GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

WEDNESDAY, MAY 22, 2024
LEAD EDITOR: JEFF WILLIAMS

- **Elevated RRP balances at the US Fed imply limited funding volatility** (link)
- **US FDIC Chair Gruenberg steps down** (link)
- **Markets scale back BoE rate cut expectations after inflation eased less than expected** (link)
- **Japan's 10-year government bond yield hit a decade high of 1%** (link)
- **The Reserve Bank of New Zealand kept its Official Cash Rate on hold as expected** (link)
- **Hungary delivers 50bp rate cut as expected, with more cautious forward guidance** (link)
- **Term-spreads of Chinese government bonds climbed to the widest in nine months** (link)

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Inflation fears refuse to go away

While investors await the Fed minutes to be released later today, as well as the much-anticipated earnings results from Nvidia, the latest UK inflation data has cast further pessimism on the likely pace of easing of advanced economy central banks. After April data showed prices rising quicker than expected in the UK, markets have significantly cut back on expectations of interest rate cuts for the BoE. Only 40 bp are now priced in for the year, down from 55 bp yesterday. Rates in other advanced economies are up this morning as well, with both the German bund and US treasury 2-year yields higher by 4bp. Yesterday, Fed speakers Waller and Bostic both pushed back on the likelihood of near-term interest rate cuts. The remarks seemed to have been largely anticipated however and did not meaningfully move pricing. Today's Fed minutes release, however, will likely offer further insight. Beyond that, the Nvidia's earnings announcement set for after the market close will be a key driver. Investors will be focused as much on the outlook presented by management as on the earnings themselves. Equities in Europe are modestly lower this morning while US equity futures are little changed.

Key Global Financial Indicators

Last updated: 5/22/24 8:46 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		5321	0.3	1	6	27	11.56
Eurostoxx 50		5026	-0.4	-1	2	15	11
Nikkei 225		38617	-0.8	1	3	25	15
MSCI EM		43	-0.6	1	8	10	8
Yields and Spreads					bps		
US 10y Yield		4.45	3.9	11	-16	74	57
Germany 10y Yield		2.54	4.5	12	6	9	52
EMBIG Sovereign Spread		364	2	-7	22	-118	-19
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		47.1	-0.3	0	2	-6	-2
Dollar index, (+) = $ appreciation		104.9	0.2	0	-1	2	3
Brent Crude Oil ($/barrel)		82.1	-0.9	-1	-6	8	7
VIX Index (%, change in pp)		12.2	0.3	0	-5	-5	0

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

Mature Markets

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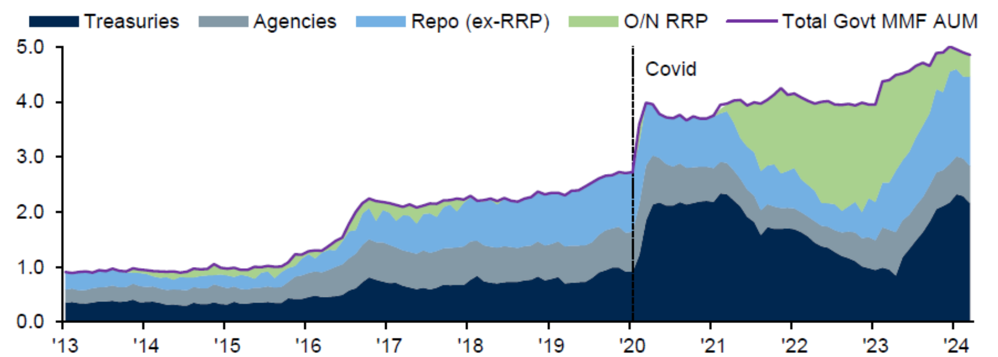
United States

Markets little changed Tuesday. Equities continued to hover near historical highs, and Treasury yields declined a few basis points across tenors. Fed Governor Waller said he doesn't expect a rate cut before the fourth quarter, and Atlanta Fed Bostic said he needs to see several more months of good inflation figures to begin rate cuts, not providing a fresh incentive to trade as both effectively validated market expectations for only one or, possibly, two cuts this year.

Cryptocurrency momentum has re-emerged in recent days amid growing optimism that the SEC will approve exchange-traded funds that invest directly in Ethereum: The cryptocurrency surged 22% over the last two days, while Bitcoin was up 5%.

Elevated Reverse Repurchase Agreement (RRP) balances imply limited repo market volatility. The assets under management (AUM) of MMFs have consistently increased since COVID-19 and will likely continue rising, while the supply of MMF investment alternatives is leveling off. Some prime funds will also convert to government MMF ahead of prime fund reform this fall, adding to demand. Analysts see that persistent RRP usage reflects the mismatch between the supply of alternative assets and MMF AUM, capping short-term funding rates to rise.

RRP fills the gap between MMF AUM and the supply of UST, Agencies, and repo ($tn)

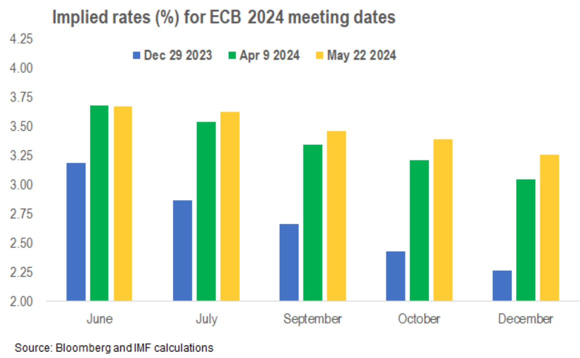


Source: Bloomberg, Federal Reserve, ICI, OFR, RBCCM.

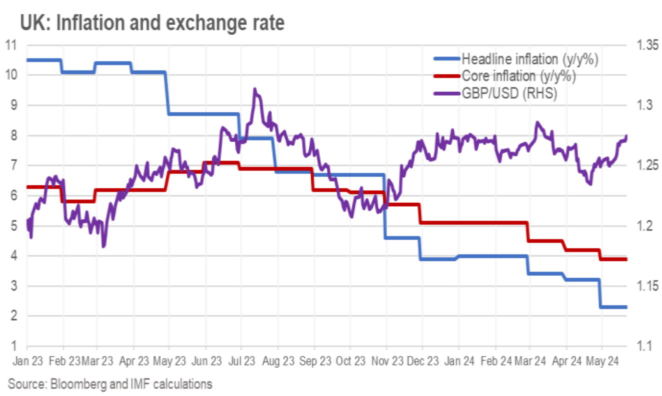
FDIC Chair Gruenberg will step down following a report that detailed allegations of harassment and discrimination during his tenure. According to Bloomberg, his exit could have significant ramifications for the Biden administration's regulatory agenda and the financial industry. If he were to leave without a replacement being confirmed, the FDIC would be split evenly 2–2 between Democrats and Republicans. The FDIC, the Fed, and OCC are working on a plan that would force big banks to hold more capital against losses, and banks have lobbied against the plan. Republicans have been receptive to banks' arguments.

Europe

European equities opened lower on the back of higher-than-expected UK inflation data. The STOXX 600 index was lower (-0.2%) in early morning trading led by declines in the energy (-1.2%) and consumer discretionary (-0.8%) sectors. Elsewhere, 10y bund yields were higher (+4bp). **Yesterday, the preliminary estimate of eurozone Q1 labor costs showed that wages rose by 4.9%y/y, up from 3.4%y/y in Q4 2023**. Focus now turns to tomorrow's flash euro area PMI and Q1 negotiated wage data. Ahead of the key Q1 wage data, President Lagarde remarked that she is "really confident that we have inflation under control..." and that "if the data we receive reinforces the confidence level that we have, that we will deliver 2% inflation in the medium-term, then there is a strong likelihood of a move on June 6." However, the path for interest rates beyond the June rate cut remains less clear with officials stressing that policy decisions beyond June will continue to be data dependent. Analysts at JP Morgan note that the new ECB staff forecasts which will be released at the June meeting and are due to be finalized this week, will likely be important for signaling future policy decisions beyond June. They expect the revised projections to show a slight uptick in core inflation in 2025 to 2.2% y/y, but to still show inflation back at the 2%y/y target in 2H2025. This morning, market pricing for ECB rate cuts in 2024 was a touch lower with around 65bp of easing priced in for this year (vs around 68bp yesterday) and the first 25bp rate cut close to fully priced in. Meanwhile, the euro was broadly flat against the dollar trading around 1.0854.

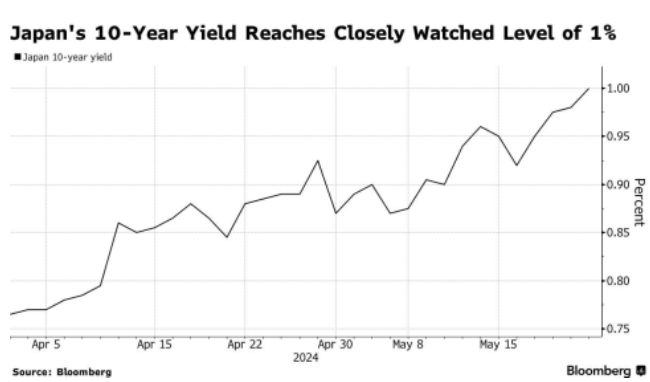


United Kingdom



The pound strengthened (+0.3%) and markets scaled back BoE rate cut expectations after April inflation eased less than expected. Data released this morning showed headline inflation easing to 2.3%y/y (versus expected 2.1% from 3.2%), core inflation easing to 3.9%y/y (versus expected 3.6% from 4.2%), while services inflation came in at 5.9% (versus expected 5.4%) Following the data release the pound strengthened against the dollar (+0.3% to 1.27) and the euro (+0.3% to 0.85). ING analysts do not see today's data release as a game-changer for the BoE and have maintained their expectations for the first BoE rate cut in August. Markets are now pricing in 40bp of easing by the BoE in 2024, compared to 55bp priced in yesterday, with 12bp of rate cuts priced in by August (compared to 25bp priced in yesterday). This morning 10Y gilts were trading sharply higher (+11bp) at 4.27% while the pound was broadly flat.

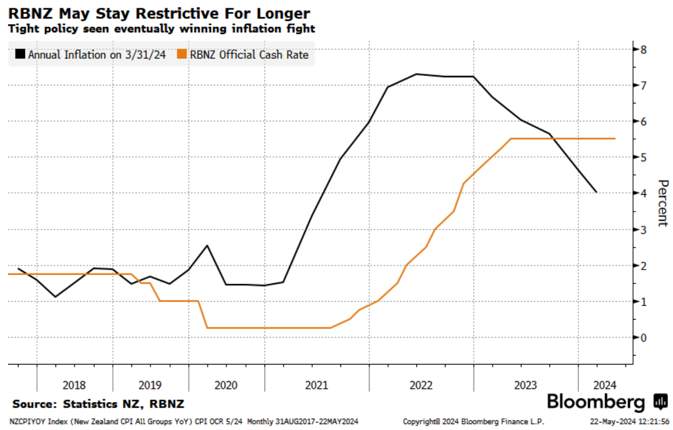
Japan



Japan's 10-year government bond yield hit a decade high of 1% (+3.1 bp), reflecting mounting speculation that the Bank of Japan (BoJ) may further tighten its monetary policy in coming months. Additionally, a weak auction of 40-year JGB added to the upward pressure on yields, with the cut-off yield slightly higher than expected at 2.27%, according to a Bloomberg survey. Traders are closely monitoring whether the BoJ will reduce the amount of bond purchase at its upcoming debt operation scheduled tomorrow. **Japanese equities declined** (NIKKEI 225: -0.8%). Some traders believe the higher bond yield has attracted some asset allocation to the bond market from equities, while expectations that BoJ will hike rates sooner than previously expected also drag on stock market sentiment. **The yen depreciated** (-0.1%). **Japan's trade balance returned to deficit in April amid the weak yen**, with imports up 8.3% y/y (consensus: +8.9% y/y, previous: -4.9% y/y), as the weak yen boosted import value in local currency terms. Exports grew 8.3% y/y (previous: +7.3% y/y), missing market expectation (+11.0% y/y) by a large margin.

New Zealand

The Reserve Bank of New Zealand (RBNZ) held its Official Cash Rate (OCR) on hold at 5.50%, as expected. The Monetary Policy Committee expressed concerns on the persistence of non-tradeable inflation, which could pose challenges to inflation expectations. In its latest projection, the central bank expected annual inflation to return to its target range of 1%-3% by end 2024, three months later than its previous forecasts made in February. The possibility of an OCR hike was discussed at the meeting. The RBNZ expected monetary policy to stay tight for longer than anticipated in the February meeting, with the updated forecast interest rate track indicating average OCR to peak at 5.65% this year, higher than the 5.60% in the February forecast, and not to fall below the current level until 2025Q3 instead of Q2. **The New Zealand Dollar appreciated** (+0.4%) and **long-end government bond yields rose** (10-year: +3.5 bp, 30-year: +3.2 bp) after RBNZ's hawkish stance.



Emerging Markets

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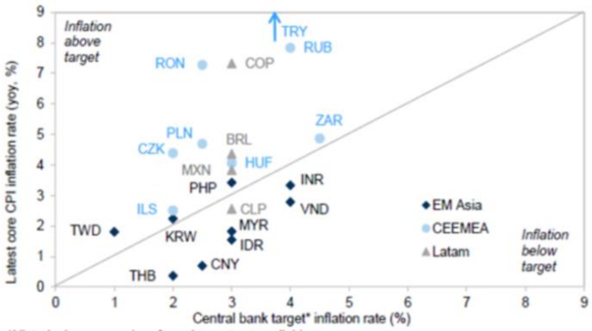
Asian equities were mixed, gaining 0.6% on net. Taiwanese equities outperformed (+1.5%), led by semiconductor stocks. Indonesian (+0.4%) and Indian (+0.3%) equities also rose, while share prices declined in Vietnam (-0.8%) and the Philippines (-0.4%). Most Asian currencies traded in a tight range, with the exception of Philippine peso, which appreciated 0.3% after the central bank warned of possible intervention in the currency after the peso weakened past the key 58 per dollar level. Long-end government bond yields were mostly little changed, except for Vietnam's 10-year yields (-5 bp). **EMEA equities and currencies are mixed today.** Equity markets were underperforming in Bulgaria (-1%) and Egypt (-0.6%) while equities in Hungary (+0.4%) gained. In CEE, currencies were mixed against the euro with the Hungarian forint (-0.3%) underperforming. On the data front, South Africa's April inflation data was marginally lower than expected—with headline inflation easing to 5.2%y/y (versus expectation to remain unchanged at 5.3%) and core inflation easing to 4.6%y/y (versus expected 4.7% from 4.9%). **Markets in LatAm were mixed on Tuesday**. Ahead of the FOMC meeting minutes release, local markets in Mexico traded lower. The benchmark equity index slid another 1.1%, and the currency sustained the largest losses among major regional currencies. Market sentiment in Brazil was also dampened by concerns over fiscal spending, with equities and currencies trading lower. According to media reports, Brazil's president, Luiz Inacio Lula da Silva, is looking to increase fiscal spending by $3 bn. Earlier in the month, the country's senate had passed a bill that modified the fiscal framework to allow this expansion. Other major regional markets closed marginally higher.

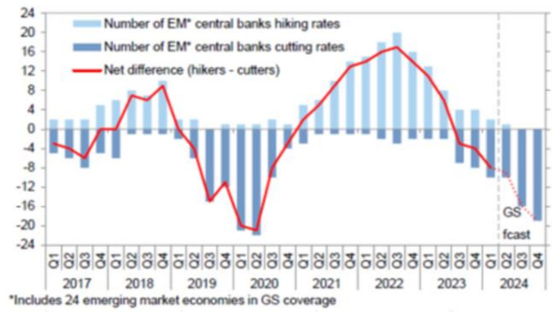
EM monetary policy

Analysts are now factoring in more rate cuts by EM central banks in 2H2024, contingent on the initiation of the Fed's easing cycle**.** It is argued that, on average, EMs have made more progress on meeting/nearing their inflation targets than most AEs. Hence, a higher number of EM central banks are seen embarking on a policy easing cycle later this year if the Fed initiates its own. However, there is some heterogeneity within EMs (LHS figure). While most EMs in Asia are below their inflation targets, some major Latin American and CEEMEA economies still have some distance to go. In fact, the policy easing cycle has been delayed further for such cases, especially now that the Fed's easing cycle is expected to be shallow. Overall, driven by Asia, the EM easing cycle is expected to broaden going forward.

Underlying inflation in most LATAM and CEEMEA economies remains above target



EM easing cycle expected to broaden in 2H2024



Source: Bloomberg, Goldman Sachs Global Investment Research

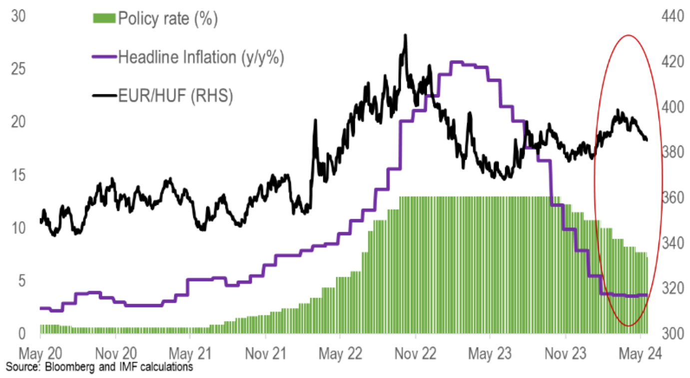
China

Term-spreads of CGB continued to widen. The CGB curve has been steepening since last December, with the gap between 10-year and 1-year government bond yields climbing to 70 bp, the widest since August 2023. Analysts believe the trend likely to continue. At the short end, investors see further room for lower yields amid speculation of monetary policy easing, while long-end yields could be relatively sticky, given the increased CGB supply, potential pickup in economic growth and regulatory warning about the risks at the back end. Long-end CGB yields were stable despite the volatility of 30-year special government bonds on the first trading day on the exchanges after the listing. Trading in both Shanghai and Shenzhen securities exchanges halted during morning session due to a surge in bond prices. Analysts attributed the abnormal fluctuations to thin liquidity and greater participation of retail investors for exchange-traded bonds, which have little impact on interbank trading. Separately, **China reportedly hinted at retaliation in trade disputes with the EU**, as a deadline approaches for the EU to announce its investigation results on China's electric vehicle subsidies. The possible tariff on cars with large engines imported from the EU could be as high as 25%, Bloomberg reports. Chinese equities gained (CSI 300: +0.3%); the RMB was little changed.

Hungary

The forint was marginally stronger yesterday after the central bank cut its policy rate by 50bp to 7.25%, as widely anticipated, with the message seen as more cautious. The accompanying statement noted that volatility in international investor sentiment and risks surrounding global and domestic disinflation warrants a careful and patient approach to monetary policy. The statement also noted that the expected divergence between monetary policy of the US Fed and the ECB could see higher volatility in emerging markets. Deputy Governor Virag indicated that rates could be cut again in June—either by 25bp or 50bp—but after this he sees very limited room for further monetary easing. Deutsche Bank analysts expect a 50bp rate cut in June but note that renewed pressure on the exchange rate could result in a 25bp rate cut. Moreover, Deutsche bank analysts now see upside risk to their forecast for the policy rate to reach 6% by end-2024 and have revised their terminal rate forecast for 2025 higher (to 5% from 4.5%). The forint appreciated marginally yesterday but was weaker this morning (-0.3% to 386.70/€).

Hungary: Currency inflation and policy rate

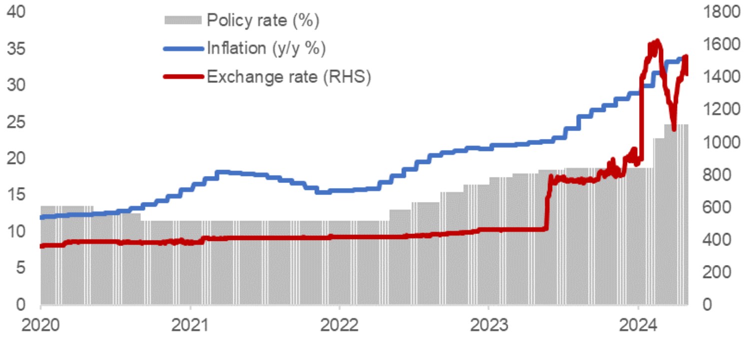


Source: Bloomberg and IMF calculations

Nigeria

The Nigerian naira appreciated after the central bank surprised with a larger-than-expected rate hike yesterday. The central bank hiked its benchmark interest rate by 150bp to 26.25%, while consensus had expected a 100bp rate hike. Bloomberg analysts, had, however, expected a 200bp rate hike given the recent weakening in the naira. Headline inflation rose less than expected to 33.7%y/y in April (est. 34.2%, from 33.2% in March), and ICBC analysts expect headline inflation to peak in May 2024 and ease to 27.5% by the end of this year. Against this backdrop the analysts expect policy rates to remain unchanged until end-2024. Bloomberg analysts, however, expect another 100–150bp hike at the July monetary policy meeting, with expectations that monthly price gains would accelerate in May as the impact of the weaker Naira would be the most pronounced then. The Nigerian naira strengthened yesterday (+3.6%) with Bloomberg data showing a further strengthening this morning (+4.2%) but remains roughly 5% weaker than at the start of Q2.

Nigeria: Policy, Inflation and Exchange rate



Source: Bloomberg and IMF calculations

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Global Financial Indicators

5/22/24 8:46 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		5323	0.3	0	6	27	12
Europe		5026	-0.4	-1	2	15	11
Japan		38617	-0.8	1	3	25	15
China		3684	0.2	2	5	-6	7
Asia Ex Japan		73	-0.8	1	9	9	9
Emerging Markets		43	-0.6	1	8	10	8
Interest Rates					basis points		
US 10y Yield		4.45	3.9	11	-16	74	57
Germany 10y Yield		2.54	4.5	12	6	9	52
Japan 10y Yield		1.01	2.9	5	12	62	40
UK 10y Yield		4.24	11.1	18	4	18	70
Credit Spreads					basis points		
US Investment Grade		116	0.0	-2	-6	-51	-17
US High Yield		340	-1.3	-7	-22	-149	-46
Exchange Rates					%		
USD/Majors		104.85	0.2	0	-1	2	3
EUR/USD		1.08	-0.2	0	2	0	-2
USD/JPY		156.6	0.3	1	1	13	11
EM/USD		47.1	-0.3	0	2	-6	-2
Commodities					%		
Brent Crude Oil ($/barrel)		82.1	-0.9	-1	-5	13	7
Industrials Metals (index)		168	-2.5	3	6	16	18
Agriculture (index)		62	0.4	3	4	-5	-1
Implied Volatility					%		
VIX Index (%, change in pp)		12.2	0.3	-0.3	-4.8	-5.0	-0.3
Global FX Volatility		6.8	0.0	-0.2	-0.5	-1.9	-1.3
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		100	0.3	0	-6	-42	-3
Italy		131	0.8	-1	-6	-55	-37
Portugal		64	-0.2	0	0	-15	0
Spain		77	0.2	0	-1	-28	-20

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

Emerging Market Financial Indicators

Last updated: 5/22/2024 8:47 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		7.24	0.0	-0.3	0	-3	-2		2.3	-0.5	-1	-4	-52	-27
Indonesia		15995	0.0	0.2	2	-7	-4		6.9	-4.3	-3	2	51	46
India		83	0.0	0.3	0	-1	0		7.4	-2.9	0	-14	23.3	19
Philippines		58	0.3	-0.9	-1	-4	-5		5.6	0.0	-3	-4	-31	-3
Thailand		36	0.0	-0.2	2	-5	-6		2.9	1.8	0	-5	17	16
Malaysia		4.70	-0.2	0.4	2	-3	-2		3.9	1.3	-3	-8	13	15
Argentina		889	0.0	-0.4	-2	-74	-9		34.4	5.5	-299	-1006	-6974	-5196
Brazil		5.14	-0.3	-0.1	1	-3	-6		11.8	11.0	21	25	-14	144
Chile		896	-0.9	1.0	6	-11	-2		5.1	0.0	0	-20	-21	22
Colombia		3814	0.1	0.9	3	19	2		8.1	0.0	-5	-27	-72	45
Mexico		16.66	-0.1	0.1	3	7	2		9.2	0.0	6	-23	73	73
Peru		3.7	0.1	-0.3	-1	-1	-1		7.0	-0.1	-2	-41	-40	37
Uruguay		38	0.3	0.8	0	1	1		9.1	2.8	-2	15	-87	-39
Hungary		358	-0.8	-1.0	3	-3	-3		6.6	5.0	17	-45	-142	80
Poland		3.94	-0.5	-0.6	3	6	0		5.2	4.3	2	-18	-28	71
Romania		4.6	-0.2	-0.5	2	0	-2		6.5	-0.3	3	2	-33	34
Russia		90.3	-0.1	1.0	4	-11	-1							
South Africa		18.2	-0.7	0.4	5	6	1		9.6	1.5	-13	-57	-54	48
Türkiye		32.18	0.1	0.1	1	-38	-8		27.6	21.0	19	-128	1855	80
US (DXY; 5y UST)		105	0.2	0.5	-1	2	3		4.47	4.1	13	-18	71	63

	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
								basis points				
China		3684	0.2	2	5	-6	7		141	1	-2	-54
Indonesia		7222	0.5	1	2	7	-1		94	-6	-3	-48
India		74221	0.4	2	1	20	3		93	0	-10	-59
Philippines		6607	-0.4	1	2	0	2		84	-6	1	-32
Thailand		1371	0.0	0	2	-10	-3		0	0	0	0
Malaysia		1622	0.0	1	4	14	12		77	-2	-7	-23
Argentina		1581107	3.0	12	25	366	70		1300	52	81	-1309
Brazil		127412	-0.3	-1	1	16	-5		214	-4	-3	-49
Chile		6710	0.8	0	5	19	8		112	-4	-4	-17
Colombia		1441	-0.1	2	7	28	21		296	1	-10	-110
Mexico		56761	-1.1	-1	0	6	-1		287	-9	-32	-109
Peru		30892	0.6	4	11	43	19		140	-4	-6	-39
Hungary		67991	0.2	-1	4	46	12		140	-8	-10	-93
Poland		88094	-0.7	0	4	35	12		93	-6	1	-41
Romania		17497	0.3	1	4	43	14		174	-7	-8	-78
South Africa		79892	0.1	1	9	2	4		311	-18	-35	-150
Türkiye		10872	-0.2	7	13	143	46		278	-3	-7	-348
EM total		43	0.4	1	8	10	8		325	-3	37	-100

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

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