GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

THURSDAY, MAY 25, 2023

- **Germany entered recession in Q1** (link)
- **UK markets reprice further after shocker inflation report** (link)
- **Analysts argue AI may boost labor-intense corporate earnings** (link)
- **Bank of Korea stays pat but flags possibility of higher terminal rate** (link)
- **Fitch upgraded outlook for Hong Kong banks to 'improving'** (link)
- **Yields on Turkish hard currency bonds fall ahead of election** (link)
- **Chile's central bank raises capital requirements for banks** (link)

Mature Markets | Emerging Markets | Market Tables

US interest rates trade higher after stronger-than-expected GDP report

The US dollar but also US rates have traded higher in past days as investors are gauging the outcome of ongoing debt ceiling negotiations against a backdrop of still high inflation and surprisingly strong US growth. Nasdaq futures, for example, rose sharply following a blow revenue forecast of chipmaker Nvidia. UK interest rates are also settling higher as traders digest yesterday's shocking upside surprise in April inflation. In contrast, German bund yields edged lower as a second reading of German GDP data unexpectedly showed that Germany was in recession in Q1.

Key Global Financial Indicators

Last updated: 5/25/23 12:57 PM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		4115	-0.7	-1	1	3	7
Eurostoxx 50		4270	0.1	-2	-2	16	13
Nikkei 225		30801	0.4	1	8	16	18
MSCI EM		38	-0.7	-2	1	-6	1
Yields and Spreads					bps		
US 10y Yield		3.75	1.0	11	35	101	-12
Germany 10y Yield		2.47	-0.2	2	9	152	-10
EMBIG Sovereign Spread		481	-3	-7	-15	-1	29
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		50.0	0.0	0	0	-5	0
Dollar index, (+) = $ appreciation		104.1	0.2	0	2	2	1
Brent Crude Oil ($/barrel)		76.9	-1.8	1	-5	-33	-10
VIX Index (%, change in pp)		19.5	-0.6	3	1	-9	-2

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

Mature Markets

back to top

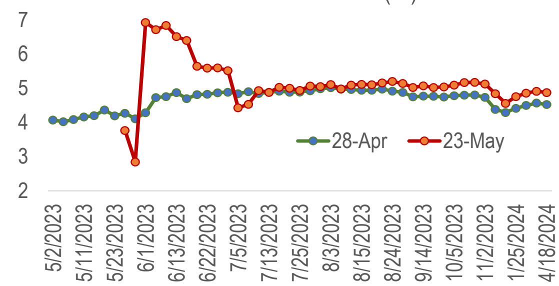
United States

This morning, Q1 GDP second release was stronger than expected (1.3%qoq saar vs. 1.1% consensus) with the core PCE price index rising at 5.0% qoq (4.9% expected). Initial jobless claims were fewer than expected (229k vs. 245k consensus), and continuing claims decreased to 1794k (1800k expected). Treasury yields traded higher across the curve following the headlines, with 2-yr yields 13 bps higher. The dollar marginally strengthened against the euro. **Market-implied probability of a 25bps hike in June rose to 37%.**

Equities (-0.7%) closed lower yesterday given the impasse in debt-limit talks, as Treasury Secretary Yellen's deadline is one week away. She said it was almost certain that the US would not have enough cash to continue to pay all of its bills on time beyond early June. The KBW regional banking index was down 1.9%. 1-year sovereign CDS traded around 160bps, implying 4% probability of technical default.

T-bills maturing on June 1 traded at higher than 7% in the morning. The US treasury yield curve bear flattened with 2-years up 11bps and 10-years up 5bps. Contacts pointed out that a technical default per se may not severely impact the economy, but draconian spending cuts due to compromise would severely affect the economy. If the view is correct, risky assets may not recover even after a deal. Another contact argued that 2023 could be worse than 2011 for risky assets since the differences in the backdrop, such as inflation (high vs. low), monetary policy (tight vs. easy), and equity valuations (rich vs. moderate), are striking.

US T-bill Term Structure (%)

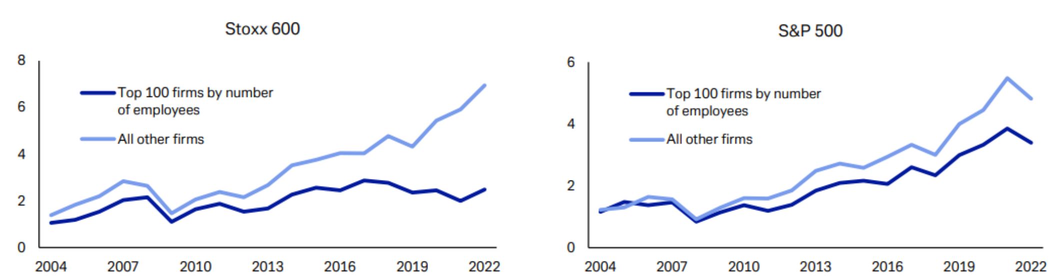


Source: Bloomberg

May FOMC minutes revealed Fed officials are split on whether more rate hikes are needed to bring down inflation. Some participants commented that additional policy firming would likely be warranted at future meetings, while several participants noted that further policy firming after this meeting might not be necessary. Treasury market reaction to the headline was limited.

DB analysts look at the possibility that AI could be the catalyst to turn around a two-decade underperformance of firms with a large number of employees versus the rest of the stock indices. They posit that AI will make workers more productive, helping upskill them and streamline repetitive and mundane tasks that are more prevalent in high-staff companies. Labor-intense firms tend to have a lower market cap, thinner margins, and lower growth rates. Thus, the profitability of high-staff firms has the highest leverage on the performance of their labor force. Ironically tech firms tend to have low staff relative to their size. Once AI technology becomes more widespread, the bigger, older, labor-intensive firms could benefit more than tech firms.

Figure 1: Median market capitalisation (indexed to 2003)



Source : Factset, Deutsche Bank

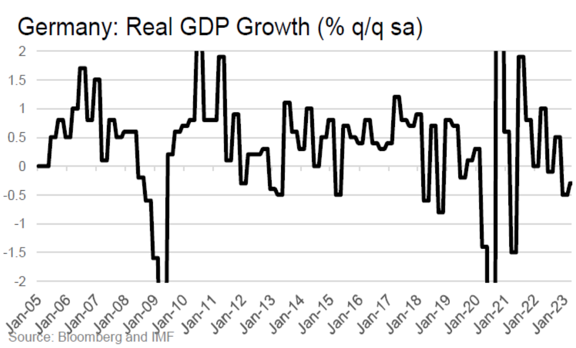
Japan

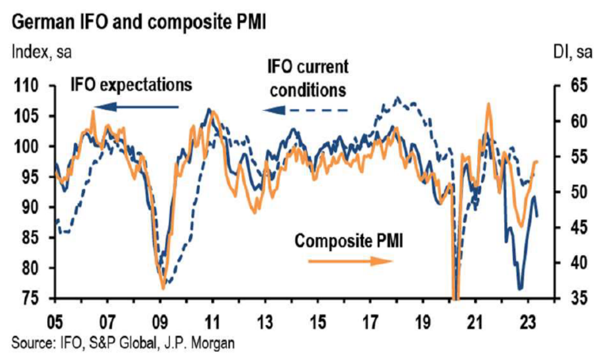
The yen appreciated +0.1%. USD/JPY has broken 139 and is approaching 140. **Nomura thought this is driven by subdued expectations for the Bank of Japan (BOJ) policy changes, rising expectations of a Fed rate hike, and sustained upward pressures on US dollar-renminbi pair. Yields on 10-year bonds were little changed.** Demand for inflation protection hit new records with 10-year break-even rate rising to 0.94% this week, highest since December. Traders bet BOJ will maintain its easy monetary policy despite rising inflationary pressures, Bloomberg reported. The TOPIX declined -0.3% whereas the Nikkei rebounded +0.4% led by chip-producing companies and supported by inflows from foreign investors.

Euro area

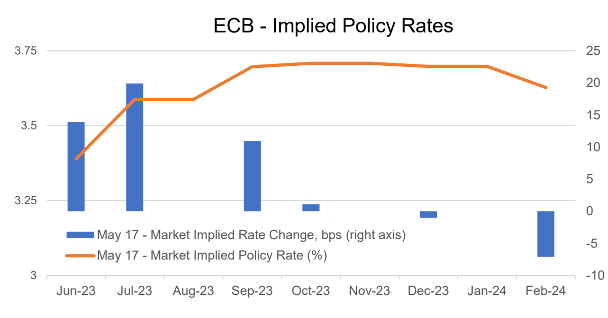
European markets were little changed after yesterday's gloom. The equity market (Stoxx Europe 600) was up 0.2%, with banking stocks gaining 0.6%. The euro was losing 0.2% vs. the dollar at 1.07/$, as the broader dollar was strengthening, reflecting the global risk off sentiment due to the debt ceiling uncertainty. German 10y bund yields were broadly flat at 2.48%, and Italian spreads were down at 183 bps.

The second reading of Q1 GDP unexpectedly shows that Germany was in recession in Q1. GDP shrank 0.3% q/q in Q1, when the initial release showed a flat reading (0% q/q). This is the second consecutive quarter of negative growth, as GDP contracted 0.5% q/q in Q4. In y/y terms, the German economy contracted 0.2% in Q1, or 0.4% more than suggested by the initial release. The near-term growth outlook in Germany looks more uncertain amid conflicting signals. JP Morgan analysts point out that while the PMI suggests a pickup in GDP growth in Q2, yesterday's IFO data for May, which disappointed, as expectations dropped more sharply than expected, suggest a contraction at around a 1% pace.



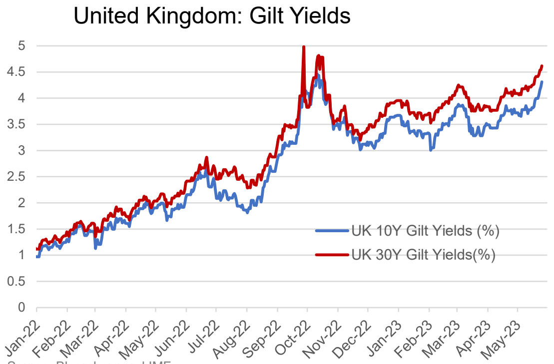


With several EC officials due to speak today, markets are speculating whether the worse than expected German data will tame the hawks. This morning, ECB vice-president de Guindos repeated that the ECB will ensure that policy rates will be brought to levels sufficiently restrictive to achieve a timely return of inflation to the 2% medium-term target, and that once there, they will be kept at those levels for as long as necessary. Slovenian governor Vasle, also said that the ECB must lift borrowing costs further to return inflation to its target. Bundesbank president Nagel, French governor Villeroy de Galhau, and Portuguese governor Centeno, are due to speak later today. Estimates of the ECB terminal rate have not moved much following the release of the German data and continue to indicate 3.7% by September, or just slightly more than two 25 bps hikes.

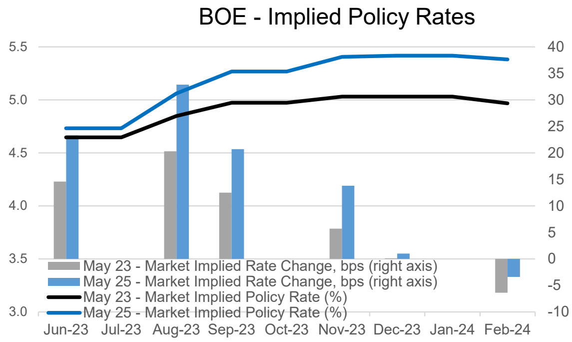


United Kingdom

Markets continued to digest yesterday's shocking upside surprise in April inflation, which came in at 8.7% y/y, or 0.5% more than expected. Yields on 10y gilts are up 10 bps today to 4.3%, and up 32 bps this week. Markets have revised up their estimate of the Bank of England terminal rate by 40 bps since the inflation data came out, to 5.4%.



Source: Bloomberg and IMF



Source: Bloomberg WIRP and IMF

Emerging Markets back to top

Asian equities fell for a third day, -0.9% on net. Taiwan Province of China equities bucked the trend led by tech stocks (+0.8%), Heng Seng index of China Enterprises lost -2.2%. The selloff for **Hong Kong** equities is gathering pace as the Hang Seng Index runs into a slew of bull/bear strategies which are set below 18,800, Bloomberg reported. **Asian currencies depreciated.** Malaysian ringgit underperformed -0.7%, followed by South Korean won (-0.7%) and Thai baht (-0.5%). **10Y bond yields rose slightly higher.** Singapore yields added +6.8bps. **Singapore**'s Q1 2023 y/y GDP growth was revised slightly higher to 0.4% from 0.1% above expectations. The official forecast for 2023 GDP growth was maintained at "0.5 to 2.5%". Analysts expect Monetary Authority of Singapore will refrain from further FX-policy tightening this year. Both **South Korea** and **Indonesia**'s central banks kept their benchmark interest rate unchanged as expected. **EMEA markets were mixed with currencies and bonds trading in a narrow range.** Equity markets rose in the Czech Republic and Hungary (+0.7% in both). In currencies, the South African rand was weakening 0.3% to the dollar (to 19.31/$), and the Hungarian forint was losing to the euro by a similar quantum (to (373.45/euro), but other central and eastern European currencies were trading in a very narrow range. Local bond yields were broadly unchanged. **The Turkish central bank left rates unchanged at 8.5% as expected. Later today, the South African Reserve Bank is expected to hike rates by 50 bps to 8.25%.** Yesterday, the Nigerian central bank met expectations and raised the policy 50 bps to 18.5%. **Latin American markets were mixed yesterday.**

China /Hong Kong SAR

Mainland CSI was down -0.2%, Heng Seng index of China Enterprises lost -2.2% amid disappointing earnings reports. **President Xi called on members of Eurasian Economic Union to deepen ties with China's Belt and Road Initiative**. During his virtual speech at a conference in Moscow, Xi reiterated that the path towards a multipolar world was "irresistible" and that China is open for Asia-Europe cooperation.

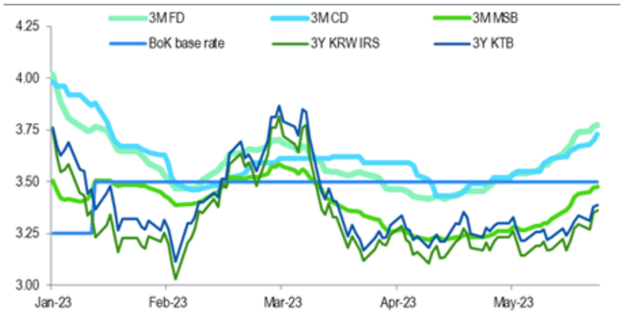
Separately, **Fitch Ratings raised Hong Kong banking sector's outlook to 'improving' from 'neutral'**. The agency stated that ongoing domestic recovery and Mainland China's reopening will support banks' business volumes, particularly in the latter half of the year. **Renminbi depreciated (offshore -0.2%, onshore -0.1%). 10Y bond yields were little changed.**

Overnight repo trading volume has also reached a fresh record of 7.65tn yuan ($1tr), Bloomberg estimated. This could indicate that traders are adding leverage due to low borrowing costs.

South Korea

The Bank of Korea (BoK) stays pat as expected flagging the possibility of a higher terminal rate. The benchmark seven-day repurchase rate was kept at 3.5%, however, Governor Rhee told markets not to rule out further hikes. The BoK cut growth forecast for 2023 to 1.4% from 1.6%. Inflation forecast was kept at 3.5% for 2023, but core inflation was raised higher to 3.3% from 3%. Separately, **South Korea will impose a 1% countercyclical capital buffer (CCyB) requirement on banks and their holding companies from May 2024**. The Financial Services Commission (FSC) said in a statement there was a need to improve banks' ability to absorb losses through preemptive capital accumulation due to higher external and internal macroeconomic uncertainties and financial risks. The CCyB ratio was first introduced in 2016 and was maintained at zero since then. **Equities fell -0.5%, won depreciated by -0.5%. 10Y yields rose by 6bps.** Standard Chartered noted that 3M Monetary Stabilization Bond (MSB) yield has risen by about +25bps since April as BOK was issuing MSB heavily to absorb liquidity.

Korea short-end rates have risen amid BoK's liquidity mopping operations *(rate, %)*



Source: Bloomberg, Standard Chartered Research

Turkey

Yields on Turkish foreign currency bonds fell 10 bps to 9.96% today, and 40 bps this week. Bloomberg reports that the central bank asked some banks to buy Eurobonds to keep a lid on yields ahead of Sunday's presidential election (second round).

Türkiye: Hard Currency Bond Yields

Source: Bloomberg and IMF

Chile

The central bank has raised capital requirements for banks by 0.5%, aiming to tighten credit conditions due to concerns about the potential impact of a global shock on the local economy. The decision to activate the counter-cyclical capital requirement contrasts with market expectations. **Analysts anticipate that the tightened credit conditions will be mitigated by interest rate cuts starting in July to counterbalance the effects.** The central bank's capital requirement increase is projected to create a buffer of approximately $930 million for publicly traded banks. The country's equity benchmark index fell 0.74%, dragged down by banks. Santander Chile retreated 1.7% and Banco de Credito e Inversiones lost as much as 3.3%. The two-year swap rates fell as much as 17 basis points to 7.49%.

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Global Financial Indicators

5/25/23 12:59 PM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		4115	-0.7	-1	1	3	7
Europe		4270	0.1	-2	-2	16	13
Japan		30801	0.4	1	8	16	18
China		3851	-0.2	-3	-3	-4	-1
Asia Ex Japan		65	-0.8	-2	0	-5	0
Emerging Markets		38	-0.7	-2	1	-6	1
Interest Rates					basis points		
US 10y Yield		3.75	1.0	11	35	101	-12
Germany 10y Yield		2.47	-0.2	2	9	152	-10
Japan 10y Yield		0.43	1.3	5	-5	21	1
UK 10y Yield		4.31	9.1	35	61	240	63
Credit Spreads					basis points		
US Investment Grade		167	-0.2	-6	9	-2	8
US High Yield		499	5.3	-8	21	-8	19
Europe IG		84	-0.2	1	0	-9	-6
Europe HY		444	-1.5	7	-5	-19	-30
Exchange Rates					%		
USD/Majors		104.08	0.2	0	2	2	1
EUR/USD		1.07	-0.2	0	-2	0	0
USD/JPY		139.6	0.1	1	4	10	6
EM/USD		50.0	0.0	0	0	-5	0
Commodities					%		
Brent Crude Oil ($/barrel)		76.9	-1.8	1	-5	-19	-9
Industrials Metals (index)		140	0.6	-3	-8	-23	-15
Agriculture (index)		64	-0.3	0	-4	-16	-6
Implied Volatility					%		
VIX Index (%, change in pp)		19.5	-0.6	3.4	0.7	-8.9	-2.2
US 10y Swaption Volatility		119.7	0.6	7.6	-3.5	16.8	-6.9
Global FX Volatility		8.7	0.0	0.1	-0.5	-1.5	-2.0
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		139	-3.6	-20	-44	-123	-66
Italy		184	-2.3	-2	-5	-16	-30
Portugal		76	-0.9	-5	-8	-40	-26
Spain		106	0.0	0	2	-4	-3

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

Emerging Market Financial Indicators

Last updated: 25/05/2023 1:01 PM	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		7.07	-0.1	-0.5	-2	-5	-2		2.8	-1.5	-4	-29	1	-23
Indonesia		14953	-0.4	-0.6	0	-2	4		6.4	0.7	4	-24	-74	-51
India		83	-0.1	-0.2	-1	-6	0		7.3	6.0	13	5	(32.7)	-16
Philippines		56	-0.5	-0.3	-1	-7	-1		5.9	1.3	4	-6	44	-11
Thailand		35	0.1	-0.6	-1	-1	0		2.7	1.5	4	18	-11	11
Malaysia		4.63	-0.7	-1.9	-4	-5	-5		3.8	3.3	7	5	-34	-24
Argentina		236	-0.3	-1.7	-7	-49	-25		107.5	226.9	686	1762	5164	1928
Brazil		4.96	0.2	-0.5	2	-3	7		11.8	3.7	-13	-72	-46	-75
Chile		807	-0.7	-1.7	1	3	5		5.4	0.0	8	26	-64	4
Colombia		4447	0.8	1.1	0	-11	9		8.8	-0.5	8	23	28	-99
Mexico		17.77	0.2	-0.3	2	12	10		8.5	-4.5	16	12	10	-26
Peru		3.7	-0.1	0.1	2	0	3		7.3	######	2	-12	-28	-64
Uruguay		39	0.2	0.6	1	3	3		10.0	0.0	13	-18	-11	-67
Hungary		347	-0.1	0.5	-1	6	8		8.2	2.0	44	29	154	-140
Poland		4.21	-0.4	0.3	0	2	4		5.5	5.0	8	6	-55	-69
Romania		4.6	0.1	0.1	-2	0	0		6.9	2.9	9	-30	-96	-77
Russia		80.1	0.4	0.3	1	-25	-7							
South Africa		19.3	-0.4	0.0	-5	-19	-12		10.1	6.2	-1	68	191	95
Turkey		19.93	-0.2	-0.7	-3	-18	-6		9.1	0.0	-75	-304	-1528	-73
US (DXY; 5y UST)		104	0.2	0.5	2	2	1		3.80	-1.9	12	35	108	-20

	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		3851	-0.2	-3	-3	-4	-1		195	-4	0	-18	18
Indonesia		6704	-0.6	1	-3	-3	-2		141	-3	-13	-76	1
India		61873	0.2	1	3	14	2		151	-10	-7	-43	9
Philippines		6560	-0.8	-1	0	-1	0		115	-3	-13	-46	18
Thailand		1535	-0.1	1	-1	-6	-8		0	0	0	0	0
Malaysia		1402	-0.5	-2	-1	-9	-6		97	-4	-4	-37	-3
Argentina		341669	0.3	4	13	274	69		2598	33	-34	664	393
Brazil		108800	-1.0	-1	5	-2	-1		264	-6	-12	-64	-10
Chile		5643	0.0	0	6	9	7		131	-2	-11	-52	-1
Colombia		1111	-1.1	-2	-7	-26	-14		409	-5	4	28	37
Mexico		53393	0.5	-3	-2	3	10		397	-7	8	1	16
Peru		21406	-0.9	-2	-3	5	0		182	-2	-4	-19	2
Hungary		46856	1.2	1	8	13	7		230	1	-3	6	8
Poland		63873	-0.4	0	3	14	11		133	-1	46	110	60
Romania		12193	-0.6	0	-2	0	5		253	1	-8	-21	-3
South Africa		75609	0.0	-3	-3	12	4		453	-16	23	38	86
Turkey		4460	0.8	-4	-9	84	-19		618	-34	80	6	178
Ukraine		507	0.0	0	0	-2	-2		4883	-289	-331	1642	804
EM total		38	0.1	-2	1	-6	1		424	-5	-3	10	49

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

back to top