GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

MONDAY, JUNE 17, 2024

LEAD EDITOR: ESTI KEMP

- **French government bond spreads expected to remain elevated on election uncertainty** (link)
- **Some analysts see the sell-off in French banking sector stocks as overdone** (link)
- **Treasury yields fell to 3-month** (link)
- **People's Bank of China kept the 1-year MLF rate unchanged at 2.5% as expected** (link)
- **Colombia's widening fiscal deficit target weigh on assets** (link)
- **Special Feature: Q1 2024 Corporate Earnings Monitor** (attached)

Mature Markets | Emerging Markets | Market Tables

Sentiment remains fragile ahead of central bank policy decisions

European equity markets remain under pressure while bonds yields stabilize somewhat. France remains in the spotlight after President Macron's announcement of a snap election last week triggered a surge in the risk premium on French assets while European equities closed the week sharply lower. This morning remarks from French far-right leader, Marine Le Pen, that her party would "respect political institutions" if it wins in the upcoming election provided some calm to markets, but European equity markets trimmed gains later in the session. While sovereign yields edged higher this morning, markets remain focused on the French-German spread dynamic, with the spread continuing to increase marginally this morning. Contacts expect the spread to remain wide in the near-term, but see limited contagion risk at this stage and ECB sources reportedly said that there are no plans to discuss support of French debt. On the policy front, the People's Bank of China kept its one-year medium term lending facility rate unchanged at 2.5%, as expected.

Key Global Financial Indicators

Last updated: 6/17/24 1:04 PM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
S&P 500		5432	0.0	2	2	23	13.87
Eurostoxx 50		4865	0.5	-3	-4	11	8
Nikkei 225		38102	-1.8	-2	-2	13	14
MSCI EM		42	0.1	0	-4	3	5
Yields and Spreads				bps			
US 10y Yield		4.26	3.5	-21	-16	49	38
Germany 10y Yield		2.42	6.4	-25	-9	-5	40
EMBIG Sovereign Spread		394	4	9	24	-50	11
FX / Commodities / Volatility				%			
EM FX vs. USD, (+) = appreciation		45.9	0.0	0	-3	-8	-5
Dollar index, (+) = $ appreciation		105.6	0.0	0	1	3	4
Brent Crude Oil ($/barrel)		82.9	0.4	2	-1	8	8
VIX Index (%, change in pp)		13.1	0.4	0	1	0	1

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

In the coming week, political development in Europe will continue to dominate market focus as France kicks off the official election campaign. It will also be a busy week of policy rate decisions which are scheduled in Australia, Brazil, Chile, China, Hungary, Indonesia, Norway, Paraguay, Switzerland, and the UK. The majority of these central banks are expected to hold, while Hungary and Chile are expected to cut their respective policy rates by 25 bps each. On the data calendar, key data to watch include retail sales and industrial productions from China (Mon) and the US (Tue), UK CPI (Wed) ahead of the BoE decision (Thu), May HICP and PMIs from the euro area, and CPI from Japan (Thu).

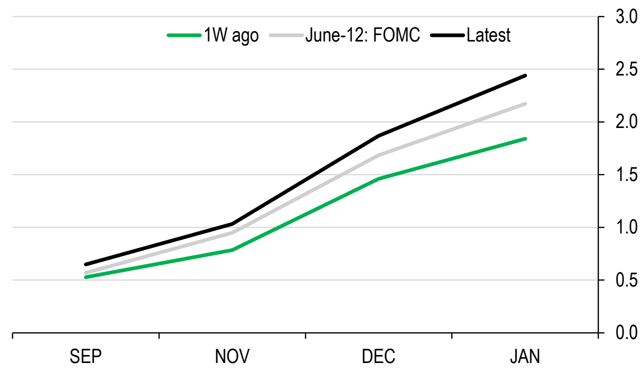
Mature Markets

back to top

United States

Treasury yields fell to a 3-month low as softer inflation data and political uncertainty in Europe outweigh the slightly more hawkish FOMC meeting. The latest Dot Plot from the FOMC meeting last Wednesday shows one rate cut in 2024 (down from 3 in March) and four rate cuts each in the next two years, keeping the total rate cuts at nine, but with a later start and faster catch-up. However, this differs from market expectations: by the end of last week, **OIS markets were still pricing in two rate cuts by year-end, with the first rate cut in November.** Investors seem to focus more on the string of softer inflation data in May (core CPI, PPI and import prices) that could indicate a further decline in the core PCE to an expected 2.6% y/y from 2.8% in April. Meanwhile, the political uncertainty from the French snap election has also pushed yields lower, especially in the latter half of last week, and is expected to remain a focus in the markets for the next two weeks.

OIS-implied Number of Rate Cuts in 2024

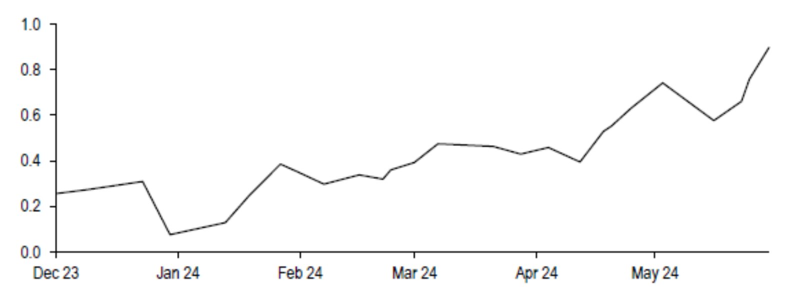


Source: Bloomberg.

Softer US inflation data together with Fed's commentary have further reduced the tail risk of additional rate hikes. Over the last week, investors have significantly pared back the expectations of a potential rate hike scenario, supported by the softer inflation data, the acknowledgement of "modest further progress" on inflation in the FOMC statement and Chair Powell's comment that rate hikes were not the base case expectation of any committee member**. In response, investors in the option markets are now pricing less than 10% of probability of additional rate hike, down from a recent peak of 30% in late April**.

Figure 1: The beginnings of policy clarity, at least in the near term

Total weight for scenarios ranging from an unchanged funds rate to 3 25bp cuts, as calculated from a decomposition of the implied probability distribution associated with Dec 2024 SOFR futures*; Dec 2023 - Current



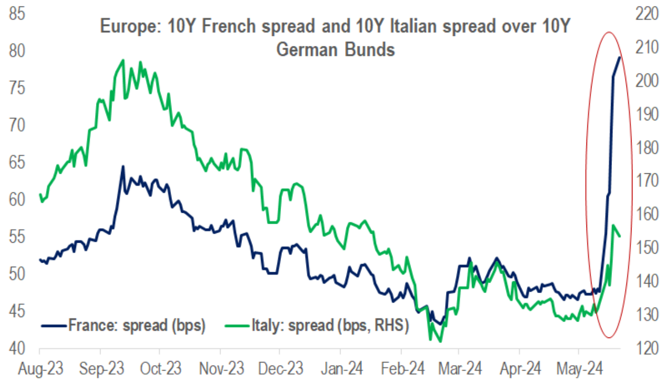
Source: J.P. Morgan., CME

* We enumerate a list of scenario-specific Normal distributions with fixed standard deviations and means that are separated by 25bp, and then require the implied distribution to be a weighted combination of these individual distributions. The weights are then solved for, by fitting to the observed prices of calls and puts at various different strikes. For more details of our approach, see What's the rush?

Euro Area

Markets remain volatile amid on-going political uncertainty. This morning, European equities opened in the green with the Stoxx 600 index +0.2% in early morning trade, only to reverse course by mid-morning, with the index around -0.3% lower. Meanwhile, European banking sector shares opened 0.1% higher. France's CAC 40 Index was also briefly trading in the green, although last week's sell-off leaves the index 0.6% lower on a year-to-date basis. The euro was broadly unchanged against the dollar at 1.0704 this morning after closing 0.9% weaker last week. Meanwhile, market expectations for ECB rate cuts have increased with markets pricing in around 44bps of easing over the remainder of 2024, up from around 32bps priced last Monday.

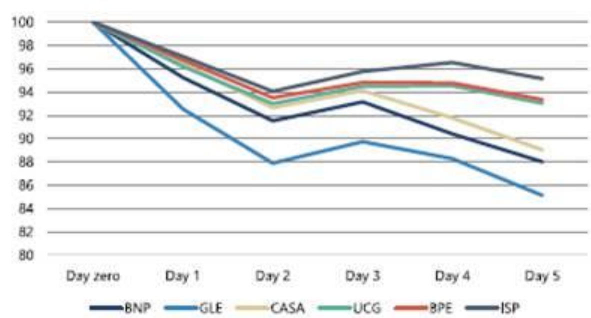
French government bond spreads expected to remain elevated on election uncertainty. This morning, the 10Y French OAT spread over 10Y German bunds climbed a further 4bps to 81bps. According to Bloomberg, the move this morning is partly due to a change in the underlying benchmark bond, rather than further selling pressure. Market participants expect the 10Y French OAT spread over 10Y German bunds to remain elevated in the near-term given the uncertainty around the political outcome in upcoming elections. Analysts at Credit Agricole note that comments by Marine Le Pen suggesting that her party will scale back spending plans might reassure investors and help to stabilize the spread in the near-term, although they note that "the road [ahead] is still long." **Contacts note limited signs of contagion and this morning the Italian 10Y BTP spread over 10Y German Bunds declined by 1bps to 156bps**.



Source: Bloomberg and IMF calculations

Analysts at Jefferies believe the sell-off in French banking sector stocks looks overdone. Jefferies analysts attribute the recent sell-off in French bank stocks to the market "discounting the snap election as a very risky move from Macron" which could result in a significant shift in the political landscape given recent EU election outcomes. However, the analysts note that French banks have sold off much more than Italian banks did in 2022 when there were similar domestic political dynamics at play in Italy following the election of Giorgia Meloni's right-wing/center-right coalition party. Drawing parallels to the subsequent rally in Italian banks after Meloni's election in 2022, the analysts reiterate their "buy" stance on French banks and view the recent sell-off as a buying opportunity.

Exhibit 7 - French banks vs Italian banks reactions in the following trading days
"Day zero" for French banks corresponds to the Friday 7 June 2024 (last trading day before the dissolution of the National Assembly) while for italian banks, it corresponds to the Thursday 18 August 2022 when the poll showing the far-right bloc leading was released.



Source: Jefferies, Factset

Japan

Japanese equities fell on rising global risk aversion. Japanese stocks (NIKKEI: -1.8%) fell on concerns over political uncertainty in France. Meanwhile, long-end JGB yields were mixed, with the 10-year yield falling to 0.927% (-0.8 bp) while the 30-year yield rising to 2.119% (+2.2 bps). Analysts noted that global risk-off sentiment boosted demand for JGBs. However, traders became more cautious about buying JGBs after the Bank of Japan announced a reduction of JGB purchases without providing figures or timeline at its June monetary policy meeting last Friday. Japanese yen depreciated to 157.6 yen per dollar (-0.1%). On the data front, **core machine orders declined 2.9% m/m in April** (consensus: -3.0%).

Emerging Markets

back to top

EMEA equities and currency markets were mixed. In CEE, the stock market outperformed in Poland, while currencies edged higher against the euro. The Hungarian forint outperformed (+0.6%) to trade at 396.11/€, after today's data showed a larger than expected decline of producers prices' growth in May (1%y/y in May, vs est. 2%, from 1.4%y/y in April). In Türkiye, the lira weakened (-0.2%) against the dollar to trade at 32.85/$, while the South African rand outperformed against the dollar (+0.8% at 18.24/$), extending Friday's gains after President Ramaphosa was reelected. **Asian markets retreated today amid global risk-off sentiment triggered by concerns around political uncertainty in France**. While many markets were closed in the region, Asian equities declined, **falling 0.1% on net while** Asian currencies were marginally weaker. Long-end government bond yields generally declined, with 10-year yields falling in China (-3.2 bps) and Korea (-2.3 bps). **Latin American currencies mostly depreciated against the dollar and equities were mixed to end the week.** The Chilean peso (-1.9%) underperformed the region, while the Colombian peso bucked trend (+0.2%). Equities in Chile (+0.3%) and Brazil (+0.1%) advanced while equities in the rest of the region retreated.

EM Fund Flows

Outflows from EM bond and equity funds have exceeded the inflows recorded from the prior week. Bond fund outflows (-$1.5bn from +$596mn) were driven by an increase in hard and local currency funds (-$866mn and -$650mn). Equity fund outflows increased (-$119mn from -$110mn), with outflows in ETFs (-$574mn) partially offset by non-ETF inflows (+$455mn). Regionally, Asia ex-Japan (+$719mn) and Latam (+$160mn) saw inflows, while EMEA (-$55mn) had outflows.

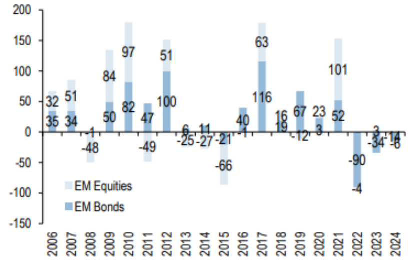
Figure 1: Weekly cross-asset flows

USD billion

Fund Flows	Asset	8w flows (8w ago → current)	This wk	YTD
	EM Bonds and Equities		-1.6	-20.6
	EM Bonds		-1.5	-14.5
	Hard Ccy		-0.9	-7.0
	Local Ccy^		-0.6	-7.5
	o.w. EM ex-China		-0.6	-6.5
	o.w. China		0.0	-1.0
	EM Equities		-0.1	-6.1
	US HG		2.6	159.4
	US HY		0.5	10.1
	Global Equities		-0.1	65.5
	EM Bond and Equity ETFs		-0.5	12.9
	EM Bond ETFs		0.1	-1.9
	EM Equity ETFs		-0.6	14.8
	Non-resident EM flows*		-1.5	11.3

Figure 2: EM bond and equity fund flows

USD billion

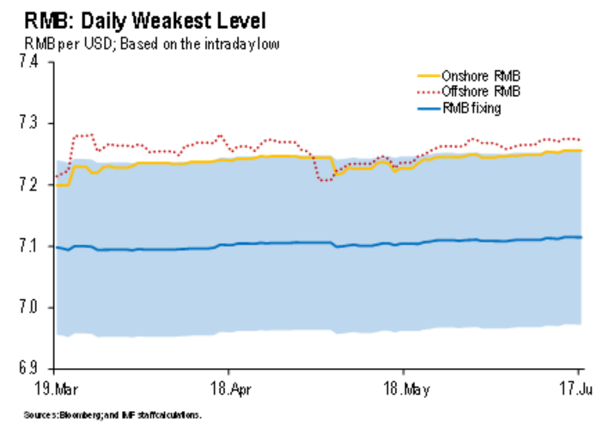


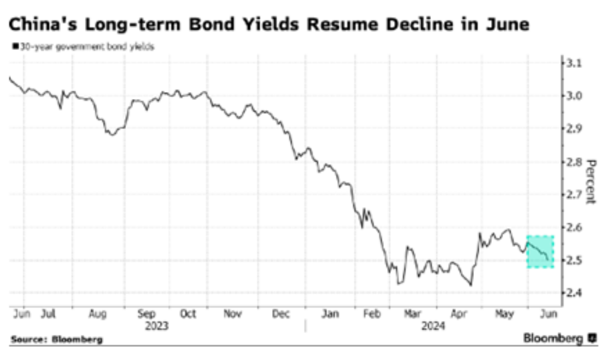
*High-frequency non-resident EM portfolio flow data where available. ^Local ccy split is retail only. Source for all charts and data in this report: J.P. Morgan, EPFR Global, Bloomberg Finance L.P.

China

The People's Bank of China (PBC) kept the 1-year medium-term lending facility (MLF) rate unchanged at 2.5% as expected. The PBC also provided MLF funding in an amount of 182 bn yuan ($25.1 bn), effectively withdrawing liquidity of about 50 bn yuan ($7.0 bn). The decision came after credit growth further moderated in May. Analysts noted that the PBC's reluctance to cut interest rates was mainly due to concerns about banks' net interest margin and depreciation pressures on Chinese renminbi. The latter factor is driven by the interest rate differential and uncertainty around the Federal Reserve's rate cuts. **RMB was little changed at 7.26 yuan per dollar.** The PBC continued setting the daily RMB fixing stronger than expected to anchor market expectations, with the deviation from market consensus amounting to 1,419 pips, as RMB continued trading near the limit (i.e., 2% from the daily fixing). **Long-end CGB yields dropped (**10-year: -3.2 bps), with the 10-year yield falling to 2.26%, as Chinese state media ramped up warnings against the bond market rally amid signs that the frenzy to buy CGBs is returning.

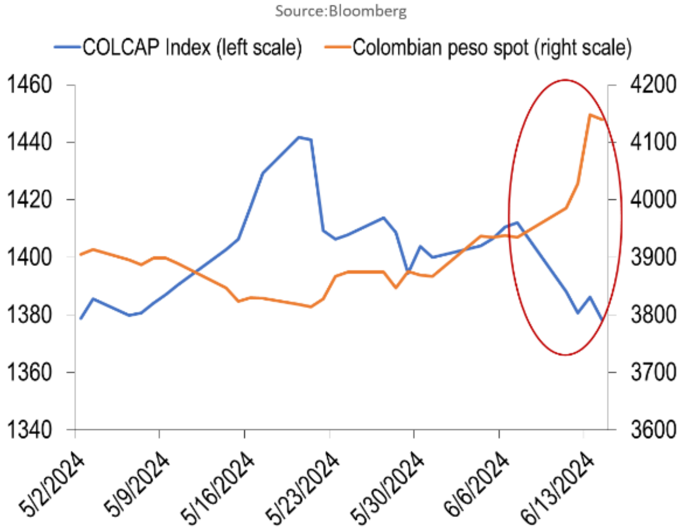
On the data front, **May activity data generally came out weaker than expected,** with disappointing data on industrial production and fixed asset investment. One exception was retail sales, which grew 3.7 percent y/y (consensus: +3.0%). Industrial production expanded 5.6% y/y (consensus: +6.2%), while fixed asset investment YTD increased 4.0% y/y (consensus: +4.2%). **There are no signs for property market stabilization following the last round of policy support measures announced in mid-May**. Property investment YTD fell 10.1% y/y (consensus: -10.0%), and housing sales and home prices continued falling in May. Chinese equities declined (CSI 300: -0.2%), led by real estate stocks (-1.9%).





Colombia

Investor concerns over Colombia's widening fiscal deficit have dragged assets down. Over the past week, the Colombian peso (-5.0%) has been the worst performing EM currency and its main equity index, COLCAP Index (-2.4%), has underperformed Latin America. Colombia revealed Friday its new 2024 target fiscal deficit of 5.6% of GDP, up from the previous target of 5.3%. Bloomberg analysts note that 5.6% would be the widest fiscal deficit since the pandemic, driven by falling tax revenues. Despite the higher deficit target, the peso (+0.2%) marginally recovered as the presentation of the fiscal plan highlighted the government's commitment to the fiscal rule.



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Global Financial Indicators

6/17/24 1:05 PM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		5439	0.0	1	3	23	14
Europe		4865	0.5	-3	-4	11	8
Japan		38102	-1.8	-2	-2	13	14
China		3536	-0.2	-1	-4	-11	3
Asia Ex Japan		72	0.1	1	-2	4	8
Emerging Markets		42	0.1	0	-4	3	5
Interest Rates					basis points		
US 10y Yield		4.25	3.5	-21	-17	49	37
Germany 10y Yield		2.42	6.4	-25	-9	-5	40
Japan 10y Yield		0.94	-0.9	-11	-1	52	32
UK 10y Yield		4.09	3.7	-23	-3	-32	56
Credit Spreads					basis points		
US Investment Grade		126	2.3	7	8	-34	-8
US High Yield		365	-4.4	15	24	-81	-20
Exchange Rates					%		
USD/Majors		105.56	0.0	0	1	3	4
EUR/USD		1.07	0.1	-1	-1	-2	-3
USD/JPY		157.9	0.3	1	1	11	12
EM/USD		45.9	0.0	0	-3	-8	-5
Commodities					%		
Brent Crude Oil ($/barrel)		83.0	0.4	2	-1	13	9
Industrials Metals (index)		149	-1.1	-3	-11	0	5
Agriculture (index)		59	-1.3	-1	-2	-18	-6
Implied Volatility					%		
VIX Index (%, change in pp)		13.1	0.4	0.3	1.1	-0.5	0.6
Global FX Volatility		7.8	0.1	0.5	1.0	-0.2	-0.3
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		125	-4.0	15	25	-6	21
Italy		152	-4.7	12	22	-4	-15
Portugal		75	-4.8	11	13	12	12
Spain		90	-3.5	13	14	-1	-7

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

Emerging Market Financial Indicators

Last updated: 6/17/2024 1:07 PM	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		7.26	0.0	-0.1	0	-1	-2		2.2	1.5	2	-3	-56	-29
Indonesia		16400	-0.8	-1.3	-2	-9	-6		7.2	21.3	30	17	94	72
India		84	0.0	-0.2	0	-2	0		7.3	0.0	-5	-13	(19.8)	4
Philippines		59	-0.1	-0.2	-1	-5	-6		5.4	0.0	-16	-16	-58	-27
Thailand		37	-0.1	0.0	-2	-5	-7		2.8	0.8	-6	-1	-5	8
Malaysia		4.72	-0.2	-0.6	0	-2	-3		3.9	0.0	0	0	12	13
Argentina		903	-0.1	-0.4	-2	-73	-10		43.2	20.1	-149	582	-6726	-4315
Brazil		5.40	-0.4	-0.8	-5	-11	-10		12.1	4.7	7	32	84	170
Chile		935	-1.9	-1.6	-2	-14	-6		5.2	0.0	-8	5	13	26
Colombia		4139	0.2	-5.0	-7	1	-7		8.3	0.0	13	32	40	70
Mexico		18.56	-0.5	-1.7	-11	-8	-9		9.7	0.5	-1	52	135	121
Peru		3.8	-0.3	-0.8	-2	-3	-2		7.0	-0.2	-5	-2	-5	37
Uruguay		39	0.1	-0.4	-1	-2	-1		9.2	2.4	5	8	-66	-30
Hungary		370	0.6	-1.3	-4	-8	-6		6.6	0.0	0	6	-112	80
Poland		4.07	0.6	-1.3	-4	0	-3		5.2	1.8	-6	8	-12	75
Romania		4.6	0.1	-0.5	-1	-2	-3		6.6	3.3	-3	9	3	41
Russia		88.7	1.0	0.1	3	-5	1							
South Africa		18.3	0.6	2.4	-1	0	0		9.4	0.0	-16	-22	-48	31
Türkiye		32.86	-0.2	-1.5	-2	-28	-10		28.6	-3.0	64	133	1083	182
US (DXY; 5y UST)		106	0.0	0.4	1	3	4		4.26	2.4	-22	-18	28	42

	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		3536	-0.2	-1	-4	-11	3		138	4	-2	-46	-20
Indonesia		6735	0.0	-2	-8	1	-7		107	15	7	-35	11
India		76993	0.0	0	4	21	7		95	3	2	-36	-21
Philippines		6384	0.0	-2	-4	-2	-1		93	11	3	-20	13
Thailand		1297	-0.8	-2	-6	-17	-8		0	0	0	0	0
Malaysia		1607	0.0	-1	-1	16	10		80	2	1	-13	-5
Argentina		1582372	-1.4	4	7	286	70		1386	-202	138	-964	-527
Brazil		119662	0.1	-1	-7	1	-11		233	13	15	-15	18
Chile		6518	0.0	-2	-2	14	5		125	6	9	-4	0
Colombia		1378	-0.6	-2	-4	17	15		325	24	30	-28	54
Mexico		52223	-0.1	-1	-9	-5	-9		323	15	27	-64	-11
Peru		29200	0.0	-1	-3	29	12		156	4	12	-12	12
Hungary		69701	0.2	-1	2	39	15		164	19	16	-60	15
Poland		85086	1.4	0	-4	25	8		107	13	8	-27	10
Romania		17791	0.5	0	2	45	16		204	20	22	-35	3
South Africa		77054	0.0	0	-3	-2	0		323	-15	-6	-70	15
Türkiye		10471	0.0	3	-2	91	40		301	19	20	-163	-13
EM total		42	0.2	0	-4	3	5		385	2	57	-3	40

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

back to top