



Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Monday, June 24, 2019

- **US Dodd-Frank Act stress tests indicate adequate bank buffers against severe scenario** ([link](#))
- **Credit quality of EU CLOs has deteriorated faster than US CLOs** ([link](#))
- **Italian yields hit one-year low as government seeks to avoid excessive deficit procedure** ([link](#))
- **Turkish assets rally as opposition claims decisive victory in Istanbul elections** ([link](#))
- **Chinese overnight repo rate falls to decade low amid PBOC liquidity support** ([link](#))
- **Colombian central bank maintains policy stance; markets price rate cut in 6-months** ([link](#))

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US dollar weaker and sovereign yields lower as markets eye G-20 summit

Global risk assets are mixed to start the week as investors continue to position around a more accommodative central bank outlook and hopes that the G-20 meeting later this week leads to resumed US-China trade talks. Stocks in Asia were mixed overnight, while major European indexes are flat to modestly lower following the release of some weaker business confidence numbers. The S&P 500 closed out a strong week (+2.3%) with a slight decline on Friday, while this morning futures are pointing to a modest gain and US Treasury and European core yields are down 2 to 4 bps across maturities. The environment of dovish central banks and trade optimism has bolstered a steepening in some advanced economy sovereign yield curves, the 2-year 10-year Treasury yield spread now at +28 bps, and a broadly weaker US dollar that has depreciated close to 2% since the FOMC meeting. EM assets have benefitted from the weaker US dollar and decline in bond yields with the broad EM FX index appreciating over 1% in the past week and most EM equities holding on to gains. However, geopolitical risks remain in focus amid elevated tensions between the US and Iran, with most of the price response seen in a 7% gain in oil prices since mid-last week. Local politics is also driving some country-specific price moves as Turkish assets have rallied amid the surprise win by the opposition candidate in the redo of the Istanbul mayoral election.

Key Global Financial Indicators

Last updated: 6/24/19 8:06 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		2950	-0.1	2	4	7	18
Eurostoxx 50		3456	-0.3	2	3	0	15
Nikkei 225		21286	0.1	1	1	-5	6
MSCI EM		43	-0.5	4	7	-3	9
Yields and Spreads			bps				
US 10y Yield		2.03	2.6	-6	-29	-86	-65
Germany 10y Yield		-0.31	-2.5	-7	-19	-65	-55
EMBIG Sovereign Spread		344	1	-17	-20	-13	-70
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		62.7	0.1	1	2	-4	1
Dollar index, (+) = \$ appreciation		96.0	-0.2	-2	-2	2	0
Brent Crude Oil (\$/barrel)		65.2	0.0	7	-5	-14	21
VIX Index (% change in pp)		15.5	0.1	0	0	2	-10

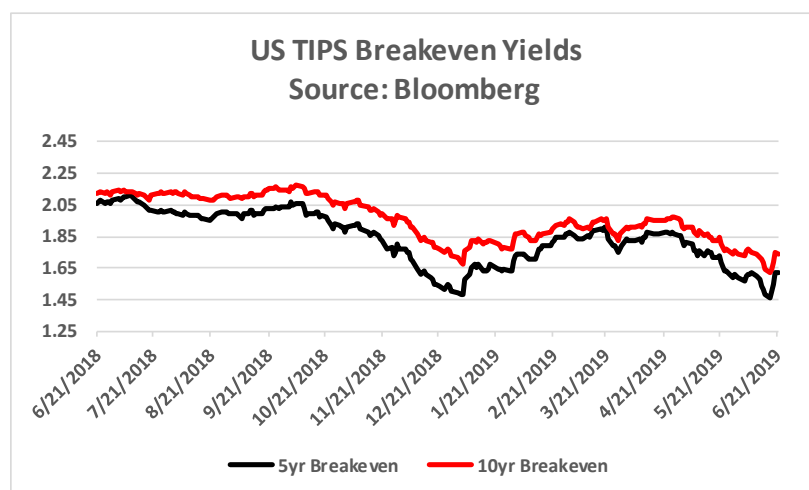
Colors denote **tightening/easing** financial conditions for observations greater than ± 1.5 standard deviations. Data source: Bloomberg.

Markets will be focused on this week's G-20 summit, as the presidents of China and the US are expected to meet on the sidelines to discuss trade. The market consensus has centered around the meeting resulting in both sides committing to re-engaging to reach an eventual agreement and a commitment to temporarily refrain from increasing tariffs. Events in the Middle East could also affect markets. Meanwhile, the US data calendar features some important releases, including durable goods on Wednesday, the latest update to Q1 GDP on Thursday and core PCE, the Fed's favored measure of inflation on Friday. The euro area calendar is much quieter, with this morning's German IFO business sentiment report followed by German consumer confidence on Wednesday and euro area CPI on Friday. The UK reports retail sales tomorrow and GDP on Friday. Japanese industrial production and CPI are due on Thursday. **In emerging markets, central banks dominate the economic calendar**, with a rate decision due from Mexico (Thu), and meeting minutes due from Chile (Mon) and Brazil (Tue). Investors will also focus on the economic activity from Argentina (Wed) and Q2 inflation report from Brazil (Thu).

United States

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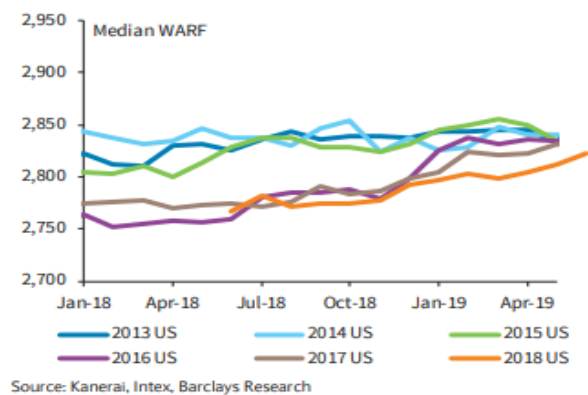
Markets took a break on Friday after Thursday's record close for the S&P 500. Stocks were little changed and Treasury yields rebounded with the 10-year finishing the week up at 2.06%. The latter move was attributed to a reversal of the prior rally rather than any change in the outlook for monetary policy or growth. Indeed, weaker than expected services and manufacturing PMI data underscored the Fed's worries about the economy despite stronger than expected existing home sales. Manufacturing PMI at 50.1 is just fractionally above a contractionary reading. Minneapolis Fed President Kashkari spurred debate with an article stating that he voted for a 50 bp cut at the FOMC meeting, and also advocated for a pledge not to raise rates "until core inflation reaches our 2 percent target on a sustained basis." He is a non-voting member this year and will be a voting member in 2020. Contacts debated how likely the Fed was to adopt such an aggressive move, in order to raise inflation expectations. Breakeven yields on US Treasury Inflation Protected Securities (TIPS) have remained stubbornly below 2% since November.



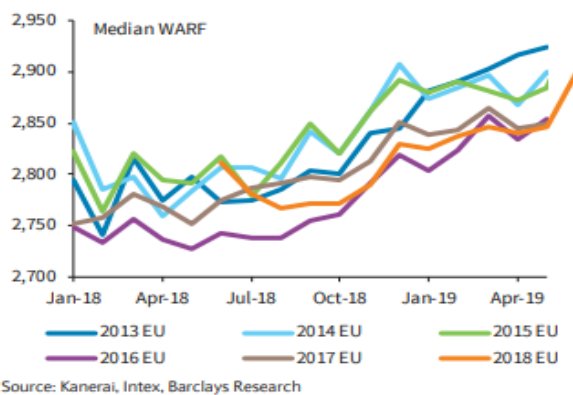
US CLOs have performed better in credit terms than their counterparts in Europe. The weighted averagerating factor (WARF) is a measure used by ratings agencies to gauge relative credit risk, with higher WARFs associated with higher risk. Recent vintage US CLOs have exhibited steady WARFs since 2017, but euro area CLO WARFs's have drifted higher since the second half of 2018. This reflects a deterioration in credit quality in assets held within European CLOs, while US credit quality has so far only declined marginally. Moody's has downgraded an increasing number of the loans in European CLOs, mainly because it has made its rating standards more conservative due to prevailing business and credit conditions. In

particular, debt levels of some borrowers had increased to levels no longer consistent with ratings, often due to acquisitions.

WARFs for US CLOs Are Flat to Slightly Higher since YE17...

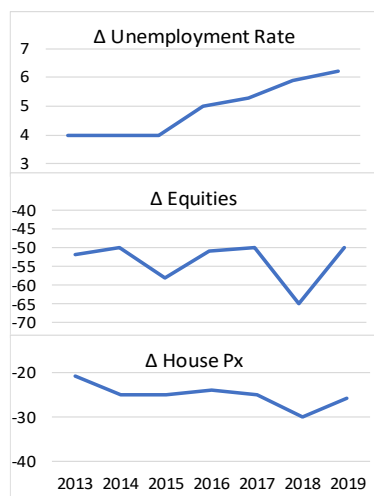


...While EU CLO WARFs Have Climbed Steadily since 2H18

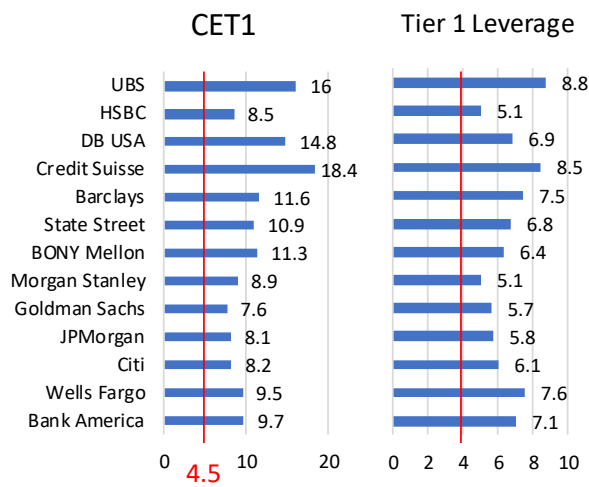


Bank stress test results indicate adequate buffers against a severe scenario; positive for capital payout plans. The Federal Reserve on Friday announced results of the 2019 Dodd-Frank Act stress test (DFAST), which estimates systemically important banks' potential losses and capital positions under adverse macroeconomic and market conditions. Using stress scenario assumptions generally in line with previous years (left-hand chart), all 18 banks tested (including both domestic banks and the combined US operations of foreign banks) 'passed' the test, maintaining stress-scenario capital adequacy and leverage ratios comfortably above regulatory minima (right-hand chart). This was widely expected given the large accumulation of capital buffers in recent years, but also reflects benign stress-scenario loss estimates: - 0.8% return on assets in the 2019 test, in line with the two previous years and well below earlier results, which reflects well on the current risk environment. Market observers believe this result positions banks for approval of aggressive capital payout plans when the Fed announces the Comprehensive Capital Analysis and Review results later this week.

Assumptions



Worst Stress Scenario Outcomes

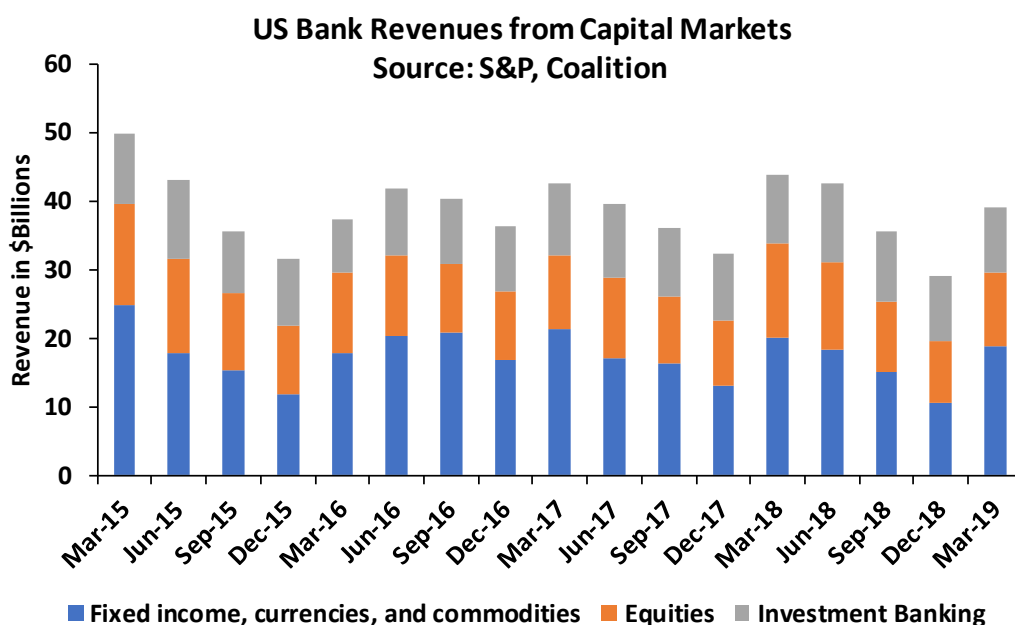


Source: Federal Reserve

Notes: All assumptions are expressed in terms of change from levels obtaining at the time of each annual stress test. Worst stress scenario outcome is the lowest estimated quarterly result over the period 1Q2019 to 1Q2021. Red vertical lines indicate regulatory minima.

Global banks

Global bank capital markets activities have proved once again to be a volatile source of revenue, with S&P predicting a 10% decline for the year. Revenues in Q1 2019 were 11% below where they were in Q1 last year. Low interest rates have eroded profit margins, while trade tensions and other uncertainties have kept trading customers on the sidelines, cutting back on commissions and other transaction related revenues. Stronger regulatory constraints have also raised capital costs. As a result, banks have tried to boost earnings from their other businesses such as corporate lending, credit cards, wealth management, etc. These efforts have been only modestly successful so far, but S&P forecasts that business conditions will force banks to continue to diversify away from capital markets and predicts that they will ultimately be successful in growing their non-market revenue.



Europe

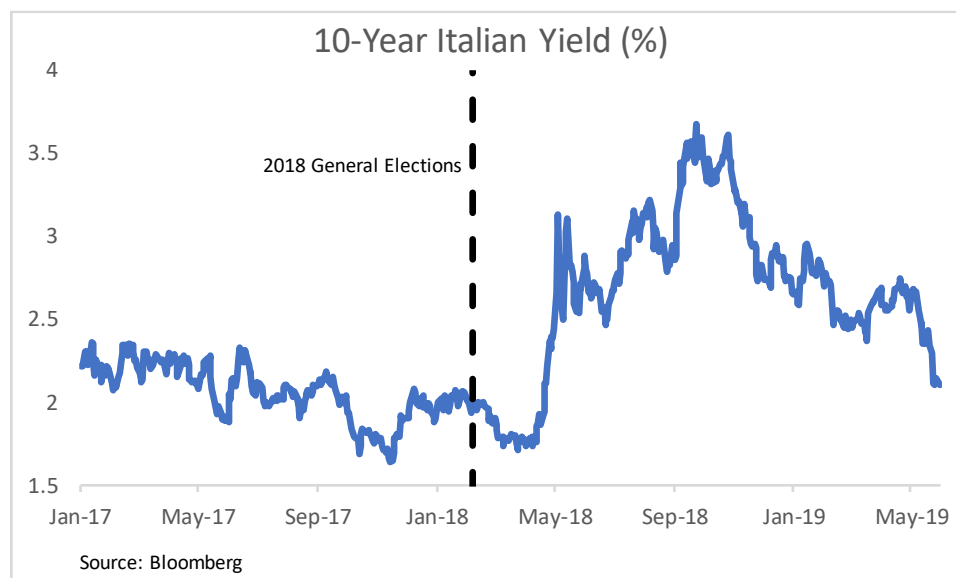
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Sovereign yields saw small declines this morning. Most 10-year benchmarks were down 1-2 bps while the UK and Italy experienced larger moves of -4 bps. Fitch affirmed Spain's long-term rating at A- with a stable outlook after markets closed on Friday. The agency cited a reduction in macroeconomic imbalances but warned that the stock of general government debt remains very large.

Equities had a quiet start to the week with the Euro Stoxx 600 flat. Banks underperformed with a 0.4% slide. Shares in French bank Natixis stabilized, however, after a 14% fall on Thursday and Friday. The asset management arm H2O announced this morning that it had sold part of its non-rated private bonds and would mark down the rest of it. It also said it would remove all entry fees across all funds. Shares in Natixis rose 3.1% in morning trading but remain a third below prices seen last month.

The Italian government will seek measures this week to stave off an excessive deficit procedure by the European Commission. According to reports, the mechanism will not be triggered at a meeting tomorrow with Italy set to be given an extra week to find areas to decrease the country's budget deficit. The finance ministry is expected to send a letter to the commission later this week while Wednesday sees a spending review sent to the Italian parliament. BTPs outperformed other government bonds this morning

with the 10-year seeing a 4-bps drop to 2.1%. That represents the lowest level for the benchmark since May 2018.



The European Commission is said to have decided to not propose extending the equivalence regime with bourses in Switzerland. No progress has been made in lengthy negotiations between the EU and Switzerland on a partnership treaty with issues such as citizens' rights, wages, and state aid standing in the way of an agreement. The commission will therefore not endorse continued equivalence which would mean that investors would lose direct access to each other's stock exchanges from July 1. Earlier, the Swiss government said that it would ban trading of Swiss shares on EU-based bourses if equivalence were not granted.

Other Mature Markets [back to top](#)

Japan

The yen was little changed while equities softened amid a dearth of significant news while investors pared positions ahead of the upcoming G-20 summit. The JGB curve steepened with the 30-year sector rising 2 bps while shorter-dated tenors were mostly steady. The move was a continuation of shifts seen late Friday and partly tracked movements in other major markets' sovereign bonds.

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Emerging market assets started the week in calm fashion. Asian currencies gained modestly on the back of dollar weakness, extending moves spurred by the Fed's dovish shift last week. The Korean won appreciated 0.7% to its strongest level in two months while the Thai baht (+0.2%) reached its strongest level in 6 years. In equities, bourses were mostly flat or slightly lower as investors remain on the sidelines ahead of the upcoming G-20 summit, while there was little reaction from Chinese equities to reports the US added five Chinese firms to the entity list on export controls. **Equities in the EMEA region were mostly higher this morning.** Gains were around 0.5% in most bourses while Turkey (+1.9%) outperformed sharply following the opposition's victory in the re-run of Istanbul's elections (see EMEA section). Turkey (+1.4%) was also the outperformer among EMEA currencies with other countries seeing marginal gains against the dollar. **Latin American markets were mixed on Friday.** Brazilian markets rallied after government agreed to vote on the pension reform in July, with the IBOV index up 1.7% and the real 0.5% stronger against the

dollar. Argentine assets also gained, in a catch-up move after closing for a holiday, with the Merval index up 1% and the peso 1.3% stronger to 42.8. Price action in other markets was relatively limited.

Key Emerging Market Financial Indicators

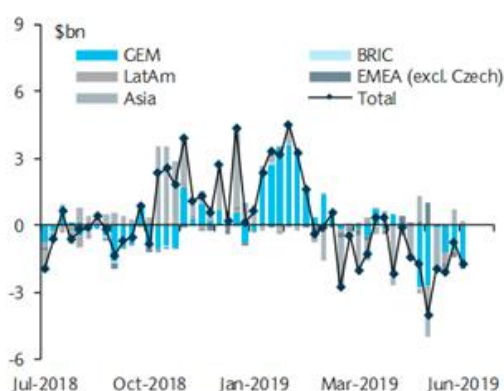
Last updated: 6/24/19 8:14 AM	Level		Change				YTD
	Last 12m	index	1 Day	7 Days	30 Days	12 M	
Major EM Benchmarks			%				%
MSCI EM Equities		42.77	-0.5	4	7	-3	9
MSCI Frontier Equities		29.48	0.4	-1	4	-1	13
EMBIG Sovereign Spread (in bps)		345	2	-16	-19	-12	-69
EM FX vs. USD		62.73	0.1	1	2	-4	1
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.88	-0.1	1	0	-5	0
Indonesian Rupiah		14144	0.1	1	2	0	2
Indian Rupee		69.35	0.3	1	0	-2	1
Argentine Peso		42.80	1.3	3	5	-36	-12
Brazil Real		3.82	0.0	2	5	-1	1
Mexican Peso		19.15	-0.2	0	-1	4	3
Russian Ruble		62.94	0.1	2	2	0	11
South African Rand		14.33	0.0	3	1	-6	0
Turkish Lira		5.79	0.4	1	5	-19	-9
EM FX volatility		8.27	1.1	-0.1	-0.2	-1.5	-1.5

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

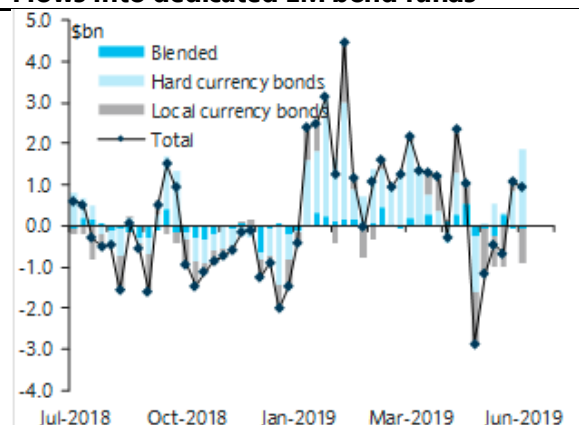
Emerging Market Flows

EM hard-currency bond funds posted strong inflows last week, but this was offset by outflows from EM local-currency bond funds and EM-dedicated equity funds. The dovish tilt by major central banks this week appears to have primarily supported EM credit, while concerns about slowing global growth amid trade tensions continue to weigh on growth-sensitive equity flows.

Flows into dedicated EM equity funds



Flows into dedicated EM bond funds



Turkey

Opposition candidate Imamoglu secured a decisive victory in the redo of the mayoral elections in Istanbul. Imamoglu had also won the original vote but the country's electoral body ordered a do-over after the ruling AKP alleged irregularities. Imamoglu's margin of victory widened substantially, going from

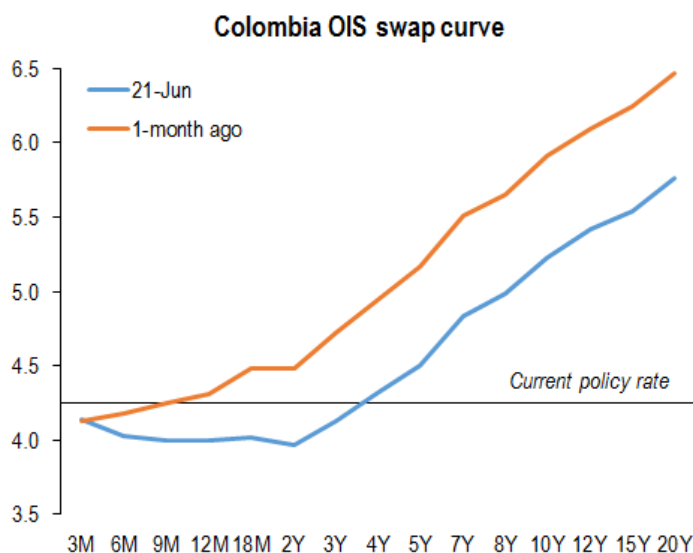
13,000 in the first vote to approximately 775,000 yesterday. Analysts cited high inflation and unemployment as among the reasons for the opposition's victory. Following the results, Binali Yildirim, former prime minister and AKP's candidate, conceded defeat while president Erdogan accepted the outcome. The results and the AKP's reaction led to a rally in Turkish assets this morning. Equities saw a 2% rise while the lira jumped by 1% against the dollar.

China

The average overnight repo rate fell to its lowest level in a decade amid ample PBOC liquidity injection. The PBOC has injected CNY 515 bn of net liquidity into the financial system over the past 7 days, helping to pull the average overnight repo rate to 0.99% on the day, its lowest level since 2009. The 7-day rate has also eased from levels seen in late May following the government's takeover of Baoshang bank; it last traded at 2.27%, compared to a recent high of 2.86%. Meanwhile, in an effort to address funding squeeze facing smaller banks and non-bank financial institutions that do not have direct credit lines to the PBOC, the authorities have raised the short-term funding quota for several large brokerages by as much as 200%. Contacts reported that PBOC and CSRC asked large banks and brokerages to increase their financing support to smaller brokers and banks, including interbank borrowing and lending, as well as purchasing bonds and short-term notes from these borrowers. **Markets in China are little changed on the day ahead of the upcoming G-20.** Bloomberg reported that trade teams from the U.S. and China are discussing next steps after Presidents Trump and Xi's meeting at the G-20 summit. **Market participants generally expect the two sides to resume and extend trade talks, with no new tariff increases while negotiation is ongoing.**

Colombia
















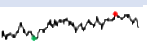
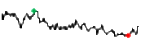












The central bank voted unanimously to keep the policy rate unchanged at 4.25% for the 13th straight month. The decision, in line with analysts' forecasts, came as recovery has stalled with subdued inflation and rising unemployment. The governor said the board has not discussed the possibility of a rate cut, even though markets have priced in such move in as soon as 6 month. The peso weakened 0.3% to 3202 against the dollar, after an impressive run of 5.5% appreciation in June on the back of dollar weakness and recovering commodity prices.



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Global Financial Indicators

Last updated: 6/24/19 8:08 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		2950	-0.1	2	4	7	18
Europe		3456	-0.3	2	3	0	15
Japan		21286	0.1	1	1	-5	6
China		3008	0.2	4	5	4	21
Asia Ex Japan		69	-0.6	4	6	-5	9
Emerging Markets		43	-0.5	4	7	-3	9
Interest Rates			basis points				
US 10y Yield		2.03	2.6	-6	-29	-86	-65
Germany 10y Yield		-0.31	-2.5	-7	-19	-65	-55
Japan 10y Yield		-0.15	0.2	-3	-8	-19	-16
UK 10y Yield		0.81	-3.1	-4	-14	-51	-46
Credit Spreads			basis points				
US Investment Grade		124	-0.5	-7	-2	15	-23
US High Yield		438	1.0	-13	-7	98	-83
Europe IG		53	-0.7	-7	-15	-20	-34
Europe HY		253	-3.0	-22	-42	-61	-100
EMBIG Sovereign Spread		344	1.0	-17	-20	-13	-70
Exchange Rates			%				
USD/Majors		96.03	-0.2	-2	-2	2	0
EUR/USD		1.14	0.2	2	2	-3	-1
USD/JPY		107.3	0.0	1	2	2	2
EM/USD		62.7	0.1	1	2	-4	1
Commodities			%				
Brent Crude Oil (\$/barrel)		65	0.0	7	-5	-14	21
Industrials Metals (index)		111	0.2	1	-2	-17	2
Agriculture (index)		42	0.6	-1	7	-7	1
Implied Volatility			%				
VIX Index (% change in pp)		15.5	0.1	0.1	-0.4	1.7	-9.9
10y Treasury Volatility Index		4.9	0.0	-0.6	0.6	1.1	0.3
Global FX Volatility		6.7	0.1	0.1	-0.1	-1.3	-2.3
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		274	-8.7	-22	-74	-107	-142
Italy		242	-1.0	-12	-25	7	-8
Portugal		84	-2.2	-4	-25	-64	-64
Spain		72	-0.3	-5	-22	-30	-45

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

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Emerging Market Financial Indicators

Last updated: 6/24/2019 8:15 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		6.88	-0.1	0.7	0	-5	0		3.3	-0.4	-2	-6	-38	6
Indonesia		14144	0.1	1.3	2	0	2		7.6	1.8	-18	-64	-10	-59
India		69	0.3	0.8	0	-2	1		6.9	4.5	-10	-44	-103	-50
Philippines		51	0.3	1.5	2	4	2		5.0	-1.0	-4	-10	-59	-132
Thailand		31	0.3	1.8	4	7	6		2.3	3.2	1	-31	-46	-36
Malaysia		4.14	0.2	0.9	1	-3	0		3.6	-0.4	-7	-19	-58	-46
Argentina		43	1.3	2.8	5	-36	-12		29.0	-51.5	-97	-323	976	596
Brazil		3.82	0.0	1.7	5	-1	1		6.9	-20.3	-25	-116	-336	-127
Chile		684	-0.1	2.3	2	-6	1		3.4	0.9	-9	-71	-147	-109
Colombia		3203	-0.3	2.2	4	-8	1		5.8	5.0	-5	-53	-67	-76
Mexico		19.15	-0.2	0.1	-1	4	3		7.7	10.5	-1	-46	-10	-99
Peru		3.3	0.3	1.4	1	-1	2		4.8	3.7	-7	-48	-101	-94
Uruguay		35	0.0	0.1	0	-10	-8		10.5	-35.5	-54	-52		-20
Hungary		285	0.2	1.0	2	-2	-2		1.6	3.5	-9	-45	-93	-60
Poland		3.73	0.3	1.7	3	-1	0		2.1	2.5	1	-31	-47	-22
Romania		4.1	0.4	1.7	3	-4	-2		4.0	-1.0	-11	-34	-65	-27
Russia		62.9	0.1	2.2	2	0	11		7.3	6.3	-18	-44	-18	-111
South Africa		14.3	0.0	3.3	1	-6	0		9.3	7.9	-13	-5	-16	-28
Turkey		5.79	0.4	1.4	5	-19	-9		17.1	1.9	-208	-376	7	21
US (DXY; 5y UST)		96.0	-0.2	-1.6	-2	2	0		1.77	-2.3	-9	-35	-100	-74

	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		3008	0.2	4	5	4	21		180	1	-1	2	-7	-14
Indonesia		6288	-0.4	2	4	8	2		185	2	-12	-15	-25	-51
India		39123	-0.2	0	-1	10	8		147	-4	-4	-5	-12	-49
Philippines		8061	0.1	2	4	14	8		72	2	-13	-14	-55	-49
Malaysia		1676	-0.4	2	5	-1	-1		129	0	-3	2	-29	-33
Argentina		40295	1.1	-2	15	33	33		828	3	-27	-77	295	13
Brazil		102013	1.7	3	9	44	16		233	0	-13	-25	-82	-40
Chile		5060	0.0	0	4	-6	-1		133	1	-4	-2	-10	-33
Colombia		1560	0.4	2	5	2	18		176	0	-15	-22	-18	-52
Mexico		43527	-0.3	1	2	-7	5		332	1	-10	18	51	-22
Peru		20492	-0.5	1	4	1	6		119	1	-10	-21	-46	-49
Hungary		40341	-0.1	-1	1	14	3		82	-1	-14	-23	-59	-66
Poland		59765	0.6	1	5	6	4		40	2	-7	-10	-30	-45
Romania		8749	0.0	3	7	8	18		175	-7	-17	-18	-1	-46
Russia		2769	0.3	1	6	23	17		202	3	-10	-7	-20	-50
South Africa		58636	-0.5	1	8	3	11		282	2	-33	-27	-12	-83
Turkey		95054	1.1	3	10	-1	4		506	-10	-38	-48	98	77
Ukraine		551	-0.2	0	-4	21	-1		516	0	-48	-131	-46	-271
EM total		43	-0.5	4	7	-3	9		345	2	-16	-19	-12	-69

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