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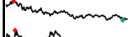
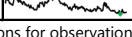
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## Debt Ceiling Talks and Disappointing Data Abroad Weigh on Risk Sentiment

**Equities are little changed while yields are lower** on disappointing data in China, weaker survey data in Germany and ongoing US debt ceiling negotiations that keep broader risk sentiment in check. In the US, President Biden and Speaker McCarthy are expected to hold another round of key debt ceiling negotiations. Some are eyeing this as the last real chance to break the impasse, and a risk that no tangible progress might be made could trigger safe havens flows. Crude oil prices are little changed today following the US's announcement to purchase up to 3 million barrels of crude oil to refill its Strategic Petroleum Reserve for August delivery. In Germany, the ZEW survey index missed expectations in both expectations and current conditions components and also recent China economic data point at a slowdown in economic momentum. Notwithstanding this, latest US retail sales figures this morning still point at robust consumer spending which propelled US Treasury yields higher. The RBA released its meeting minutes, which revealed little new information as the central bank continues to be data dependent, putting focus on Australia's wage and employment figures due later this week.

**Key Global Financial Indicators**

Last updated: 5/16/23 8:56 AM	Level		Change from Market Close				YTD	Since 23-Feb-22
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		
<b>Equities</b>			%				%	
S&P 500		4136	0.3	0	0	3	8	-2
Eurostoxx 50		4320	0.1	0	-2	17	14	9
Nikkei 225		29843	0.7	2	5	12	14	13
MSCI EM		39	1.8	0	-1	-3	4	-17
<b>Yields and Spreads</b>			bps					
US 10y Yield		3.49	-0.9	-3	-2	61	-38	150
Germany 10y Yield		2.29	-2.1	-6	-15	135	-28	206
EMBIG Sovereign Spread		491	7	8	13	22	39	78
<b>FX / Commodities / Volatility</b>			%					
EM FX vs. USD, (+) = appreciation		50.7	-0.2	0	0	-2	2	-5
Dollar index, (+) = \$ appreciation		102.4	0.0	1	1	-2	-1	6
Brent Crude Oil (\$/barrel)		75.3	0.1	-3	-13	-34	-12	-22
VIX Index (% change in pp)		17.6	0.4	0	0	-10	-4	-13

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

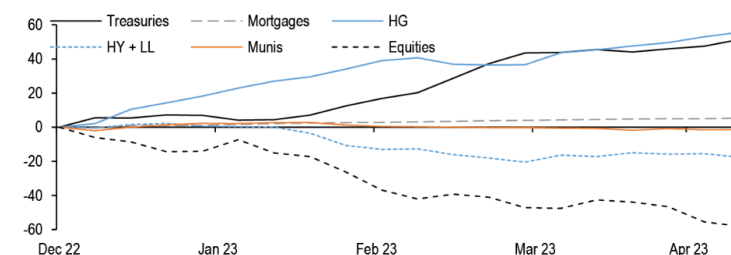
**Latest retail sales figures still point at robust consumer spending.** US retail sales bounced back in April, showing signs of resilience. Headline retail sales rose +0.4% m/m in April (expected 0.8% m/m), up from last month's upwardly revised drop of -0.7% m/m. Despite coming overall below expectations, market contacts note strength in several categories which, highlighting still robust consumer spending. Sales excluding autos and gasoline came in at +0.6% m/m beating the consensus (+0.2% m/m expected), leading to a +5bps upward jump in two-year yields to 4.04%, rebounding from an initial decline in reaction to the release of the headline number.

### Investors are buying up safer assets in an environment with multiple risks threatening financial stability.

Worries about the debt ceiling are growing, with the US sovereign credit default swap (CDS) spreads near record highs and an inversion in the CDS curve signaling heightened worries about US sovereign risk. The latest jobless claims data point to a labor market that may finally be beginning to cool down as the economy slows. Other economic data also suggest that the US could be at risk of a recession. The recent Fed bank lending survey showed both a tightening of bank lending standards and a sharp reduction in the demand for credit among companies to the lowest level since the survey began as both creditors and debtors pull back given that the economic environment has grown more uncertain. JP Morgan data show that investment grade bond funds and Treasury bond funds have seen inflows of \$56 bn and \$51 bn respectively in 2023, while equity and high yield funds saw large outflows.

Figure 3: Investors continue to move their cash into high quality fixed income funds and out of riskier fund types

Cumulative change in fund flows into their respective fund types; \$bn



Source: EPFR, J.P. Morgan

**Markets are pricing very dovish outcomes for the US interest rate environment.** Inflation swap markets are indicating that CPI will fall to 3% by June, where it is expected to stay for some time. Treasury Inflation Protected Securities (TIPS) breakeven yields (widely followed as proxies for the market's forecasts for future inflation) have fallen to 2.13% for 5-year TIPS and 2.21% for 10-year TIPS. Although the real yield on two-year TIPS remains above 2%, the 10-year TIPS real yield has fallen to 1.33%. In the overnight index swap (OIS) market, investors think there will be 75 bps of rate cuts by year-end despite Fed Chair Powell's remark at the latest FOMC press conference that rate cuts are highly unlikely this year. Some analysts think Fed rhetoric needs to get even more hawkish to change market expectations.

Exhibit 5: YoY realized and market-implied CPI

Market reflecting inflation will fall back below 3% by June



Source: BofA Global Research, Bloomberg

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Exhibit 6: Fed rate cuts in 2H '23 & BKX bank index

Near term Fed cuts built with bank stress

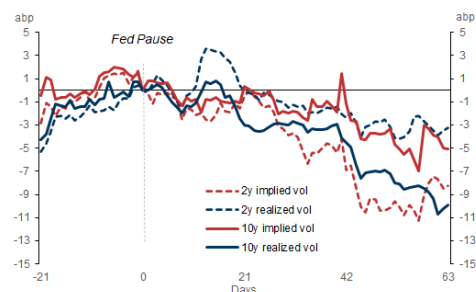


Source: Bloomberg

BoFA GLOBAL RESEARCH

**Historically, US interest rate volatility declines when the Fed is on hold.** Goldman Sachs analysts show that in previous episodes when the Fed was going on hold, rates volatility has fallen, with longer-dated volatility falling more than shorter-dated one. This is because a key element of uncertainty—the path of short-term interest rate expectations—gets eliminated as the market thinks the Fed will stay on hold. However, Goldman Sachs analysts also argue that this time around, the decline may be lower than what was seen historically as there are multiple risks on the horizon, including the debt ceiling, US regional banks and a potential recession.

**Exhibit 1: Implied and realized rate vol has historically dropped after Fed pauses, although the decline may be muted in this cycle**  
Average change in 3m2y and 3m10y implied and delivered US rates volatility, indexed to prior Fed pauses



Source: Goldman Sachs, Goldman Sachs Global Investment Research

## Euro Area

**Equities are little changed while EGB yields are lower.** The ECB peak forward rate is now trading at 3.60% in September and then drops to 3.54% by December (still above longer-term measures for the nominal neutral rate around 3.1%).

**The German ZEW expectations index unexpectedly fell.** The latest reading is at -10.7 for May (expected -5.0) from 4.1 in April, reflecting the third consecutive drop. The current assessment component also weakened to -34.8 (expected 37.0) from -32.5 in April.

**ECB Supervisory board chair Enria sees no need for "major changes" on bank rules while opening the case for a calibration of the Liquidity Coverage Ratio.** In a Eurogroup meeting, the chair also stated that it may be beneficial to explore how high deposit base concentration and a predominant reliance on uninsured deposits could be dealt with in the Pillar 2 framework. The ECB has also reviewed TLTRO exit strategies of selected banks that showed "*material reliance*" on that source of funding, which was also pointed at in the latest Global Financial Stability Report.

## Japan

**The Japanese government sees structural wage gains as a priority issue.** After attending a Council on Economic and Fiscal Policy meeting on Monday, PM Kishida stated the government aims to link recent wage increases to a stable virtuous cycle between wages and prices, where wage gains and costs are appropriately passed on to prices. Yields on 10Y bonds declined -1.7 bps, the yen strengthened +0.2%. Investors are turning more bullish on yen, according to Bloomberg.

**The Topix index reaches its highest since August 1990.** The bullish sentiment prevalent in Japanese equity markets became lifted by foreign buying and solid corporate earnings, and market contacts further noting that Japanese equities benefit from attractive valuations that attract global allocator's flows amid ongoing corporate governance reforms. Japan's top three banks are set to forecast their highest profits in years, driven by a pickup in client activities and subdued bad loan costs.

### Japan's Topix Outperforms S&P 500 This Year



## Emerging Markets

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**EMEA markets have shown mixed performances.** Turkish bank stocks continued to underperform, declining by another -8%. The South African rand remained little changed as analysts are calling for a hike of 50 bps by the South African Reserve Bank at its next meeting in response to currency weakness after a “string of negative news headlines.”

**Asian stock markets posted mixed results while currencies mostly weakened.** Mainland China markets declined (Shanghai -0.6%, Shenzhen -0.7%) as economic data fell short of expectations; Indonesia lost -0.6%, Taiwan Province of China (POC) outperformed +1.3%. The Thai baht depreciated -0.5% amid continued uncertainty around election outcomes.

**Markets in Latin America broadly gained.** Equity markets rallied across the region, led by Mexbol +0.6% except for Colombia's, which declined -1.0%. The Colombian peso gained the most against the US dollar by +1.4%, followed by the Mexican peso and the Brazilian real that gained +0.8% and +0.6%.

## China

**Most recent economic data prints point at further slowdown of China's economic momentum.** China's industrial production rose in April by +5.6% y/y (vs. expected +10.9%) from +3.9% in March while retail sales came in at +18.4% y/y (vs. +21.9% expected) from +10.6% in March. Growth in fixed-asset investment slowed to +4.7% ytd (vs. expected +5.7%). Analysts noted that weak consumer confidence, employment concerns, slowing housing market were key economic drags, offsetting base effects from the lockdown measures a year before. Accordingly, mainland China markets declined (Shanghai -0.6%, Shenzhen -0.7%) with consumer discretionary sector leading the fall. The Hang Seng China Enterprises Index fractionally gained by +0.1%.

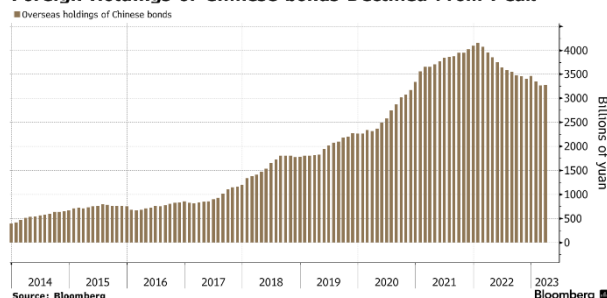
**The PBOC reiterated it will focus on efforts to help expand demand.** In its Monetary Policy Report for Q1 2023 published on Monday, the People's Bank of China (PBOC) stated that it maintains a prudent, targeted and forceful monetary policy. The report also stated that the central bank will keep a reasonable level of liquidity, maintaining a “reasonable aggregate” and “stable pace” of credit/money supply. Market contacts also expect the PBoC to continue guiding down deposit rates and cutting the medium-term lending facility rate later this year.

**Foreign ownership of Chinese bonds declines as overseas investors resumed selling.** Foreign holdings of China bonds in the interbank market decreased by \$6bn in April due to concerns over rising US interest rates, geopolitical tensions, and convertibility of the currency, leading to outflows from China's bond market. Furthermore, market contacts also refer to profit taking as another argument given that China's sovereign bond market has had a seven-week rally, so that the market could consolidate in the near-term absent further deterioration in economic data. Nevertheless, global investors still hold significantly more Chinese bonds compared to a decade ago.

## Overseas Investors Resumed Net Selling of China Bonds



## Foreign Holdings of Chinese bonds Declined From Peak

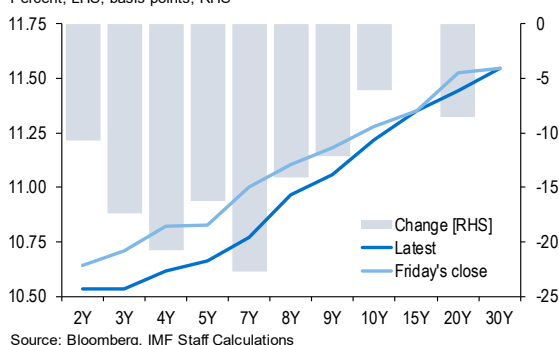


## Colombia

## Colombia's sovereign yield curve bull steepened as growth came in below expectations.

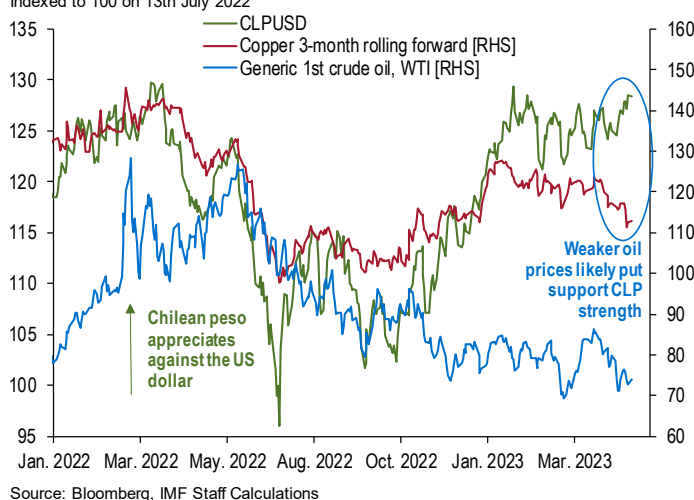
The latest growth print for the first quarter in 2023 yesterday missed expectations with 3.0% y/y (expected 3.4% y/y) from 2.9% y/y in Q4 2022. The lower-than-expected print came following the country's aggressive hiking cycle where the central bank hiked 25bps at its last meeting. Colombia has faced one of the most persistent inflation dynamics in the region. Recent inflation prints seem to suggest that inflation might have peaked, albeit inflation levels remain far away from the central bank's 3% target. In reaction to the latest GDP release, the term structure of Colombian sovereign yields bull steepened.

## Colombian sovereign yield curve rallies following disappointing growth print



**The Chilean peso continues outperform despite falling copper prices.** The currency remains one of the best performers across emerging markets, even though it fractionally depreciated against the dollar yesterday by -0.2%. China's re-opening rumors back in November prompted increasing copper prices, which in turn propelled the peso's initial rally after a tumultuous summer. The peso continued to gain year-to-date despite falling in copper prices. Against this backdrop, market contacts see weaker oil prices as one reason for the peso's outperformance. Chile remains a net oil importer country within the region.

## Chilean peso continues to gain against the dollar despite lower copper prices.

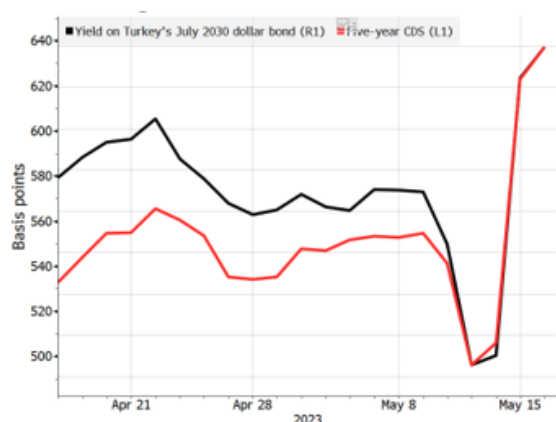




## Türkiye

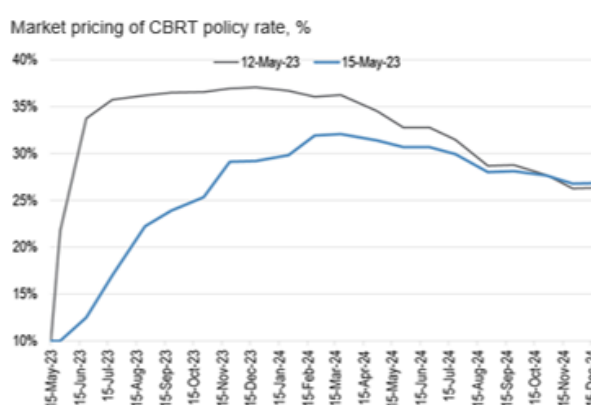
**Türkiye's assets reversed last week's rally after presidential election goes into second round.** The Turkish presidential election is heading to a second round on May 28, following news that none of the two leading candidates was able to win at least 50% of the votes. With all ballots accounted for, current President Erdogan is leading with 49.5% while his main opponent Kemal Kilicdaroglu, has 44.9% of the votes, according to Turkey's national election board. Public polls were predicting Kilicdaroglu to have a lead, with results shaking markets. The BIST 100 Index and the lira fell by -6.14% and -0.44% while the 5-year sovereign CDS contract rose by more than +125 bps to around 650 bps after the voting outcome. Additionally, market implied policy rates massively dropped. Whereas last Friday, markets priced them to reach up to 35% over the next 3 months and staying there for around 6 months, market pricing now only reaches 16% within the next 3 months with rates peaking in March 2024.

**Türkiye's Bond yields & CDS spreads jump...**



Source: Bloomberg

**...while market priced out near-term policy rate hikes**



Source: JP Morgan, Snapshot date May 15, 2023

*This monitor is prepared under the guidance of Jason Wu (Assistant Director), Charles Cohen (Deputy Division Chief), Nassira Abbas (Deputy Division Chief), and Antonio Garcia-Pascual (Deputy Division Chief). Fabio Cortes (Senior Economist), Reinout De Bock (Senior Economist-London Representative), Sanjay Hazarika (Senior Financial Sector Expert), Esti Kemp (Financial Sector Expert-London Representative), Johannes S Kramer (New York Representative), Aurelie Martin (Senior Economist-London Representative), Tom Piontek (Senior Financial Sector Expert) and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Yingyuan Chen (Financial Sector Expert), Deepali Gautam (Research Officer), Shoko Ikarashi (Externally Financed Appointee), Phakawa Jeasakul (IMF Resident Representative in Hong Kong SAR), Harrison Kraus (Research Assistant), Yiran Li (Research Assistant), Kleopatra Nikolaou (Senior Financial Sector Expert), Natalia Novikova (IMF Resident Representative in Singapore), Mustafa Oguz Caylan (Research Officer), Silvia Ramirez (Senior Financial Sector Expert), Patrick Schneider (Financial Sector Expert), Ying Xu (Economist), Dmitry Yakovlev (Senior Research Officer), and Akihiko Yokoyama (Senior Financial Sector Expert). Javier Chang (Senior Administrative Assistant) Olga Lefebvre (Staff Assistant), and Srujana Sammeta (Staff Assistant) are responsible for the word processing and production of this monitor.*

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## Global Financial Indicators

5/16/23 8:55 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
<b>Equities</b>			%				%
United States		4135	0.3	0	0	3	8
Europe		4320	0.1	0	-2	17	14
Japan		29843	0.7	2	5	12	14
China		3978	-0.5	-1	-4	-1	3
Asia Ex Japan		67	2.4	-1	-2	-1	3
Emerging Markets		39	1.8	0	-1	-3	4
<b>Interest Rates</b>			basis points				
US 10y Yield		3.49	-0.9	-3	-2	61	-38
Germany 10y Yield		2.29	-2.1	-6	-15	135	-28
Japan 10y Yield		0.40	-1.0	-3	-8	15	-3
UK 10y Yield		3.77	-4.7	-9	10	204	10
<b>Credit Spreads</b>			basis points				
US Investment Grade		173	0.3	3	15	7	15
US High Yield		510	1.4	5	41	21	29
<b>Exchange Rates</b>			%				
USD/Majors		102.40	0.0	1	1	-2	-1
EUR/USD		1.09	0.1	-1	0	4	2
USD/JPY		135.9	-0.1	1	1	5	4
EM/USD		50.7	-0.2	0	0	-2	2
<b>Commodities</b>			%				
Brent Crude Oil (\$/barrel)		75.3	0.1	-3	-12	-20	-11
Industrials Metals (index)		144	-1.5	-6	-10	-19	-13
Agriculture (index)		67	-0.5	0	-3	-15	-3
<b>Implied Volatility</b>			%				
VIX Index (% change in pp)		17.6	0.4	-0.1	0.5	-9.9	-4.1
US 10y Swaption Volatility		134.6	0.0	0.0	0.0	17.9	7.0
Global FX Volatility		8.8	0.0	-0.1	-1.1	-2.2	-1.9
<b>EA Sovereign Spreads</b>			10-Year spread vs. Germany (bps)				
Greece		171	1.0	-7	-14	-88	-34
Italy		187	-0.6	-6	1	-3	-27
Portugal		81	-0.7	-4	-4	-31	-21
Spain		107	-0.2	-2	3	0	-3

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

## Emerging Market Financial Indicators

Last updated: 5/16/2023 8:23 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		6.97	-0.2	-0.7	-1	-3	-1		2.9	-6.4	-13	-29	1	-20
Indonesia		14820	-0.1	-0.6	0	-1	5		6.4	-0.5	-7	-23	-95	-51
India		82	0.1	-0.2	0	-6	1		7.1	-4.9	-9	-27	(36.2)	-30
Philippines		56	0.0	-0.5	0	-6	-1		5.9	0.0	0	-10	45	-15
Thailand		34	-0.5	-0.7	1	2	2		2.7	0.5	6	8	-67	3
Malaysia		4.50	0.0	-1.1	-2	-2	-2		3.7	0.6	-4	-18	-77	-39
Argentina		231	0.1	-1.1	-6	-49	-23		99.5	55.2	267	977	4634	1132
Brazil		4.89	0.0	1.9	1	3	8		11.8	5.2	-66	-61	-50	-76
Chile		786	-0.2	1.4	2	9	8		5.3	0.3	5	1	-104	-4
Colombia		4493	1.3	0.4	-1	-10	8		8.5	0.0	-34	-47	-62	-131
Mexico		17.45	-0.1	1.9	3	15	12		8.2	0.0	-10	-31	-41	-49
Peru		3.7	-0.2	1.1	3	3	4		7.2	0.2	#####	-30	-64	-77
Uruguay		39	0.2	-0.5	0	6	2		10.0	-7.5	0	-28	-13	-69
Hungary		339	0.0	-0.2	0	10	10		7.7	-6.0	-26	-79	68	-190
Poland		4.12	0.5	0.8	3	8	6		5.3	7.0	12	-27	-78	-83
Romania		4.5	-0.1	-1.3	-1	4	2		6.9	-2.3	-22	-37	-107	-82
Russia		80.3	-0.6	-3.2	2	-20	-8							
South Africa		19.0	-0.1	-2.2	-4	-15	-11		9.7	1.3	24	39	121	56
Turkey		19.71	-0.2	-0.9	-2	-21	-5		11.6	0.0	-110	-73	-1334	176
US (DXY; 5y UST)		102	0.0	0.8	1	-2	-1		3.45	-2.1	-5	-16	62	-56

	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	7 Days	30 Days	12 M	
								basis points					
China		3978	-0.5	-1	-4	-1	3		201	0	7	-7	24
Indonesia		6677	-0.5	-2	-2	0	-3		146	4	6	-62	6
India		61932	-0.7	0	3	14	2		162	-3	6	-23	20
Philippines		6589	1.0	-1	1	0	0		120	5	5	-39	23
Thailand		1540	-0.1	-2	-4	-5	-8		0	0	0	0	0
Malaysia		1424	0.4	-1	-1	-8	-5		103	0	3	-32	3
Argentina		320583	-0.3	5	16	256	59		2591	-5	216	697	386
Brazil		109029	0.5	3	3	1	-1		276	-1	7	-32	2
Chile		5598	0.0	1	3	15	6		135	-1	-4	-34	3
Colombia		1148	-1.0	-1	-8	-24	-11		423	0	24	40	51
Mexico		55261	0.6	0	1	9	14		410	9	24	27	29
Peru		21626	0.4	-3	-4	8	1		182	0	-2	-8	2
Hungary		45988	0.1	-2	6	11	5		221	11	-11	17	-1
Poland		63958	0.4	1	4	16	11		137	5	60	135	64
Romania		12127	0.7	0	-3	0	4		252	4	-3	18	-3
South Africa		78408	0.2	1	-1	13	7		451	27	44	38	84
Turkey		4564	1.4	1	-10	91	-17		586	68	109	-16	146
Ukraine		507	0.0	0	0	-2	-2		5404	2	302	1997	1325
EM total		39	-0.3	0	-1	-3	4		429	10	22	19	53

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