GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

WEDNESDAY, JUNE 21, 2023

- **US housing market shows signs of recovery** (link)
- **ECB officials continue to differ on September rate hike prospects** (link)
- **Higher than expected May inflation shocks UK markets** (link)
- **BoJ's minutes revealed discussion of yield curve control review** (link)
- **South Africa's headline inflation eases more than expected** (link)

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UK inflation surprise has global impact

UK inflation data for May surprised markets, coming in higher than expected, with core inflation higher compared to the prior month compared to expectations of remaining unchanged. The data release of course sent UK yields significantly higher (UK 2y yield rose 14bp) but also drove an increase in Euro area and US treasury yields. The bund 2-year yield initially rose 6 bp on the release before mostly recovering later in the day while the UST 2-year rose 4 bp. Some market participants believe that the UK inflation surprise may spur other central bankers to keep pressing for tighter monetary policy. Later today, markets will be watching Fed Chair Powell's testimony to congress to gauge the relative hawkishness of his comments. Meanwhile, in Europe, ECB officials continue to offer various opinions on how much further the central bank has to go. European equity markets are generally slightly weaker this morning, along with US equity futures. Emerging market currencies meanwhile are more mixed with LatAm and CEEMEA currencies generally somewhat stronger, and Asian currencies weaker.

Key Global Financial Indicators

Last updated: 6/21/23 8:18 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		4389	-0.5	1	5	17	14	4
Eurostoxx 50		4337	-0.1	-1	-1	24	14	9
Nikkei 225		33575	0.6	0	8	28	29	27
MSCI EM		40	-2.0	0	3	-1	6	-16
Yields and Spreads					bps			
US 10y Yield		3.75	3.3	-3	8	48	-12	176
Germany 10y Yield		2.41	0.4	-4	-2	64	-16	218
EMBIG Sovereign Spread		450	5	5	-32	-50	-2	37
FX / Commodities / Volatility					%			
EM FX vs. USD, (+) = appreciation		49.8	0.0	0	-1	-4	0	-6
Dollar index, (+) = $ appreciation		102.6	0.0	-1	-1	-2	-1	7
Brent Crude Oil ($/barrel)		75.9	0.0	4	0	-34	-12	-22
VIX Index (%, change in pp)		13.7	-0.2	-1	-3	-16	-8	-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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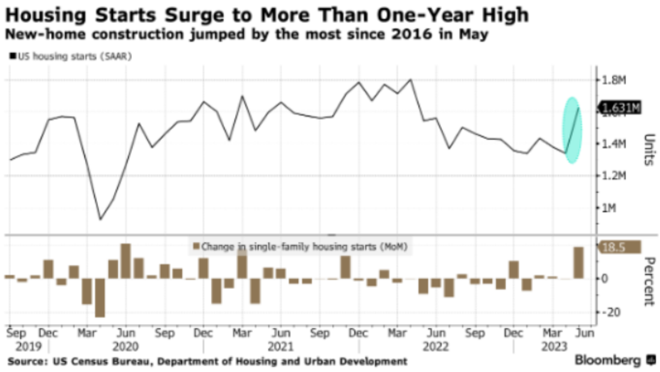
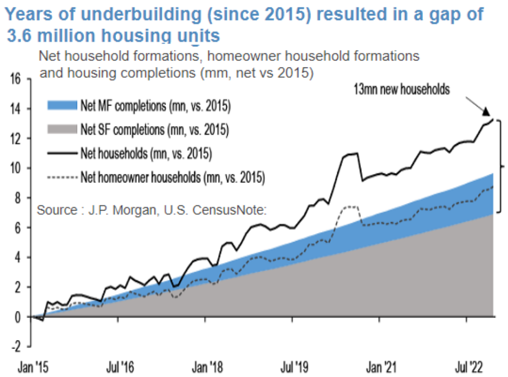
United States

Yesterday, the S&P 500 fell by 0.5%, with the Energy sector underperforming other sectors (-2.0%). Consumer Discretionary was the only sector that appreciated (+0.8%), mostly driven by a spike in Tesla Inc prices (+5.3%). Amid the risk-off sentiment, US Treasury 10-year yield fell by 4 bp, driven mostly by real yields.

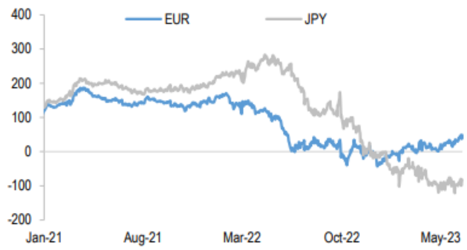
US housing starts surged in May along with an increase in applications to build, according to Bloomberg. Beginning home construction rose by 21.7% (a 1.63 million annualized rate, left chart below) despite the surveyed expectations showing virtually no change in this indicator. The figures resonate with Federal Reserve Chair Jerome Powell's comments that the housing market has shown signs of stabilizing and with Monday's positive surprise in the release of US homebuilder sentiment. Homebuilders, which are responding to limited inventory in the resale market, have grown more upbeat as demand firms, materials costs retreat and supply-chain pressures ease. JPMorgan analysts estimated that the relative underbuilding compared to the pace of net household formation resulted in a deficit gap of 3.6 million housing units (right chart), supporting new construction.





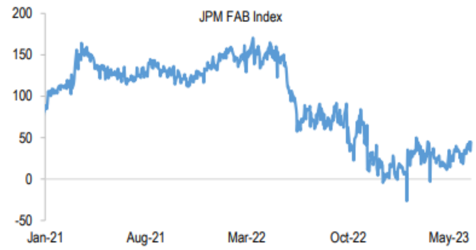
US Investment Grade bonds are becoming more attractive to foreign investors. Costs of hedging USD-denominated assets for foreign investors with EUR-, GBP-, and JPY-denominated portfolios have decreased after the recent policy rate decisions by the Fed (pause in the hiking cycle) and ECB (a hike). Consequently, the 10Y US HG FX-hedged yield pickup – i.e., the difference between the FX-hedged yield of USD-denominated IG bonds and the yield of a respective foreign sovereign bond – has increased (left chart below). Aggregating across foreign investors from all around the world, the weighted-average yield pickup remains positive (right chart), but significantly below its levels before the Fed's hiking cycle began.

Figure 1: 10y US HG FX hedged yield pickup



Source: J.P. Morgan, Bloomberg Finance L.P.

Figure 2: JPM Foreign Attractiveness of US HG Bonds

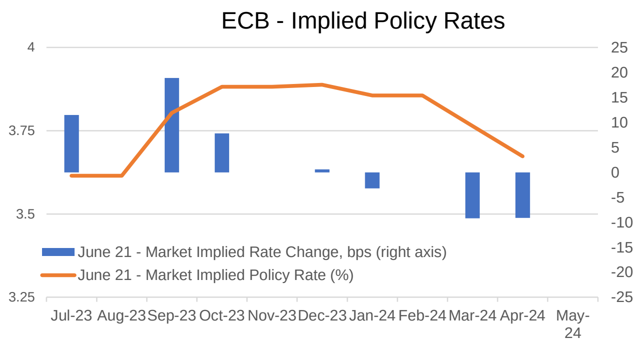


Source: J.P. Morgan, Bloomberg Finance L.P., Department of the Treasury

Euro Area

European markets are subdued today, after large moves in bond yields yesterday afternoon. The equity market (Stoxx Europe 600) is broadly stable (-0.1%), but with banking stocks gaining strongly (+0.6%). The euro was also broadly unchanged at 1.09/$. German 10y bund yields were stable at 2.40% after dropping 11 bp yesterday, and Italian spreads were unchanged at 163 bp.

ECB officials continue to voice differentiated opinions about the future pace of monetary policy in the euro area. In the hawkish camp, this morning, Slovak governor Kazimir said that the ECB can pause interest rate hikes in September only if it is certain that core inflation is under control. Yesterday, French governor Villeroy de Galhau said that the ECB has completed most of its interest rate increases and that possible further hikes would be less important in fighting inflation than the duration of tight monetary policy. The market pricing for ECB rates has not changed much since yesterday.

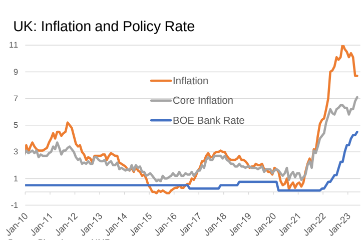


Source: Bloomberg WIRP and IMF

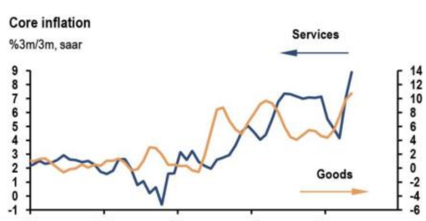
Finnish central bank governor and ECB Board Member Olli Rehn announced his bid for the Finnish Presidency. He subsequently said that he will take leave from his role at the Bank of Finland and won't actively perform official duties to ensure the independence and integrity of the central bank. Bloomberg reports that he did not specifically comment on his ECB tasks. The presidential election is expected to be held in January 2024.

United Kingdom

Higher than expected inflation for May shocked UK markets. Headline inflation for May came in at 8.7%, unchanged from April, when markets were expecting it to drop to 8.4% y/y. Core inflation actually increased to 7.1% y/y, whereas it was expected to be unchanged from April at 6.8% y/y. m/m headline inflation was also 0.7%, showing strong momentum. Today's reading was the fourth consecutive upside surprise to inflation. In the aftermath of the release, 2y gilt yields increased 14 bp to 5.09%, but subsequently fell to 5%, a level last seen durable in 2008. 10y gilt yields increased 4 bp to 4.37%.

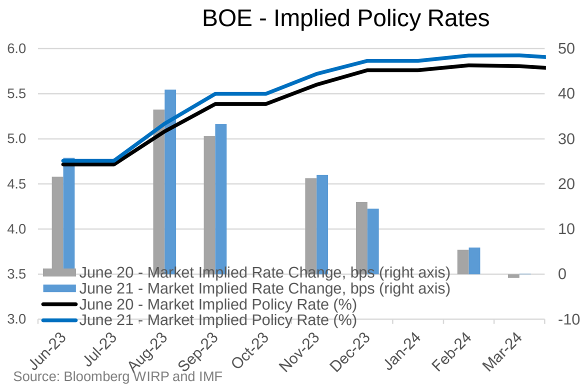


Source: Bloomberg and IMF



Source: ONS and JP Morgan Research.

Markets are now pricing in 32 bp in rate hikes for tomorrow Bank of England 's (BoE) decision, or about 4 bp higher than yesterday. The terminal rate is seen at 5.9% in February, about 10 bp higher than yesterday. After the release of the inflation data, JP Morgan analysts argued that the BoE MPC should act forcefully by hiking 50 bp tomorrow and assigned a 1/3 probability to such an outcome. They stuck to their 25 bp call, arguing that the BoE has provided no signal of a step up and no forward guidance on what would prompt a potential step up in the tightening pace, and also pointing out that no new forecasts will be released tomorrow.



Japan

Minutes from the Bank of Japan (BoJ) April meeting revealed that one member suggested reconsidering the yield curve control (YCC) program. The member reportedly stated that YCC may have hampered smooth financing. On Wednesday, however, Governor Ueda and Board Member Adachi reiterated their support to maintain an accommodative monetary policy stance given significant uncertainties over the BOJ's base case for inflation and recent improvements in market functioning. **Japanese stocks rose 0.5% and yen depreciated 0.3%. Yields on 10Y bonds declined 0.9bp.**

Emerging Markets

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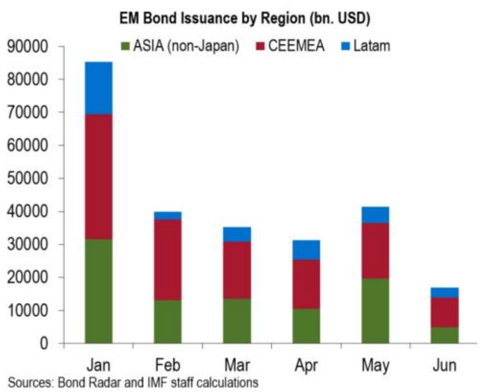
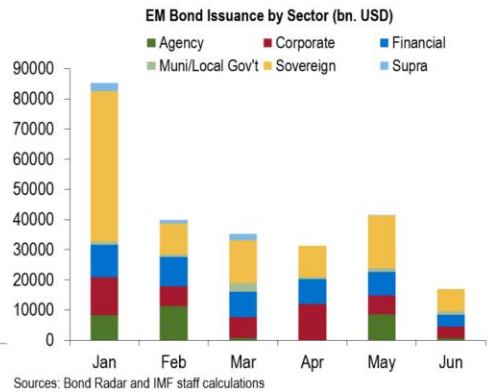
Asian equities extended losses (-1%). Chinese stocks led the sell-off (CSI 300 – 1.5%, Hong Kong China Enterprise index -2.4%). Indonesia outperformed (+0.6%), Malaysian equities rose 0.4%. Malaysia is seeking to cut the "time-to-market" for IPOs, Bloomberg reported. Total IPO proceeds in Kuala Lumpur are up just 0.7% y/y, while Jakarta surged 77% ytd as several firms ranging from renewable energy to those tied to the electric-vehicles supply chain tapped investors through large-size offerings. Asian currencies depreciated. The South Korean won weakened 0.9% amid risk aversion and after June exports to China declined 12.5% y/y based on 20-days proxy data. The Thai baht lost 0.3%, while the Indonesian rupiah rose 0.2%. 10-year bond yields broadly declined. Singapore yields fell 4.3bps Philippines 2.5bp and Indonesia 2.4bp. South Korea will start a gradual exit from regulatory easing on liquidity requirements as local markets recover from the pandemic and a recent credit crunch. The LCR ratio will be raised to 95% between July and December from 92.5% now, with the ratio for 2024 to be decided at the end of this year. **EMEA equities are mixed this morning,** while currencies are trading marginally stronger against the dollar. Local rates in Eastern Europe are mostly lower, with the exception of Hungary where 10y yields were 10bp higher (at 7.1%). Financial assets in the Czech Republic were little changed ahead of the monetary policy meeting later today, where the central bank is expected to leave the repurchase rate unchanged at 7%. The Turkish lira was little changed today while local currency yields were roughly 20bp lower ahead of the central bank monetary policy meeting tomorrow, where consensus expects the policy rate to be increased from 8.5% to 20%. In Zambia indicative prices show that the kwacha was little changed against the dollar this morning, after appreciating by roughly 11% yesterday following reports that official creditors have made "significant progress" and could even be close to making a restructuring offer. **Latin American assets were mixed Tuesday.** Stocks fell in Colombia (-1.1%), Mexico (-1.0%), Brazil (-0.2%) and Peru (-

0.2%), while Chile equity markets gained 0.5%. The Chilean peso (-1.0%) was one of the worst performers in emerging markets. Other currencies depreciated in Mexico (-0.8%), Peru (-0.2%) and Brazil (-0.2%), while the Colombian peso strengthened 0.2% against the US dollar.

EM Bond Issuance

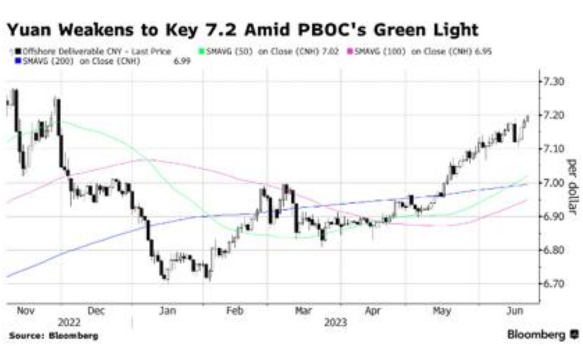
Bond issuance declined more than 75% from the week before. Only $2.0 bn was priced last week, among which, $1.8bn were corporate/financial. DBS, Bank of China and UniCredit Czech&Slovakia dominated the insurance with $690mn, $500mn and $537mn, respectively. All issuances are relatively short-term bonds with maturity less than 5 years. The majority of the new issuances are investment grade. YTD total issuance now stands at $250.0 bn.

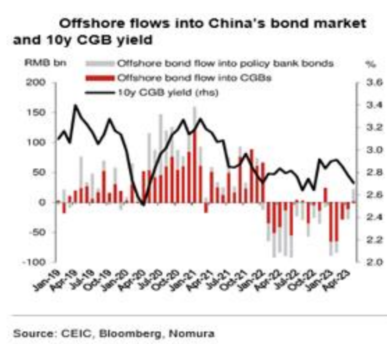




China

Chinese stocks slumped 1.5% and the renminbi weakened 0.2% with the offshore pair briefly breaching the key 7.2 level. Investors trimmed positions ahead of the market holiday after modest policy support, according to Bloomberg**.** The People's Bank of China (PBoC) set the yuan's reference rate at 7.1795 per dollar on Wednesday, the weakest since November 29**.** China said United States made a "public political provocation" after United States President Biden referred to Chinese President Xi Jinping as a dictator. Separately, foreign holding of China bonds increased in May. Foreign investors net bought $22.5bn on the market, offsetting a $19.7bn maturity. Nomura estimated that inflows last month were mainly led by policy bank bonds, while CGBs only received a small amount of offshore inflows. Analysts thought May bond inflows could reflect market expectations of rate cuts in China, due to the weak macroeconomic outlook, and thus is not necessarily positive for RMB. In June so far, high frequency data show that offshore flows were similar to those in May. Separately, sales of premium properties have gathered pace but are still unable to prop up the entire property market. Sales of luxury properties between 10mn yuan ($1.4mn) and 30mn yuan ($4.2mn) surged 45% in the first five months of 2023, according to real estate think tank CRIC Research Centre.

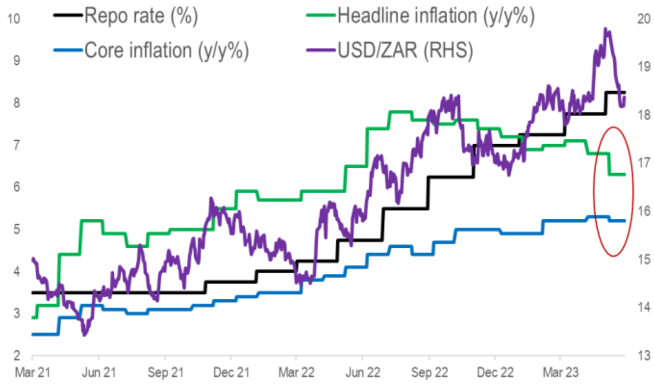




South Africa

The rand was little changed after headline inflation slowed to a 13-month low in May. Data released this morning showed headline inflation easing more than expected to 6.3%y/y in May (versus expected 6.5% from 6.8%), while core inflation eased to 5.2%, in line with expectations (from 5.3%). The South African rand was little changed this morning and has appreciated by almost 7% so far this month, after falling to the weakest level on record in May. At the latest monetary policy meeting, the central bank hiked the repurchase rate by 50bp to 8.25% in a unanimous decision and noted expectations for further currency weakness given upside risks to inflation, larger domestic and external financing needs. The rand remains roughly 7.5% weaker than at the start of the year. While some analysts think that the central bank has reached the peak of its tightening cycle, market pricing indicates a roughly 50% chance of the central bank hiking its key rate by 25bp at the upcoming meeting in July.

South Africa - Inflation and currency



Source: Bloomberg and IMF calculations

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Global Financial Indicators

6/21/23 8:18 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		4385	-0.5	0	5	16	14
Europe		4337	-0.1	-1	-1	24	14
Japan		33575	0.6	0	8	28	29
China		3864	-1.5	0	-3	-10	0
Asia Ex Japan		67	-2.3	0	2	-3	4
Emerging Markets		40	-2.0	0	3	-1	6
Interest Rates					basis points		
US 10y Yield		3.75	3.3	-3	8	48	-12
Germany 10y Yield		2.41	0.4	-4	-2	64	-16
Japan 10y Yield		0.38	-1.1	-5	-2	14	-4
UK 10y Yield		4.41	7.6	2	42	176	74
Credit Spreads					basis points		
US Investment Grade		154	-0.3	-5	-15	-11	-4
US High Yield		452	0.1	2	-45	-66	-29
Exchange Rates					%		
USD/Majors		102.56	0.0	-1	-1	-2	-1
EUR/USD		1.09	0.0	1	1	4	2
USD/JPY		141.9	0.3	1	2	4	8
EM/USD		49.8	0.0	0	-1	-4	0
Commodities					%		
Brent Crude Oil ($/barrel)		75.9	0.0	4	1	-21	-9
Industrials Metals (index)		145	-0.8	0	0	-15	-12
Agriculture (index)		71	0.5	7	11	-2	4
Implied Volatility					%		
VIX Index (%, change in pp)		13.7	-0.2	-0.9	-3.1	-16.5	-7.9
US 10y Swaption Volatility		98.9	-1.5	-2.9	-21.2	-32.4	-26.8
Global FX Volatility		8.2	0.0	0.3	-0.5	-2.9	-2.5
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		130	-1.9	-1	-29	-87	-75
Italy		164	0.9	0	-21	-29	-51
Portugal		67	-0.2	-3	-13	-38	-35
Spain		94	0.6	-1	-11	-14	-15

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

Emerging Market Financial Indicators

Last updated: 6/21/2023 8:24 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		7.19	-0.1	-0.3	-2	-7	-4		2.8	3.1	8	1	-10	-27
Indonesia		14952	0.4	-0.3	0	-1	4		6.3	-2.7	5	-13	-118	-63
India		82	0.1	0.1	1	-5	1		7.4	-8.9	-9	19	(38.3)	-9
Philippines		56	-0.2	0.5	0	-2	0		5.9	0.0	0	6	26	-9
Thailand		35	0.0	-0.5	-1	1	-1		2.8	-2.5	7	12	0	17
Malaysia		4.65	-0.1	-0.5	-2	-5	-5		3.8	1.8	7	4	-52	-25
Argentina		249	-0.4	-1.8	-7	-51	-29		111.9	-0.1	39	774	5029	2369
Brazil		4.81	-0.4	0.1	3	7	10		11.2	-5.1	-17	-78	-151	-138
Chile		804	-1.0	0.0	-1	10	6		5.0	0.5	3	-34	-138	-35
Colombia		4159	0.2	0.4	9	-2	17		7.8	0.0	-18	-97	-130	-195
Mexico		17.18	0.2	-0.4	4	17	13		8.3	0.0	-5	-19	-83	-47
Peru		3.6	-0.2	0.3	1	2	4		6.9	-0.8	-21	-41	-81	-103
Uruguay		38	0.5	1.7	2	6	5		9.9	0.2	0	-11	-93	-79
Hungary		339	0.5	1.1	2	11	10		7.4	-16.5	0	-60	-93	-221
Poland		4.07	0.1	1.0	2	8	8		5.2	-5.0	-5	-24	-220	-93
Romania		4.5	0.0	0.6	1	3	2		6.5	-2.9	-12	-34	-265	-116
Russia		84.4	0.3	-0.5	-5	-35	-12							
South Africa		18.4	-0.3	-0.4	4	-14	-8		9.8	-9.0	5	-29	111	67
Turkey		23.56	0.1	0.0	-16	-26	-21		17.1	-33.0	-67	722	-269	724
US (DXY; 5y UST)		103	0.1	-0.7	-1	-2	-1		4.00	4.5	1	27	63	-1

	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		3864	-1.5	0	-3	-10	0		186	1	-9	-6	9
Indonesia		6703	0.6	0	0	-4	-2		146	7	4	-54	6
India		63523	0.3	0	3	23	4		131	-3	-21	-42	-11
Philippines		6424	-0.4	0	-3	4	-2		117	8	1	-28	20
Thailand		1522	-1.0	-3	0	-2	-9		0	0	0	0	0
Malaysia		1393	0.4	1	-2	-3	-7		93	-1	-7	-32	-7
Argentina		409417	4.5	7	21	370	103		2374	61	-235	157	169
Brazil		119622	-0.2	2	8	20	9		253	7	-10	-91	-21
Chile		5783	0.5	1	2	14	10		132	6	3	-41	0
Colombia		1161	-1.1	-2	3	-17	-10		368	14	-38	-18	-4
Mexico		54366	-1.0	0	0	13	12		380	-6	-16	-48	-1
Peru		22535	-0.1	1	4	15	6		168	3	-11	-34	-12
Hungary		49857	0.1	0	7	22	14		222	2	-11	-19	0
Poland		67233	0.5	0	4	24	17		139	7	5	39	66
Romania		12258	-0.1	2	0	-1	5		238	3	-14	-75	-17
South Africa		75675	-1.4	-3	-3	13	4		421	29	-40	-37	54
Turkey		5255	0.1	-2	17	104	-5		496	27	-130	-174	56
Ukraine		507	0.0	0	0	-2	-2		4623	-401	-377	746	544
EM total		40	-0.4	0	3	-1	6		396	9	-30	-34	20

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

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