GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

FRIDAY, MAY 5, 2023

- **US employment data for April stronger than expected** (link)
- **Fed's backstop lending dropped sharply on resolution of First Republic Bank** (link)
- **US smaller banks' deposit and loan dynamics were better than feared after Q1 turmoil** (link)
- **ECB hikes 25 bps and signals more hikes ahead** (link)
- **German factory orders and euro area retail sales disappoint in March** (link)
- **Caixin services PMI weakened slightly more than expected in April** (link)
- **Ecuador's debt for nature swap proceeds as $1.6bn of sovereign bonds are purchased** (link)

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Strong US employment data sends rates higher

This morning's US employment report for April came in stronger than expected. While prior month's job figures were revised lower, the decline in the unemployment rate to 3.4% (from 3.5%) and the higher-than-expected rise in average hourly earnings sent treasury yields higher as markets reassessed the future path of monetary policy. The initial reaction from markets essentially undid the rate decline following the FOMC release from Wednesday, and subsequent press conference. The end-year implied Fed funds rate rose 6 bp on the release. Ahead of the jobs report, equity markets were moving higher, boosted by improved sentiment in US regional bank stocks. Earnings reports thus far has shown that deposit flight from smaller banks was not as bad as markets had feared. Meanwhile, the implied terminal rate for the ECB has moved lower despite the bank's strong signal yesterday that further hikes are likely. Through the September ECB meeting, markets are pricing 45 bp in additional hikes, 8 bp lower than was priced on Wednesday.

Key Global Financial Indicators

Last updated: 5/5/23 8:13 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		4061	-0.7	-2	-1	-2	6	-4
Eurostoxx 50		4309	0.5	-1	0	17	14	8
Nikkei 225		29158	0.1	2	3	9	12	10
MSCI EM		39	0.8	0	-1	-6	3	-18
Yields and Spreads					bps			
US 10y Yield		3.40	2.1	-2	9	36	-48	141
Germany 10y Yield		2.26	7.4	-5	8	122	-31	204
EMBIG Sovereign Spread		492	1	3	7	47	41	80
FX / Commodities / Volatility					%			
EM FX vs. USD, (+) = appreciation		50.9	0.0	1	1	-3	2	-4
Dollar index, (+) = $ appreciation		101.4	0.0	0	0	-2	-2	5
Brent Crude Oil ($/barrel)		74.4	2.6	-6	-12	-33	-13	-23
VIX Index (%, change in pp)		18.9	-1.2	3	0	-12	-3	-12

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

Mature Markets

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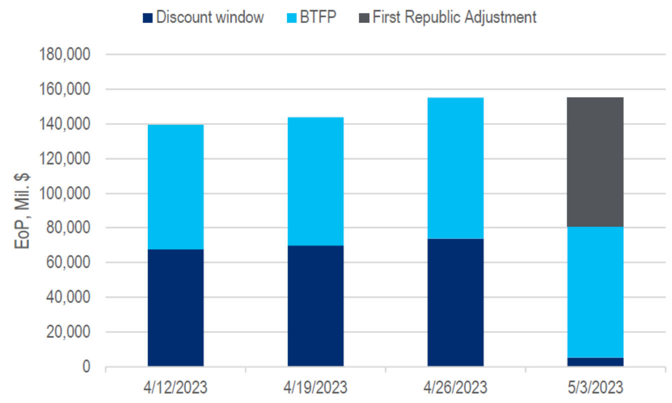
United States

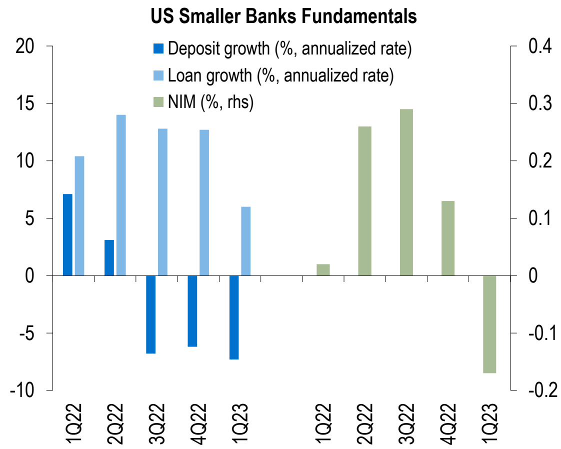
Nonfarm payrolls surprised strongly on the upside by adding 253K jobs in April, 68K above the consensus forecast, though prior reading was revised down by an even larger 71K to 165K. Similarly, private payrolls increased to 230K against a 66K downward revision in prior reading. Unemployment rate unexpectedly fell to 3.4% (from 3.5%) vs an expected increase to 3.6%, with the labor force participation rate stable at 62.6%. Average hourly earnings accelerated to 0.5% m/m from 0.3% m/m with the annual rate rising to 4.4% y/y. Treasury yields jumped in a flattening move following the report, with the 2-year yield up 12bp to 3.91% and 10-year yield up 7bp to 3.45%.

Fed's backstop lending dropped sharply due to the resolution of First Republic Bank (FRC). Lending through the discount window dropped $68.5bn to $5.3bn during the week ending on May 3, driven by the decline in loans from FRC that was $63.5bn as of Mar 31. Lending through the Bank Term Funding Program (BTFP) fell modestly by $5.5bn to $75.7bn. However, after adjusting for FRC's $13.8bn borrowing from the facility, BTFP lending was slightly up on the week. Other credit extensions increased by $57.8bn, largely due to FDIC lending as part of the FRC purchase agreement. On the liability side, the Treasury General Account balance fell $107.9bn to $188.3bn due to typical larger outlays at the beginning of the month. RRP balance dropped by about $21bn but is expected to move higher in the coming month as growing concerns about the debt ceiling will drive more inflows into money market funds.

Figure 1. Discount Window down $68.5 bln but that's largely because of First Republic; total lending didn't change much after adjustment



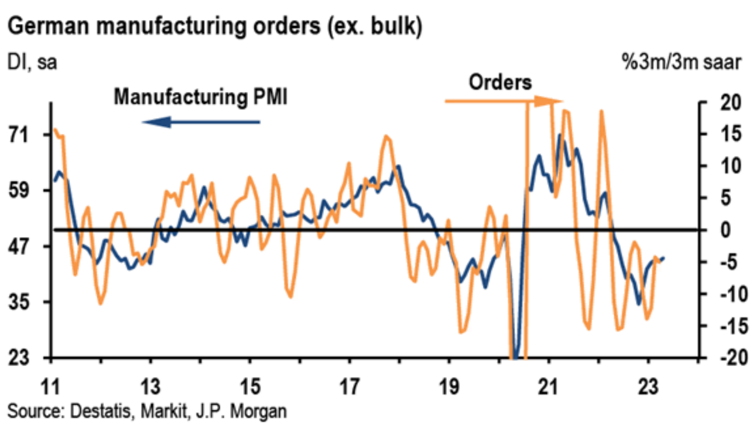
Smaller US banks' Q1 earnings showed deposits and loan dynamics were better than feared. Deposits declined at a 7.3% annualized rate, which was modestly worse than the pace seen in the last 2 quarters. While outsized deposit flows appear to have been avoided, many banks continue to expect that a sustained deposit migration from low-cost deposits into higher yielding alternatives will continue. Interest-bearing deposit costs increased 75 bp q/q to 1.8%, with cumulative deposit beta still running at a modest 38%. The higher funding costs contributed to a 17bp drop in banks' net interest margin. With a large yield differential compared to T-bills and money market funds, bank NIMs are likely to remain under sustained pressure, as deposit drains from QT continues. Loan growth decelerated to a 6% annualized rate from last year's high base, with most banks still expecting mid-single digit loan growth in 2023. Banks are curtailing lending to CRE, in particular office space, but so far there are little signs of a broader "credit crunch." Underlying credit risks were largely stable, with provision and net charge-off still below long-term averages.



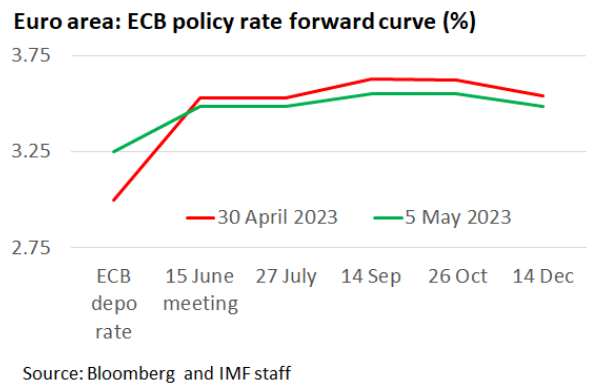
Euro area

Equities (+0.6%) rose and German yields are 7–8 bp higher across maturity segments ahead of the U.S. payrolls report. Bank stocks (+2%) outperformed inspired by a broader rally in US stocks futures.

Key economic data releases such as German factory orders and euro area retail sales disappointed in March. Euro area retail sales volumes dropped 1.2% m/m in March, compared to close to flat expected. German factory orders fell 11% m/m in March, compared to a drop of 2.3% expected. The decline in factory orders was broad-based with both domestic and particularly foreign orders declining strongly. Cars and machinery posted strong declines. JP Morgan points out that some weakness in German industrial data is consistent with surveys, if somewhat surprising, given the drop in energy prices and rebound in services.



The euro (+0.1%) was little changed today after the ECB slowed its tightening pace to 25 bp yesterday but sent a strong signal that a couple more hikes of 25 bp are likely given still significant upside risks to inflation. ECB sources have also confirmed that those ECB GC members favoring an interest-rate increase of 50 bp "did not put up much of a fight." The ECB president emphasized that the Bank Lending Survey shows that the demand from corporates is "really, really down" on the back of higher interest rates, which is a clear indication that ECB policy is in restrictive territory. Pricing for the terminal rate in 2023 has shifted lower.



Turning to Quantitative Tightening, the ECB decided to stop APP reinvestment which will imply a reduction of the balance sheet of around €25bn/m (from around €15 bn/m per month until the end of June 2023). The ECB will continue to flexibly reinvest principal payments from the PEPP program until at least the end of 2024. Analysts at SocGen write that an earlier-than-expected decision on APP was qualified by an "expected" ending as of July, likely to leave some flexibility if market volatility rises materially.

Emerging Markets

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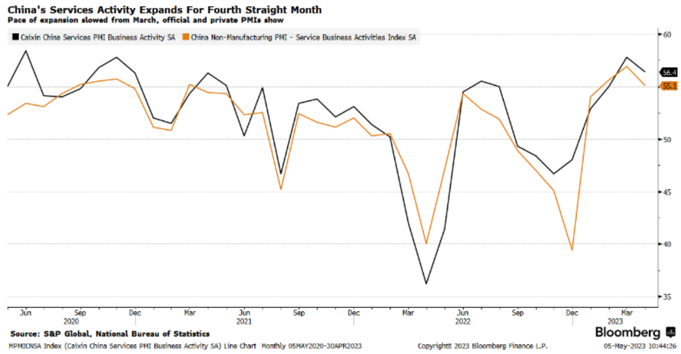
Asian equities and currencies were mixed. Share prices rose in Hong Kong SAR (+0.5%) and Malaysia (+0.3%) but fell in Indonesia (-0.8%) and India (-0.7%). Most Asian currencies continued to gain on US rate cut bets, led by the Malaysian ringgit (+0.4%) and Korean won (+0.3%). The former was also supported by a surprise interest rate hike by the central bank on Wednesday. The Indonesian rupiah was little changed, despite slightly better-than-expected GDP growth in Q1 (+5.03% y/y). To support the Indonesia rupiah, the authorities expect to step up tighter rules in the near future for exporters to retain foreign exchange earnings at domestic banks. 10-year government bond yields declined in China (-3 bp), Singapore (-3 bp), and Malaysia (-2 bp), while other Asian economies saw little changed. Elsewhere, inflationary pressure eased in the Philippines with its headline inflation down to an eight-month low of 6.6% in April from 7.6% in March, well below the market expectation. Core inflation also edged lower to 7.9% from 8.0%. The Philippine peso gained (+0.1%), while share prices were virtually unchanged. **Stocks in South Africa (+1%) and Poland (+1%) traded with a positive tone in line with global markets.** Currencies were higher in Poland and Hungary but fell in South Africa. Local rates were mixed. **Latin American assets were mixed Thursday.** Stocks lost in Peru (-0.6%) and Mexico (-0.5%), while Brazil equity markets gained 0.4%. Currencies appreciated in Chile (0.7%), Colombia (0.4%), and Brazil (0.2%), while the Peruvian sol (-0.2%) weakened against the dollar.

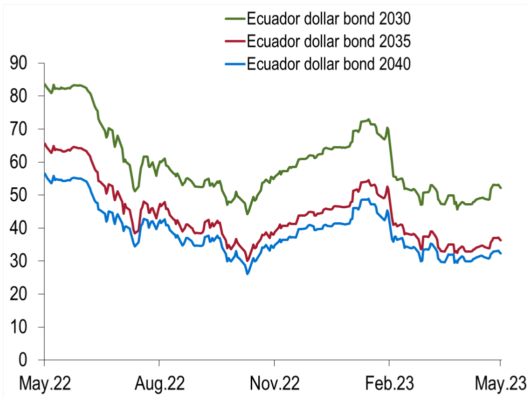
China

Caixin services PMI weakened slightly more than expected in April. While PMI data (both official and Caixin) pointed to the continuation of the post-COVID recovery in services activity, Caixin services PMI dropped from 57.8 in March to 56.4 in April, slightly lower than expectations (consensus: 57.0). Caixin composite PMI thus weakened from 54.5 to 53.6. Despite strong domestic tourism spending during the recent Labor Day holidays, home sales in 40 major cities during the holidays period remained 22% lower than the 2019 level, signaling still weak confidence in the property market. Market participants have increasingly become concerned about the uneven economic recovery. Equities declined (CSI 300: -0.3%); RMB appreciated slightly (+0.04%); long-term CGB yields fell (10-year: -3 bp). The People's Bank of China continued withdrawing interbank liquidity in an amount of 162 bn RMB ($23.4 bn). The key interbank repo rate (DR007) declined to 1.78% (-54 bp). Separately, state-owned enterprises and domestically listed companies were required to review the ability of auditors to safeguard information security, as part of a fresh move by Chinese authorities to tighten the management of sensitive corporate information.



Ecuador

Credit Suisse Group has reportedly acquired $1.63 billion of Ecuador's distressed sovereign bonds from bondholders for a significantly reduced price of $800 million. The bank's purchase is part of a debt-for-nature swap, where a portion of the high yielding sovereign bonds will be replaced with less costly debt, resulting in savings to fund Ecuador's conservation and sustainability efforts. To lower the cost and refinancing risk, the Inter-American Development Bank has guaranteed a new debt instrument. Ecuador's bonds have lost 19% of their value this year, making them one of the worst performers in emerging markets.



Source: Bloomberg and IMF staff

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Global Financial Indicators

	Level		Change				
5/5/23 8:13 AM	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		4072	-0.7	-2	0	-2	6
Europe		4309	0.5	-1	0	17	14
Japan		29158	0.1	2	3	9	12
China		4017	-0.3	1	-3	3	4
Asia Ex Japan		66	0.8	0	-2	-5	2
Emerging Markets		39	0.8	0	-1	-6	3
Interest Rates					basis points		
US 10y Yield		3.40	2.1	-2	9	36	-48
Germany 10y Yield		2.26	7.4	-5	8	122	-31
Japan 10y Yield		0.42	0.0	3	-6	19	0
UK 10y Yield		3.76	10.4	4	33	179	9
Credit Spreads					basis points		
US Investment Grade		168	-0.2	7	4	13	9
US High Yield		512	-5.1	31	7	90	32
Exchange Rates					%		
USD/Majors		101.38	0.0	0	0	-2	-2
EUR/USD		1.10	0.0	0	1	4	3
USD/JPY		134.2	-0.1	-2	2	3	2
EM/USD		50.9	0.0	1	1	-3	2
Commodities					%		
Brent Crude Oil ($/barrel)		74.4	2.6	-7	-12	-20	-12
Industrials Metals (index)		151	-0.1	-2	-2	-20	-8
Agriculture (index)		67	1.1	1	-1	-12	-2
Implied Volatility					%		
VIX Index (%, change in pp)		18.9	-1.2	3.1	-0.2	-12.3	-2.8
US 10y Swaption Volatility		124.7	-0.8	13.5	-15.1	1.5	-1.0
Global FX Volatility		9.2	0.0	0.2	-1.1	-1.3	-1.5
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		182	-5.2	-5	-9	-59	-23
Italy		191	-1.8	5	8	-8	-23
Portugal		85	-1.5	3	0	-29	-17
Spain		109	-0.5	5	7	-1	0

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

Emerging Market Financial Indicators

Last updated: 5/5/2023 8:14 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		6.91	0.0	0.1	0	-4	0		3.0	1.5	-8	-16	11	-8
Indonesia		14678	0.0	0.0	2	-2	6		6.4	1.3	-9	-25	-54	-50
India		82	0.0	0.1	1	-7	1		7.2	-0.4	-11	-28	(93.2)	-27
Philippines		55	0.1	0.1	-2	-5	1		5.9	-10.0	-10	-10	50	-15
Thailand		34	0.1	1.2	1	2	3		2.6	-5.5	0	-2	-44	-6
Malaysia		4.44	0.4	0.6	-1	-2	-1		3.7	-3.0	0	-17	-71	-33
Argentina		226	-0.2	-1.6	-7	-49	-22		96.2	119.6	531	741	4334	796
Brazil		5.00	-0.3	-0.2	1	1	6		12.3	12.1	-16	-39	-10	-26
Chile		798	0.7	0.5	1	7	7		5.1	1.0	-12	3	-123	-22
Colombia		4610	0.4	0.9	-1	-12	5		8.9	0.0	-18	31	6	-89
Mexico		17.89	0.1	0.6	2	13	9		8.3	-1.0	-9	-1	-60	-43
Peru		3.7	-0.2	0.1	1	1	2		7.5	#######	0	4	-56	-49
Uruguay		39	0.0	-0.8	-1	6	2		10.0	0.0	-19	-33	-7	-69
Hungary		338	0.2	0.2	2	7	10		7.8	5.0	-3	-46	75	-180
Poland		4.16	0.3	0.1	3	7	5		5.2	3.5	-20	-16	-91	-96
Romania		4.5	0.0	0.0	1	5	3		7.0	-3.5	-9	-16	-1	-65
Russia		77.2	1.5	3.5	4	-16	-4							
South Africa		18.4	-0.5	-0.4	-2	-13	-7		9.3	5.0	-5	32	73	14
Turkey		19.50	-0.1	-0.2	-1	-24	-4		12.8	50.0	-11	254	-891	295
US (DXY; 5y UST)		101	0.0	-0.3	0	-2	-2		3.35	2.0	-13	-2	34	-66

	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		4017	-0.3	1	-3	3	4		201	5	7	-3	24
Indonesia		6788	-0.8	-2	0	-6	-1		151	3	-13	-46	11
India		61054	-1.1	1	2	11	0		163	2	-3	-11	21
Philippines		6686	0.0	2	3	-1	2		123	3	-18	-27	26
Thailand		1533	0.0	0	-4	-7	-8		0	0	0	0	0
Malaysia		1431	0.4	1	0	-9	-4		104	1	5	-23	4
Argentina		281753	-2.5	-8	11	226	39		2580	-95	216	817	375
Brazil		102174	0.4	0	1	-3	-7		285	7	10	-7	11
Chile		5376	0.1	-1	3	11	2		141	4	-9	-30	9
Colombia		1159	0.0	-1	-3	-27	-10		429	1	38	50	57
Mexico		54667	-0.5	1	2	8	13		402	6	6	33	21
Peru		21619	-0.6	-2	-1	3	1		184	6	-10	-17	4
Hungary		46261	-0.1	4	5	9	6		223	-3	-18	19	1
Poland		62336	0.7	1	6	12	8		138	62	50	118	65
Romania		12199	0.3	-1	-1	-2	5		260	4	-2	15	5
South Africa		77921	0.8	0	2	12	7		433	15	21	38	66
Turkey		4431	-1.2	-7	-10	80	-20		526	21	27	-2	86
Ukraine		507	0.0	0	0	-2	-2		5397	112	383	1818	1318
EM total		39	0.8	0	-1	-6	3		427	8	12	31	51

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

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