



- Fed speakers insist signs of inflation are temporary ([link](#))
- Usage of Fed overnight repo facility at highest since December 2016 ([link](#))
- ECB officials push back against talk of tightening ([link](#))
- Yuan at strongest versus dollar since 2018 ([link](#))
- New Zealand joins camp of hawkish central banks ([link](#))
- **Special Feature: EM Inflation and Monetary Policy Update (Attachment)**

[Mature Markets](#)

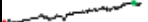





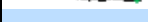
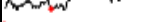


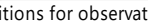
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Markets drift in search of direction

US equity index futures posted small gains but most of Europe is in the red this morning despite a mostly positive session in Asia. US Treasury yields are holding steady after several days of rallies, while the dollar continues to be weak. Many commodity prices have followed the dollar lower in recent sessions. The lack of a market narrative is keeping most moves small today. With the end of the month approaching, many investors are keeping their powder ahead of a potentially eventful June, when key Fed and ECB meetings are due to be held and many important market moving data releases are expected. Fed and ECB officials have come out with numerous dovish comments today and yesterday, while New Zealand and Hungary have joined Norway and Canada in the camp of hawkish central banks. Meanwhile, US President Biden call for a minimum global corporate sales tax of 15% met opposition from Ireland, whose Finance Minister expressed “significant reservations.”

Key Global Financial Indicators

Last updated: 5/26/21 8:03 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		4188	-0.2	1	0	40	12
Eurostoxx 50		4026	-0.2	2	0	34	13
Nikkei 225		28642	0.3	2	-1	34	4
MSCI EM		54	1.0	1	-1	45	5
Yields and Spreads			bps				
US 10y Yield		1.56	0.2	-11	-1	86	65
Germany 10y Yield		-0.20	-3.6	-9	5	23	37
EMBIG Sovereign Spread		337	2	6	-2	-195	-14
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		57.6	-0.1	0	1	6	-1
Dollar index, (+) = \$ appreciation		89.8	0.2	0	-1	-9	0
Brent Crude Oil (\$/barrel)		68.4	-0.3	3	4	89	32
VIX Index (% change in pp)		18.4	-0.4	-4	1	-10	-4

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

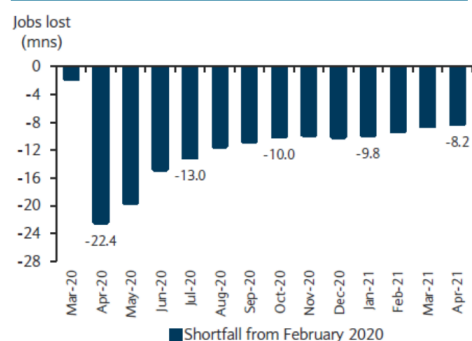
Mature Markets

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United States

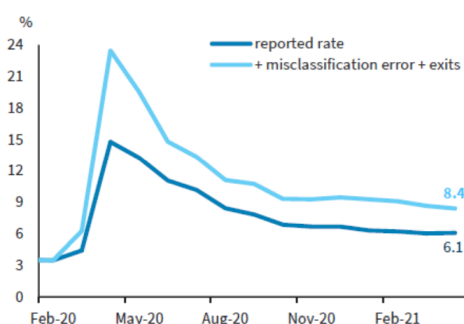
Numerous FOMC members issued statements over the past two days reiterating their views that current signs of inflation are likely to be temporary. From the Fed's point of view, employment still has a long way to go, and progress on the jobs front has slowed down considerably. Markets did not seem to disagree, with the 10-year Treasury yield breaking below its 50-day moving average and falling 10 bps over the past few sessions. However, Fed Vice Chair Clarida also said that the FOMC could begin talking about tapering at forthcoming meetings. In addition, the University of Michigan survey back on May 14 showed that consumers expect inflation to hit 4.6% over the next 12 months. The inflation debate is likely to continue to dominate the market narrative in the weeks ahead.

Recent progress toward erasing pandemic job losses looks slow



Source: Bureau of Labor Statistics; Haver Analytics; Barclays Research
[Global Economics Weekly: Growth rotations and input market frictions](#) (21 May 2021)

In the Fed's view, full employment is a long way off

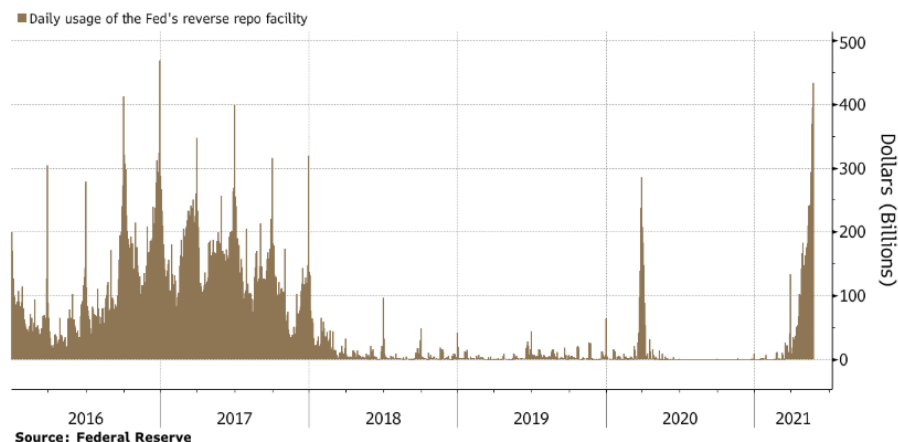


Note: Unemployment is corrected for unemployed persons misclassified as "employed and absent from work" and for labor force exits since Feb 2021.
 Source: Barclays Research
[Global Economics Weekly: Growth rotations and input market frictions](#) (21 May 2021)

Usage of the Fed's overnight reverse repo facility (RRP) hit the highest level since December 2016, Bloomberg reported. RRP volume hit \$433 bn, with 48 counterparties participating. JP Morgan thinks there are two contributing factors. The expiration of Supplementary Leverage Ratio (SLR) exemptions could be causing banks to invest cash released by the \$350 bn shrinkage in the Treasury General Account (TGA) in money market funds (MMFs), leaving the latter with more funds to invest. In addition, the slowing supply of Treasury bills (down \$500 bn since January) has induced the MMFs to park all their extra cash at the facility while searching for alternative investments.

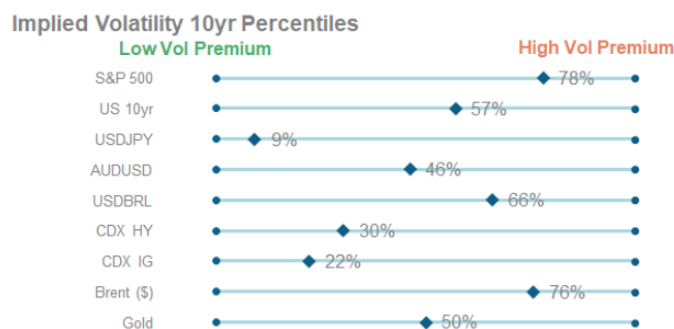
Full Speed Ahead for Reverse Repo

Usage of the Fed's facility climbed to the highest level in years



Implied volatility is high by historical standards, especially for the S&P 500 and oil markets. However, it remains quite low for credit markets, where spreads remain tight but pretty stable. Morgan Stanley thinks the volatility picture resembles an early cycle market although the very stretched level of valuations is more indicative of a late cycle market, a potentially worrying development. However, the analysts think “patient” central banks, fairly stable interest rates and the rebounding economy will continue to support markets.

Exhibit 1: Implied vols are still above average

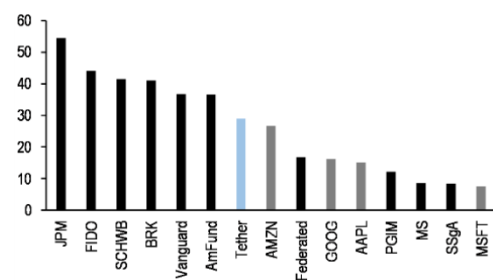


Source: Bloomberg, Morgan Stanley Research

Crypto assets are playing a growing role in US money markets. The connection between the two arises from collateralized assets held by stablecoins. These are a form of digital currency whose value is designed to remain very stable by being tied to an external asset whose value is itself highly stable. The largest stablecoin is Tether (USDT), which is an asset backed stablecoin tied to the US dollar. Tether holds its collateral in the form of cash and money market instruments, and analysis by JP Morgan finds that the size of its holdings puts in the top ten holders of commercial papers and certificates of deposit. Although Tether's own market share and trading volumes are declining, the rise of other similarly structured stablecoins implies that they will become an increasingly important of the infrastructure of US money markets. There were \$60 bn of new stablecoins issued already so far this year.

Exhibit 3: If considered alongside on and offshore prime money market funds, the Tether reserve fund would already be firmly in the top ten

Holdings of CP/CD among prime MMFs, corporates* and Tether ; \$bn

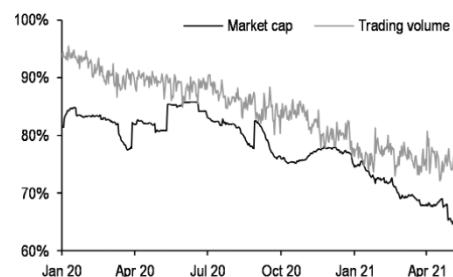


Note: Corporates estimated from 10-Qdisclosure for 1Q 2021. We use cash and equivalent corporate debt instruments where disclosed explicitly, otherwise <1yr from maturity. Money market fund holdings are assumed to be all prime and are scaled using overall allocation to CP/CD across the complex.

Source: J.P. Morgan, iMoneyNet, coinmarketcap.com, Cranes, company disclosure

Exhibit 4: The cryptocurrency market is slowly diversifying its use of stablecoins, but Tether still dominates by both market capitalization and trading activity

USDT market share of market capitalization and trading volume in BTC and ETH; %

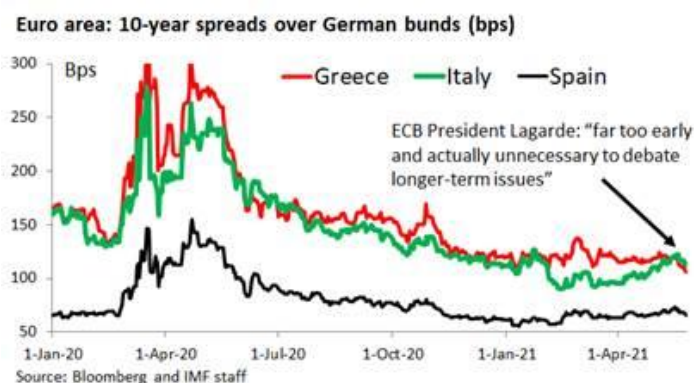


Source: J.P. Morgan, coinmarketcap.com, NYDIG

Euro area

German 10-yr bund yields (-3 bps to -0.20%) traded lower as ECB officials continue to push back against expectations of any tightening on 10 June. Yesterday, **Banque de France governor Villeroy said that the idea of reducing PEPP purchases in Q3 is “purely speculative”** and that the ECB has “well beyond the June meeting” to decide on asset purchases. The governor also added that the ECB’s regular (non-pandemic) asset purchase program could be modified to include additional flexibilities, that the current depo rate is not a floor, and that forward guidance should state more clearly that the ECB is ready to temporarily overshoot its 2% target.

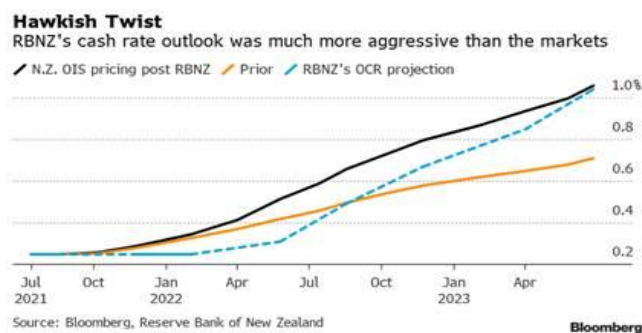
Core yields were lower and 10-yr Italian yields (-4 bps to 0.92%) and Spanish yields (-4 bps to 0.45%) also fell. Southern European spreads are little changed after tightening 7-13 bps in the past 5 days.



Nevertheless, contacts expect that the ECB may reduce asset purchases over the summer if only because of the more limited supply during the holiday months. They also believe that the ECB could potentially link the pace of asset purchases more explicitly to financial conditions.

New Zealand

The Reserve Bank of New Zealand (RBNZ) kept its policy rate unchanged but signaled that rate hikes are on the horizon. The official cash rate (OCR) was kept at 0.25% as expected; the size of the Large Scale Asset Purchase Program also remained unchanged. The RBNZ published a conditional OCR projection, which indicated rate hikes from mid-2022. The OCR projection was more hawkish than previously perceived by market participants. In response, traders priced in two 25 bps rate increases by end-2022, from one hike before the decision. The RBNZ stressed that the OCR projection was conditional on the economic outlook evolving broadly as anticipated. Long-end government bond yields rose (10-year: +8.1 bps; 20-year: +7.5 bps); New Zealand dollar appreciated (+0.9%). equities gained (+0.1%).



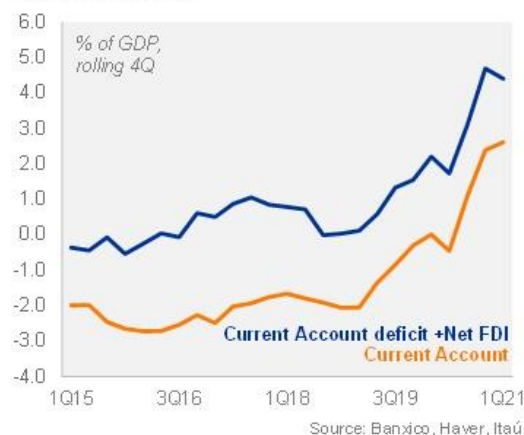
Source: Bloomberg.

Emerging Markets

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Most EMEA and Asian markets were higher and local currencies appreciated. Markets in **Latin America** followed US markets down yesterday and local bond markets rallied with US Treasuries. **In India**, the government evacuated almost 2 million people from the coast to safer places as a powerful cyclone hit the country. **Hungary stayed on hold at 0.6% while signaling readiness for proactive policy tightening.** Most analysts see a 25 bps rate hike in the upcoming June meeting as the base case scenario, which is also already reflected in interest rate forwards pricing. **In Mexico**, the Q1 current account balance was much worse expected at \$5.1 bn versus the \$2.6 bn market forecast.

Current account

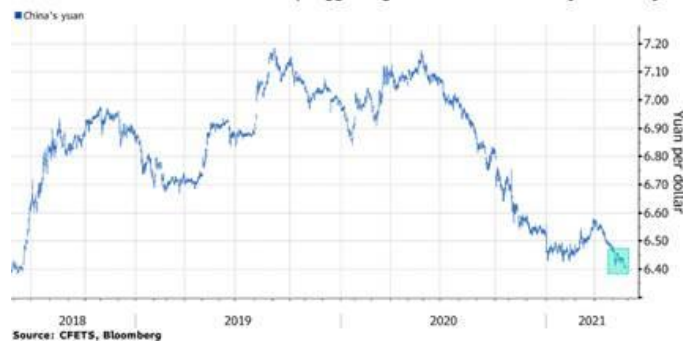


China

The Chinese yuan appreciated (onshore: +0.2%; offshore: +0.4%) as today's RMB fixing was slightly stronger than market expectations by 2 pips, a signal that the central bank is comfortable with the recent strengthening of RMB (to the strongest level since 2018). State media also chimed in with comments supporting RMB appreciation. One article cited a forecast by the largest brokerage firm, which expected RMB to reach 6.2 yuan per dollar this year. Separately, **China banned retail sales of commodity-linked financial products.** The China Banking and Insurance Regulatory Commission instructed banks to stop selling these instruments and liquidate their existing books for the products. **Equities were little changed.** Some analysts noted that the increase in margin debt for the past four consecutive weeks, the longest streak since December 2020 (that episode was ended after the central bank tightened liquidity conditions), could further drive up share prices in the near term.

Greenlighting Gains

PBOC sets fix in line with estimates, suggesting it's comfortable with yuan's rally

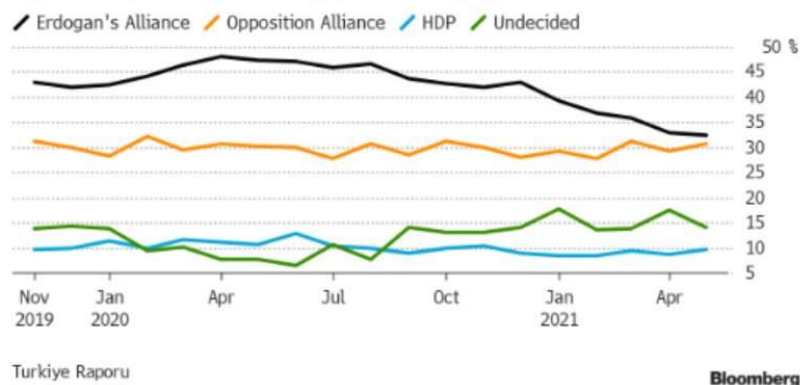


Source: Bloomberg.

Turkey

Market volatility increased as investors weighed the risks of potential early elections. Turkey's equity benchmark dropped 3.5% and the lira depreciated by 1.2% yesterday as contacts noted concerns among investors around possibility of early elections following a series of video blogs with allegations against Turkish politicians that attracted millions of viewers on YouTube. Contacts noted that the tapes are seen as a potential source of tension between the ruling coalition (AKP and MHP parties). An early election is seen a source of potential uncertainty given the decline in the ruling AKP's party popularity. So far, **President Erdogan has ruled out a snap vote with the next election expected in 2023.**







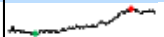



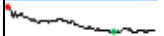













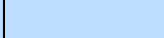



Opposition parties close the gap with ruling alliance



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Global Financial Indicators

Last updated: 5/26/21 8:05 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		4192	-0.2	2	0	40	12
Europe		4026	-0.2	2	0	34	13
Japan		28642	0.3	2	-1	34	4
China		3593	0.3	2	4	27	3
Asia Ex Japan		93	1.4	2	-2	46	4
Emerging Markets		54	1.0	1	-1	45	5
Interest Rates			basis points				
US 10y Yield		1.56	0.2	-11	-1	86	65
Germany 10y Yield		-0.20	-3.6	-9	5	23	37
Japan 10y Yield		0.07	-0.4	-1	-1	7	5
UK 10y Yield		0.75	-3.2	-9	0	54	56
Credit Spreads			basis points				
US Investment Grade		93	0.9	-1	0	-90	-2
US High Yield		346	-0.6	2	12	-318	-34
Europe IG		51	-0.2	-1	1	-22	3
Europe HY		253	-2.2	-8	3	-196	11
Exchange Rates			%				
USD/Majors		89.78	0.2	0	-1	-9	0
EUR/USD		1.22	-0.2	0	1	11	0
USD/JPY		108.9	0.1	0	1	1	5
EMUSD		57.6	-0.1	0	1	6	-1
Commodities			%				
Brent Crude Oil (\$/barrel)		68	-0.3	3	4	89	32
Industrials Metals (index)		156	0.7	0	1	60	17
Agriculture (index)		56	-0.2	-3	-3	62	17
Implied Volatility			%				
VIX Index (% change in pp)		18.4	-0.4	-3.8	0.8	-9.6	-4.3
US 10y Swaption Volatility		65.7	-1.3	-6.9	-9.9	5.4	5.5
Global FX Volatility		7.1	0.0	-0.2	0.0	-0.9	-0.9
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		106	-0.8	-13	-10	-103	-14
Italy		113	0.0	-10	7	-85	1
Portugal		66	-0.4	-6	0	-46	6
Spain		66	-0.3	-6	0	-40	4

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

Emerging Market Financial Indicators

Last updated: 5/26/2021 8:08 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		6.39	0.3	0.7	1	12	2		3.2	0.1	-5	-6	60	-10
Indonesia		14328	0.2	-0.4	1	3	-2		6.4	-1.5	-6	-8	-110	37
India		73	0.3	0.4	3	4	0		6.3	-0.9	-4	-9	17	31
Philippines		48	0.0	-0.6	1	5	0		4.3	6.2	-1	23	-9	68
Thailand		31	0.3	0.6	1	2	-4		1.8	0.0	3	0	53	52
Malaysia		4.14	0.1	-0.4	-1	5	-3		3.3	0.3	2	7	51	73
Argentina		94	0.0	-0.2	-1	-28	-11		45.6	0.0	-14	-91	-105	-1051
Brazil		5.32	0.2	-0.2	2	0	-2		8.3	-8.4	-12	43	275	270
Chile		734	-0.7	-3.0	-4	10	-3		4.0	6.8	25	51	174	125
Colombia		3737	0.1	-2.1	-1	1	-8		6.9	-5.6	18	67	158	182
Mexico		19.86	0.2	0.4	0	12	0		6.7	-5.9	-9	9	44	116
Peru		3.8	-0.3	-2.2	0	-10	-5		4.9	3.3	3	-22	73	135
Uruguay		44	0.1	0.3	0	-2	-4		7.8	11.1	15	38	-281	53
Hungary		287	-0.7	0.4	5	10	3		2.3	-5.3	-14	34	69	77
Poland		3.68	-0.5	1.0	2	10	1		1.1	-2.8	-16	24	10	51
Romania		4.0	-0.1	0.6	1	10	-1		2.7	-1.0	2	13	-131	0
Russia		73.7	-0.2	0.2	2	-4	1		6.8	0.7	0	10	153	108
South Africa		13.8	0.2	1.9	3	26	6		9.7	-7.7	-20	-31	-20	5
Turkey		8.45	0.2	-0.4	-2	-20	-12		17.9	14.7	22	3	655	475
US (DXY; 5y UST)		90	0.2	-0.4	-1	-9	0		0.77	0.0	-9	-6	42	41

	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	1 Day	7 Days	30 Days	12 M	YTD
								basis points						
China		5321	0.0	3	5	38	2		199	0	-2	-9	30	-9
Indonesia		5816	0.0	0	-2	26	-3		158	0	-9	-25	-5	-29
India		51018	0.8	2	4	61	7		152	-3	-9	-16	-120	1
Philippines		6341	2.3	2	0	15	-11		83	0	-9	-17	13	-22
Malaysia		1578	0.0	-1	-3	10	-3		113	0	-2	-3	9	3
Argentina		56222	0.0	3	19	37	10		1459	0	19	8	-570	91
Brazil		122988	0.0	0	2	44	3		253	0	0	-16	58	3
Chile		4091	0.0	-1	-16	10	-2		126	0	-6	-16	-14	-18
Colombia		1204	0.0	-5	-6	12	-16		207	0	-4	-15	44	2
Mexico		48827	0.0	-2	0	35	11		348	0	-9	-34	55	-12
Peru		20238	0.0	-7	5	31	-3		133	0	-4	-3	22	1
Hungary		46133	0.8	1	7	28	10		65	0	-6	-15	-42	-31
Poland		64266	0.3	2	8	34	13		-22	0	-4	-11	-54	-21
Romania		11634	0.0	0	4	34	19		183	1	1	-3	-157	-20
Russia		3708	0.6	2	3	35	13		159	0	-5	-3	19	-7
South Africa		66222	0.2	1	-2	31	11		357	0	-4	-35	25	-23
Turkey		1407	0.5	-4	2	37	-5		421	0	-5	-47	34	-24
Ukraine		529	0.0	0	0	6	6		479	0	12	-21	127	-12
EM total		54	0.4	1	-1	45	5		421	0	17	-10	97	128

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

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