GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

TUESDAY, MAY 23, 2023

- **Talks on debt limit resume between US House Speaker and President Biden** (link)
- **Measure of global corporate debt trading in distress remains elevated** (link)
- **Outperformance of services relative to manufacturing widens in euro area** (link)
- **Committee rules sale of Credit Suisse was not a bankruptcy credit event** (link)
- **Hong Kong SAR to allow retail investors to trade crypto assets** (link)
- **Corporate nearshoring drives surge in foreign direct investment to Mexico** (link)

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Global risk sentiment subdued as US debt limit deal remains elusive

Global risk assets are range bound this morning despite optimistic signals from US officials last night that a debt ceiling deal could be reached this week. Global equities started the week with a mixed session on Monday, as early gains were not able to hold across markets with investors awaiting the latest update on US debt limit discussions. Yesterday evening saw negotiators making progress surrounding the US debt ceiling as US House Speaker McCarthy signaled discussions were on the right path and that his meeting with President Biden was productive. However, with no deal in place yet, risk appetite has not been able to establish much traction as most Asian equity indices posted losses overnight and European bourses and US futures are trading slightly lower. PMI data in Europe showed a further slide in manufacturing activity, but also that the service sector remains firmly in expansionary territory. In response, core sovereign bond yields are rising, primarily on the short-end of the curve, as two-year yields are up 4–8 bps in the US, Germany, and UK, and has been partially driven by further hawkish commentary from central bank officials.

Key Global Financial Indicators

Last updated: 5/23/23 8:02 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		4193	0.0	1	1	6	9	-1
Eurostoxx 50		4362	-0.5	1	-1	18	15	10
Nikkei 225		30958	-0.4	4	8	16	19	17
MSCI EM		39	0.8	0	1	-5	4	-17
Yields and Spreads				bps				
US 10y Yield		3.74	2.9	21	17	89	-13	175
Germany 10y Yield		2.49	2.7	13	1	147	-9	226
EMBIG Sovereign Spread		480	-1	-11	-10	-9	28	67
FX / Commodities / Volatility				%				
EM FX vs. USD, (+) = appreciation		50.1	-0.2	-1	-1	-6	0	-6
Dollar index, (+) = $ appreciation		103.5	0.3	1	2	1	0	8
Brent Crude Oil ($/barrel)		76.6	0.8	2	-6	-32	-11	-21
VIX Index (%, change in pp)		17.6	0.3	0	1	-11	-4	-13

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

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United States

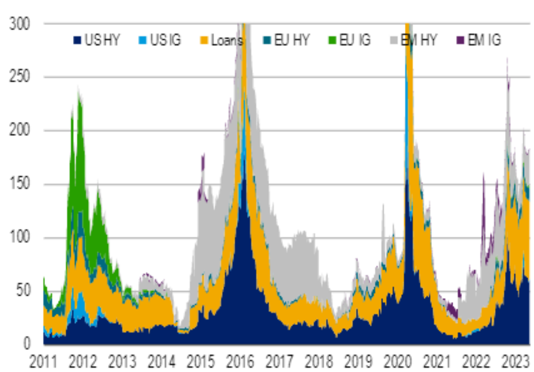
S&P 500 index closed up 0.1%, and the KBW US regional banking index gained 3% on Monday. After the market close, President Biden and Republican House Speaker McCarthy met to try to make progress on debt limit talks. Both were cautiously optimistic about a deal after the meeting. Still, disagreements remain as Democrats have resisted large-scale domestic spending cuts, and Republicans have resisted any tax changes as part of the debt deal. US Treasury Secretary Yellen warned earlier Monday that it's now highly likely that the Treasury will run out of sufficient cash in early June. The T-bills yield spread between June 1 and May 30 maturities widened to more than 250 bps.

Corporate earnings have been better than feared. With 95% of S&P 500 firms having reported, analysts view Q1 earnings as much better than feared. According to Goldman Sachs, real corporate revenues, excluding the volatile energy sector, continued to rise steadily, estimated at +0.6% annualized over the last two quarters, consistent with the below potential but non-recessionary growth environment.

There were mixed signals from Fed officials on Monday. St. Louis Fed Bullard indicated two more rate hikes this year, and Minneapolis Fed Kashkari believed the Fed should signal that tightening is not over if the bank pauses next month. Meanwhile, Atlanta Fed Bostic supported a June pause, and Richmond Fed Barkin preferred to keep his options open. Ten-year US Treasury yields rose 4.4 bps to 3.72%. The market-implied probability for a June FOMC hike is about 25%.

Figure 4: Deep distress volumes over time

Deep distress: HY price<60pt, IG OAS>1000bp, loan price<75pt



Source: BofA Global Research

Deep-distressed corporates may increase after debt-limit negotiations are resolved. BofA analysts argue that the amount of the deep-distress segment (defined as high-yield corporate bond prices below 60 pts, investment-grade spreads above 1000 bps, or loan prices below 75pt), is $140 bn of US assets and $210 bn globally. The healthcare and technology sector in loans, Pemex in EM energy, China real estate, and high-yield health and cable and telecommunication sectors are among the top ten sector contributors to deep distress. The deep-distress segments will likely grow from here: A series of headlines hints at a possible resolution to the debt-ceiling negotiations, bringing the US Treasury back to the market to finance the $1.4 tn budget deficit. Most of these supply pressures will be in the second half of 2023 since the Treasury Department could not maintain its regular borrowing schedule in recent months. Meanwhile, as flows into MMFs out of bank deposits continue, capital will get even more scarce over time, and the most vulnerable areas of US corporate credit will continue to be exposed to the ongoing liquidity drain.

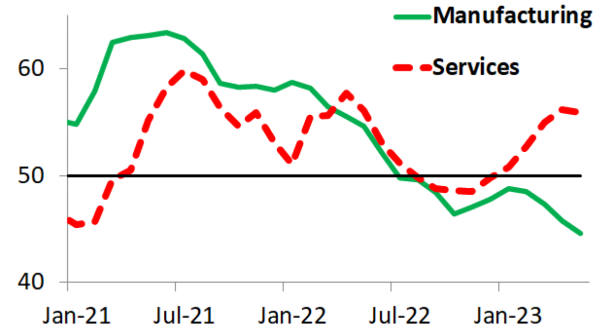
Europe

Equities (-0.2%) are little changed after flash PMI data disappointed marginally on a further slide in the manufacturing sector.

Yields are 3–4 bps higher across the German bund curve as the euro area services sector remains firmly in expansionary territory. HSBC upgraded its ECB outlook with additional hikes of 25 bps in July and September on top of the quarter point hike expected in June, for a peak depo rate of 4%. **HSBC does not have any rate cuts in its forecast up to end-2024.** The bank pointed to activity remaining remarkably buoyant in the service sector, an easing income squeeze, consumer confidence well off its lows and supportive fiscal policy.

The euro area composite flash PMI fell 0.8 points to 53.3 in May (53.5 expected) from 54.1 in April. The manufacturing sector drove the decline; the outperformance of services relative to manufacturing is now the widest observed since January 2009.

Euro Area: PMI data (>50 is expansion)

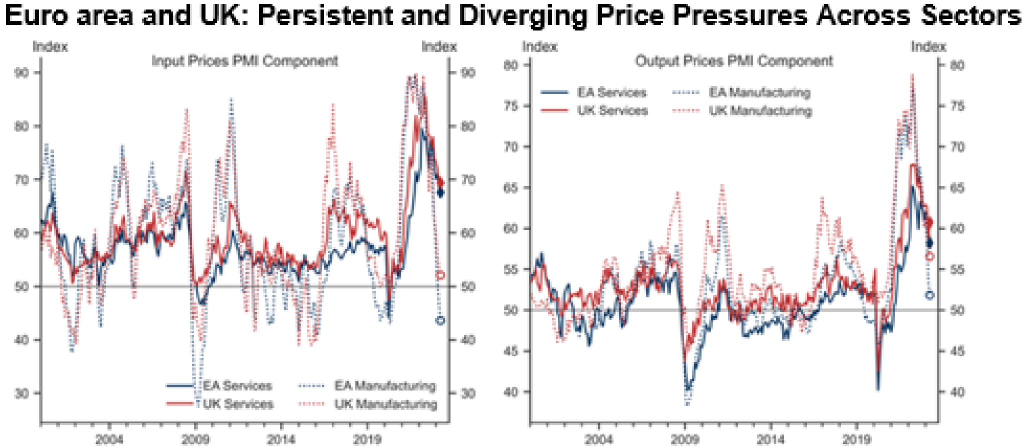


Source: Bloomberg, Markit and IMF staff

The UK composite flash PMI fell 0.9 points to 53.9 and was also led by manufacturing. Nevertheless, gilt yields are 8 bps higher as JP Morgan points out that even with the decline reported today, the UK economy is still realizing strong growth of closer to 1.8%.

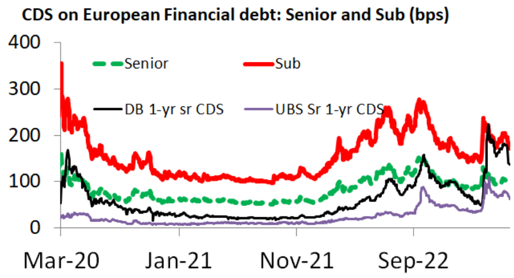
The PMI surveys suggest that price pressures are also becoming more divergent across sectors. Input prices have continued to moderate across both services and manufacturing in the euro area, but prices charged by firms rose in the services sector. Analysts at Goldman Sachs point out that domestic price pressures appear even more pronounced in the UK.

Euro area and UK: Persistent and Diverging Price Pressures Across Sectors



Source: GS

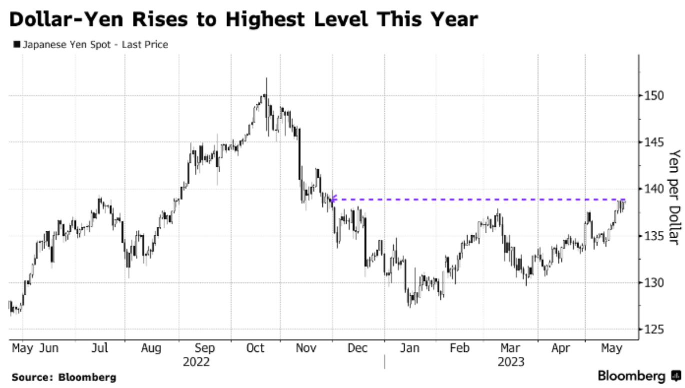
The Credit Derivatives Determinations Committee determined that the sale of Credit Suisse to UBS was not a bankruptcy credit event. The question to the panel had related to both senior and subordinated Credit Suisse Group swaps. Bloomberg reports that some hedge funds have been buying up the default protection in recent weeks. Last week, the committee also ruled against a payout query related to the write-down of Credit Suisse's Additional Tier 1 securities in March.



Source: Bloomberg, itraxx and IMF staff

Japan

Japanese stocks declined -0.7%. Jibun Bank's purchasing managers index (PMI) of activity in Japan's service sector rose 0.9 to a record 56.3 in May (consensus: 51.8), manufacturing PMI added 1.3 to 50.8. Separately, **restrictions on exports of 23 types of chipmaking technology will take effect in late July,** Japan's Ministry of Economy Trade and Industry said on Tuesday. The measures were announced in March, when Japan joined the US in tightening shipments of semiconductor production equipment to China. **Yields on 10-year bonds increased 1.5 bps, the yen appreciated +0.1%.**



Emerging Markets

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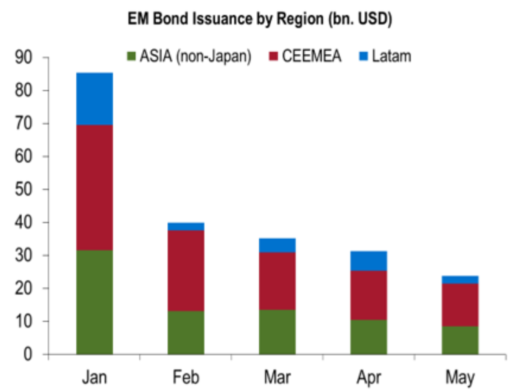
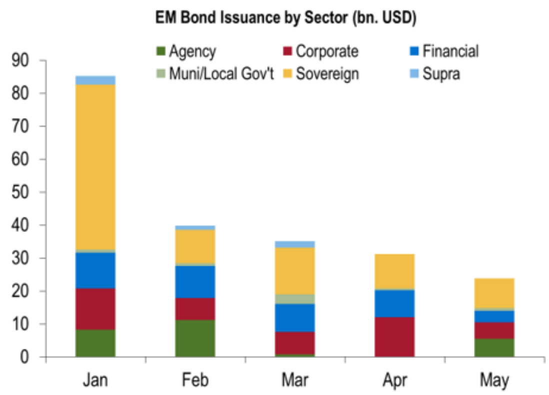
Latin American assets were mixed yesterday. Stocks lost in Mexico (-1.53%), Colombia (-1.13%) and Brazil (-0.48%), while Chile and Peru equity markets gained 0.67% and 0.09%, respectively. Currencies appreciated in Brazil (0.62%), Chile (0.30%) and Colombia (0.04%), while the Mexican peso (-0.63%) and the Peruvian sol (-0.19%) weakened against the US dollar. **Asian equities declined -0.4%.** Mainland China extended declines (CSI -1.4%) as selling by foreigners accelerated, South Korea gained +0.4%, and India outperformed (+0.5%) driven by rally in Adani Group shares. **Asian currencies were mixed.** South Korean won appreciated further +0.4%, Thai baht weakened -0.7% amid continued political uncertainty. **10-year bond yields increased slightly.** Singapore yields added +10.3 bps as the April inflation prints exceeded expectations with core CPI unchanged at 5% y/y (consensus: 4.7%) and headline accelerating to 5.7% (previous: 5.5%). **Philippine's** credit rating outlook was upgrade to stable from negative by Fitch, and the country's long-term foreign currency debt rating was affirmed at BBB. **EMEA markets were generally up, with the exception of Hungary ahead of the central bank's policy rate decision later today.** Equity markets were registering small gains, except for South Africa (-1%). In currencies, the Hungarian forint stood out, weakening 0.8% vs. the euro (at 376.9/euro) while other central and eastern European currencies were broadly flat. Later today the Hungarian central bank is expected to keep the policy rate on hold at 13%, but market participants fear that a cut in the overnight depo rate (18%) might be announced at the press conference. The Nigerian central bank is expected to hike rates 50 bps to 18.5%.

Emerging Market Bond Issuance

Emerging market bond issuance almost tripled compared to the week before. EM bonds priced $16.6 bn last week, among which, $9.0 bn was sovereign, $4.6 bn corporate/financial and $2.6 bn agency. Saudi Arabia dominated the new issuance with $6.0 bn sovereign bonds issued. All new issuances are fixed-rate bonds with maturity varying from 2 to 10 years. The weighted average yield is 5.03%. More than 71% of the new issuances are investment grade. 87% of new issuances are hard currency bonds. YTD total issuance now stands at $215.5 bn.



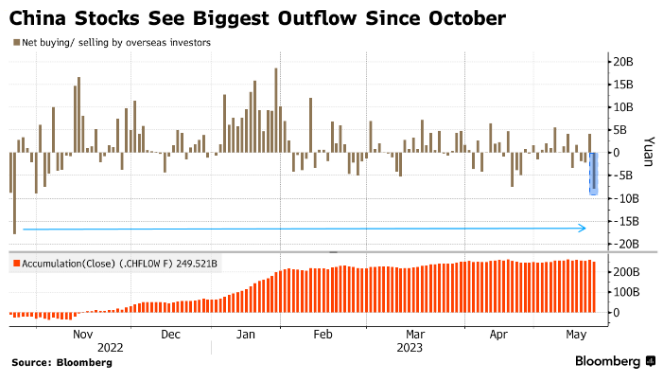
Sources: Bond Radar and IMF staff calculations



Sources: Bond Radar and IMF staff calculations

China / Hong Kong SAR

Chinese stocks fell (CSI -1.4%) as selling by foreigners accelerated. Foreign investors offloaded the largest number of Chinese stocks since end-October on Tuesday with net selling of 8 bn yuan ($1.1 bn) via the trading links with Hong Kong. Separately, **dollar bonds issued by Chinese conglomerate Dalian Wanda Group Co. remain under pressure.** Dollar bonds issued by Wanda units started slumping last month as the third application for a mall operation to go public lapsed in Hong Kong SAR. The selloff in Wanda's $400 mn note due July 23 began last week, with the price dropping from 90 to around 70 cents. There are $995 mn of local and offshore bonds set to mature in 2023 along with $182 mn of interest due, Bloomberg estimated. In addition, there is a 3.8 bn yuan ($539 mn) note that investors can demand early repayment on in September. Separately, **Hong Kong SAR will allow retail investors to trade crypto.** City's Securities and Futures Commission detailed the conclusions of a consultation on retail participation in crypto markets. The agency stuck with a plan to let individual investors buy and sell bigger tokens like Bitcoin and Ether starting June 1 when a new licensing regime for virtual-asset platforms begins. **Renminbi depreciated a further -0.3%, 10-year bond yields were little changed.**

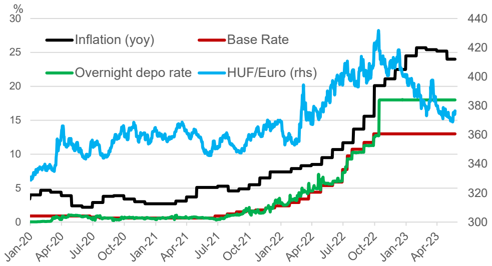


Hungary

Hungarian assets are underperforming ahead of the Hungarian National Bank (NBH) rate decision and press conference later today. The Hungarian forint is weakening 0.8% to 376.9/euro, and 10y bond yields are up 5 bps to 8.61%. While markets expect that the NBH keep the policy rate (base rate) unchanged at 13%, they fear that a 100 bp cut in the overnight depo rate (18%) will be announced in the press conference, marking a first step in the convergence of the overnight depo rate to the base rate, and effectively easing of monetary policy. The overnight depo rate was raised to 18% in October to stem the depreciation of the forint and is the de facto anchor of monetary policy. JP Morgan analysts expect that

NBH will reduce the overnight depo rate gradually in a sequence of 100 bp cuts and reach convergence (13%) by September. Comments from PM Orban this morning saying that he will continue to block EU aid for Ukraine did not help market sentiment.

Hungary: Policy Rates, Forint and Inflation



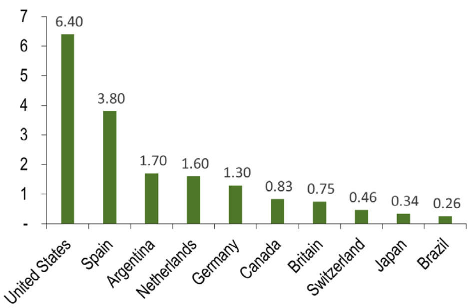
Source: Bloomberg and IMF

Mexico

Mexico's foreign direct investment surged by an impressive 48% y/y in the first quarter of 2023, reaching $18.6 bn. The increase is attributed to corporate nearshoring efforts, as companies seek to be closer to North American consumers. Manufacturing received around $10 bn of the investment, while financial services received $6 billion. Most investments were made to expand existing operations, particularly in utilities and plant capacity. If the trend continues, total FDI for the year could reach $43 bn, marking a 51% increase compared to 2022 excluding media mergers and corporate restructuring activities.

Mexico Foreign Direct Investmen 1Q23

Bn USD



Source: Bloomberg and IMF staff

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Global Financial Indicators

Last updated: 5/23/23 8:04 AM	Level Last 12m	Latest	Change 1 Day	7 Days	30 Days	12 M	YTD	Since 23-Feb-22
Equities					%		%	%
United States		4188	0.0	2	1	5	9	-1
Europe		4362	-0.5	1	-1	18	15	10
Japan		30958	-0.4	4	8	16	19	17
China		3913	-1.4	-2	-2	-1	1	-15
Asia Ex Japan		67	0.9	0	0	-4	3	-16
Emerging Markets		39	0.8	0	1	-5	4	-17
Interest Rates					basis points			
US 10y Yield		3.74	2.9	21	17	89	-13	175
Germany 10y Yield		2.49	2.7	13	1	147	-9	226
Japan 10y Yield		0.40	1.1	1	-7	16	-2	21
UK 10y Yield		4.13	6.5	31	37	216	46	265
Credit Spreads					basis points			
US Investment Grade		167	-2.3	-6	10	-5	9	24
US High Yield		488	-8.7	-20	14	-21	8	81
Europe IG		82	0.5	-4	-1	-14	-9	10
Europe HY		433	3.7	-18	-6	-38	-41	82
Exchange Rates					%			
USD/Majors		103.53	0.3	1	2	1	0	8
EUR/USD		1.08	-0.4	-1	-2	1	1	-5
USD/JPY		138.4	-0.1	2	3	8	6	20
EM/USD		50.1	-0.2	-1	-1	-6	0	-6
Commodities					%			
Brent Crude Oil ($/barrel)		76.6	0.8	2	-6	-18	-9	-8
Industrials Metals (index)		142	-1.7	-2	-10	-24	-14	-25
Agriculture (index)		65	-0.2	-2	-4	-16	-5	-7
Implied Volatility					%			
VIX Index (%, change in pp)		17.6	0.3	-0.4	0.8	-10.9	-4.1	-13.5
US 10y Swaption Volatility		120.5	0.4	2.7	5.5	10.2	-5.2	26.2
Global FX Volatility		8.7	0.0	0.1	-0.4	-1.6	-2.0	1.2
EA Sovereign Spreads					10-Year spread vs. Germany (bps)			
Greece		140	-1.8	-31	-43	-132	-65	-100
Italy		185	-0.6	-2	-2	-17	-29	14
Portugal		77	-1.2	-4	-5	-38	-24	-15
Spain		105	0.0	-2	1	-7	-4	2

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

Emerging Market Financial Indicators

Last updated: 5/23/2023 8:06 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		7.05	-0.3	-1.1	-2	-6	-2		2.8	3.5	-5	-32	-2	-25
Indonesia		14880	0.1	-0.4	0	-1	5		6.4	0.5	1	-24	-75	-51
India		83	0.0	-0.7	-1	-6	0		7.3	9.1	12	-8	-50	-19
Philippines		56	0.2	0.6	0	-6	0		5.9	1.3	1	-9	44	-14
Thailand		35	-0.7	-2.1	-1	-1	0		2.7	6.2	9	19	-21	11
Malaysia		4.57	-0.5	-1.6	-3	-4	-4		3.7	-1.0	8	-10	-51	-30
Argentina		234	-0.7	-1.6	-6	-49	-24		104.8	60.3	523	1503	4930	1655
Brazil		4.98	-0.3	-0.8	1	-3	6		12.1	8.9	20	-61	10	-51
Chile		796	0.3	-1.2	2	4	7		5.3	0.0	2	11	-71	-1
Colombia		4531	-0.2	0.5	0	-11	7		8.8	8.0	20	-14	-21	-98
Mexico		17.92	-0.1	-2.4	0	11	9		8.5	1.0	20	3	-2	-27
Peru		3.7	-0.2	-0.7	2	1	3		7.4	0.5	21	-2	-31	-52
Uruguay		39	0.3	0.6	1	4	3		10.0	-1.4	0	-19	-12	-69
Hungary		349	-0.9	-2.7	-2	2	7		8.2	19.0	46	37	149	-142
Poland		4.18	-0.4	-1.1	0	3	5		5.5	5.7	16	-3	-41	-64
Romania		4.6	-0.3	-1.2	-3	0	0		6.9	-1.2	0	-36	-106	-83
Russia		80.1	0.4	0.7	2	-27	-7							
South Africa		19.3	-0.3	-1.1	-6	-18	-12		10.2	5.0	44	73	202	101
Turkey		19.85	-0.2	-0.6	-2	-20	-6		9.1	7.0	-78	-310	-1523	-76
US (DXY; 5y UST)		104	0.3	1.0	2	1	0		3.81	4.8	28	15	94	-19

	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	YTD
								basis points					
China		3913	-1.4	-2	-2	-1	1		195	-6	2	-19	18
Indonesia		6737	0.1	0	-1	-3	-2		140	-6	-7	-81	0
India		61982	0.0	0	3	15	2		155	-7	0	-40	13
Philippines		6604	-0.3	0	0	0	1		115	-5	-6	-44	18
Thailand		1535	0.4	0	-1	-6	-8						
Malaysia		1412	-0.5	-1	-1	-8	-6		99	-4	0	-41	-1
Argentina		338979	0.1	6	17	275	68		2592	1	-54	640	387
Brazil		110213	-0.5	1	6	0	0		261	-15	-11	-68	-13
Chile		5692	0.7	1	9	11	8		131	-4	-9	-55	-1
Colombia		1124	-1.1	-2	-8	-23	-13		406	-17	2	1	34
Mexico		53466	-1.5	-3	-1	4	10		394	-16	6	-12	13
Peru		21652	0.1	0	-3	6	2		180	-2	-5	-25	0
Hungary		46503	-0.1	1	5	7	6		231	10	1	4	9
Poland		65451	0.0	2	5	14	14		130	-7	47	86	57
Romania		12324	0.4	1	-1	1	6		250	-3	-6	-29	-6
South Africa		77117	-1.1	-1	-1	13	6		450	-1	28	13	83
Turkey		4480	0.3	0	-11	88	-19		652	66	133	39	212
Ukraine		507	0.0	0	0	-2	-2		4871	-533	-312	1759	792
EM total		39	-1.0	0	1	-5	4		424	-5	2	3	49

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

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