GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

FRIDAY, MAY 31, 2024
LEAD EDITOR: JEFF WILLIAMS

- **US PCE reported in line with expectations while real personal spending dipped in April** (link)
- **Historical data suggests slowing GDP and strong earnings might boost S&P** (link)
- **Euro area sovereign yields resume upward trend after upside inflation surprise** (link)
- **Tokyo's inflation accelerated in May** (link)
- **China's May manufacturing PMI unexpectedly slipped back into contraction** (link)
- **Türkiye's Q1 GDP slightly lower than expected** (link)
- **Zambia's inflation accelerates in May** (link)

Mature Markets | Emerging Markets | Market Tables

Dollar dips on mixed data

While euro area inflation surprised modestly on the upside, PCE data in the US came in mostly in line with expectations and real personal spending unexpectedly fell in April. The combined US data caused treasury yields to decline modestly, while sovereign yields rose in Europe after the inflation data release. Following the euro-area inflation release, the yield on the German 10-year rose 5 bp. The overall impact of declining US yields and rising European yields has helped boost the euro by 0.4% this morning to its highest level in about 2 weeks. Data released by Japan's finance ministry revealed authorities spent ¥9.8 trn (about USD$62 bn) to support the yen over the past month. While analysts anticipated data to reveal that authorities had intervened, the published amount was somewhat larger than expected. Later today, S&P will release its rating review of France, with some analysts speculating a downgrade to AA- is possible. Emerging markets currencies are benefitting from the better risk appetite and weakening dollar, with the Polish zloty (+0.9%) leading gains.

Key Global Financial Indicators

Last updated: 5/31/24 8:12 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		5235	-0.6	-1	4	25	9.76
Eurostoxx 50		4983	0.0	-1	1	18	10
Nikkei 225		38488	1.1	0	1	22	15
MSCI EM		42	-0.3	-2	3	11	5
Yields and Spreads					bps		
US 10y Yield		4.55	0.6	9	-13	91	67
Germany 10y Yield		2.69	4.0	11	11	41	67
EMBIG Sovereign Spread		369	1	-1	-4	-107	-14
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		46.8	0.1	0	1	-6	-3
Dollar index, (+) = $ appreciation		104.6	-0.1	0	-1	0	3
Brent Crude Oil ($/barrel)		81.8	-0.1	0	-7	13	6
VIX Index (%, change in pp)		14.3	-0.1	2	-1	-4	2

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

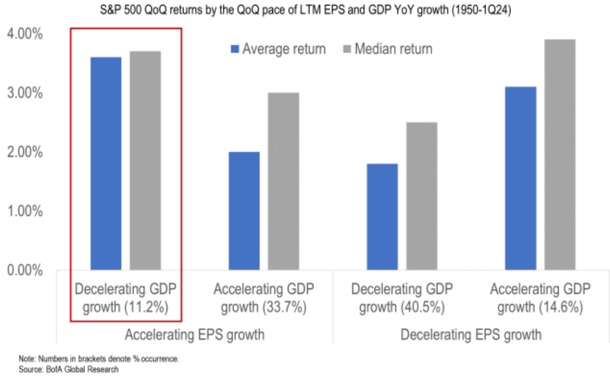
Mature Markets back to top

United States

This morning's data showed the core PCE deflator, the Fed's preferred inflation gauge, remained at 2.8% y/y (vs 2.8% expected; 2.8% prior), reflecting a slight deceleration of its monthly pace to 0.2% (0.3% prior), in line with expectations. According to Bloomberg analysts, the moderation was possibly due to less volatile items such as airfares. The monthly pace of PCE inflation was 0.3% (vs. 0.3% expected; 0.3% prior), with an annual pace of headline inflation maintained at 2.7% (expected and prior 2.7%). Personal income grew 0.3% in April (vs. 0.3% expected; 0.5% prior), while personal spending moderated to 0.2% from a revised 0.7%, slightly below expectations of 0.3%. Treasury yields fell about 2–3 bp following the release.

Historical data suggests slowing GDP and strong earnings might boost S&P. The S&P 500 could gain up to 3.6% based on the average return observed during previous quarters when corporate earnings accelerated and economic growth decelerated, according to Bank of America Global Research. That compares to an average return which is about 1.6 pp lower when GDP and earnings growth are both accelerating (left chart). Thanks to strong corporate earnings, the S&P 500 Index has gained 10% YTD. Analysts note that the so-called Magnificent Seven tech mega caps saw profits soar over 50%, while tech and communications saw earnings growth of 30%. According to Deutsche Bank, the S&P 500 has now risen for 23 of the last 30 weeks. Based on BofA Fund Manager Survey in May, 38% of respondents believe large-cap growth is expected to drive the US equity market going forward (16% of respondents attribute the performance to large-cap value). This week, the growth-to-value stock ratio reached its highest point since April 2022 (right chart).

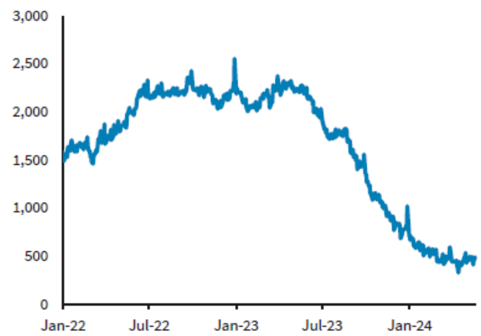
Accelerating EPS and decelerating GDP has been the best backdrop for stocks



S&P growth vs value ratio highest in over two years

Reduced RRP balances could lower bank reserves further, analysts warn. RRP balances have mostly stopped declining since April and have stabilized at around $450bln (left chart), after falling by $350bln in 1Q24. Lower net bill issuance since April reduced the supply of RRP alternatives and narrowed the spread between bill yields and the RRP, according to Barclays Research. As a result, money market funds reduced their aggregate bill holdings by 6% by the end of April. With bond issuance rising, steady RRP balances could further reduce bank reserves, analysts warn. As MMFs are not able to directly buy longer-term debt (using bank deposits, and reserves as a result), reserves have decreased by over $250 billion since April, of which roughly $100 billion is owing to the use of RRP and the Treasury's account at the Fed—analysts at Macrobond suggest. While bank reserves are still around $3.4tn (right chart), analysts expect part of these will be used up during QT. Barclays projects that, with constant RRP balances, bank reserves could drop to $2.8–2.9 trillion in December if the Fed keeps tapering QT at the June rate, and the year-end Treasury cash target is $750bln.

FIGURE 1. RRP balances ($bn)



Source: Federal Reserve, Barclays Research

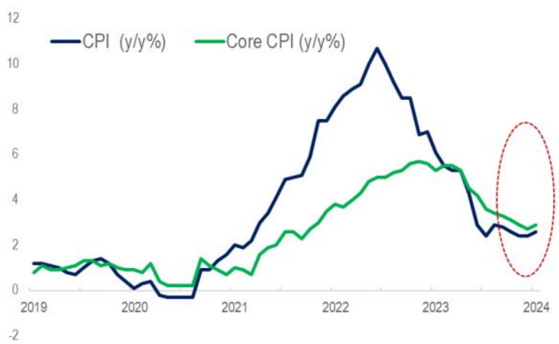
FIGURE 2. Bank reserves ($bn)

Source: Federal Reserve, Barclays Research

Europe

Euro area sovereign yields were higher this morning following an upside surprise in preliminary euro area inflation data ahead of US data due later today. Euro area sovereign yields resumed their upward trend after euro area preliminary inflation for May surprised on the upside (10y bund yield +5bp to 2.70%). European equities were little changed while the euro was marginally stronger against the dollar (+0.1% at 1.08). **Markets are also focused on S&P's rating review of France, due later today.** Citi analysts note that S&P's current negative outlook on France implies a higher risk of a downgrade. The analysts believe that the market is not currently pricing in a rating downgrade, while Commerzbank analysts think a downgrade to AA-/stable would not be a major surprise given the negative outlook and the deficit trajectory that has worsened since December.

Eurozone inflation

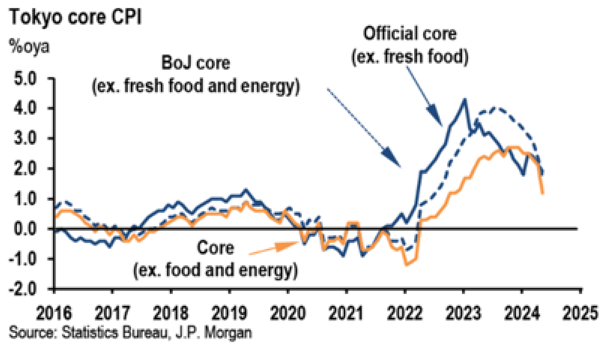


Source: Bloomberg and IMF calculations

Markets scale back ECB rate cut expectations beyond June after euro area preliminary May inflation surprised on the upside. Preliminary data released this morning showed headline inflation increasing to 2.6%y/y in May (versus expected 2.5%y/y from 2.4%), and core inflation increasing to 2.9% (versus expectations to remain unchanged at 2.7%). Sovereign yields increased in the aftermath of the data release, with 10y bund yields (+5bp) trading at around 2.70%. Contacts highlight that 10y bund yields have increased by roughly 40bp so far this quarter, even though euro-zone inflation has overall been easing. Bloomberg analysts argue that reflects concerns that inflation could remain sticky and remain closer to 3% than 2%. **Markets continue to price in roughly 24bp of rate cuts for the ECB meeting next week but have further scaled back rate cut expectations thereafter** and are now pricing in roughly 76bp of easing by April 2025, compared to 81bp priced in yesterday. HSBC analysts continue to expect the ECB to cut rates in September and December, but caution that persistent services inflation could make the ECB more cautious going forward.

Japan

Japanese equities rallied 1.7%, with gains across all sectors. **Tokyo May inflation accelerated**. Headline inflation and core inflation (ex-fresh food) rose to +2.2%y/y (previous: +1.8%) and +1.9%y/y (previous: +1.6%) respectively. J.P. Morgan attributed higher core inflation to the end of a temporary reduction of the renewable energy promotion fee and believe that price momentum will pick up in June and July as the government plans to end electricity and gas subsidies. Separately, retail sales rebounded more than expected at +2.4%y/y (previous: +1.1%) in April, while industrial production remained in contraction at -1%y/y (previous: -6.2%). The yen depreciated 0.2%. Japan's Ministry of Finance will release May foreign exchange intervention data late Friday, with investors suspecting that the BOJ intervened in May to support the yen. 10Y bond yields were little changed.



Commodities

Analysts are bullish about commodities as demand growth is steady, the geopolitical risk premium for oil is declining, and there remain structural tailwinds for industrial metals and gold. Goldman introduced the 5D bull market trends that create structural opportunities: 1. Disinvestment: investment in commodity production capacity has been low since the mid-2010s. 2. Decarbonization & climate change: these create significant investment opportunities. 3. De-risking (Hedging): geopolitical de-risking and strategic restocking support demand for gold and critical commodities 4. Datacenters & AI: AI adoption could fuel productivity growth. 5. Defense spending: military spending could support demand for metals and distillate fuels. It is expected that commodity total returns will rise from 13% YTD to 18% by year-end.

The 5D Bull Market

Commodities	Disinvestment	Decarbonization & Climate Change	De-risking (Hedging)	Datacenters & AI	Defense Spending
Energy					
Crude Oil	◷		◷		
Refined Oil Products	✓ ◷		◷		✓ ◷
Natural Gas				◷	
Power		✓ ◷		◷	
Uranium	✓ ◷	✓ ◷	◷	◷	✓ ◷
Industrial Metals					
Copper	✓ ◷	✓ ◷	◷	◷	✓ ◷
Aluminum	✓ ◷	✓ ◷	◷	◷	✓ ◷
Battery Metals (Lithium, Cobalt, Nickel)		✓ ◷	◷	◷	✓ ◷
Precious Metals					
Gold			✓ ◷		
Silver		✓ ◷			✓ ◷
Agriculture & Softs		✓ ◷	✓ ◷		
Freight	✓	✓ ◷	✓ ◷		

✓ Already Supporting Commodity Returns ◷ Will Support Commodity Returns

Source: Goldman Sachs Global Investment Research

Emerging Markets

back to top

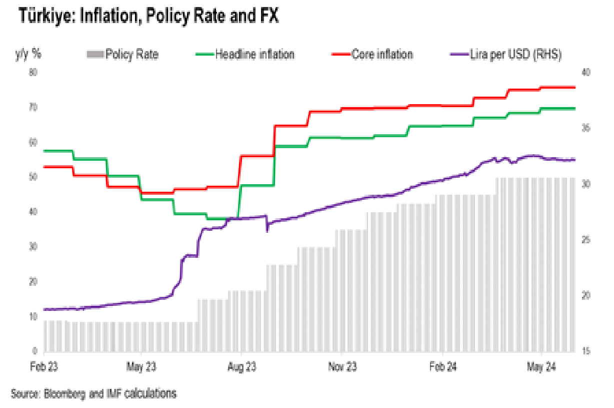
Asian equities were mixed and declined 0.4% on net. Taiwan POC (-0.9%), Hong Kong SAR (-0.8%) and Mainland China (-0.4%) declined. Bloomberg reported that **China is ending tariff concessions on import items from Taiwan POC**. China's Ministry of Finance said on Friday that concessions on 134 items would be halted starting from June 15. The move will impact 10.2% of $95.7bn worth of Taiwan's cross-strait shipments based on 2023 estimates. Asian currencies were mixed. The South Korean won depreciated 0.4%, while the Philippine peso appreciated 0.2%. Asian 10Y bond yields fell and followed US treasury yields lower. **EMEA equities and currencies were mostly higher today**. In CEE, stock markets gained and currencies appreciated against the euro, with the Polish zloty (+0.7%) and the Hungarian forint (+0.4%) leading. In South Africa, equities traded laterally and the rand was stronger (+0.2%) against the dollar, after the central bank left its policy interest rate unchanged at 8.25% yesterday, as expected. In Türkiye the lira was stable against the dollar, while the stock market gained 1.2%. **Latin American assets were mixed Thursday.** Stocks declined in Brazil (-0.9%) and Chile (-0.6%), while Colombia's equity market rose by 0.7%. Currencies depreciated with the Chilean peso falling 0.7%. Argentina's dollar bond prices rose across the curve as President Milei's deregulation plan moved closer to a senate vote.

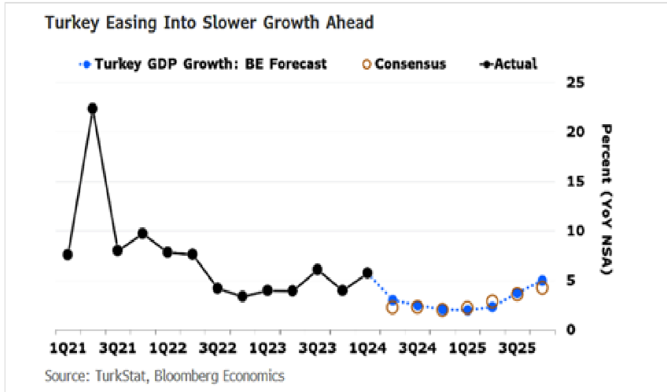
China

Chinese equities fell 0.4% dragged by weak PMI data. Manufacturing PMI unexpectedly slipped back into contraction at 49.5 (previous: 50.4) in May, while non-manufacturing PMI declined to 51.1 (previous: 51.2). The National Bureau of Statistics attributed the PMI slowdown to high base and insufficient effective demand. Market participants said the latest US tariffs will be a major headwind to China's manufacturing activity in the coming months. **Local media reiterated earlier reports that the People's Bank of China (PBC) may sell bonds when necessary.** PBC-backed Financial News wrote that the central bank would choose to sell government bonds if the massive outflow of bank deposits into the sovereign bond market continues and the demand for risk-free asset rises further. A reasonable yield for the 10Y bond should be between 2.5% and 3%, the paper added. Separately, **China Securities Regulatory Commission fined indebted property giant Evergrande 4.18bn yuan ($577mn).** The financial regulator cited fraudulent bond issuance and violations on information disclosures in its statement. Chinese authorities are reportedly weighing a record fine for PricewaterhouseCoopers (PWC) over Evergrande's auditing work. Penalties may be announced as soon as this week, Bloomberg reported. 10Y bond yields gained 2bp and the renminbi depreciated 0.1%.

Türkiye

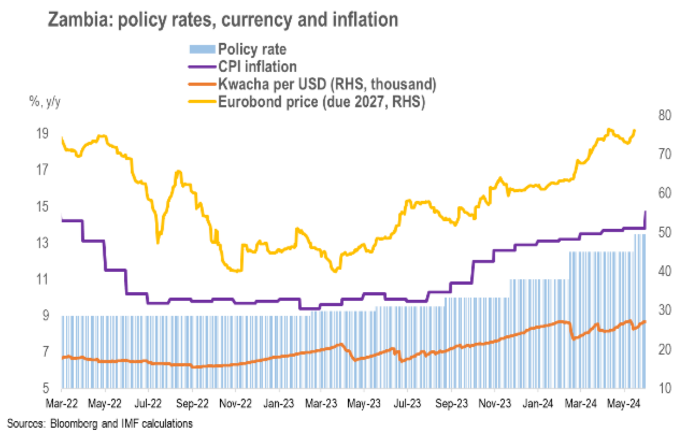
The lira was stable this morning against the dollar, while stocks rose 1.2%, as today's data showed that Türkiye's GDP grew in Q1 2024 by 5.7%y/y, less than expected (median est. 5.8%), and from 4% in Q4 2023. According to Goldman Sachs, the significantly tighter policy since March, as the central bank continues to focus on disinflation, points to a slowdown in H2, so that they continue to expect 2024 growth to stay at 2.8%y/y. Economists at Bloomberg also believe that the central bank's tighter monetary policy is set to weigh further on growth, which they expect to be at 3.2%y/y in 2024, well below the 5% growth level that Türkiye's economy reached before the pandemic. Analysts at BBVA see instead the slowdown as limited, as aggregate demand remains strong and growth has barely adjusted against the backdrop of the central bank having lifted the policy rate up to 50%. May's inflation print is due on June 3, and consensus expects it to reach 74.8%y/y, from 69.8%y/y in April.





Zambia

Zambia's kwacha was stronger (+3.3%) against the dollar today, after yesterday's data showed that CPI inflation rose to 14.7% y/y in May from 13.8% in April. JP Morgan expected inflation to increase in May since the currency depreciated by 7% against the dollar in April, subsequently prompting a 14% hike in gasoline prices in May. In addition, the drought induced by El Niño, reportedly the worst in at least four decades, has forced the country to more increase imports of food and electricity. Zambia has received commitments for $500m of international assistance, including $180m from the IMF as it expects to conclude its third program review. However, President Hichilema said last month that the country needs up to $900m of aid this year. Food inflation accelerated to 16.2%y/y in May, from 15.7% in April, and non-food inflation reached 12.7%y/y, versus 11.2% in April. The central bank raised its key interest rate by 100bp to 13.5% in early May and expects inflation to stay at 9.8%y/y in 2024.The Governor said on May 15 that "The bank stands ready to take appropriate action should inflation persist above the 6% to 8% target band". According to JP Morgan, the May inflation print probably marks a peak, as strong base effects from food should moderate inflation in the second half of 2024.



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Global Financial Indicators

5/31/24 8:12 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities					%		%
United States		5239	-0.6	-1	4	25	10
Europe		4983	0.0	-1	1	18	10
Japan		38488	1.1	0	1	22	15
China		3580	-0.4	-1	-1	-7	4
Asia Ex Japan		71	-0.2	-2	4	10	6
Emerging Markets		42	-0.3	-2	3	11	5
Interest Rates					basis points		
US 10y Yield		4.55	0.6	9	-13	91	67
Germany 10y Yield		2.69	4.0	11	11	41	67
Japan 10y Yield		1.07	0.6	7	19	63	46
UK 10y Yield		4.37	2.0	11	2	18	83
Credit Spreads					basis points		
US Investment Grade		116	0.4	0	-1	-49	-17
US High Yield		349	-0.6	6	3	-149	-36
Exchange Rates					%		
USD/Majors		104.63	-0.1	0	-1	0	3
EUR/USD		1.09	0.2	0	2	2	-2
USD/JPY		157.1	0.2	0	0	13	11
EM/USD		46.8	0.1	0	1	-6	-3
Commodities					%		
Brent Crude Oil ($/barrel)		81.8	-0.1	0	-5	17	7
Industrials Metals (index)		163	0.0	0	3	16	15
Agriculture (index)		62	0.6	0	5	-3	-1
Implied Volatility					%		
VIX Index (%, change in pp)		14.3	-0.1	1.6	-1.3	-3.6	1.9
Global FX Volatility		6.9	0.0	0.1	-0.6	-2.0	-1.2
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		100	-1.1	-1	1	-49	-3
Italy		130	0.3	0	-3	-50	-37
Portugal		60	-0.9	-4	-3	-15	-4
Spain		73	-0.3	-3	-4	-32	-24

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

Emerging Market Financial Indicators

Last updated: 5/31/2024 8:13 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	-0.1	0.0	0	-2	-2		2.2	0.5	-2	-12	-57	-28
Indonesia		16253	0.1	-1.6	0	-8	-5		6.9	-4.0	-1	-32	55	44
India		83	-0.2	-0.4	0	-1	0		7.4	-1.1	6	-14	8.3	20
Philippines		59	0.2	-0.6	-1	-4	-5		5.6	0.0	-3	-16	-38	-6
Thailand		37	-0.2	-0.2	1	-6	-7		2.8	-0.5	1	-7	21	15
Malaysia		4.71	0.0	0.1	1	-2	-2		4.0	13.3	14	6	33	31
Argentina		894	-0.1	-0.5	-2	-73	-10		38.3	10.0	330	-193	-7089	-4805
Brazil		5.20	0.0	-0.7	0	-3	-7		12.0	-1.0	19	11	32	159
Chile		918	-0.7	-0.9	5	-12	-4		5.4	0.0	16	1	14	46
Colombia		3866	0.2	0.0	1	14	0		8.5	0.5	16	3	-15	86
Mexico		16.98	0.2	-1.7	1	4	0		9.4	-0.2	18	-18	106	93
Peru		3.7	0.3	-0.3	0	-2	-1		7.1	0.4	3	-16	-9	45
Uruguay		39	-0.1	-0.6	-1	0	0		9.2	-1.2	3	4	-85	-37
Hungary		358	0.4	-1.2	2	-3	-3		6.7	-2.0	-12	-29	-125	96
Poland		3.93	0.6	-0.2	3	8	0		5.3	-0.4	-5	-3	-1	86
Romania		4.6	0.2	0.0	2	1	-2		6.6	-0.1	7	-5	-22	42
Russia		90.1	0.3	-0.6	4	-10	-1							
South Africa		18.7	0.2	-1.6	0	5	-2		9.9	13.0	13	-16	-40	79
Türkiye		32.21	0.0	0.0	1	-36	-8		28.0	-3.0	19	-23	1894	128
US (DXY; 5y UST)		105	-0.1	-0.4	-1	0	3		4.58	0.9	5	-14	82	73

	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		3580	-0.4	-1	-1	-7	4		139	0	3	-52	-19
Indonesia		6971	-0.9	-3	-2	5	-4		96	6	-1	-49	0
India		73961	0.1	-2	0	18	2		91	0	-9	-52	-25
Philippines		6433	1.0	-3	-3	-1	0		83	4	-1	-33	3
Thailand		1346	-0.4	-1	-2	-12	-5		0	0	0	0	0
Malaysia		1597	-0.5	-1	0	16	10		78	1	-3	-16	-7
Argentina		1643011	4.8	9	24	380	77		1308	-130	88	-1263	-605
Brazil		122707	-0.9	-2	-3	13	-9		211	-3	-1	-51	-4
Chile		6639	-0.6	-2	2	21	7		114	0	-5	-20	-11
Colombia		1404	0.7	0	3	28	17		304	-4	0	-101	33
Mexico		55353	0.3	-1	-2	5	-4		294	-1	-13	-102	-40
Peru		30406	-0.3	1	4	44	17		150	0	0	-32	6
Hungary		68456	0.5	-1	0	45	13		143	3	-7	-92	-6
Poland		86337	0.7	-2	2	35	10		94	2	3	-43	-3
Romania		17622	0.3	0	3	44	15		175	0	-7	-82	-26
South Africa		77114	-0.1	-2	1	3	0		323	4	-12	-132	15
Türkiye		10568	0.8	-1	5	116	41		274	-3	2	-303	-40
EM total		42	-1.1	-2	3	11	5		330	-4	1	-91	-16

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

back to top