



Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Tuesday, June 25, 2019

- Foreign demand for US corporate debt expected to rise due to higher relative yields ([link](#))
- US leveraged loan issuance slows as investor demand wanes amid falling rates ([link](#))
- UK PM frontrunner Boris Johnson reiterates stance of possible no deal Brexit ([link](#))
- Chinese bank shares fall on reports of US probe into North Korea sanction violations ([link](#))
- Geopolitical tensions intensify between the US and Iran ([link](#))
- Argentine oil company YPF seeking to issue USD bonds as borrowing costs fall ([link](#))
- **SPECIAL FEATURE: Facebook announces Libra digital currency (see attachment)**

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Heightened geopolitical risks weigh on investor sentiment

Global sovereign bond yields continue to edge lower as uncertainties around economic growth, trade, and geopolitical tensions persist. Heightened political anxiety between the US and Iran and building concerns over the upcoming US-China trade meeting have dampened risk appetite this morning. Global equity markets pulled back with most major Asian bourses posting losses, highlighted by 1% declines in Chinese equities on reports Chinese banks could suffer consequences from a US probe into North Korean sanctions violations. European indexes are also trading lower for the third consecutive session, while S&P 500 futures point to a slight decline at the open. These uncertainties have partially sustained some safe haven demand that has pushed 10-year Treasury yields back down to the 2% threshold and 10-year Bund yields near record lows of -0.32%. Investors have also reinforced the move lower in bond yields by continuing to price in an aggressively lower path for policy rates in the US. Markets have priced in a 25 bp policy rate cut and about a 30% chance of a 50 bp cut at the July FOMC meeting, with a total of about three 25 bp cuts by year end.

Key Global Financial Indicators

Last updated: 6/25/19 8:08 AM	Level Last 12m Latest	Change from Market Close				YTD
		1 Day	7 Days	30 Days	12 M	
Equities		%				%
S&P 500	2945	-0.2	2	4	8	17
Eurostoxx 50	3447	-0.3	0	3	2	15
Nikkei 225	21194	-0.4	1	0	-5	6
MSCI EM	43	-0.8	4	7	-1	9
Yields and Spreads		bps				
US 10y Yield	2.01	-4.0	-5	-31	-87	-68
Germany 10y Yield	-0.32	-1.2	0	-20	-65	-56
EMBIG Sovereign Spread	348	1	-6	-16	-14	-66
FX / Commodities / Volatility		%				
EM FX vs. USD, (+) = appreciation	62.8	0.1	1	2	-3	1
Dollar index, (+) = \$ appreciation	96.1	0.1	-2	-2	2	0
Brent Crude Oil (\$/barrel)	64.6	-0.4	4	-6	-14	20
VIX Index (% change in pp)	15.4	0.1	0	-1	-2	-10

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

United States

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The rally in US Treasuries resumed ahead of the G-20 meeting while equity markets took a break after last week's record close. Investors sought protection in safe haven assets in case the headlines from Tokyo turn out to be negative, steepening the US yield curve and pushing the 10-year Treasury yield back down towards the 2% level. However, it was a quiet session overall, with relatively low trading volumes and muted volatility. Speculation is building that if the Fed cuts rates in July, it will also announce an earlier than expected end to balance sheet reduction.

Foreign buying of US corporate bonds is on the rise and is expected to ramp up further. The collapse of euro area yields leading up to and after the ECB meeting leaves the US market almost the only game in town for positive rates of interest. The percentage of global debt with negative yields has reached 25% and investors are finding it increasingly hard to find suitable investments. The recent FOMC meeting has further heightened foreign demand for US corporate bonds because it sparked dollar depreciation which has lowered hedging costs for non-dollar investors. With Fed rate cuts priced in as early as July 31, hedging costs could fall even more. Contacts report that foreign buyers are trying to buy as much as they can before the market gets away from them and the US yield pickups eventually disappear.

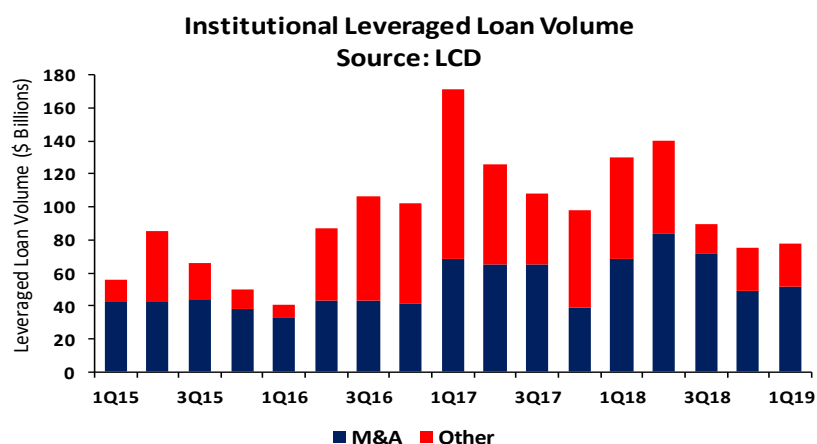
Figure 10: How to make 50bps in the Eurozone

Investment	Yield (bps)	Hedge (bps)	Yield after hedge (bps)
30-year Bunds	27		27
3-5 year EUR IG	48		48
1-3 year US IG (12m fwd hedge)	262	215	47
7-10 year US IG (spot hedge)	349	293	56
<1 year US HY (spot hedge)	434	293	141

Note: Spot dollar hedge is the current cost of rolling 3-month forward fx contracts. Forward hedge is the 12-month out cost of that dollar hedging strategy computed by subtracting the difference between the 1st and 12th Fed funds futures

Source: Bloomberg, ICE Data Indices, LLC, BofA Merrill Lynch Global Research

Leveraged loan issuance in US markets has begun to fall significantly as both borrowers and lenders turn away from the market. Investor demand began to dry up in the midst of the market turmoil last year, which reduced the risk appetite for leveraged loans. The Fed's subsequent dovish turn in 2019 year further reduced demand as floating rate leveraged loans are less attractive in a falling rate environment. For issuers, the steady decline in interest rates has made bonds more attractive than leveraged loans as they are able to lock in very low funding costs in an environment where the search for yield has kept demand for new bonds at a very high level. S&P thinks that the systemic risk of leveraged loans has declined significantly with the drying up of new supply, with direct exposure for banks estimated at less than 10% of the market.



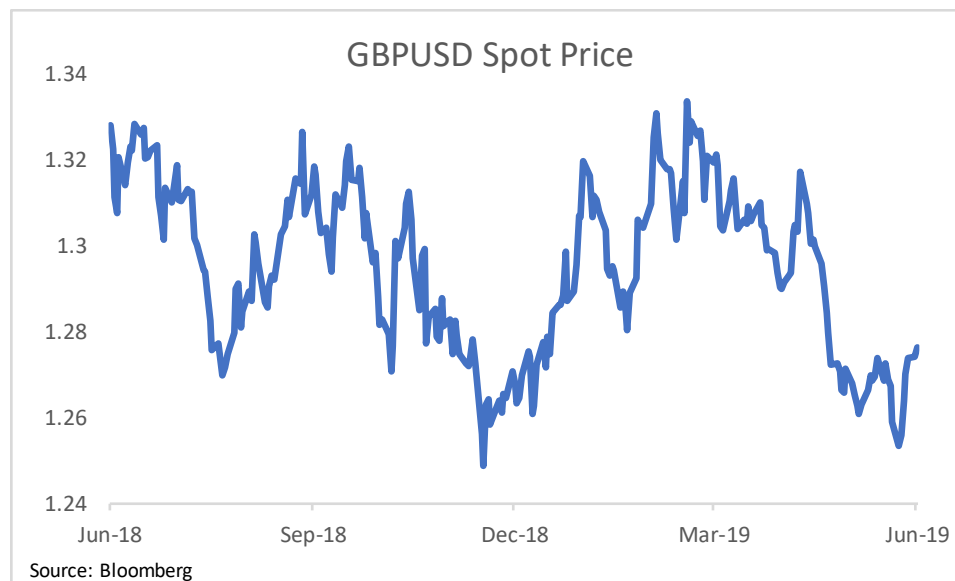
Europe

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Sovereign yields declined as geopolitical concerns and continued growth worries weighed on markets. Most 10-year yields were down by 1-2 bps apart from Italian bonds which were flat. The 10-year Bund yield was down 2 bps, reaching a new low of -0.33%. **Equities retreated amid the broader risk-off sentiment.** The Euro Stoxx 600 was down by 0.2%, its third consecutive decline. Banks were among the worst performing sectors, dropping by 1%.

Unicredit (-0.9%) is said to have put a potential bid for Commerzbank (-1.8%) on hold, according to reports. The Italian lender was reportedly interested in a takeover that would have diversified its balance sheet away from its domestic base. Failed merger talks between Commerzbank and Deutsche Bank seemed to pave the way for Unicredit but the German bank was said to need breathing space before it could consider another deal.

Boris Johnson, the frontrunner to become the next prime minister, reiterated his stance that a no deal Brexit might be unavoidable. Johnson also argued that parliament would now support a no deal although other MPs have argued that a majority could support a no confidence vote in the government if it pursued no deal. The new prime minister will have limited time to put in place a Brexit strategy as the result of the leadership race will only be known towards the end of July, followed by a six-week parliamentary recess. The UK will leave the EU on October 31 by default if no new legislation is put in place. The harsh rhetoric during the leadership contest has contributed to a weakening of the pound. However, it has gained for six straight days against the dollar, in part due to the dovish turn of the Fed. The currency was marginally stronger again this morning at \$1.276.

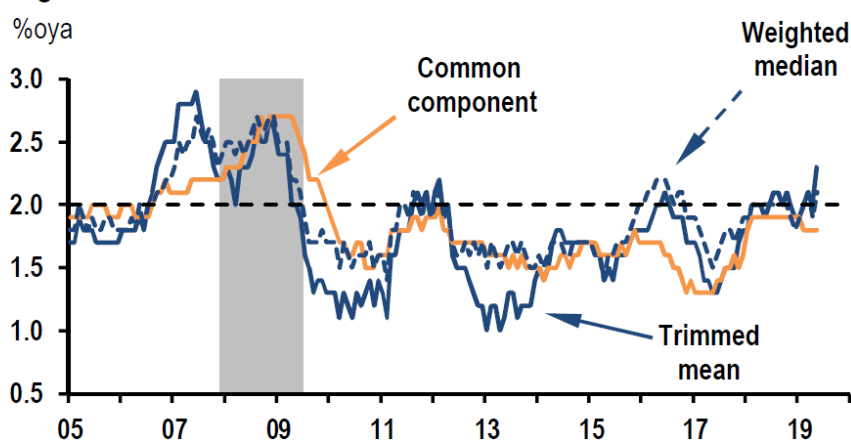


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Canada

Strong economic data have raised questions about whether the Bank of Canada will be able to cut rates to match the expected Fed rate cuts. The average of its three favored inflation measures has now risen above the Bank of Canada's 2% inflation target. Retail sales have been up three months in a row and while the latest print was below forecasts, there were upward revisions to prior months. The employment picture is also favorable and the Canadian policy rate at 1.75% is 75 bps below the US policy rate. In addition, the Canadian dollar has appreciated versus the US dollar through much of the year. However, many analysts argue that the Bank of Canada will have to react to Fed rate cuts with cuts of its own. Any Fed cuts are likely to be in response to worrying trends in the US economy that are likely to have knock-on effects in the Canadian economy. The manufacturing sector is a particular worry due to its importance to Canada's economic strength and the uncertain global outlook for manufacturing in the midst of the US-China trade dispute. The odds of a rate cut in October, derived from derivatives in the overnight index swap (OIS) market, have risen to more than 35% from 28% a month earlier.

Figure 1: Bank of Canada three core CPI measures



Source: Statistics Canada, J.P. Morgan

Japan











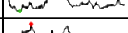



The yen appreciated to its strongest level since January while equities fell as investors assessed the latest developments surrounding Iran and the upcoming US-China trade negotiation. The yen gained as much as 0.5% intraday before settling at +0.3% to ¥106.98, its strongest level since the flash crash in early January. Meanwhile, equities fell (-0.3%) on a mix of concerns. Still, shares of defense companies, including Ishikawa Seisakusho, Howa Machinery and Hosoya Pyro-Engineering rose following reports that President Trump had considered withdrawing from a longstanding defense treaty with Japan. Trading volume remained relatively low head of the G20 summit, with volume on the Topix 15% less than its 30-day average.

Emerging Markets

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Emerging market equities declined amid the risk-off tone in global markets. In Asia, equities fell while currencies were little changed amid geopolitical strains and the US administration continuing to downplay expectations for the upcoming meeting between Presidents Trump and Xi. Shares in China (-0.9% for the Shanghai Composite and -1% for the Shenzhen Composite) and Hong Kong (-1.2%) underperformed. Meanwhile, Asian currencies were little changed: the Thai baht appreciated 0.14%, pacing gains while the Malaysian ringgit shed 0.1%, underperforming others. **EMEA equities declined by approximately 0.5%.** Currencies in the region were little changed against the dollar. **Latin American markets closed mixed yesterday with fairly limited price actions.** The Argentine peso appreciated 0.8% against the dollar, supported by the news that its largest oil company YPF is returning to the international debt market. Markets elsewhere closed within 0.5% change on the day.

Key Emerging Market Financial Indicators

Last updated: 6/25/19 8:13 AM	Level		Change				YTD
	Last 12m	index	1 Day	7 Days	30 Days	12 M	
Major EM Benchmarks			%				%
MSCI EM Equities		42.71	-0.9	4	7	-1	9
MSCI Frontier Equities		29.62	0.5	2	5	0	13
EMBIG Sovereign Spread (in bps)		348	1	-6	-16	-14	-66
EM FX vs. USD		62.81	0.1	1	2	-3	1
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.88	0.0	0	0	-5	0
Indonesian Rupiah		14125	0.1	1	2	0	2
Indian Rupee		69.35	0.0	0	0	-2	1
Argentine Peso		42.43	0.9	4	6	-36	-11
Brazil Real		3.83	-0.2	1	5	-2	1
Mexican Peso		19.23	-0.2	-1	-1	3	2
Russian Ruble		62.71	-0.2	2	3	0	11
South African Rand		14.30	0.5	2	1	-5	0
Turkish Lira		5.77	0.7	1	5	-19	-8
EM FX volatility		8.21	0.0	-0.2	-0.3	-1.4	-1.6

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

China

Chinese equities slumped and the RMB weakened against the dollar amid caution ahead the G20 summit and following US news reports that a number of Chinese banks had violated North Korean sanctions. The Shanghai Composite fell as much as 1.7% intraday before settling at -0.9% for the day, its first decline in 7 sessions. Bank shares were under particular stress following reports that a several Chinese banks, including China Merchants Bank, could suffer consequences from a US probe into North Korean sanctions violations. In addition, a number of large Chinese banks were found to be in contempt for failing to comply with subpoenas related to a probe into North Korean sanctions violations. China Merchants Bank, Bank of Communications, and Shanghai Pudong Development Bank fell by as much as 8.5% intraday before partially paring their losses. Shares of Merchants Bank ended the day 4.8% lower, its biggest loss since 2015.

Iran

Geopolitical tensions heightened as authorities in Iran said that the diplomatic path with the US was “closed”. The comments came following additional sanctions by the US, targeted at key officials. US Treasury secretary Mnuchin also announced that financial restrictions would be introduced against Javad Zarif, Iran’s foreign minister, later this week. A spokesperson for the foreign ministry said that the Trump administration was in the process of “destroying all the established international mechanisms for maintaining global peace and security”. Following the announcement of the new sanctions, president Trump declared that he had the authority to strike Iran without congressional approval.

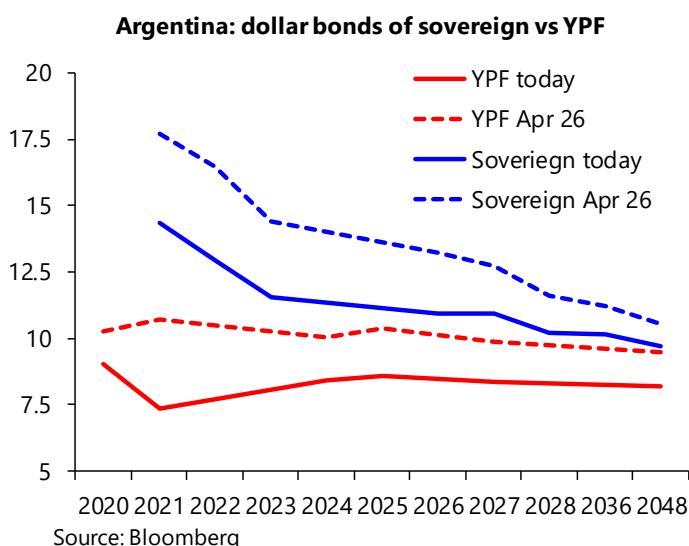
Korea

Comments from Bank of Korea Governor Lee reinforced expectations for a rate cut next month, though market reaction was limited. In the press briefing following the semi-annual review of its inflation target, BoK Governor Lee said inflation is expected to miss the central bank’s forecast of 1.1% for the year from April and will take longer to reach BoK’s 2% target. The Korean won was unchanged on the day, short-dated government bond yields edged higher (the 1-year note unchanged and the 2-year note up by 2 bps) while the Kospi shed 0.2%.

Argentina

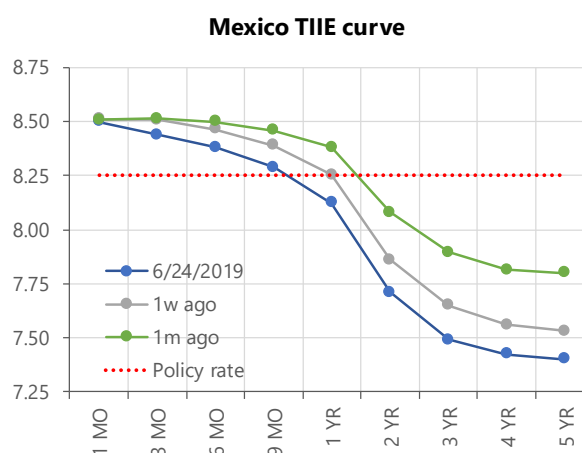
The Presidential campaign kicks off this week after candidates formally registered with the electoral court, while new polls show Fernandez narrowly leading. As widely expected, the candidates with the highest voter intentions are President Macri, Fernandez (former cabinet chief) and Lavagna (former economy minister), though Lavagna is currently trailing by a wide margin. The primary is scheduled on Aug 11, followed by the general election on Oct 27, with the runoff on Nov 24.

Argentina’s biggest oil company YPF is seeking to sell dollar bonds for the first time since 2017, as borrowing costs have declined. The state-controlled company is offering at least \$500 mn of 10-year dollar notes to yield a little over 9%, according to media reports, for refinancing and other general purposes. The yield on the firm’s 2021-dollar-note has dropped around 400 bps since April to 7.37% as Argentine bonds rallied after President Macri’s VP choice boosted his outlook for the election. The intended offer came despite the US Supreme Court rejecting appeals from Argentina and YPF, clearing the way for a shareholder lawsuit to move forward over the 2012 nationalization of YPF. The peso appreciated 0.8% against the dollar to 42.2.



Mexico

High core inflation and slowing growth complicates Banxico's monetary policy outlook. Annual inflation decelerated to 4% y/y in the first half of June, back to the inflation target, but core inflation remained stubbornly high, edging up to 3.9% y/y. Separately, the GDP proxy IGAE economic activity indicator contracted 1.4% y/y in April, well below the expected 0.4% y/y fall, and the weakest print since 2013. While the fall in annual inflation is a welcomed development, the combination of high core inflation and slowing growth is creating a difficult position for the central bank. Banxico is expected to remain on hold on Thursday, but investors will pay close attention to the board's view on the policy dilemma. The latest Citibanamex survey as of last week shows the central bank is expected to keep rate on hold until December, in line with what is priced in the interbank TIIE markets, where investors have successively been pulling forward the expected date of a rate cut. Yesterday, TIIE rates fell across the curve, led by the front end, following US rates lower. The MEXBOL index gained 0.5%, with the peso 0.3% weaker to 19.2.



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Global Financial Indicators

Last updated: 6/25/19 8:07 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		2945	-0.2	2	4	8	17
Europe		3447	-0.3	0	3	2	15
Japan		21194	-0.4	1	0	-5	6
China		2982	-0.9	3	5	4	20
Asia Ex Japan		69	0.1	5	6	-4	9
Emerging Markets		43	-0.8	4	7	-1	9
Interest Rates			basis points				
US 10y Yield		2.01	-4.0	-5	-31	-87	-68
Germany 10y Yield		-0.32	-1.3	0	-20	-65	-56
Japan 10y Yield		-0.16	-0.1	-3	-9	-19	-16
UK 10y Yield		0.81	-0.6	0	-15	-48	-47
Credit Spreads			basis points				
US Investment Grade		125	0.5	-5	-2	13	-23
US High Yield		441	1.1	-4	-4	97	-80
Europe IG		55	0.8	-1	-13	-18	-32
Europe HY		261	3.9	0	-34	-53	-92
EMBIG Sovereign Spread		348	1.0	-6	-16	-14	-66
Exchange Rates			%				
USD/Majors		96.07	0.1	-2	-2	2	0
EUR/USD		1.14	-0.1	2	2	-3	-1
USD/JPY		107.1	0.2	1	2	3	2
EM/USD		62.8	0.1	1	2	-3	1
Commodities			%				
Brent Crude Oil (\$/barrel)		65	-0.4	4	-6	-14	20
Industrials Metals (index)		113	1.0	1	0	-14	3
Agriculture (index)		43	0.9	1	8	-4	2
Implied Volatility			%				
VIX Index (% change in pp)		15.4	0.1	0.2	-0.5	-2.0	-10.1
10y Treasury Volatility Index		5.0	0.1	-0.4	0.7	0.9	0.4
Global FX Volatility		6.8	0.0	0.1	0.0	-1.2	-2.2
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		285	11.1	1	-63	-96	-131
Italy		250	4.0	7	-17	0	0
Portugal		82	-1.5	-3	-28	-69	-66
Spain		72	0.4	1	-22	-30	-46

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: 6/25/2019 8:12 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)							
	Level		Change (in %)					YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	Last 12m		Latest	1 Day	7 Days	30 Days	12 M		
	vs. USD		(+) = EM appreciation					% p.a.							
China		6.88	0.0	0.3	0	-5	0		3.2	-0.6	-1	-6	-37	5	
Indonesia		14125	0.1	1.4	2	0	2		7.6	2.7	-17	-48	-14	-56	
India		69	0.0	0.5	0	-2	1		6.9	0.4	-9	-37	-105	-50	
Philippines		51	0.1	1.2	2	4	2		5.0	-0.3	-5	-10	-57	-132	
Thailand		31	0.0	2.0	4	7	6		2.3	0.2	0	-26	-45	-36	
Malaysia		4.14	-0.1	0.9	1	-3	0		3.7	2.1	-4	-16	-56	-44	
Argentina		42	0.9	3.7	6	-36	-11		28.7	-24.4	-121	-482	983	572	
Brazil		3.83	-0.2	0.7	5	-2	1		6.9	1.2	-28	-110	-334	-126	
Chile		681	0.5	2.9	2	-6	2		3.4	2.9	-6	-68	-144	-106	
Colombia		3203	-0.3	2.2	4	-8	1		5.8	0.0	-17	-51	-64	-76	
Mexico		19.23	-0.2	-0.6	-1	3	2		7.7	-1.4	-11	-39	-6	-101	
Peru		3.3	0.0	1.4	1	-1	2		4.8	-0.4	-13	-43	-97	-95	
Uruguay		35	0.3	0.5	0	-11	-8		10.5	-5.8	-49	-77		-26	
Hungary		285	-0.4	1.3	2	-2	-2		1.6	-1.5	-11	-37	-95	-61	
Poland		3.74	-0.2	1.8	3	-1	0		2.0	-3.0	-5	-27	-51	-25	
Romania		4.1	-0.1	1.8	3	-4	-2		4.0	0.0	-11	-34	-67	-27	
Russia		62.7	-0.2	2.1	3	0	11		7.3	-3.2	-17	-44	-20	-114	
South Africa		14.3	0.5	1.6	1	-5	0		9.4	7.8	-6	9	0	-20	
Turkey		5.77	0.6	1.0	5	-19	-8		16.8	-32.0	-207	-441	13	-11	
US (DXY; 5y UST)		96.1	0.1	-1.6	-2	2	0		1.75	0.0	-9	-37	-100	-76	

	Equity Markets							Bond Spreads on USD Debt (EMBIG)							
	Level		Change (in %)					YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	Last 12m		Latest	1 Day	7 Days	30 Days	12 M		
									basis points						
China		2982	-2.0	3	5	4	20		180	0	0	2	-9	-14	
Indonesia		6320	-3.1	1	4	8	2		188	1	-7	-12	-22	-48	
India		39435	3.7	1	0	11	9		151	4	-4	-2	-8	-45	
Philippines		8034	0.3	1	4	15	8		74	0	-10	-12	-54	-47	
Malaysia		1677	0.6	1	5	0	-1		129	0	-2	2	-29	-33	
Argentina		40112	-4.0	-1	14	39	32		861	5	31	-44	312	46	
Brazil		102062	-3.1	4	9	44	16		236	1	-6	-22	-81	-37	
Chile		5091	-1.0	1	4	-4	0		133	0	-3	-2	-8	-33	
Colombia		1560	-2.1	2	5	2	18		183	3	-3	-15	-17	-45	
Mexico		43744	-2.2	2	3	-6	5		337	1	0	23	52	-17	
Peru		20750	-0.6	3	5	3	7		125	1	-2	-15	-44	-43	
Hungary		40136	-4.3	-2	0	14	3		84	0	-14	-21	-59	-64	
Poland		59699	-0.7	1	5	6	3		40	-2	-10	-10	-33	-45	
Romania		8633	7.5	1	5	8	17		179	4	-15	-27	7	-42	
Russia		2744	10.1	-1	5	23	16		205	2	-2	-4	-20	-47	
South Africa		58510	4.3	0	8	5	11		289	3	-14	-20	-10	-76	
Turkey		95861	-4.0	2	11	2	5		503	-6	-29	-51	80	74	
Ukraine		551	-2.2	0	-4	20	-1		531	13	-20	-116	-46	-256	
EM total		43	-0.9	4	7	-1	9		348	1	-6	-16	-14	-66	

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