GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

TUESDAY, MARCH 14, 2023

- **US inflation largely in line with expectation** (link)
- **Expectations for US policy rate tightening collapse** (link)
- **Contagion to US regional banks intensified on Monday** (link)
- **Japanese yields lower as pressure on Bank of Japan to tighten eases** (link)
- **Markets revise ECB terminal rate sharply lower ahead of Thursday's meeting** (link)
- **UK labor market remains tight** (link)
- **Analysts see low risk of SVB-like liquidity event in Central and Eastern Europe** (link)
- **Hold-to-maturity embedded losses seen as manageable for large Brazilian banks** (link)
- **Special Feature: 2022 Q4 Corporate Earnings Monitor (attached)**

Mature Markets | Emerging Markets | Market Tables

Mixed markets after a hectic Monday

Markets were mixed after bank shares in the US and Europe sold off sharply and core rates recorded moves not seen in decades yesterday. For example, the US 2-yr yield realized the largest one-day decline since Black Monday in 1987 as contagion from the failure of Silicon Valley Bank spreads to regional banks and other US financial institutions. The new terminal rate for the Fed is less than one hike above the current rate. In contrast, most analysts still expect the ECB to hike 50 bps on Thursday with traders pricing slightly less than that. Japanese bank stocks have underperformed their Asian peers in recent days. Chinese markets have been relatively insulated from the global turmoil so far, with limited movements of onshore bond yields and credit spreads so far. Most emerging market currencies have also been stable. The rise in spreads on investment-grade EM Eurobonds has been muted but many frontier markets saw a spike in yields.

Key Global Financial Indicators

Last updated: 3/14/23 11:43 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		3856	-0.2	-5	-7	-8	0
Eurostoxx 50		4125	0.7	-4	-3	10	9
Nikkei 225		27222	-2.2	-4	-1	7	4
MSCI EM		38	0.2	-4	-6	-9	0
Yields and Spreads			bps				
US 10y Yield		3.62	4.7	-34	-12	149	-25
Germany 10y Yield		2.36	9.6	-34	-8	199	-22
EMBIG Sovereign Spread		486	12	44	38	-11	34
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		50.1	0.1	0	-1	-1	0
Dollar index, (+) = $ appreciation		103.8	0.2	-2	1	5	0
Brent Crude Oil ($/barrel)		79.4	-1.8	-5	-7	-26	-8
VIX Index (%, change in pp)		26.2	-0.3	7	7	-6	5

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

Mature Markets

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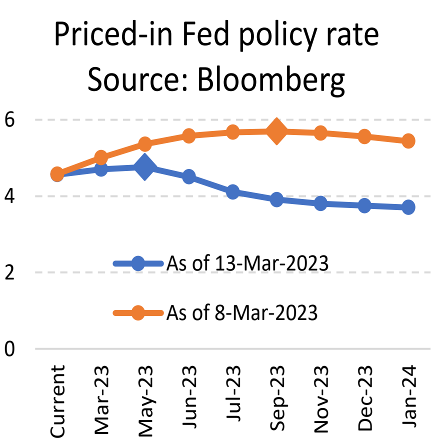
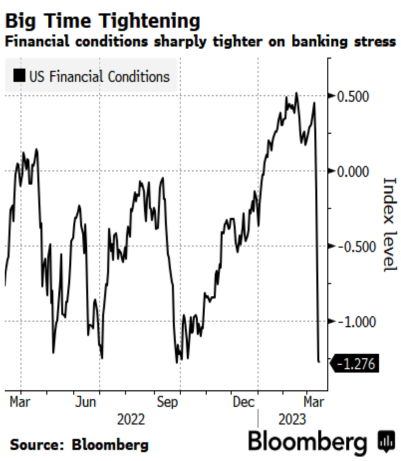
United States

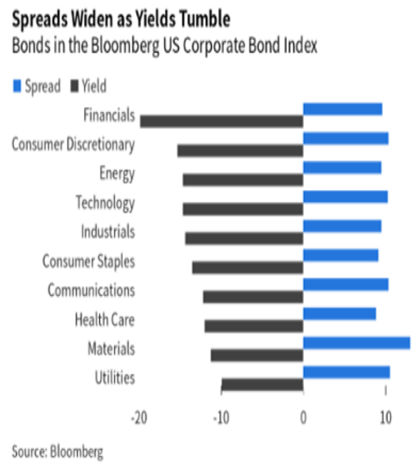
US CPI data for February released this morning was exactly in line with expectations, except for monthly core CPI, which was higher than expected. *Headline* inflation was posted at 0.4% MoM and 6.0% YoY; core CPI 0.5% MoM (vs 0.4% expected) and 5.5% YoY. Contacts have low conviction on whether today's reading will outweigh the financial stability concerns during the next FOMC meeting. Market reaction seemed muted on impact.

Yesterday, S&P 500 fell by -0.2%: most of the sectors posted modest gains, outweighed by large drops in the contagion-driven financial sector (-3.8%) and energy stocks (-2.0%). Markets dramatically revised the priced-in path of the Fed policy rates, implying a much lower terminal rate (4.84%) much sooner (May-2023). **US Treasury yields dropped: 2Y, 5Y, and 10Y fell by 60 bps, 29bps, and 15 bps. Correspondingly, the US dollar depreciated 0.9% versus major currencies.** Credit spreads widened.

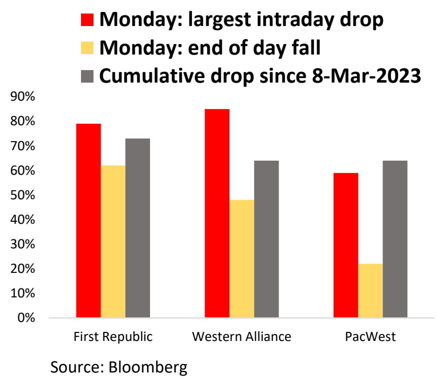
The priced-in forward path of the Fed policy rate collapsed amid the fears that further tightening may trigger new risk events in the financial system (left chart below)**.** Notably, the priced-in policy rate for the Sep-2023 FOMC meeting is now almost 2 percentage points lower than it was priced-in a few days ago. Correspondingly, 2Y US Treasury yield experienced the largest one day fall since Black Monday in 1987. The new terminal rate is less than one hike above the current rate, implying that markets assign non-zero probability to the scenario of the Fed effectively halting its hiking cycle. The priced-in policy rates decline rapidly, making the whole US Treasury bond curve lie below the current Fed funds target rate. Simultaneously, the indicator of the US financial conditions fell into the restrictive territory (middle chart), suggesting that the lower forward policy rates will be counterbalanced by tighter financial conditions. Credit spreads widened but were offset by the drop in the risk-free yields (right chart)—meaning that the yields of the investment grade debt remained roughly the same.

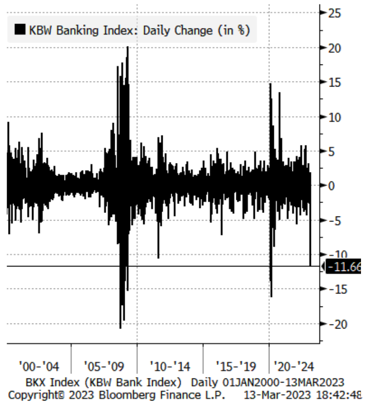


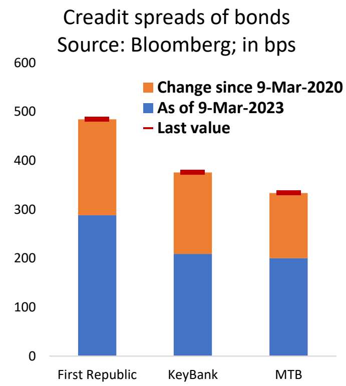




Contagion from the failure of Silicon Valley Bank spread to regional banks and other financial institutions yesterday. The most vulnerable banks experienced intraday swings even larger than last Friday (left chart below), each losing about 2/3 of their value since March 8, 2023. KBW banking index reported one of the largest daily losses in two decades (middle chart). On Monday, the negative price action affected not only equity prices but also credit spreads (right chart for a select group of banks)—implying that investors are concerned not only about impaired profitability but also about rising risks of potential insolvency of smaller and regional banks.



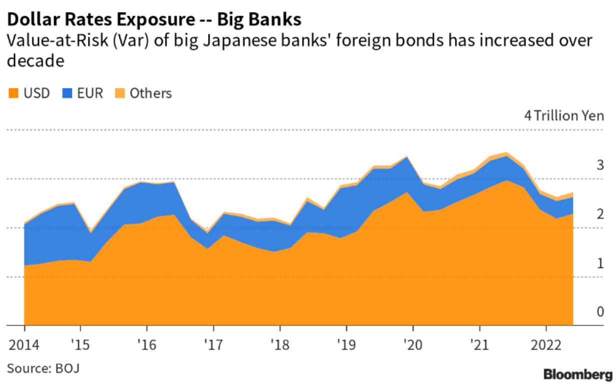




Japan

JGB yields fell as the pressure for the Bank of Japan (BOJ)'s policy normalization eased. The 10-year JGB yield dropped to 2.17% (-10.1 bps) as a global bond rally eased the pressure on the BOJ, while longer-end JGB yields declined (30-year: -21.0 bps). The 10-year OIS rate also fell to 0.53%, the lower level since November 2022. **Market participants speculated that the BOJ will hold off from altering its policy settings for now as the Federal Reserve is likely to pause its rate hikes given the stress in the US banking system.**

Japanese equities declined (-2.2%), with bank stocks down by 7.4%. Japanese bank stocks have underperformed their Asian peers in recent days. Markets had some concern about Japanese banks' exposure to USD bonds. Based on the BOJ's estimates, the value-at-risk of big Japanese banks for their holding of USD bonds increased to 2.3 tn yen ($17 bn) as of 2022Q2, compared to 1.2 tn yen ($9 bn) in early 2014, if interest rates rise by 200 bps. Nevertheless, the BOJ noted that banks' interest rate risk is well contained, at about 10% of capital for big banks and 5% for smaller regional banks. In addition, some analysts noted that lower JGB yields could also hurt banks' net interest margins, dampening their share prices. Japanese yen depreciated (-0.7%).

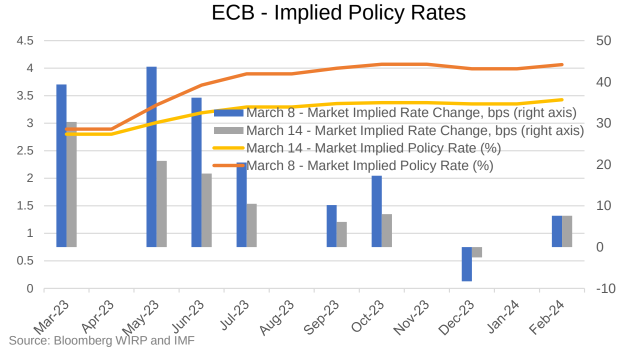


Euro area

Equities were little changed after losing about 4% in the previous three sessions. Bank stocks were still down 0.4%, having lost 10.5% in the previous three sessions. The euro was up 0.2% vs. the dollar, to 1.07/$ as the broad dollar continued to weaken.

German 10y bund yields were up 10 bps to 2.36%, still 30 bps lower than last Wednesday. During a short time this morning, German 2y bond yields fell to 2.42%, or below the ECB deposit rate (2.5%), but have now rebounded to 2.7%. Italian spreads are down 4 bps to 189 bps.

Markets have repriced the ECB terminal rate down sharply, at about 3.4% in October, or about 70 bps lower than last Wednesday. Markets are pricing in 39 bps of hikes for Thursday's ECB meeting, from 50 last Wednesday. **In contrast to the US where many analysts have changed their Fed call, most analysts have maintained their calls unchanged for Thursday's ECB decision and the ECB terminal rate**. Analysts at JP Morgan, Goldman Sachs and HSBC have maintained their calls of a 50-bps hike on Thursday. They have also maintained their terminal rate estimates at 3.75% for Goldman Sachs and JPMorgan and 3.5% for HSBC. **Note that the market's conviction has dipped slightly, as it is now pricing in 39 bps of hikes for Thursday's ECB meeting, from 50 last Wednesday.** Analysts highlight that the SVB case is special but take note that it also reflects pressures created by the tightening of monetary policy. JP Morgan analysts believe that the ECB would stick to the Separation principle: using the balance sheet to manage financial stress and using the deposit rate to set the required policy stance.



Source: Bloomberg WIRP and IMF

United Kingdom

Equities were down 0.3%, and the British pound was appreciating 0.2% against the dollar to 1.22 £/$. Yields on 10y gilts were up 13 bps to 3.5% ahead of the presentation of tomorrow's budget speech. The budget is expected to show a shallower recession than previously expected, and less borrowing in the short term. The most discussed measures ahead of the budget related to what will happen to gas and electricity price caps for households and whether there will be some one-off payments to public sector workers. Markets are pricing in 17 bps in hikes for the march meeting—down from 27 bps pre SVB—and a terminal rate at 4.3% in June (from 4.85% pre SVB).

The last batch of UK labor market data before the BOE meeting on March 23 shows that the labour market remains tight. Unemployment was unchanged in January and came in slightly lower than anticipated (3.7% vs. 3.8% expected). At the same time, the run rate of average weekly earnings was unchanged in January from December (5.7% 3m/yoy), and weekly earnings ex-bonus came in one tenth below expectations (6.5% 3m/yoy). **Goldman Sachs analysts wrote that wage growth is past its peak and likely to slow meaningfully through the year.**

Emerging Markets back to top

Asian equities declined, down 2.1% on net, as the turmoil sparked by SVB's troubles continued spreading. Share prices fell notably in Thailand (-3.1%), Korea (-2.6%), Hong Kong SAR (-2.3%), the Philippines (-2.3%), and Indonesia (-2.1%). Most Asian currencies depreciated, led by Korean won (-0.7%), Chinese yuan (-0.5%) and Indian rupee (-0.4%), on the back of dollar strengthening supported by safe-haven demand. **Long-end government bond yields declined, with 10-year yields falling in Singapore (-16.1 bps), Vietnam (-16.0 bps) and Indonesia (-10.4 bps).** In India, wholesale prices increased 3.85% y/y in February, moderating from a 4.73% increase in January (consensus: +4.0%). **Equities in EMEA were mostly trading lower while currencies weakened against their reference currencies.** Equities in Türkiye (-1.5%) and South Africa (-0.9%) underperformed while the Hungarian forint (-0.2%) was underperforming against the euro. **Local currency bond yields were mostly higher,** with 10-yr yields in Hungary up 17bps and those Poland up +9bps, while 10-yr yields in the Czech Republic and Türkiye were marginally lower. On the data front Romania's industrial production data for January showed a decline of -6.1%y/y (from -6.3%) while retail sales in the Czech Republic declined marginally less than expected in January (-7.7%y/y versus expected -7.9% from -8.1%). **Latin American assets continued to fall in line with global markets.** Stocks lost in Colombia (-2.80%), Chile (-1.05%), Brazil (-048%) and Peru (-0.06%), while Mexican equity market rose 0.41%. Currencies depreciated in Mexico (-2.16%), Colombia (-1.17%), Chile (-0.95%), Brazil (-0.64%) and Peru (-0.41%). Local currency bond spread tightened by around 20 bps in Brazil, Chile, and Peru.

Emerging Market Bond and Equity Flows

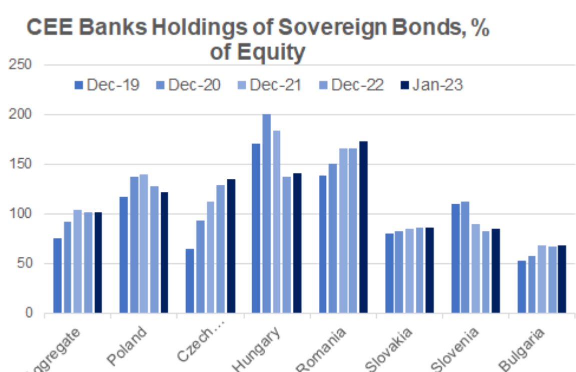
Emerging Markets bond funds outflow halved. Both hard-currency bond funds (-$571mn, from -$739mn) and local-currency bond funds (-$220mn, from -$835mn) posted their fourth consecutive weekly outflow. Outflows were dominated by non-ETF (- $843mn) and ETFs broke a three-week outflow streak with small inflows (+$52mn). **EM equity funds inflows accelerated (+$1.6bn, from +$1.4bn).** Inflows were mainly into non-ETF (+$995mn). Across regional funds inflow in Asia ex-Japan (+$351mn), while outflow in Latam (-$27mn) and EMEA (-$35mn). The year-to-date flows currently stand at +$5.3bn and +$38.5bn for bonds and equities, respectively.

China

Chinese equities declined (CSI 300: -0.6%), outperforming regional peers. Chinese markets have been relatively insulated from the global turmoil parked by the failure of US banks, with limited movements of onshore bond yields and credit spreads so far. Analysts noted that RMB assets are likely to be shielded from the market turbulence as investors look for China's economic recovery. RMB depreciated (-0.5%).

Central and Eastern Europe

CEE banks' holdings of sovereign debt have increased, but relatively low sovereign debt-to-GDP levels in the region is seen to limit the risk to banks. As focus on banks' holdings of sovereign debt has increased over the past few days, **Bloomberg analysts highlight that CEE banks' holdings of sovereign debt has increased by roughly 30% since end-2019 to €213 bn.** This amounts to roughly 100% of capital, compared to 60% for euro-area banks. The highest sovereign holdings are in Romania (roughly 170%) and Hungary (roughly 140%), while those in the Czech Republic have increased at the steepest pace—now making up around 135% of equity. Bloomberg estimates that held-to-collect (HTC) securities amount to roughly €90bn at the ten largest banks in the region, making up between 5% and 10% of bank assets. Bloomberg analysts see the risk of a liquidity crunch similar to SVB as low given capital and liquidity positions supporting CEE banks' strength.



Source: Bloomberg and IMF staff calculations

CEE Debt Holdings in Focus

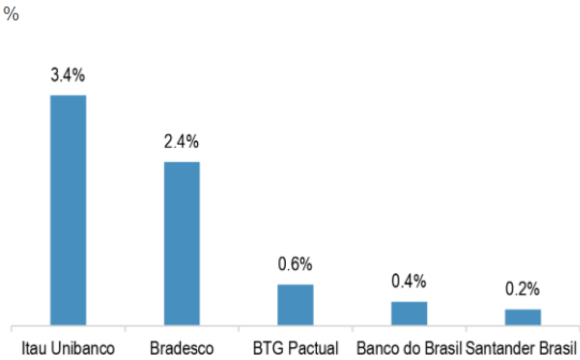
EUR mln	Securties/Investment Assets	o/w HTC Securities	HTC % of Total Assets
PKO	28,968	9,806	11%
Pekao	15,182	5,960	10%
Santander	13,304	3,312	6%
Mbank	12,184	2,866	6%
Millennium	4,407	832	4%
ING Slaski	10,767	2,863	6%
Esrte	64,039	33,000	10%
Raiffeisen	27,131	14,581	7%
Komercni	9,406	5,773	11%
OTP	17,854	12,275	15%
Source: Company Data			

Source: Bloomberg Intelligence

Brazil

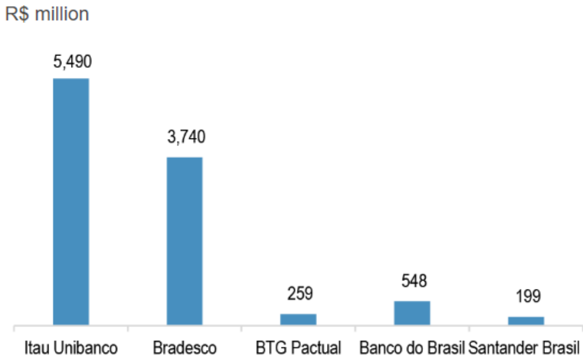
The Finance Minister said the impact of SVB's failure was "less turbulent than expected" after contacting the central bank chief and Brazilian banks over the weekend. Analysts note several reasons for this. First, available for sales securities (AFS) markdowns are already reflected in Brazilian banks' book value for Basel reasons. Second, hold-to-maturity (HTM) embedded losses are relatively small for Brazilian large banks. Finally, large-cap banks in Brazil have focused on maintaining liquidity.

Figure 1: HTM Embedded Losses as % of Equity



Source: Company reports. Note: BBAS ex-hybrid instruments and minorities.

Figure 2: HTM Securities - Embedded Losses



Source: Company reports

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Global Financial Indicators

Last updated:	Level		Change				
3/14/23 11:45 AM	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		3856	-0.2	-5	-7	-8	0
Europe		4125	0.7	-4	-3	10	9
Japan		27222	-2.2	-4	-1	7	4
China		3245	-0.7	-1	-1	6	5
Asia Ex Japan		65	0.6	-4	-6	-6	0
Emerging Markets		38	0.2	-4	-6	-9	0
Interest Rates				basis points			
US 10y Yield		3.62	4.7	-34	-12	149	-25
Germany 10y Yield		2.36	9.6	-34	-8	199	-22
Japan 10y Yield		0.27	-7.4	-23	-24	8	-15
UK 10y Yield		3.48	10.8	-34	-4	188	-19
Credit Spreads				basis points			
US Investment Grade		176	15.4	33	33	10	18
US High Yield		525	47.5	112	83	85	44
Europe IG		93	-2.1	17	15	13	2
Europe HY		462	-14.6	68	61	81	-12
Exchange Rates					%		
USD/Majors		103.79	0.2	-2	1	5	0
EUR/USD		1.07	-0.1	2	0	-2	0
USD/JPY		134.1	0.7	-2	1	13	2
EM/USD		50.1	0.1	0	-1	-1	0
Commodities					%		
Brent Crude Oil ($/barrel)		79	-1.8	-5	-7	-26	-8
Industrials Metals (index)		158	0.2	0	-4	-30	-5
Agriculture (index)		67	-0.2	-2	-6	-10	-3
Implied Volatility					%		
VIX Index (%, change in pp)		26.2	-0.3	6.7	7.3	-5.5	4.6
US 10y Swaption Volatility		167.9	1.1	35.0	58.2	60.7	41.3
Global FX Volatility		11.0	0.0	1.1	0.6	1.2	0.3
EA Sovereign Spreads				10-Year spread vs. Germany (bps)			
Greece		194	-10.1	14	14	-39	-11
Italy		187	-5.1	4	9	28	-27
Portugal		91	-2.8	4	7	7	-10
Spain		108	-2.4	5	16	11	-1

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

Emerging Market Financial Indicators

14/03/2023 1:03 PM	Level		Change (in %)					Since	Level		Change (in basis points)					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
		vs. USD	(+) = EM appreciation							% p.a.						
China		6.87	-0.3	1.4	-1	-7	0	-8		3.1	-2.0	-7	1	33	8	29
Indonesia		15385	-0.1	-0.1	-1	-7	1	-7		6.7	-10.9	-25	1	1	-21	23
India		82	-0.4	-0.7	0	-7	0	-10		7.5	-4.0	-24	7	64.5	7	
Philippines		55	-0.3	-0.2	0	-5	1	-7		6.0	-5.0	-3	8	95	-3	100
Thailand		34	0.1	1.8	-2	-3	0	-6		2.5	1.0	-19	-28	16	-17	24
Malaysia		4.48	0.2	-0.3	-3	-6	-2	-7		3.8	-5.2	-18	-3	17	-20	18
Argentina		201	0.3	-0.5	-4	-46	-12	-47		89.3	31.0	124	202	4133	113	4138
Brazil		5.23	0.4	-0.7	-1	-2	1	-4		13.2	7.6	-43	-43	49	61	167
Chile		796	1.0	0.9	-1	2	7	-1		5.3	11.0	-40	-24	-77	-8	-66
Colombia		4764	0.1	0.0	1	-20	2	-18		9.4	0.0	-26	11	116	-41	149
Mexico		18.72	1.0	-3.3	-1	12	4	8								
Peru		3.8	-0.4	-0.3	2	-2	0	-2		7.9	0.0	-23	-9	116	-8	189
Uruguay		39	0.0	0.0	-1	9	1	8		10.3	0.0	8	63	193	-35	217
Hungary		366	0.1	-1.8	-4	-7	2	-13		8.4	13.0	7	27	256	-125	354
Poland		4.37	-0.2	1.8	2	-1	0	-7		5.4	16.5	-42	-6	76	-83	147
Romania		4.6	-0.1	1.6	-1	-1	1	-5		7.1	-11.2	-30	-22	116	-55	198
Russia		75.3	0.2	0.6	-2	61	-1	8		10.6	0.0	0	22	-2069	-128	-60
South Africa		18.1	0.4	2.1	-1	-17	-6	-17		9.1	-1.5	-13	25	105	-4	154
Turkey		18.98	0.0	-0.3	-1	-22	-1	-27		11.3	1.0	-60	-32	-1471	142	-1117
US (DXY; 5y UST)		104	0.2	-1.7	1	5	0	8		3.79	9.0	-52	-21	170	-22	189

	Level		Change (in %)					Since	Level		Change (in basis points)				Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22	Last 12m	Latest	7 Days	30 Days	12 M	YTD	23-Feb-22
									basis points						
China		3985	-0.6	-2	-3	0	3	-14		173	8	-1	-54	-4	-35
Indonesia		6642	-2.1	-2	-4	-4	-3	-4		168	31	15	-42	28	-17
India		57900	-0.6	-4	-6	4	-5	1		162	19	13	-33	20	8
Philippines		6393	-2.3	-5	-6	-9	-3	-13		135	24	9	-20	38	-2
Thailand		1524	-3.1	-6	-7	-7	-9	-10		0	0	0	0	0	0
Malaysia		1394	-2.0	-4	-6	-11	-7	-12		98	5	-3	-50	-2	-35
Argentina		225228	-4.7	-11	-13	165	11	147		2331	280	346	514	126	594
Brazil		103121	-0.5	-1	-4	-6	-6	-8		289	30	25	-38	15	-42
Chile		5339	0.0	-1	0	16	1	22		156	22	19	-21	24	-18
Colombia		1154	-2.8	-7	-6	-24	-10	-24		432	43	48	54	60	40
Mexico		53012	0.4	-2	1	0	9	3		404	39	42	31	23	34
Peru		21592	-0.1	-2	-2	-12	1	-8		196	18	9	7	16	6
Hungary		41959	0.4	-3	-10	-2	-4	-12		236	28	24	69	14	83
Poland		58224	0.0	-4	-3	-3	1	-7		101	36	21	28	28	85
Romania		12277	0.2	-1	0	0	5	-7		254	24	14	5	-2	22
Russia		2282	0.5	-1	2	-8	6	-26							
South Africa		74847	-0.9	-5	-6	4	2	0		396	51	27	18	29	7
Turkey		5284	-0.7	-2	17	153	-4	162		488	32	-38	-145	48	-75
Ukraine		507	0.0	0	0	-2	-2	-2		4822	120	395	778	743	3349
EM total		38	-1.4	-4	-6	-9	0	-20		415	35	30	-181	40	-43

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

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