



- Investors see monetary policy as the key risk to market stability over geopolitics ([link](#))
- UK inflation rises to multi-decade high ([link](#))
- Japan's real GDP contracted smaller than expected in 2022Q1 ([link](#))
- Expected block of Russia's debt repayments raises default odds ([link](#))
- Chinese equities declined amid renewed concern about COVID-19 outbreaks ([link](#))

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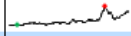




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Hawkish outlook may make rally short-lived

Global equities are little changed after bouncing sharply yesterday. The rise in interest rates, driven by increasingly hawkish expectations in both the US and Europe, appears to be dampening risk appetite. The US 10-year is once again hovering around 3% after rising 11 bp yesterday. Fed Chair Powell's comments that the Fed could raise rates above neutral seemed to signal to markets that a further correction could be tolerated. Additionally, expectations for the ECB's policy rate continue to rise. More than one full 25 bp hike is priced in for the July meeting and more than 100 bp is priced in for the year. In China, even as the Covid situation in Shanghai has improved, outbreaks in other cities have renewed fears of additional lockdowns. Russian Eurobonds are sharply lower on reports that a temporary sanctions exemption that allows the government to make payments on its hard currency debt may not be renewed after it expires on May 25.

Key Global Financial Indicators

Last updated: 5/18/22 8:11 AM	Level		Change from Market Close					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
Equities			%				%	
S&P 500		4089	2.0	2	-7	-1	-14	-3
Eurostoxx 50		3727	-0.4	2	-3	-7	-13	-6
Nikkei 225		26911	0.9	3	0	-4	-7	2
MSCI EM		41	2.5	3	-6	-23	-15	-13
Yields and Spreads			bps					
US 10y Yield		3.00	1.1	8	14	136	149	101
Germany 10y Yield		1.08	2.9	9	23	118	125	85
EMBIG Sovereign Spread		467	-7	-1	64	136	100	54
FX / Commodities / Volatility			%					
EM FX vs. USD, (+) = appreciation		52.1	0.1	1	-2	-10	-1	-2
Dollar index, (+) = \$ appreciation		103.6	0.2	0	3	15	8	8
Brent Crude Oil (\$/barrel)		113.6	1.5	6	0	65	46	17
VIX Index (% change in pp)		26.8	0.7	-6	5	5	10	-4

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

Mature Markets

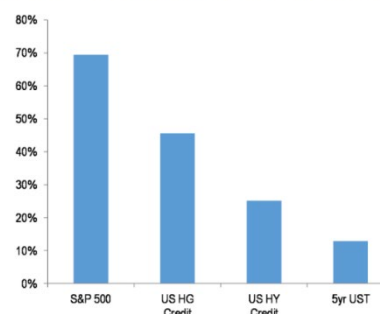
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United States

The S&P500 rallied 2% on Tuesday amid a broad-based rally in global equities. In public comments, Fed Chair Powell stated that the Fed would be willing to raise rates above neutral if needed, while also noting that a slight increase in the unemployment rate would still be consistent with a strong labor market and an acceptable result of further policy tightening. **The Treasury curve flattened, with 2-year (+14 bps) and 10-year (+11 bps) yields moving higher** in response to Powell's comments. Powell's conviction to further tighten financial conditions appears to be getting through to investors. The latest BofA Fund Manager Survey shows that investors have lowered their estimates of the Fed *put*, implying another 14% decline in equities would be needed before the Fed would consider changing course.

JPMorgan analysts believe that equity markets may be pricing in too much recession risk, with stocks reflecting nearly a 70% probability of recession, far higher than rate markets (10–20%) and high yield credit (25%). JPM looked at the average move in different asset prices leading up to and during recessions compared to the latest developments. The elevated recession *probability* also stands in contrast to recent economic data showing resilient growth, with retail sales for April largely in line with expectations at 0.9% m/m (vs 1% expected), while industrial production beat expectations at 1.1% m/m (vs 0.5%), up from 0.9% previously. On average, US recessions have coincided with a stock market drawdown of 26%, compared to the 15% decline in the S&P500 seen this cycle (from the recent peak). Forecasters (Bloomberg average) see a 30% chance of recession within one year.

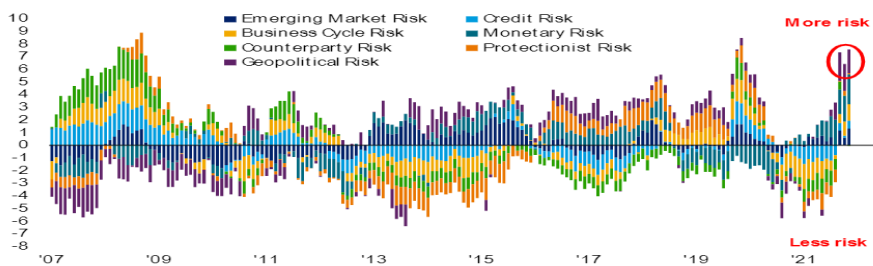
Figure 8: Probability of a recession as currently priced across US equity, credit and rate markets



Source: J.P. Morgan, As of May 12th close

Investors once again see monetary policy as the key risk to financial market stability over geopolitics. BofA survey respondents also increased their rate hike expectations for this tightening cycle by the Fed from 7.4 in the April edition to 7.9 currently. A plurality of respondents believe the Fed will hike 8 times this cycle (with 6 hikes the most common response in April), while nearly 20% now see 10 hikes as the most likely outcome.

Chart 12: Monetary risk overtakes geopolitical as the greatest risk to financial market stability
At this time how would you rate these potential risks to Financial Market Stability?



Source: BofA Global Fund Manager Survey

Euro Area

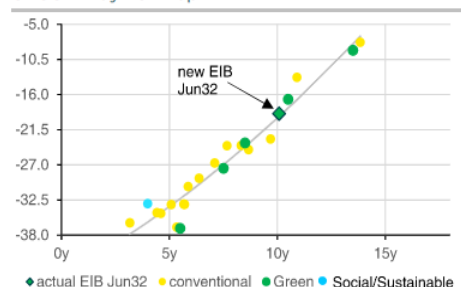
Equities are little changed and German 10-yr bund yields (+2 bps) edged higher as final headline inflation for the euro area was slightly below expectations at 7.4% yoy in April. Core inflation was 3.5% y/y, as expected. Bank stocks (+0.8%) gained. Shares in ABN Amro fell almost 10% after the Dutch lender reported bigger-than-expected costs related to money laundering.

Money markets continue to price about 100 bps of hikes in 2022, with the ECB hiking 25 bps in July, September, October, and December. Finnish central bank governor Ollie Rehn sees ECB's June forecast likely to be near the adverse scenario of March but added that the ECB should exit negative rates quickly to prevent an unanchoring of inflation expectations.

According to news reports, the ECB has made some changes to the format of its monetary policy meetings. ECB president Lagarde has reportedly given national central bank presidents bigger say in meetings with board member presentations limited to 20 pages and ECB staff wrapping up seminars by lunchtime on the first day of the two-day policy meeting. The two-day policy meeting now starts on Wednesday morning rather than the afternoon and the Thursday session begins 30 minutes earlier than previously, all with the aim of leaving more space for debate, according to ECB sources.

The EU Commission will announce details of REPowerEU, the plan on how the EU will end its dependence on Russian fossil fuels by 2027. The overall size could be reportedly as much as €195 bn (around 1.4% of EU GDP). Some contacts believe that more joint issuance could be used to fund these investments. **Demand for green sovereign paper remains strong in primary markets** with the EIB launching a new 10-yr benchmark yesterday (€4bn size, €23bn book) but Commerzbank points out that the bond was placed less than 1 bp away from the active secondary curve as poor performance of longer-dated bonds may be eroding investor willingness to pay for green.

EIB active z-spread structure by bond format, as of COB May 16 in bp



Source: Bloomberg, Commerzbank Research

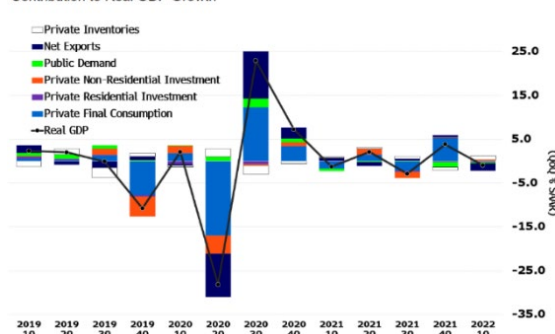
United Kingdom

The pound (-0.7%) fell and 2-yr gilt yields are little changed after headline inflation reached a 40-year high but was slightly below expectations at 9% y/y in April (9.1% expected) or 2.5% m/m (2.6% m/m expected). A hike of 50% in the utility price cap drove three quarters of the 200-bp inflation rise from March. Core services inflation hit the strongest since at least 2001 (when records for CPI components begin). Hospitality services prices also made a significant contribution as the VAT rate returned to 20% in April. Core inflation rose to 6.2% y/y, as expected, from 5.7% y/y in March.

Japan

Real GDP contracted 0.2% q/q in Q1, less than expected (consensus: -0.4%), after growing 1.1% in 2021Q4. The economic contraction mainly stemmed from moderating consumption amid the Omicron-driven COVID-19 outbreak. External demand also dampened due to lackluster automobile exports on the back of supply constraints. However, the economy still performed better than expected, benefiting from stronger-than-expected private consumption. Some analysts warned about weak economic activity in 2022Q2, with recent data pointing to a relatively low level of mobility including during the Golden Week holidays period. **The cabinet yesterday approved a 2.7 tn yen (\$20.9 bn) extra budget** to fund measures that support households and businesses amid rising energy prices. This is part of the measures announced in April. Equities gained (NIKKEI: +0.9%), while the yen was little changed. Long-end JGB yields were mixed (10-year: -0.2 bp; 30-year: +0.4 bp).

Contribution to Real GDP Growth

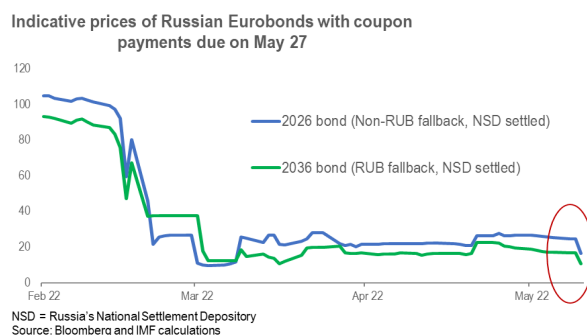


Emerging Markets [back to top](#)

Most Asian equities gained, +0.3% on net, led by Indonesian (+2.1%) and Philippine (+2.0%) equities, following a rally of U.S. equities yesterday. Meanwhile, Chinese equities declined (CSI 300: -0.3%). Most Asian currencies depreciated, led by the Indonesian rupiah (-0.3%) and Thai baht (-0.3%). Long-end government bond yields were mixed, with 10-year yields rising in Hong Kong SAR (+9.2 bps) while falling in Taiwan Province of China (-7.2 bps). In Philippines, Governor Benjamin Diokno said that the space to keep the monetary policy stance accommodative has considerably narrowed, ahead of the central bank's policy meeting tomorrow. The Philippine peso was little changed; government bond yields rose (10-year: +3.9 bps). In Sri Lanka, the grace period for the government to make coupon USD bond payments (\$78 bn) ended today. The government also missed another payment (\$105 mn) due to Chinese banks. The country is set to default for the first time since it gained independence in 1948. Its USD bond maturing in 2030 traded at 38.9 cents on the dollar. **Equity markets in EMEA were mostly trading higher while currencies weakened against the dollar.** The Turkish lira (-0.7%) was underperforming, continuing its declining trend amid reports of strong dollar demand by corporates. **Latin American assets rallied Tuesday.** Equities surged led by Chile (+3.2%) and Mexico (+1.8%). The Chilean stock index was driven by the country's fertilizers and agricultural chemicals sector, as wheat (+2.4%) soared to a new all-time high, while soybeans (+1.3%) and sugar (+1.6%) went up as well. Currencies appreciated led by Brazil (2.5%), while the Argentine peso depreciated by 0.2%.

Russia

Indicative prices of Russia's Eurobonds fell by roughly 6 points amid reports that the U.S. is set to block Russia's ability to make payments to U.S. bondholders before the next coupon payments are due. According to a Bloomberg report, the U.S. is expected to let a temporary exemption, that allowed Russia to make debt repayments after sanctions were imposed, lapse when it expires on May 25. While some uncertainty remains over the final decision, analysts have previously highlighted that the exemption will likely only be extended in case of a significant de-escalation by Russia, and some analysts now see a Russian default as a baseline scenario.

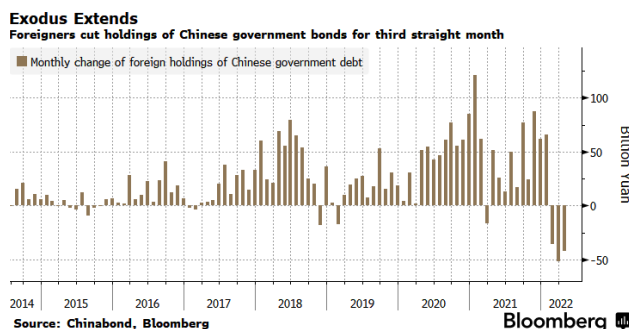


Russia's next coupon payments are due on May 27: on a Eurobond maturing in 2026 that allows for payments in euros, sterling, or Swiss Francs, as well as on a Eurobond maturing in 2036 with a ruble-payment fallback option. Both payments have a 30-day grace period. To date, Russia has reportedly paid all sovereign Eurobond coupon and principal payments that have come due. **The offshore Russian ruble was trading stronger this morning (+0.6%) and equities in Moscow gained (+2.1%).**

China

Chinese equities declined amid renewed concerns about disruptive COVID-19 outbreaks.

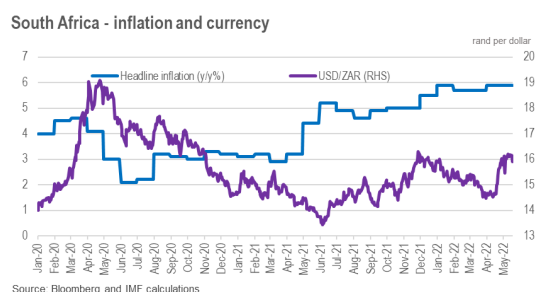
While the situation in Shanghai has improved, virus flareups in other major cities renewed concerns about potential disruptions from lockdowns to contain the spread of the virus. Chinese equities (CSI 300: -0.3%) underperformed regional peers. Vice Premier Liu He said that the government will support the development of digital economy companies and their IPOs. At a symposium with tech firms, his remarks signaled for an easing of regulatory risk for China's tech firms. Share prices of U.S.-listed Chinese tech firms rose yesterday (+5.2%), while Hong Kong-listed tech stocks declined today (-0.3%) after a big rally yesterday ahead of the meeting. China saw bond outflows for a third straight month in April. Overseas investors sold about 42 bn yuan (\$6.2 bn) of bonds on net. RMB depreciated (-0.2%), while CGB yields dropped (1-year: -4.0 bps; 10-year: -0.8 bp). House prices declined 0.3% m/m in April, with more pronounced pressures in lower-tiered cities. The decline in house prices occurred amid COVID-related disruptions on real estate transactions, continued easing in housing policies at the city level, and still weak homebuyers' confidence due to financial stress of property developers.



South Africa

Rate hike expectations remain in place after data showed the rate of headline inflation in April remained unchanged from the previous month at +5.9%y/y, as expected, while core inflation came in slightly higher than expected (+3.9%y/y vs expected +3.8%).

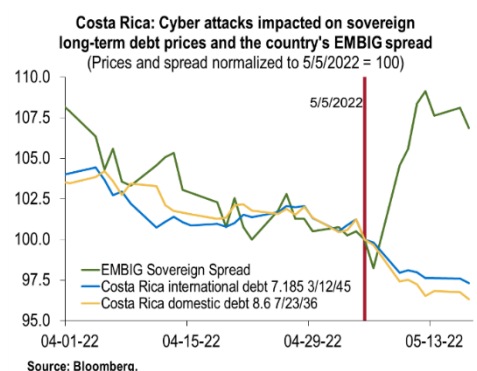
Against a backdrop of firm inflation, the SARB has increased interest rates by 25bps at each of the previous three meetings to take the key rate to 4.25%. While consensus sees the South African Reserve Bank (SARB) increasing interest rates at the monetary policy meeting tomorrow, there are mixed views on the size of the expected hike—economists surveyed by Bloomberg mostly expect a 50bps hike, while Goldman Sachs analysts see a 25bps hike against a backdrop of higher inflation but also indications of softer economic growth. Analysts, however, flag risks for a larger hike amid a weaker rand—with the rand having depreciated by roughly 8.4% since the start of April—and a hawkish shift by the US Fed. JPMorgan analysts expect a 50bps hike tomorrow followed by another 50bps hike in July, and sees the key rate at 6.75% by mid-2023.



Costa Rica

Cyber attacks impact Costa Rica's sovereign debt markets.

Costa Rica experienced a wave of cyber attacks on the country's state institutions, including the finance ministry. The incidents severely impacted foreign trade and tax collection, forcing the finance ministry to deactivate its tax collection systems, and leading to the announcement of a state of emergency by the newly elected president Chaves. According to press reports 27 government institutions are affected, with the perpetrators, a group called Conti, asking for a ransom of \$20 mn. In the wake of the continuing incidents the country's sovereign long-term debt realized losses and its EMBIG sovereign spread reversed from its recent decline.



Uruguay

Uruguay's central bank lifted its monetary policy rate by 75 bps to 9.25%. The bank motivated the step with actual and expected inflation remaining outside of the bank's target corridor and hinted at least two additional 50 bps hikes ahead. J.P. Morgan analysts welcomed the central bank's monetary tightening stance, as it could help to mitigate the inflationary effects of a still expansionary fiscal stance

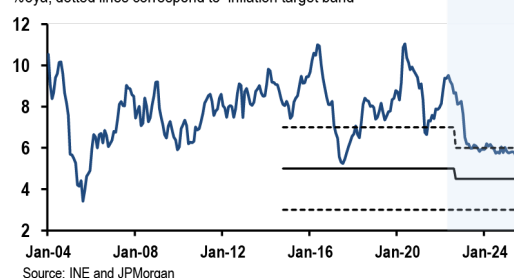
Figure 1: Inflation expectations

%oya, CBU survey, median



Figure 2: Headline CPI





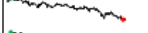













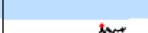

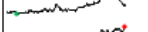




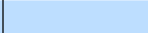


%oya, dotted lines correspond to inflation target band



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Global Financial Indicators

Last updated: 5/18/22 8:11 AM	Level		Change					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
Equities			%				%	%
United States		4072	2.0	3	-7	-1	-15	-4
Europe		3727	-0.4	2	-3	-7	-13	-6
Japan		26911	0.9	3	0	-4	-7	2
China		3992	-0.3	0	-3	-23	-19	-14
Asia Ex Japan		70	2.9	4	-4	-24	-16	-12
Emerging Markets		41	2.5	3	-6	-23	-15	-13
Interest Rates			basis points					
US 10y Yield		3.00	1.1	8	14	136	149	101
Germany 10y Yield		1.08	2.9	9	23	118	125	85
Japan 10y Yield		0.25	-0.1	0	0	16	17	5
UK 10y Yield		1.90	1.5	7	1	103	93	42
Credit Spreads			basis points					
US Investment Grade		166	0.7	4	18	72	54	23
US High Yield		477	-0.4	6	84	135	139	70
Europe IG		92	0.8	-1	13	41	44	21
Europe HY		445	3.6	-6	70	189	203	93
Exchange Rates			%					
USD/Majors		103.59	0.2	0	3	15	8	8
EUR/USD		1.05	-0.3	0	-2	-14	-7	-7
USD/JPY		129.0	-0.3	-1	2	18	12	12
EM/USD		52.1	0.1	1	-2	-10	-1	-2
Commodities			%					
Brent Crude Oil (\$/barrel)		114	1.5	6	1	76	50	25
Industrials Metals (index)		180	-0.5	0	-15	12	4	-4
Agriculture (index)		79	-0.7	4	1	34	30	13
Implied Volatility			%					
VIX Index (% change in pp)		26.8	0.7	-5.8	4.6	5.4	9.6	-4.3
US 10y Swaption Volatility		114.2	-5.4	-4.8	-6.9	42.6	35.2	19.9
Global FX Volatility		10.6	0.0	0.0	1.6	3.4	3.2	3.1
EA Sovereign Spreads			10-Year spread vs. Germany (bps)					
Greece		252	-0.4	6	45	134	101	12
Italy		192	0.1	1	28	71	57	20
Portugal		112	0.2	3	13	42	48	21
Spain		107	-0.3	3	13	36	33	4

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

Data source: Bloomberg.

Emerging Market Financial Indicators

Last updated: 5/18/2022 8:14 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)								
	Level		Change (in %)				YTD	Since 23-Feb-22	Level		Change (in basis points)				YTD	Since 23-Feb-22
	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		6.74	-0.1	-0.3	-6	-5	-6	-6		2.8	-5.5	-8	-9	-39	-5	-6
Indonesia		14689	-0.3	-0.9	-2	-3	-3	-2		7.3	-0.6	-8	35	86	95	83
India		78	0.0	-0.4	-2	-6	-4	-4		6.3	0.0	0	9	75	0	
Philippines		52	0.0	-0.3	0	-9	-3	-3		5.5	0.0	10	20	114	98	48
Thailand		35	-0.1	0.2	-3	-9	-4	-7		3.2	-7.0	-15	57	134	136	99
Malaysia		4.40	-0.2	-0.4	-3	-6	-5	-5		4.4	-5.1	1	25	123	80	73
Argentina		118	-0.2	-1.0	-4	-20	-13	-9		54.4	104.9	166	426	852	385	645
Brazil		4.94	0.0	4.1	-6	7	13	1		13.2	87.4	63	118	363	251	168
Chile		851	0.8	1.8	-4	-16	0	-7		6.4	0.0	4	-5	264	95	46
Colombia		4033	0.6	1.1	-7	-9	1	-3		9.2	10.5	23	112	335	278	132
Mexico		19.89	0.3	2.1	0	0	3	2		8.7	9.5	-15	3	184	122	90
Peru		3.8	0.2	0.7	-1	-1	6	-1		7.9	-0.1	-19	52	294	198	188
Uruguay		41	2.2	2.9	2	9	10	5		10.1	0.0	0	83	260	140	197
Hungary		364	0.6	-0.7	-5	-21	-11	-12		7.0	-6.0	-27	79	435	247	217
Poland		4.41	0.0	0.8	-3	-16	-9	-8		6.1	-0.3	-36	80	413	256	219
Romania		4.7	-0.2	0.1	-3	-14	-7	-7		8.0	0.5	33	156	527	316	283
Russia		64.4	0.9	3.5	26	14	17	27		11.1	-15.3	-47	-128	374	230	-11
South Africa		15.9	0.1	1.2	-8	-12	0	-5		8.5	-3.0	-9	41	98	104	88
Turkey		15.95	-0.6	-3.9	-8	-48	-17	-13		24.7	-11.0	-32	222	652	37	227
US (DXY; 5y UST)		104	0.2	-0.3	3	15	8	8		2.98	1.2	8	19	216	171	107

	Equity Markets							Bond Spreads on USD Debt (EMBIG)								
	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		3992	-0.3	0	-3	-23	-19	-14		210	4	4	0	7	2	
Indonesia		6793	2.2	0	-6	18	3	-2		203	-3	42	34	38	18	
India		54209	-0.2	0	-4	9	-7	-5		184	6	13	21	52	30	
Philippines		6728	2.0	1	-4	8	-6	-9		148	-17	32	56	47	11	
Thailand		1620	0.4	0	-3	4	-2	-4		0	0	0	0	0	0	
Malaysia		1555	0.4	0	-2	-2	-1	-2		137	9	23	17	20	4	
Argentina		90803	0.9	9	0	62	9	-1		1930	78	242	439	250	193	
Brazil		108789	0.0	6	-6	-12	4	-3		311	4	37	66	0	-20	
Chile		5023	0.0	7	3	21	17	15		167	-9	26	29	27	-7	
Colombia		1506	-0.7	0	-6	19	7	0		386	-6	44	151	38	-6	
Mexico		51464	1.8	5	-5	3	-3	0		386	1	45	57	54	16	
Peru		20267	1.1	2	-14	-7	-4	-13		188	-13	25	40	38	-2	
Hungary		42717	1.9	4	-1	-7	-16	-11		200	-2	55	60	76	47	
Poland		56659	0.7	5	-11	-11	-18	-10		-1	-7	-9	-40	-33	-17	
Romania		12121	0.5	-1	-7	4	-7	-8		229	-14	33	48	37	-3	
Russia		2467	1.8	3	5	-33	-35	-20		3411	-577	938	3228	3234	2897	
South Africa		69252	-0.6	1	-6	3	-6	-8		408	-14	76	80	53	19	
Turkey		2404	0.4	-2	-4	65	29	19		589	11	76	127	11	26	
Ukraine		519	0.0	0	0	-2	-1	0		3320	-174	132	2807	2561	1847	
EM total		41	-0.1	3	-6	-23	-15	-13		406	-8	31	57	20	-52	

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

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