MSCI EM		54	-0.7	-2	2	36	5
Yields and Spreads			bps				
US 10y Yield		1.44	0.0	-6	-18	74	52
Germany 10y Yield		-0.20	0.0	5	-7	22	37
EMBIG Sovereign Spread		336	2	8	6	-137	-14
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		56.8	0.1	-2	-1	4	-2
Dollar index, (+) = \$ appreciation		92.1	-0.1	2	2	-6	2
Brent Crude Oil (\$/barrel)		73.5	0.0	1	11	74	42
VIX Index (% change in pp)		20.5	-0.3	4	0	-15	-2

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

Purchasing Managers Indexes, a key gauge for economic strength, are the main data focus this week for the US and the euro area, with strong results expected for both. The Bank of England meeting on Thursday will be closely scrutinized for clues about future policy, while the Mexican central bank meeting on the same

day will also be of interest given the recent weakness in the currency. The central bank of Hungary is expected to be the first European central bank to hike rate to tackle rising inflation when it meets tomorrow.

Selected Data Releases for the Week Ahead

Data Release	Consensus Forecast
US Manufacturing PMI Tue.	61.5
US Services PMI Tue.	69.9
US durable goods Thu.	3%, 0.8% ex-transportation
Euro area PMI Manufacturing Wed.	62
Euro area PMI Services	57.7
Bank of England meeting Thu.	
Bank of Mexico Thu.	
Source: Bloomberg	

Mature Markets

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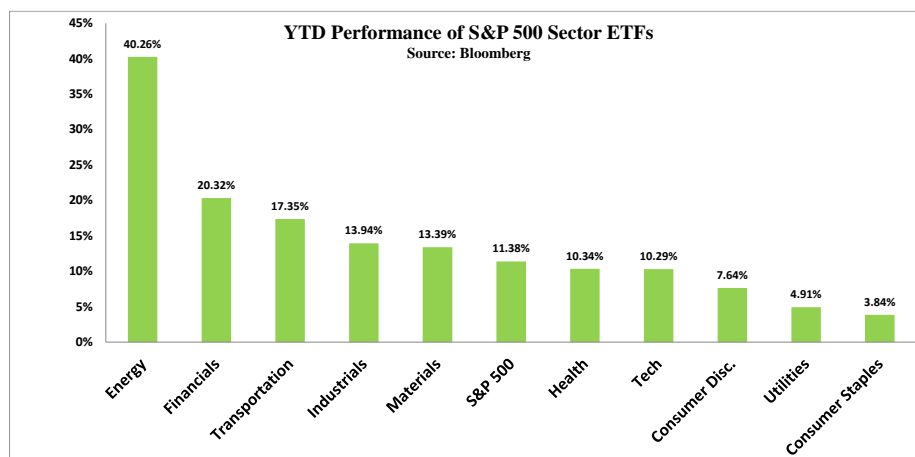
United States

Markets are still mulling over the implications of the Fed's unexpected hawkish turn last Wednesday. Fed governor Bullard's remark on Friday that "I put us starting in late 2022" provoked further debate. There are multiple Fed speakers this week, including Fed Chair Powell tomorrow, and their remarks will attract especially strong scrutiny. Among the main developments in the US bond market post-FOMC were a steepening of the yield curve at the very front end in eurodollar futures, and a pronounced flattening at the long end. The 5-year/30-year sector saw the biggest two-day curve flattening in a decade. Treasury Inflation Protected Securities (TIPS) breakeven yields declined significantly. Longer maturity Treasury yields reversed their immediate post-FOMC selloff to end below where they were before the FOMC. There are competing explanations, but one school of thought among contacts is that the market agrees with the Fed's line that inflation will probably be transitory, while accepting the message that Fed liftoff could begin in 2023 with relative equanimity. They think the Fed had to tighten a little to avoid market complacency and bolster its inflation fighting credibility. Others disagree, seeing the Fed's hawkish tilt as a sign that its commitment to the flexible inflation target could be weakening. Meanwhile, US stocks have suffered four consecutive days of losses, with the S&P 500 down over 2% over the period. The Dow had its worst week since October, losing nearly 3.5%

Key US Bond Market Moves Since June 16 FOMC Friday Close

	Close on Tuesday	Close on Friday
2yr Treasury	0.16%	0.26%
5yr Treasury	0.78%	0.88%
10yr Treasury	1.49%	1.44%
30yr Treasury	2.18%	2.02%
December 2023 eurodollar futures	0.94%	1.12%
5yr TIPS breakeven yield	2.49%	2.38%
10yr TIPS breakeven yield	2.39%	2.24%
2-10 Treasury spread	133 bps	118 bps
5-30 Treasury spread	140 bps	113 bps
Source: Bloomberg		

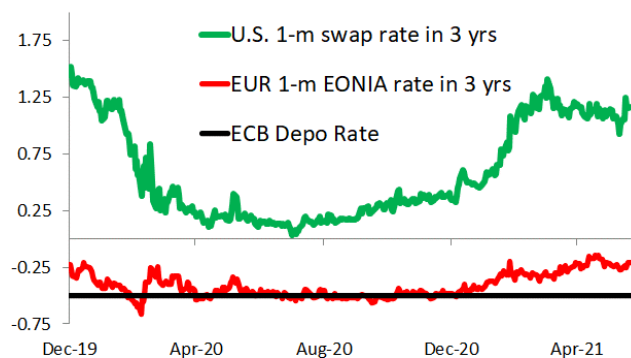
Cyclical sectors have led the US equity rally this year in contrast to previous years when tech stocks were the biggest gainers. The ongoing post-pandemic recovery and hopes for even stronger growth down the road have boosted commodities and the energy sector more broadly. The prospect of higher rates and a steepening yield curve in the months ahead has boosted the financial sector. The reopening of the economy benefits airlines and other transportation-related sectors, and the housing boom and rising production have pushed industrials and materials higher. There is widespread optimism about the recovery.



Euro Area

According to the latest ECB survey, **most analysts expect the pandemic PEPP QE program to end in March with no increase in the ECB's regular APP QE program afterwards. The median expectation is for a first depo rate hike in May 2024** (and median expectation for a hike in other rates at end 2024). **The median expectations for long-run HICP inflation is 1.8% yoy and for long-run core inflation is 1.6% yoy.** The survey period was from 25 May 2021 to 28 May 2021, and 26 analysts participated.

Euro area: Money market rate in 3 years (%)



Source: Bloomberg and IMF staff

German 10-yr bund yields (-1 bps to -0.20%) and 10-yr Italian spreads (-1 bps) opened the week lower as ECB President Lagarde sees "good progress" in talks on the ECB strategy review. The ECB Governing Council met this weekend for its annual retreat, which focused on the monetary policy strategy review and marked the first in-person meeting since the beginning of the pandemic. **Press reports suggest that there has been some convergence to the idea of a symmetrical 2% inflation target.**

U.S. and Euro area: 10-yr rates minus 2-yr rates
(steepness, bps)

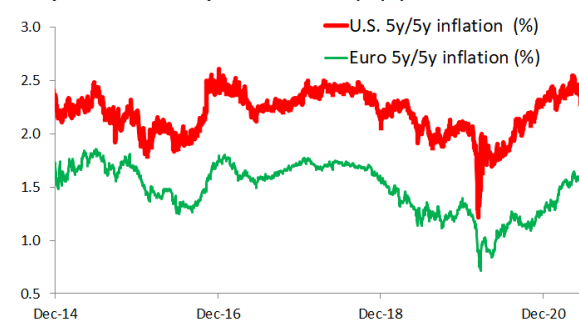


Source: Bloomberg and IMF staff

In fiscal developments, some EU countries are reportedly pushing for a return to EU budget rules in 2023. Last week, German CDU chair Laschet said that EU budget rules must be reinstated after the pandemic. In contrast, Italian PM Draghi called for more economic stimulus in European countries to help bring growth back to pre-pandemic levels, pointing to the need for additional effort.

Euro area 5-yr/5-yr inflation swaps have dipped below 1.50% again, trading 9 bps lower in the past five days as global developments and spillovers from the U.S. remain a key driver for market-based inflation expectations in the euro area.

Five-year Forward Five-year Inflation Swaps (%)



Source: Bloomberg, and IMF staff

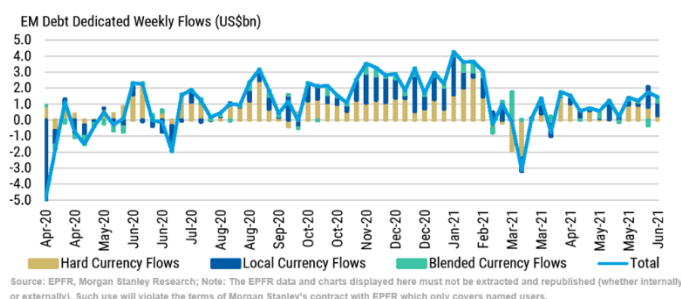
Emerging Markets

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EMEA equity markets were trading little changed except for Egypt (+2.2%). **EMEA currencies were trading mixed** with the South African rand (+0.5%) appreciating while the Russian ruble (-0.3%) depreciated as contacts noted deterioration in sentiment following signals of new U.S. sanctions. **The selloff of Asian equities continued on broad-based losses (-1.0%) and currencies also depreciated.** Vietnam's central bank aims to keep policy rates stable in 2021H2 but it will remain vigilant on rising consumer price inflation. **Most Latin American markets lost ground on Friday.**

EM fund flows

EM debt flows were slightly slower but held up well last week, based on EPFR data and Morgan Stanley Research. Hard currency and local currency flows declined from the previous week's levels, but blended currency flows rebounded and turned positive (figure). As a result, total EM debt dedicated flows declined \$300 mn to \$1,437 mn last week. Flows to global funds slowed to \$104 mn but flows to regional/country funds strengthened to \$1,334 mn, driven by an increase in flows to EM Asia (\$1,502 mn), while Latam and CEEMEA saw outflows.



Belarus

European officials revealed plans to ratchet up sanction against Belarus for the force-landing of the Ryanair flight and the arrest of the opposition journalist earlier in May. According to media reports, the measures are expected to include restriction on imports of oil and potash products, both major exports for Belarus. The sanctions are also set to affect the financial sector with restrictions imposed on lending and securities trading. The package will be discussed during the European Council meeting this week. **Belarus Eurobond credit spreads widened by 70 bps as the severity of proposed sanctions surprised investors.** Contacts also noted reduced market making capacity among European banks amid sanctions uncertainty.



China

China is intensifying its crackdown on cryptocurrency mining. Local authorities in Sichuan, which is arguably the largest hydro-based crypto mining hub in China, have ordered local government-owned power companies to stop supplying electricity to crypto mining projects, Bloomberg reported. City-level governments have been asked to start checks in their areas and shut down the projects if found. Bloomberg reported that many mines in Sichuan were closed as of Sunday, citing the Global Times newspaper, without saying where it got the information. The clampdown means that 90% of the country's Bitcoin mining capacity will be shut down, at least for the short term, the paper said. Sichuan's move joins other provinces, which have already announced crackdowns or partial bans on crypto-mining operations. **China's central bank kept its loan prime rates (LPR) unchanged, as expected.** The one-year LPR was steady at 3.85% while the five-year LPR was maintained at 4.65%, unchanged since April 2020.

Colombia

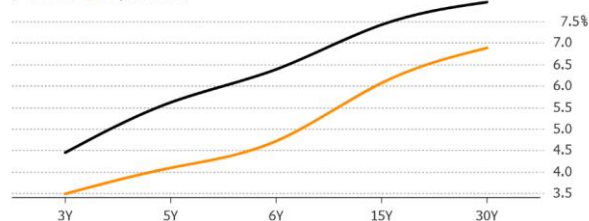
The government is to cut back its long term bond offerings and switch to intermediate maturity issuance after a sharp rise in interest rates made longer maturity debt less attractive due to the inherent interest rate risk. Colombia sold \$1.3 bn of 30-year bonds back in September in the face of strong investor demand, but these bonds are now trading at 90% of their par value, having fallen 13% from their highest levels, according to Bloomberg data. Rising inflation and the continued virus crisis are among

the factors weighing on demand. Social unrest and an impending Presidential election are additional factors. Peru and Chile are facing similar challenges with their long maturity bonds, and for similar reasons.

Steeper Curve

Yields have risen since Colombia sold 30-year bonds in September

June 18 September 30



Source: Bloomberg
Note: Yield for peso-denominated, government bonds

Bloomberg

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Global Financial Indicators

Last updated: 6/21/21 8:04 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		4168	-1.3	-2	0	35	11
Europe		4095	0.3	-1	2	25	15
Japan		28011	-3.3	-4	-1	25	2
China		3529	0.1	-2	1	19	2
Asia Ex Japan		93	-0.6	-2	2	35	4
Emerging Markets		54	-0.7	-2	2	36	5
Interest Rates			basis points				
US 10y Yield		1.44	0.0	-6	-18	74	52
Germany 10y Yield		-0.20	0.0	5	-7	22	37
Japan 10y Yield		0.05	-0.9	1	-3	3	3
UK 10y Yield		0.75	-0.3	1	-8	51	55
Credit Spreads			basis points				
US Investment Grade		91	2.4	0	-2	-57	-4
US High Yield		328	4.5	-1	-14	-265	-52
Europe IG		48	0.3	2	-4	-19	1
Europe HY		239	1.5	7	-22	-152	-2
Exchange Rates			%				
USD/Majors		92.10	-0.1	2	2	-6	2
EUR/USD		1.19	0.2	-2	-2	6	-3
USD/JPY		110.1	-0.1	0	1	3	7
EM/USD		56.8	0.1	-2	-1	4	-2
Commodities			%				
Brent Crude Oil (\$/barrel)		74	0.0	1	11	74	42
Industrials Metals (index)		148	-0.3	-7	-4	44	12
Agriculture (index)		54	-1.8	-6	-6	53	12
Implied Volatility			%				
VIX Index (%, change in pp)		20.5	-0.3	4.1	0.3	-14.7	-2.3
US 10y Swaption Volatility		68.5	1.2	3.0	-3.3	5.1	8.4
Global FX Volatility		7.0	0.1	0.5	-0.1	-1.6	-1.1
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		103	-0.2	2	-8	-68	-17
Italy		107	-0.7	3	-10	-71	-5
Portugal		62	-1.3	-2	-6	-30	2
Spain		64	-1.5	0	-4	-27	2

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

Emerging Market Financial Indicators

Last updated: 6/21/2021 8:06 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		6.47	-0.2	-1.1	-1	9	1		3.3	-0.3	2	5	32	-1
Indonesia		14428	-0.4	-1.6	-1	-2	-3		6.4	9.3	16	-9	-90	34
India		74	-0.3	-1.1	-2	3	-1		6.3	-1.0	9	5	28	40
Philippines		49	-0.5	-1.6	-2	3	-1		4.3	-0.5	7	-1	19	67
Thailand		32	-0.4	-1.6	-1	-2	-5		1.8	-0.2	0	2	36	52
Malaysia		4.15	-0.2	-0.8	0	3	-3		3.3	-1.7	1	0	41	71
Argentina		95	0.0	-0.3	-1	-27	-12		44.9	-4.1	-75	-92	-286	-1129
Brazil		5.08	0.3	-0.3	6	4	2		8.5	16.2	26	8	311	289
Chile		748	-1.5	-3.5	-5	9	-5		4.2	0.4	11	43	174	143
Colombia		3760	-0.8	-3.2	-3	0	-9		6.6	7.9	1	-8	102	156
Mexico		20.61	0.2	-3.1	-3	9	-3		6.8	4.6	12	-8	61	117
Peru		4.0	-0.9	-1.5	-5	-11	-8		5.5	14.6	40	54	113	186
Uruguay		44	-0.3	-0.8	1	-3	-4		7.9	3.9	3	26	-228	64
Hungary		298	0.7	-3.0	-4	4	0		2.3	2.7	12	-10	65	81
Poland		3.81	0.7	-2.3	-3	3	-2		1.2	-0.3	7	-7	31	59
Romania		4.1	0.3	-1.9	-2	4	-4		2.7	0.0	2	2	-99	0
Russia		73.3	-0.5	-1.7	0	-6	1		6.9	-4.6	-1	10	160	118
South Africa		14.3	0.6	-3.4	-2	21	3		9.7	2.8	23	-20	-52	5
Turkey		8.79	-0.6	-3.7	-4	-22	-15		17.7	-2.7	8	11	717	463
US (DXY; 5y UST)		92	-0.2	1.7	2	-6	2		0.89	2.0	11	7	57	53

	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		5090	-0.2	-3	-1	24	-2		199	0	-2	-9	30	-9
Indonesia		5996	-0.2	-1	4	22	0		158	0	-9	-25	-5	-29
India		52574	0.4	0	4	51	10		140	-1	-4	-21	-99	-11
Philippines		6827	-0.4	-1	10	8	-4		83	0	-9	-17	13	-22
Malaysia		1572	-1.1	-1	1	4	-3		113	0	-2	-3	9	3
Argentina		65136	0.0	-1	16	59	27		1459	0	19	8	-570	91
Brazil		128405	0.0	-1	5	33	8		253	0	0	-16	58	3
Chile		4294	0.0	0	5	7	3		126	0	-6	-16	-14	-18
Colombia		1257	0.0	0	1	8	-13		207	0	-4	-15	44	2
Mexico		50320	0.0	-2	1	31	14		348	0	-9	-34	55	-12
Peru		18576	0.0	-6	-10	9	-11		133	0	-4	-3	22	1
Hungary		48256	0.3	-2	4	29	15		65	0	-6	-15	-42	-31
Poland		65635	-0.5	-2	3	30	15		-22	0	-4	-11	-54	-21
Romania		11608	0.0	1	-1	33	18		185	2	5	3	-103	-18
Russia		3807	0.1	-1	4	38	16		159	0	-5	-3	19	-7
South Africa		65521	-0.2	-3	-1	21	10		357	0	-4	-35	25	-23
Turkey		1383	-0.6	-5	-5	22	-6		421	0	-5	-47	34	-24
Ukraine		531	0.0	0	0	6	6		479	0	12	-21	127	-12
EM total		54	-0.3	-2	2	36	5		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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