GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

MONDAY, MAY 23, 2022

- **US equity markets remain volatile amid growing fears of recession** (link)
- **ECB President sees possibility of ECB ending negative interest rates in Q3** (link)
- **EM fund flows continue to suffer outflows** (link)
- **EM hard currency bond issuance continues to struggle** (link)
- **India's government unveils inflation-fighting measures** (link)
- **Local rates in Eastern Europe trade lower** (link)
- **S&P unexpectedly upgrades South Africa's credit outlook** (link)

Mature Markets | Emerging Markets | Market Tables

Markets open the week cautiously following Biden comments

European bourses and US equity futures rose modestly this morning after President Biden separate comments on China tariffs and Taiwan POC. Biden said that the tariffs on China imposed by the Trump administration were under consideration. Separately, he said that that the US military would intervene to defend Taiwan POC in any attack from China. Moreover, his **a**dministration also announced a trade initiative for a dozen Indo-Pacific countries in an effort to foster economic engagement in the region as the US seeks to counter China’s influence. Concerns about the COVID situation in Beijing were also contributing to the cautiousness of investors to start the week, with the VIX hovering near 30 percentage points, well above long-term historical averages. In bond markets, US Treasury and Bund yields rose modestly, with measures of option-implied volatility in rates markets also remaining elevated. Elsewhere, the dollar weakened significantly this morning as Biden comments on the potential easing of tariffs on China supported the renminbi while the euro appreciated to its highest level to the dollar in four weeks after ECB’s president Lagarde said that they are likely to be in a position to exit negative interest rates by end-Q3, reaffirming expectations that rates will start increasing in July.

Key Global Financial Indicators

Last updated: 5/23/22 8:08 AM	Level: Last 12m	Latest	Change from Market Close: 1 Day	7 Days	30 Days	12 M	YTD	Since 23-Feb-22
Equities					%		%	
S&P 500		3901	0.0	-3	-9	-6	-18	-8
Eurostoxx 50		3673	0.4	0	-4	-9	-15	-8
Nikkei 225		27002	1.0	2	0	-5	-6	2
MSCI EM		41	0.4	2	-3	-23	-16	-13
Yields and Spreads					bps			
US 10y Yield		2.82	3.8	-6	-8	120	131	83
Germany 10y Yield		0.97	2.1	3	-1	110	114	74
EMBIG Sovereign Spread		489	3	20	78	154	122	76
FX / Commodities / Volatility					%			
EM FX vs. USD, (+) = appreciation		53.2	1.2	3	1	-8	1	0
Dollar index, (+) = $ appreciation		102.2	-0.9	-2	1	14	7	6
Brent Crude Oil ($/barrel)		113.5	0.9	-1	6	71	46	17
VIX Index (%, change in pp)		29.4	-0.1	2	1	9	12	-2

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

The Week Ahead

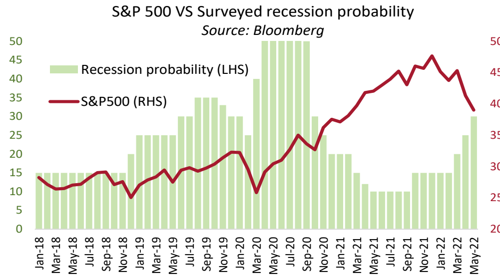
The FOMC Meeting minutes will be released on Wednesday and GDP on Thursday. Several interest rate decisions are scheduled for this week (with surveyed expectations for policy rate changes shown in brackets): on Monday, Israel (+25 bps) and Ghana (+200 bps); on Tuesday, Indonesia (unchanged), New Zealand (+50 bps), and Nigeria (unchanged); on Thursday, South Korea (+25 bps), and Turkey (unchanged).

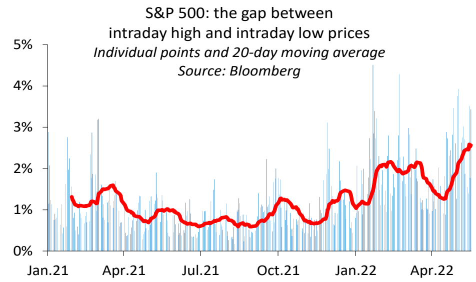
Mature Markets

back to top

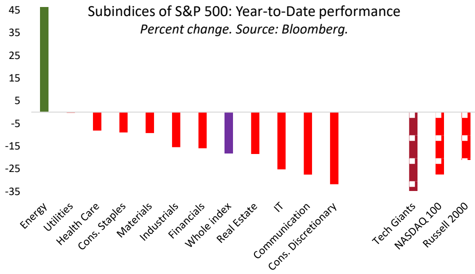
United States

The S&P 500 experienced large intraday swings on Friday, dropping by more than 2% by noon, while fully recovering in late trading. The volatility was caused by investor concerns about the Fed's pace of tightening and the increasing probability of a recession in the medium-term. US Treasury 10-year nominal yields fell by 5 bps, mostly driven by lower breakeven inflation. The dollar appreciated 0.3% versus major currencies. **The cumulative fall of S&P 500 year-to-date is close to 20% amid an increasing probability of a forthcoming recession** (left chart below). Bearish sentiment and short positioning appear to be self-reinforcing as many market participants have been looking for a trigger to kick start a correction in asset prices. Additionally, the Fed seems to be comfortable to continue its tightening amid current financial conditions—thus, making investors believe that no *Fed put* is going to be executed any time soon to support the markets. Yet, the **divergence in outlooks among investors makes intraday volatility elevated** (right chart with the difference between intraday high and intraday low prices).





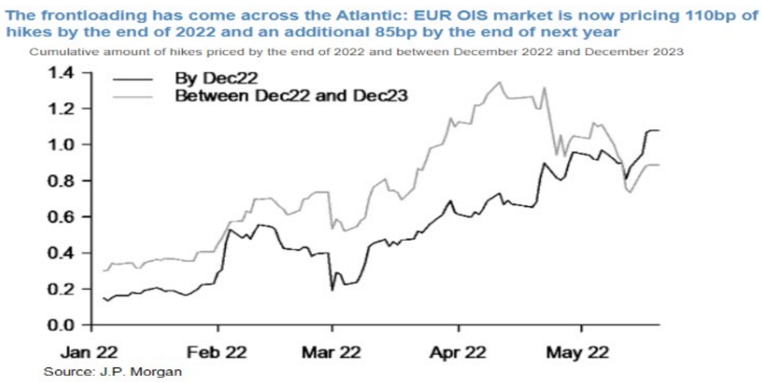
The decline in equities is starkly heterogenous across sectors (left chart below)**.** The consumer discretionary sector was hit the most due to concerns that corporate profit margins are getting eroded as input costs would not be fully passed to consumers and consumer spending might be slowing down. These effects were already observed in Target and Walmart quarterly results, with analysts expecting this to become evident in other sectors as well. Information technology and communications services sectors have been hit as well, with tech equities being among the most shorted stocks. Even though the price-to-earnings ratio for tech-heavy indexes (e.g., Nasdaq 100 on the right chart) is returning to its pre-covid levels, analysts noted that there is further potential for price declines.



Euro-area

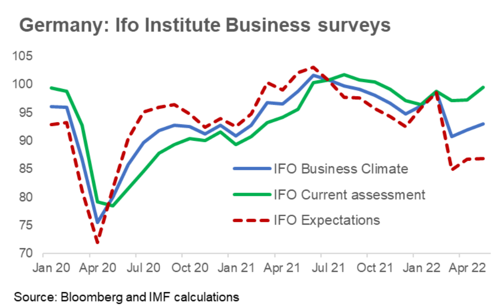
Euro-area equity markets rose (Stoxx 600 Europe +0.5%). The euro appreciated (+1%) and sovereign yields increased (10-year bund +4 bps) following comments from ECB President Lagarde and an upside surprise in Germany's Ifo business climate survey data. The euro remains roughly 6% weaker than at the start of the year.

ECB President Lagarde said the current outlook allows for interest rates to move out of negative territory by the end of Q3 - she expects net asset purchases to end very early in the third quarter, allowing the ECB to raise the interest rate increase in July. Dutch central bank governor Knot last week hinted at the possibility of a +50 bps hike, while Lagarde's comments instead indicate two +25 bps increases. Lagarde also noted that new instruments could be designed and deployed to ensure monetary policy transmission. **Cumulative interest rate tightening expected in the euro area this year now exceeds the total tightening expected in 2023**. Markets started pricing in additional hikes in 2022 last week following hawkish commentary from ECB General Council members, and with the additional frontloading **EUR OIS markets are pricing in roughly +110 bps of hikes in 2022, and an additional +85 bps by end-2023.** JP Morgan analysts expect this trend to continue in the absence of a large macro shock.



Analysts noted that ECB hawks could use the weaker euro as an argument for a larger interest rate hike in July, as a higher policy rate could strengthen the euro and weigh on inflation via the exchange-rate channel. While ING analysts estimate that a weaker euro has a relatively small impact on inflation, they argue that the exchange rate channel is likely the only efficient way to ease inflationary pressures. Analysts point out that while the exchange rate was not a focal point in the ECB April meeting, ECB officials have started to comment on the weakness of the currency over the past few days.

Germany's May Ifo Institute business climate index, a leading indicator for Germany, surprised on the upside for the second consecutive month, increasing to 93.0 (vs expected 91.4 from a revised 91.9 in April). Businesses assessed their current situation as better than in April, while the expectations index also edged higher to 86.9 from 86.8, ahead of the expected marginal decline to 86.5. **While not expecting Germany's economy to dive as it did in 2020, analysts remain cautious over Germany's outlook citing stagflation concerns and the longer-term impact of the war in Ukraine.** Separately, the European Commission preliminary May consumer confidence indicator surprised on the upside, increasing to -21.1 (vs expected -21.5, from 22), while remaining below its long-term average.



Australia

Anthony Albanese was elected as Prime Minister. He led the Labor party to win the election, ending nine years of the Conservative government. Analysts noted that a Labor government will likely increase spending, which would have an impact at the margin on the central bank policy. The new government is expected to take a tougher stance on climate policy. The **Australian dollar appreciated (+1.0%),** in part driven by a short squeeze following some improvement in global risk-on sentiment. Equities were little changed; long-end government bond yields were mixed (10-year: +1.5 bps; 30-year: -0.5 bp).

Emerging Markets

back to top

Asian equities were mixed. Hong Kong (-1.3%), Indonesian (-1.3%), and Chinese (CSI 300: -0.6%) declined, while share prices rose in India (+0.7%) and Thailand (+0.6%). **Most Asian currencies appreciated,** led by Chinese yuan (+0.4%) and Singapore dollar (+0.4%). Long-end government bond yields generally declined, with 10-year yields falling in Thailand (-12 bps), Malaysia (-10 bps), and Taiwan POC (-10 bps). In **Singapore,** core CPI inflation increased to 3.3% y/y in April from 2.9% in March (consensus: 3.4%). Headline CPI inflation stayed at 5.4%. In **EMEA, equities and currencies gained in line with global markets.** The central bank of Israel is expected to hike rates 25 bps to 0.6% (today) while the central bank of Ghana is expected to hike 200 bps to 19% (today). Some analysts are calling for a hike of 100 bps in Nigeria (Tuesday) while the central bank of Turkey is expected to keep rates unchanged at 14% (Thursday). **Latin American equities were mixed while most currencies appreciated on Friday.** Equities rallied in Brazil (1.4%) and Mexico (0.5%) but declined in Argentina (-0.6%). Meanwhile, currencies appreciated in Mexico (+0.3%) and Brazil (+1.1%). The Colombian peso outperformed (+2.9%) as the latest polls revealed surging support for presidential election outsider.

EM Fund Flows

EM bond funds saw large outflows last week, while EM equity funds outflows eased. EM bonds outflows breached -$5 bn last week, split between hard currency bond funds outflows (-$1.2 bn) and local currency bond funds (-$3.9 bn). The local currency bond outflows were led by China outflows reaching a record -$2.7 bn, and EM ex-China outflows hitting their highest level since the pandemic (-$1.2 bn). Meanwhile, EM equity funds saw minimal outflows at -$0.1 bn, from -$1.8 bn last week. Within the regional equity funds, outflows were seen in Latin America (-$92 mn) and EMEA (-$44 mn), while Asia ex-Japan saw inflows ($1.1 bn).

Weekly Cross-asset Flows (USD billion)

USD billion

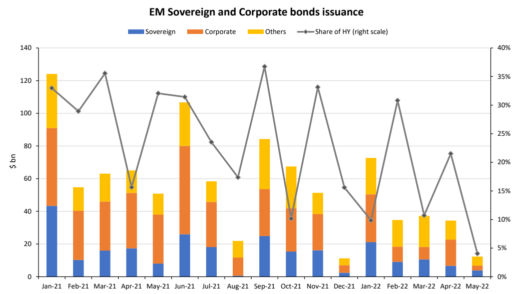
	Asset	8w flows (8w ago → current)	This wk	YTD
Fund Flows	**EM Bonds and Equities**		-5.2	-1.5
	EM Bonds		-5.1	-33.5
	Hard Ccy		-1.2	-18.0
	Local Ccy^		-3.9	-15.5
	o.w. EM ex-China		-1.2	-5.4
	o.w. China		-2.7	-10.4
	EM Equities		-0.1	32.0
	US HG		-3.7	-36.6
	US HY		-2.8	-35.5
	Global Equities		-2.7	75.6
	EM Bond and Equity ETFs		-0.1	35.9
	EM Bond ETFs		-2.0	-4.6
	EM Equity ETFs		1.9	40.5
	Non-resident EM flows*		-4.1	-58.5

*High frequency non-resident EM portfolio flow data

Source: JP Morgan

EM Bond Issuance

EM hard currency bond issuance continues to struggle, particularly for high-yield borrowers. As global financial conditions tightened, EM are issuing fewer bonds. As of today, EM bond total issuance was at $12 bn in May 2022, against $50 bn a year ago, and $73 bn in January 2022. High-yield issuance has been particularly impacted, with its share in total EM issuance dropping to only 4% this month. On the sovereign side, EM issuance has declined from $21 bn in January 2022 to a modest $4 bn in May, with no high-yield issuance so far this month.

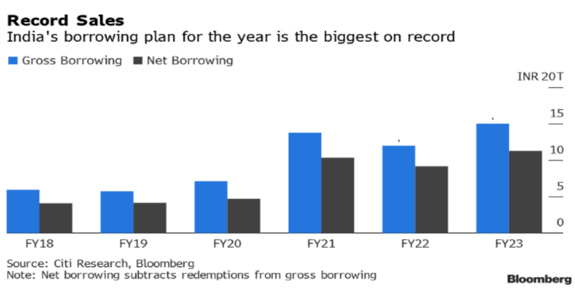


China

Chinese equities declined on concerns about the COVID situation in Beijing (CSI 300: -0.6%; Heng Seng China Enterprises: -1.5%). Beijing reported a record number of COVID cases, reviving concerns about a potential lockdown. Meanwhile, Shanghai proceeded with its gradual re-opening. Premier Li Keqiang also said that the government is taking active measures to help foreign firms deal with the impact of COVID-19 outbreaks, including issues around production resumption, inbound business travel, and logistics and transportation. The renminbi (RMB) appreciated (+0.4%), supported by the news that the US tariffs imposed by the Trump administration could be removed. **Didi's shareholders set to vote on de-listing today.** The company proposed to get de-listed first and address data security issues before exploring a new listing. Analysts noted that Didi's proposed de-listing, if realized, will likely weaken investors' confidence in Chinese stocks.

India

The government unveiled inflation-fighting fiscal measures. The measures, which include lower fuel taxes, are estimated to cost about $26 bn. Markets are closely watching the implications on the government's bond borrowing program and the Reserve Bank of India (RBI)'s monetary policy. Some analysts noted that a two-pronged approach to control inflation from both monetary and fiscal sides could mean that the RBI may not need as many policy rate hikes as initially expected. At the same time, additional fiscal borrowing could push up bond yields and impact the corporate bond market. The Indian rupee slightly depreciated (-0.1%); equities gained (+0.7%); government bond yields were little changed (1-year: flat; 10-year: +0.9 bp; 30-year: +0.8 bp).

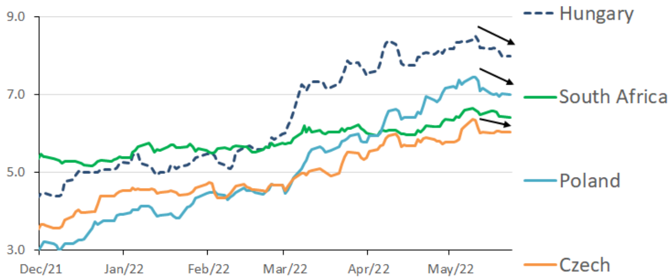


Eastern Europe

Local rates in Eastern Europe have settled at somewhat lower rates. Following recent upside inflation surprises, analysts have revised terminal rate forecasts for Czech Republic and Hungary, and some expect that Poland, Hungary and Czech Republic will start cutting interest rates in 2023. Analysts are closely following fiscal consolidation plans in Hungary to assess implications for inflationary pressures. Analysts at

Citi expect Polish wage growth to remain strong and see the key policy rate reaching 6.5% in July (+75 bps in June and +50 bps in July).

Eastern Europe: 2-yr swap rates (local currency, %)



Source: Bloomberg and IMF staff.

South Africa

5-year and 10-year local rates opened the week around 9 bps lower after S&P unexpectedly upgraded its sub-investment grade outlook of BB- to positive from stable, signaling the next move could be a ratings upgrade. The more optimistic assessment reflects the *expectation that favorable terms of trade, a path toward contained fiscal expenditure, and the implementation of some structural reforms could lead to a continued easing of fiscal and external pressures.* **The rand (+0.7%) also gained.**

Russia

The ruble appreciated +6% against the dollar following reports that Russia may ease capital controls later this week, with the share of FX revenues exporters must convert into rubles dropping from 80% to 50%. The Bank of Russia also denied reports that it resumed FX purchases to keep the ruble from strengthening. On Wednesday May 25, the U.S. Treasury is expected to let the waiver that allows Russia to pay Eurobond investors expire.

This monitor is prepared under the guidance of Ranjit Singh (Assistant Director), Nassira Abbas (Deputy Division Chief), Charles Cohen (Deputy Division Chief), and Antonio Garcia-Pascual (Deputy Division Chief). Fabio Cortes (Senior Economist), Reinout De Bock (Economist-London representative), Sanjay Hazarika (Senior Financial Sector Expert), Tom Piontek (Financial Sector Expert) and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Sergei Antoshin (Senior Economist), Yingyuan Chen (Financial Sector Expert), Mohamed Diaby (Economist, EP), Dimitris Drakopoulos (Senior Financial Sector Expert), Torsten Ehlers (Senior Financial Sector Expert), Deepali Gautam (Research Officer), Frank Hespeler (Senior Financial Sector Expert), Shoko Ikarashi (Externally Financed Appointee), Phakawa Jeasakul (IMF Resident Representative in Hong Kong SAR), Esti Kemp (London Representative), Kleopatra Nikolaou (Senior Financial Sector Expert), Natalia Novikova (IMF Resident Representative in Singapore), Patrick Schneider (Research Officer), Dmitry Yakovlev (Senior Research Officer), Akihiko Yokoyama (Senior Financial Sector Expert), and Xingmi Zheng (Research Assistant). 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.

Global Financial Indicators

Last updated: 5/23/22 8:09 AM	Level		Change					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
Equities				%			%	%
United States		3908	0.0	-3	-9	-6	-18	-8
Europe		3673	0.4	0	-4	-9	-15	-8
Japan		27002	1.0	2	0	-5	-6	2
China		4054	-0.6	2	1	-21	-18	-12
Asia Ex Japan		69	0.4	2	-2	-24	-16	-12
Emerging Markets		41	0.4	2	-3	-23	-16	-13
Interest Rates				basis points				
US 10y Yield		2.82	3.8	-6	-8	120	131	83
Germany 10y Yield		0.97	2.1	3	-1	110	114	74
Japan 10y Yield		0.24	-0.2	-1	-1	16	17	4
UK 10y Yield		1.91	2.0	18	-5	108	94	43
Credit Spreads				basis points				
US Investment Grade		171	-1.0	5	17	80	60	29
US High Yield		505	-4.1	17	112	161	168	99
Europe IG		97	-3.5	3	12	45	49	25
Europe HY		472	-16.3	21	73	215	230	120
Exchange Rates				%				
USD/Majors		102.22	-0.9	-2	1	14	7	6
EUR/USD		1.07	0.9	2	-1	-13	-6	-6
USD/JPY		127.6	-0.2	-1	0	17	11	11
EM/USD		53.2	1.2	3	1	-8	1	0
Commodities				%				
Brent Crude Oil ($/barrel)		114	0.9	-1	7	81	50	25
Industrials Metals (index)		185	-0.4	3	-12	20	7	-2
Agriculture (index)		78	0.5	-1	2	36	28	11
Implied Volatility				%				
VIX Index (%, change in pp)		29.4	-0.1	1.9	1.2	9.2	12.1	-1.7
US 10y Swaption Volatility		115.5	3.5	-2.7	-10.4	47.6	36.5	21.2
Global FX Volatility		10.6	0.1	-0.4	1.2	3.6	3.2	3.2
EA Sovereign Spreads				10-Year spread vs. Germany (bps)				
Greece		275	-2.7	15	73	164	124	35
Italy		200	-5.4	10	30	84	65	29
Portugal		116	-2.6	4	14	47	52	24
Spain		112	-2.1	6	15	43	37	8

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

Emerging Market Financial Indicators

Last updated: 5/23/2022 8:13 AM	Exchange Rates: Level		Change (in %)					Since	Local Currency Bond Yields (GBI EM): 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		6.65	0.7	2.1	-1	-3	-4	-5		2.8	-2.3	-2	-2	-31	-1	-2
Indonesia		14672	-0.2	0.2	-1	-2	-3	-2		7.2	-3.7	-20	19	72	80	69
India		78	0.0	0.4	-1	-6	-4	-4		6.3	0.0	0	9	75	0	
Philippines		52	-0.1	0.4	0	-8	-2	-2		5.4	-2.5	3	15	103	95	45
Thailand		34	0.8	1.6	0	-8	-3	-6		3.0	-10.5	-37	21	104	110	73
Malaysia		4.39	0.0	0.1	-1	-6	-5	-5		4.2	-13.7	-19	4	102	64	56
Argentina		118	-0.1	-0.9	-4	-20	-13	-9		55.5	77.0	227	490	995	489	750
Brazil		4.84	0.9	4.6	1	10	15	4		11.8	-26.6	-55	-31	220	109	25
Chile		836	0.1	2.9	-3	-14	2	-6		6.1	0.0	-26	-36	221	66	17
Colombia		3976	1.9	3.4	-5	-6	2	-2		8.8	-25.0	-33	64	273	234	88
Mexico		19.82	0.2	1.0	2	0	4	2		8.5	-16.0	-24	-24	139	94	62
Peru		3.7	0.2	1.7	0	-1	7	0		7.8	-1.5	-5	4	293	188	178
Uruguay		40	0.4	3.1	1	10	11	5		10.1	0.0	-1	70	250	139	196
Hungary		359	1.5	4.3	-3	-21	-10	-11		6.7	4.5	-37	1	393	214	184
Poland		4.34	1.1	3.0	0	-15	-7	-7		5.9	5.8	-19	23	391	238	201
Romania		4.6	0.9	2.1	-1	-13	-6	-6		7.9	-5.6	-2	146	516	310	277
Russia		58.1	7.0	10.7	29	26	29	41		10.5	1.2	-83	-198	308	170	-71
South Africa		15.7	0.8	2.7	0	-11	1	-4		8.1	-11.0	-40	-11	76	69	53
Turkey		15.81	0.6	-1.6	-7	-47	-16	-13		24.3	-16.0	-63	253	606	-2	188
US (DXY; 5y UST)		102	-0.8	-1.8	1	14	7	6		2.82	2.6	0	-11	200	156	92

	Equity Markets: Level		Change (in %)					Since	Bond Spreads on USD Debt (EMBIG): 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		4054	-0.6	2	1	-21	-18	-12		214	6	9	3	11	6
Indonesia		6841	-1.1	4	-5	19	4	-1		221	13	47	49	56	36
India		54289	-0.1	2	-5	7	-7	-5		195	10	23	36	63	41
Philippines		6688	-0.9	3	-4	8	-6	-9		159	0	29	64	58	22
Thailand		1635	0.8	3	-3	5	-1	-4		0	0	0	0	0	0
Malaysia		1543	-0.4	0	-4	-2	-2	-3		140	5	25	19	23	7
Argentina		88119	-0.6	3	-4	57	6	-4		1952	58	250	455	272	215
Brazil		108488	1.4	1	-2	-12	3	-3		329	21	57	80	18	-2
Chile		4983	0.1	2	2	22	16	14		186	17	32	44	46	12
Colombia		1459	3.4	-4	-10	17	3	-3		405	22	62	161	57	13
Mexico		51518	0.4	4	-3	3	-3	0		406	23	49	74	74	36
Peru		20300	0.4	2	-13	-1	-4	-13		205	15	28	51	55	15
Hungary		42825	2.5	4	-1	-8	-16	-10		227	23	77	85	103	74
Poland		56844	2.1	3	-7	-11	-18	-10		44	42	36	6	12	28
Romania		12209	1.4	1	-6	5	-7	-8		278	44	73	95	86	46
Russia		2323	-2.1	-2	4	-37	-39	-25		3411	-577	938	3228	3234	2897
South Africa		68705	1.7	-1	-5	4	-7	-8		437	24	100	114	82	48
Turkey		2357	-0.7	-3	-5	62	27	17		613	11	109	148	35	50
Ukraine		519	0.0	0	0	-2	-1	0		3112	-295	-399	2614	2353	1639
EM total		41	0.6	2	-3	-23	-16	-13		421	11	34	68	35	-37

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

back to top