



Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Friday, June 28, 2019












- Banks pass US CCAR, get greenlight for larger-than-expected capital payouts ([link](#))
- Brazil's CB further downgrades 2019 growth outlook ([link](#))
- Mexico kept policy rate unchanged but signals dovish shift ([link](#))
- US PCE inflation comes in slightly higher than expected ([link](#))

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Markets await G-20 trade talks

Investors remain squarely focused on US-China trade negotiations set to take place at the G-20 on Saturday. Markets were on edge yesterday and overnight as investors parsed conflicting signals about whether US Pres. Trump and Chinese Pres. Xi would insist on preconditions to resuming trade talks at this weekend's G-20 trade negotiation. One widely expressed investor view going into this weekend is that markets have largely priced-in a "kick the can down the road" scenario, but even this outcome looks vulnerable to disappointment given how positions have hardened on both sides. Equity markets are mixed this morning after rising about half a percentage point yesterday, with US equity futures pointing to a higher open. Bonds are little changed but yields have skewed slightly tighter.

Key Global Financial Indicators

Last updated: 6/28/19 8:09 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		2925	0.4	-1	4	8	17
Eurostoxx 50		3457	0.4	0	3	3	15
Nikkei 225		21276	-0.3	0	0	-4	6
MSCI EM		43	0.2	0	7	1	10
Yields and Spreads			bps				
US 10y Yield		2.01	-3.3	-4	-25	-82	-67
Germany 10y Yield		-0.33	-0.5	-4	-16	-64	-57
EMBIG Sovereign Spread		345	-1	2	-21	-25	-69
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		62.9	0.1	0	3	-3	1
Dollar index, (+) = \$ appreciation		96.2	0.0	0	-2	1	0
Brent Crude Oil (\$/barrel)		66.7	0.2	2	-5	-14	24
VIX Index (% change in pp)		15.8	0.0	0	-2	-1	-10

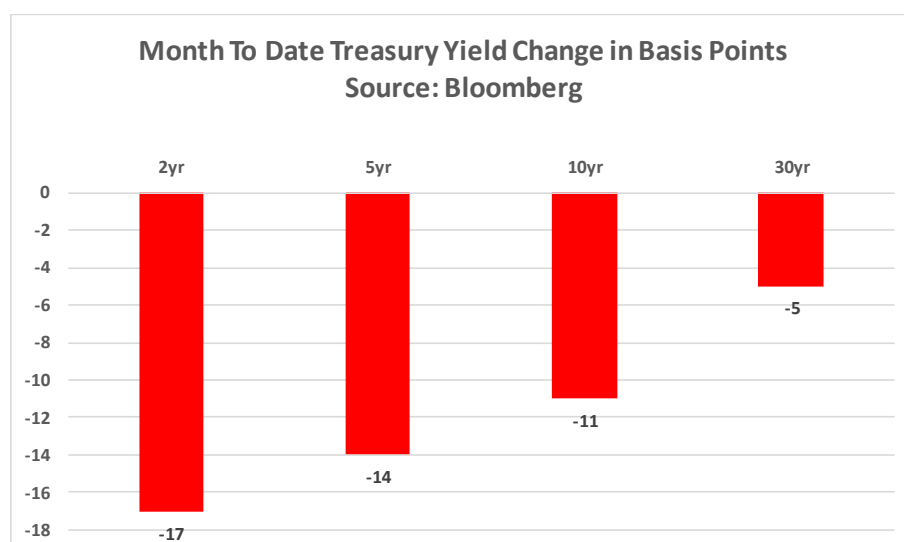
Colors denote **tightening/easing** financial conditions for observations greater than ± 1.5 standard deviations. Data source: Bloomberg.

United States

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The core PCE deflator, the Fed's favored inflation gauge, came in on target at 0.2% MoM while the annualized number was slightly stronger than expected at 1.6% YoY (vs. 1.5%). The headline numbers also met forecasts at 0.2% and 1.5% respectively. Personal income was stronger than expected at 0.5% (vs. 0.3%). Markets were little changed immediately following the data.

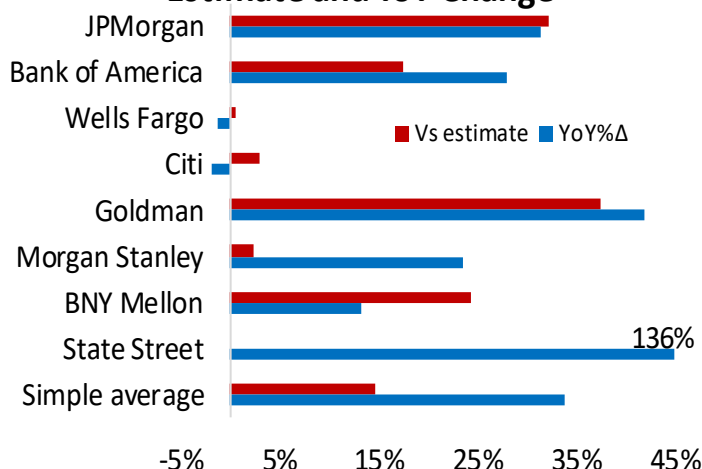
Stocks posted modest gains and Treasuries rallied, with the 10-year yield ending just above 2%. The seven-year note auction was reasonably well-received. With today marking the end of the quarter, most market participants will be involved in closing their books and marking their position, so activity will probably be light absent any negative news headlines. Meanwhile, expectations of a Fed rate cut have led to a rally in the Treasury market so far in June with a steepening of the yield curve as two-year yields have fallen much further than the long end. A slew of weaker than expected data releases appear to have reinforced the case for Fed action, especially in the housing sector and services and manufacturing PMIs. Markets are predicting that rates will be around 90 bps lower by the end of 2020, with two full rate cuts priced in this year.



Large banks passed the Fed's stress tests, qualifying for large capital payouts. All 18 systemic banks operating in the US received approval of their capital plans from Federal Reserve examiners in this year's Comprehensive Capital Analysis and Review (CCAR). The results were consistent with robust 'first-round' Dodd-Frank stress test (DFAST) results announced earlier this week and allows the largest US banks to proceed with capital payouts (dividends plus buybacks) that are in most cases far larger than in 2018 and well above market estimates. JPMorgan scaled back its initial request to the Fed after its DFAST results, but its payouts were still about 30% above last year's and one of only two such 'mulligans' (revisions), compared with six in 2018. Large foreign banks, also subject to CCAR examination, registered generally positive but somewhat more mixed results. This may reflect that these firms are applying to pay capital 'up' to their foreign parents rather than out to shareholders, and the Fed's judgement reflects an assessment of US rather than global financial and operating positions. Deutsche Bank surprised positively – its US subsidiary passed examination this year after failing three times in recent years. Credit Suisse was the only slight disappointment, receiving a "conditional non-objection", not strictly a failing grade but a mandate to address specific weaknesses before October 27th. Upon announcement of results, most US banks immediately announced a combination of dividend payout and share repurchase actions. The largest

US money-center and investment banks rose 1.8 – 2.6% in after-hours trading. Among foreign banks, Deutsche Bank is +2.4% and Credit Suisse +0.8% today.

US G-SIBs: 2019 Payout vs. Estimate and YoY Change

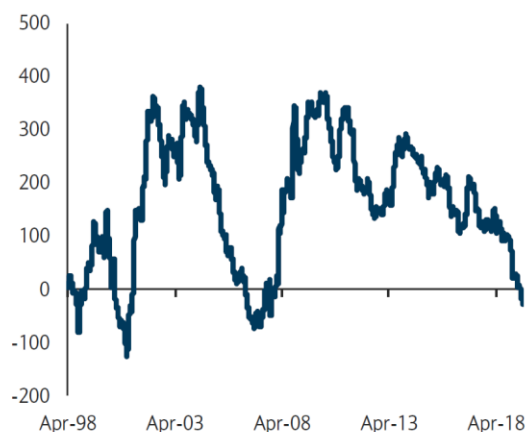


Source: Bloomberg

Inflows into US money market funds (MMFs) increased steadily after MMF reform was instituted in October 2016 but they have accelerated sharply since Fed policy turned dovish in October. The demand for MMFs is especially strong because short term money markets offer some of the most attractive yields in the US interest rate complex due to the partially inverted yield curve. The 10-year Treasury yield has fallen below the Secured Overnight Funding Rate (SOFR), the benchmark which US authorities have selected as the replacement for LIBOR, and all the T-Bill maturities (1/3/6/12 months) are also trading at yields above the 10-year. Inflows to MMFs are up \$300 bn, or 11% of assets under management since October. Weighted average maturities (WAMs) of MMF holdings have also shrunk as fund managers favored shorter maturities.

FIGURE 1

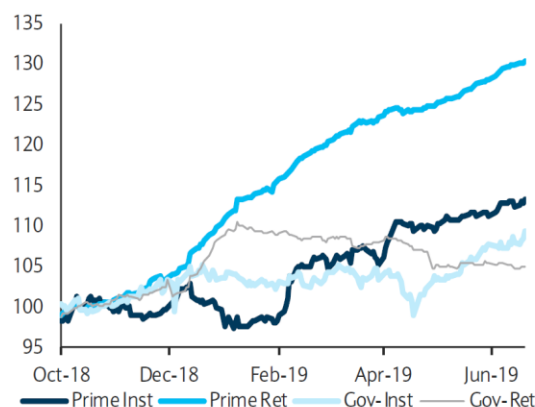
TSY 10y yield less overnight SOFR (bp)



Note: Pre-2014 values for SOFR are based on the NY Fed's daily dealer survey.
Source: Federal Reserve, Barclays Research

FIGURE 2

Money fund balances (October 2018=100)

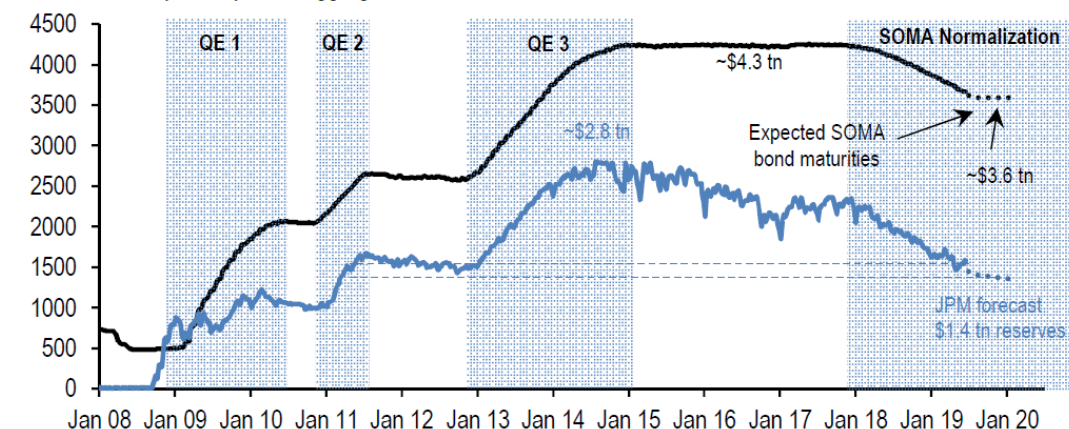


Source: Crane's Data, Barclays Research

Many expect the Fed to end balance sheet contraction at the time of the first rate cut, which markets think will occur at the next FOMC meeting on July 31. If that occurs, the Fed's balance sheet is expected to stabilize at roughly \$3.6 tn, or \$700 bn below the peak of \$4.3 tn at the end of 2017 before the start of normalization. This is equivalent to about 40% of what the Fed added to its balance sheet during QE3. The Fed's mortgage backed securities (MBS) holdings are expected to gradually roll off and be replaced by Treasuries. Few analysts expect any significant change in the average maturity of the Fed's bond portfolio.

Exhibit 9: We expect the balance sheet contraction will end with the first rate cut, BUT reserves will continue to contract

Historical and expected path of aggregate Fed balance sheet and reserves; \$bn



Source: J.P. Morgan

Europe

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European stocks are higher: EuroStoxx 600 (+0.2%), DAX (+0.5%), and CAC 40 (+0.1%). Bank stocks (+0.3%) are largely in line with major indices. **Euro area sovereign bond markets are steady**, with very small moves across countries and tenors. Ten-year yields in Germany at -0.31% (+1 bp); France at 0.00% (+1 bp); Spain at 0.39% (flat). Italian 10-years, however, dropped 5 bps to 2.08%, on rumors that the EC's Excessive Deficit Procedure against Italy could be delayed to the Fall.

Italy: Spreads to Other Sovereigns (in bps)



Source: Bloomberg
CFRTR1US Curncy (FRANCE CDS USD SR 5Y D14) FI: Ita-Periph Spreads Daily 01JAN20

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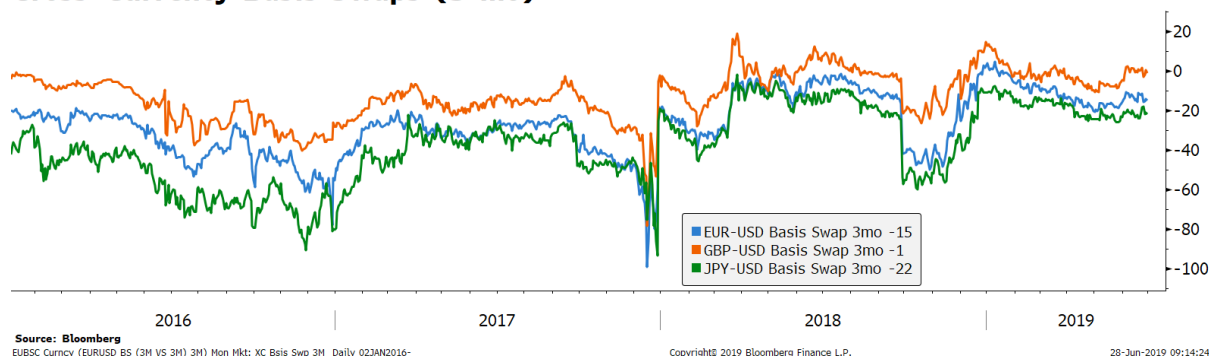
European credit markets have seen renewed volatility in recent months on the back of a more uncertain macro outlook. Corporate spreads have wavered since early-March as major central banks became more dovish, and optimism regarding an end to the global trade war ebbed. High-yield and investment grade credit spreads are now at 256 bps and 53 bps, respectively. These are similar levels

compared to a year ago. **In money markets, dollar funding conditions remain ample**, as measured by relatively tight cross-currency basis spreads among the major currency pairs.

European Corporate Credit Spreads



Cross-Currency Basis Swaps (3 mo)



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Japan







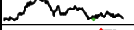


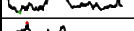



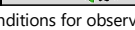
The yen held steady while equities softened as investors await the outcome of the U.S.-China meeting at the G-20 summit this weekend. The yen settled at JPY 107.7/dollar, partially reversing losses seen earlier in the week. In equities, the Topix shed 0.1%, with telecommunications and machinery makers shouldering the brunt of losses. Minutes from the June 19th- 20th BoJ meeting revealed one unnamed member's concern about lowering interest rates further as they approach the unfavorable "tipping point" – the level at which lower rates start to hurt the economy more than the benefits they confer. Meanwhile, the BoJ left its bond purchase amounts unchanged at its regular operation on Friday, including JPY 480 bn of 5-10 year notes and JPY 200 bn of 10-25 year bonds.

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Emerging market equities were mixed ahead of the highly anticipated U.S.-China summit on Saturday. Asian stocks suffered modest but broad-based losses. Volumes were limited with losses largest in Chinese bourses (Shanghai, -0.6% and Shenzhen, -1.0%). By contrast, Asian currencies appreciated relative to the dollar, with the Korean won (+0.3%) pacing gains while the offshore RMB, which held steady, underperformed. EMEA bourses were mixed, with outsized gains in Saudi Arabia (+1.3%) and smaller advances in the Czech Republic (+0.3%) and South Africa (+0.3%). Hungarian and Bulgarian stock indices led the regional losses, both dropping about 0.2%. Currencies were little changed. Latin American markets also traded within narrow ranges ahead of the weekend G20 meeting. In Mexico, interbank swap rates fell by 5 to 10 bps following a more dovish than expected policy communique (rate unchanged), while stocks in defensive sectors sold off, shedding 1% off the main Mexbol index. Argentine stocks rose 3% supported

by shares of YPF (+1.2%) and Pampa (+8%), after the two firms acquired a power plant from the state-run energy and power firm leasa.

Key Emerging Market Financial Indicators

Last updated: 6/28/19 8:16 AM	Level		Change				YTD
	Last 12m	index	1 Day	7 Days	30 Days	12 M	
Major EM Benchmarks			%				%
MSCI EM Equities		42.97	0.2	0	7	1	10
MSCI Frontier Equities		29.52	0.2	1	3	2	13
EMBIG Sovereign Spread (in bps)		344	-2	1	-22	-26	-70
EM FX vs. USD		62.89	0.1	0	3	-3	1
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.87	0.1	0	1	-4	0
Indonesian Rupiah		14126	0.1	0	2	2	2
Indian Rupee		69.03	0.1	1	1	0	1
Argentine Peso		42.70	0.0	2	5	-36	-12
Brazil Real		3.83	-0.1	0	5	1	1
Mexican Peso		19.18	0.0	0	0	3	2
Russian Ruble		62.93	0.2	0	3	0	10
South African Rand		14.17	0.0	1	4	-3	1
Turkish Lira		5.77	0.0	1	5	-21	-8
EM FX volatility		8.19	0.0	0.0	-0.2	-1.8	-1.6

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

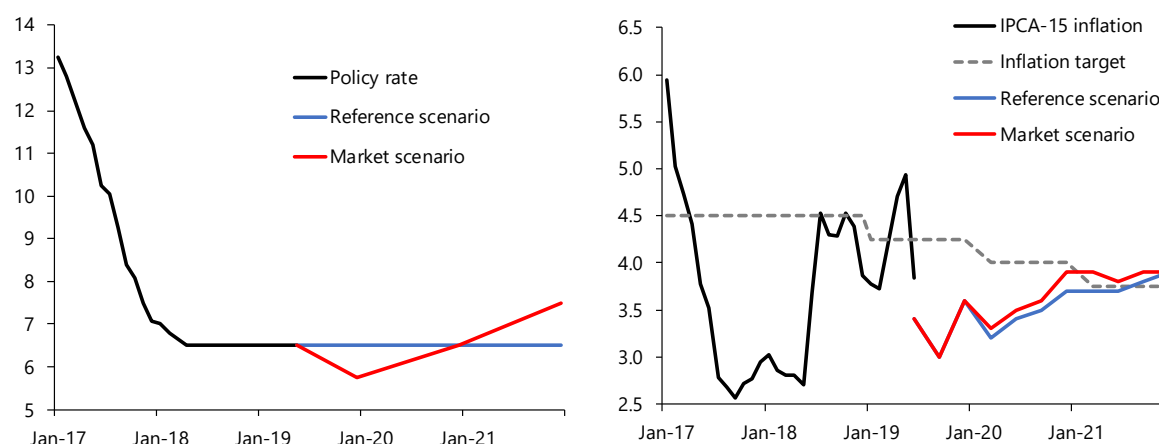
China

The RMB was little changed and equities fell as investors await the outcome of the Trump-Xi summit over the weekend. Expectations appear to coalesce around a positive statement with further negotiations extended beyond the G20. Still, uncertainties remain high. In an interview, President Trump said although it was "possible" that a trade deal between the US and China could ultimately be reached, he was also ready to proceed with additional tariffs on the remaining \$300 bn of Chinese exports if negotiations fail to get back on track. Meanwhile, the Wall Street Journal reported that President Xi plans to present a set of preconditions for ending the trade dispute, including removing the ban on the sale of US technology to Huawei as well as asking the US to lift all existing punitive tariffs and abandon efforts to ask China to buy more US goods than it previously agreed last December. The onshore CNY appreciated 0.2% on the day to CNY 6.866/dollar, its strongest level in a week; the offshore CNH held steady at CNH 6.871/dollar. Both the Shanghai and Shenzhen Composites reversed gains garnered in the previous session (-0.6% and -1%, respectively) and are little changed relative to levels seen earlier in the week.

Brazil

The central bank downgraded growth forecasts and projects below-target inflation until 2020, strengthening expectations of a mild easing cycle. The board lowered 2019 the growth forecast from 2% to 0.8% and sees a current account deficit of 1% of GDP, down from 1.6%. Inflation is expected to run below target until 2020 and rise above target in 2021. Overall, the report did not provide new information on the rate outlook, again highlighting the importance of reform for inflation and growth and that monetary policy is already accommodative, similar to the June meeting minutes. The central bank's "market scenario" - reflecting the market consensus - has the Selic rate falling to 5.75% by end 2019 and rising to 6.5% by end-2020 and 7.5% by end-2021. Financial markets closed little changed on the day.

Brazil: Key Scenario Assumptions in Q2 Inflation Report



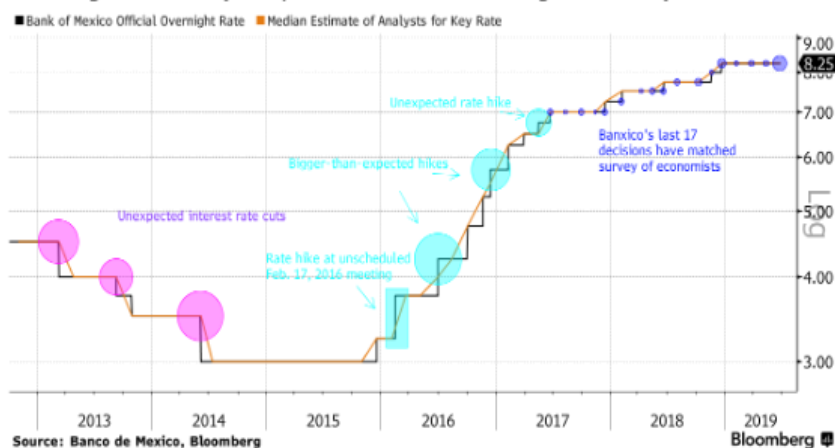
Note: 1/ scenario starts in 2019Q2. 2/ In the reference scenario, the policy and exchange rates are assumed to be constant (with the exchange rate at USD/BRL 3.85). In the market scenario, the USD/BRL rate is 3.8 in 2019, 3.9 in 2020 and 3.85 in 2021.

Mexico

Banxico left rate unchanged at 8.25% in a split vote, with a dovish shift in the communique. The rate decision was in line with expectations, but the decision was not unanimous as one member voted for a 25-bps cut. On the balance of risks, the board sees higher downside risk to growth, and remains cautious around inflation risks, a departure from the "upside risk" noted in the May statement. Overall, the statement struck a somewhat more dovish tone, but came short of signaling an imminent rate cut. Attention is now shifting to the August policy meeting, where analysts see a rate cut as now possible. TIE swap rates fell across the curve by 6 to 13 bps, still pricing the first rate cut in early Q4, but slightly larger easing cycle of 125 bps. The peso weakened slightly following the statement to close flat on the day at 19.17. The MEXBOL index dropped 1%, weighed by defensive sectors (utilities -4.7%, telecom -2.5%) reacting to lower rate expectations.

Steady Hand

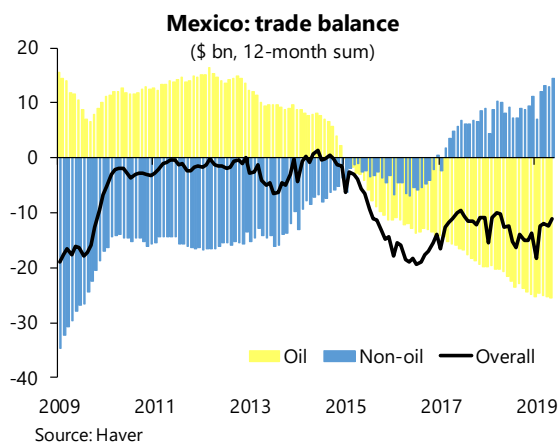
Following a run of surprises, Banxico's moves have aligned with expectations



Source: Banco de Mexico, Bloomberg

Bloomberg

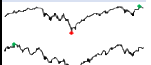
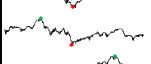
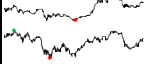

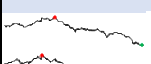
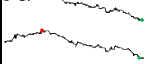
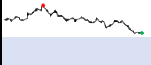
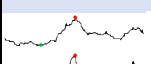
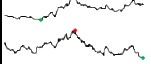
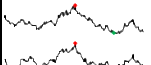






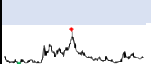
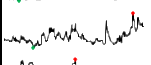

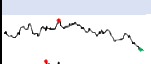
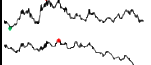
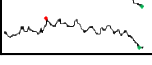
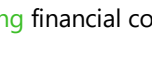





The trade balance surprisingly posted a large surplus in May despite further deterioration in oil balance. Trade balance came in at a \$1.03 bn surplus, while consensus forecast was for a \$1.03 bn deficit which was close to last May's \$1.55 bn deficit. On a 12-month basis, overall trade deficit is now tracking at \$9.5 bn, down from \$13.6 bn at end of 2018. The improvement in the past 12 months was driven exclusively by the non-oil surplus as the oil balance deficit widened, with both at record levels.



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Equities			%				%
United States		2925	0.4	-1	4	8	17
Europe		3457	0.4	0	3	3	15
Japan		21276	-0.3	0	0	-4	6
China		2979	-0.6	-1	2	7	19
Asia Ex Japan		70	1.0	0	7	-1	10
Emerging Markets		43	0.2	0	7	1	10
Interest Rates			basis points				
US 10y Yield		2.01	-3.3	-4	-25	-82	-67
Germany 10y Yield		-0.33	-0.5	-4	-16	-64	-57
Japan 10y Yield		-0.16	-1.7	0	-9	-19	-16
UK 10y Yield		0.82	0.0	-2	-10	-44	-46
Credit Spreads			basis points				
US Investment Grade		121	-1.4	-3	-6	10	-26
US High Yield		440	-2.1	4	-12	81	-81
Europe IG		52	-1.4	-2	-17	-23	-35
Europe HY		252	-4.0	-4	-45	-76	-100
EMBIG Sovereign Spread		345	-1.0	2	-21	-25	-69
Exchange Rates			%				
USD/Majors		96.17	0.0	0	-2	1	0
EUR/USD		1.14	0.1	0	2	-2	-1
USD/JPY		107.7	0.0	0	2	3	2
EM/USD		62.9	0.1	0	3	-3	1
Commodities			%				
Brent Crude Oil (\$/barrel)		67	0.2	2	-5	-14	24
Industrials Metals (index)		113	0.1	2	0	-13	3
Agriculture (index)		42	0.3	1	4	-4	1
Implied Volatility			%				
VIX Index (% change in pp)		15.8	0.0	0.4	-1.7	-1.0	-9.6
10y Treasury Volatility Index		4.8	0.0	-0.1	0.0	0.9	0.2
Global FX Volatility		6.7	0.0	0.1	0.0	-1.5	-2.3
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		277	-1.7	-6	-58	-96	-139
Italy		242	-3.5	-1	-42	-4	-8
Portugal		81	1.1	-5	-27	-70	-67
Spain		73	1.5	1	-22	-31	-44

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: 6/28/2019 8:17 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		6.87	0.1	0.0	1	-4	0		3.3	0.2	1	-7	-35	7
Indonesia		14126	0.1	0.2	2	2	2		7.5	-3.3	-4	-56	-48	-65
India		69	0.1	0.8	1	0	1		7.0	-0.8	10	-28	-104	-45
Philippines		51	-0.1	0.5	2	4	2		4.9	-3.9	-11	-20	-71	-141
Thailand		31	0.4	0.5	4	8	5		2.3	2.6	3	-28	-38	-37
Malaysia		4.13	0.3	0.4	1	-2	0		3.6	-0.8	0	-17	-58	-45
Argentina		43	0.0	1.5	5	-36	-12		28.0	-18.7	-152	-558	892	496
Brazil		3.83	-0.1	-0.1	5	1	1		6.9	-0.1	-17	-103	-317	-123
Chile		680	0.0	0.5	3	-5	2		3.4	-1.0	5	-66	-142	-105
Colombia		3198	-0.4	-0.1	5	-8	2		5.7	-0.7	4	-52	-68	-77
Mexico		19.18	0.0	-0.3	0	3	2		7.6	-10.5	2	-47	-11	-108
Peru		3.3	0.1	0.6	2	-1	2		4.9	3.3	13	-33	-79	-85
Uruguay		35	0.0	0.0	-1	-11	-8		10.4	-10.1	-46	-81		-31
Hungary		284	0.2	0.3	3	0	-1		1.6	0.6	6	-33	-90	-57
Poland		3.73	0.1	0.3	3	1	0		2.0	1.9	2	-23	-51	-22
Romania		4.2	-0.2	-0.1	3	-3	-2		4.1	9.0	8	-25	-77	-18
Russia		62.9	0.2	0.2	3	0	10		7.3	-0.2	6	-42	-25	-111
South Africa		14.2	0.0	1.2	4	-3	1		9.3	-0.8	6	-5	-16	-30
Turkey		5.77	0.0	0.8	5	-21	-8		16.8	15.8	-26	-438	-6	-7
US (DXY; 5y UST)		96.1	-0.1	-0.1	-2	1	0		1.77	0.0	-2	-30	-94	-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		2979	0.2	-1	2	7	19		180	4	1	5	-9	-14
Indonesia		6359	1.7	1	5	12	3		186	-4	3	-15	-31	-50
India		39395	-0.1	1	-1	12	9		150	3	-1	-3	-13	-46
Philippines		8000	0.1	-1	3	13	7		79	-4	9	-7	-54	-42
Malaysia		1672	2.0	-1	4	0	-1		127	2	-2	3	-33	-35
Argentina		41128	-0.4	3	19	54	36		847	-2	22	-73	256	32
Brazil		100724	-0.7	0	4	40	15		234	-2	1	-25	-90	-39
Chile		5074	-0.3	0	6	-3	-1		135	4	3	0	-11	-31
Colombia		1548	0.3	0	6	-1	17		182	-2	6	-17	-19	-46
Mexico		43317	-0.8	-1	3	-8	4		331	-1	0	16	46	-23
Peru		20666	0.2	0	5	4	7		125	-1	7	-17	-47	-43
Hungary		40417	-0.4	0	0	15	3		90	-2	7	-11	-56	-58
Poland		60190	1.9	1	6	9	4		41	7	3	-7	-32	-44
Romania		8798	3.5	1	3	10	19		183	4	1	-22	5	-38
Russia		2776	1.3	1	6	23	17		206	0	7	-4	-17	-46
South Africa		58166	0.0	-1	7	4	10		282	-3	2	-26	-37	-83
Turkey		96252	6.0	2	11	0	5		473	-7	-43	-79	56	44
Ukraine		542	-1.9	-2	-6	17	-3		507	0	-9	-147	-101	-280
EM total		43	0.2	0	7	1	10		344	-2	1	-22	-26	-70

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