Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Tuesday, May 7, 2019

- **US markets remain on edge amid uncertainty around tariff threats (link)**
- **Rising goodwill impairments could signal credit stresses for US companies (link)**
- **Consortium of Italian banks and BlackRock plan rescue of Banca Carige (link)**
- **Reserve Bank of Australia unexpectedly leaves policy rate unchanged at 1.50% (link)**
- **Chinese equities post modest rebound as trade meeting with US to proceed (link)**
- **Turkish lira under pressure after Electoral Commission authorizes election re-run (link)**
- **Bank Negara Malaysia lowers policy rate by 25 bps, its first cut since 2016 (link)**

US | Europe | Other Mature | Emerging Markets | Market Tables

Market sentiment remains fragile as trade tensions keep investors on edge

News that the US tariff escalation did not break off scheduled trade talks with China for later this week has helped global markets tentatively stabilize this morning. China's Vice Premier Liu He will still lead a delegation to the US this week, despite a group of US officials reiterating late yesterday that tariffs were set to rise on Friday. Most Asian bourses have recouped part of yesterdays's losses, including Chinese equities gaining about 1%, while Japanese stocks fell around 1.5% in a catch up move as traders returned from a long holiday. European stocks are declining modestly and core euro area yields are lower with the 10-year Bund yield is down 4 bps to -0.03% on softer data and earnings releases. Yesterday, equity volatility initially surged as US tariff threats reignited fears of a trade war ahead of the next round of US-China trade talks later this week. The risk-off headlines sent Asian stocks plunging and spilled over to other regions during the day. However, US equities suffered relatively minor losses, with the S&P 500 closing down 0.4%, as investors tried to decipher whether the tariff threat was just a negotiating tactic rather than a deliberate and decisive plan. Most EM assets were also weaker on the rising trade worries, with Turkish assets underperforming following a decision by the nation's Electoral Commission to re-run some mayoral elections, which have added to the political uncertainties surrounding the country.

Key Global Financial Indicators

Last updated: 5/7/19 8:08 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
S&P 500		2932	-0.4	0	1	10	17
Eurostoxx 50		3432	-0.9	-2	0	-4	14
Nikkei 225		21924	-1.5	-1	3	-2	10
MSCI EM		43	-2.5	-2	-2	-6	11
Yields and Spreads				bps			
US 10y Yield		2.47	-5.6	-3	-3	-48	-22
Germany 10y Yield		-0.03	-3.8	-5	-4	-56	-27
EMBIG Sovereign Spread		347	2	2	7	15	-67
FX / Commodities / Volatility				%			
EM FX vs. USD, (+) = appreciation		62.0	-0.1	-1	-2	-8	0
Dollar index, (+) = $ appreciation		97.7	0.2	0	0	5	2
Brent Crude Oil ($/barrel)		70.3	-1.3	-3	0	-8	31
VIX Index (%, change in pp)		16.7	1.3	4	4	2	-9

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

United States

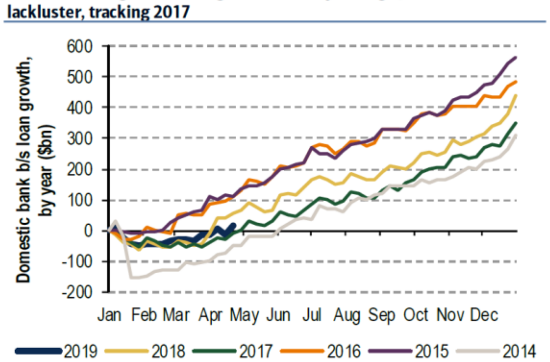
back to top

After the market close yesterday, US Trade Representative Robert Lighthizer confirmed to the press that the government plans to raise tariffs on $200 bn of Chinese imports to 25% on Friday. He justified the decision on the grounds that China had backed away from earlier promises. As of now, the trade talks are set to continue on Thursday and Friday. Equity futures sold off in after-hours trading and Treasuries extended their intra-day rally, **while this morning US Treasury yields have steadied with the 10-year little changed at 2.48% and S&P 500 futures pointing to a 0.5% decline at the open.** Yesterday, US markets had a more measured response to the Sunday tariff surprise, as the heavy selling in the Asian session and the sharp declines in the European session gave way to a calmer US session with much lower trading volumes. Sentiment remained fairly positive in the belief that the presidential tariff threat was just a negotiating tactic, but the after-hours news headline showed this maybe overly optimistic. The S&P 500 was down as much as 1.6% at the market open on Monday before it staged a gradual recovery through the day and ended with a moderate 0.4% loss. The VIX ended at 15.35 after going as high as 18.80.

One consequence of the selloff was a revival of bets on a rate cut after Fed Chair Powell's apparent success in lowering the odds in last week's press conference with a full 25 bps cut now predicted by April 2020, down from June 2020 on Friday. The flight to safety pushed 10-year Treasury yields back below the 2.50% level they have tested through much of the spring. There was some worry about the risk from the record shorts in VIX futures, but the fallout seemed to be contained for now as traders held their nerve. The Fed Funds effective rate declined to 2.40% yesterday from 2.41% on Friday and 2.45% on Thursday as the Fed's 5 bps cut to IOER to 2.35% took hold in the money markets.

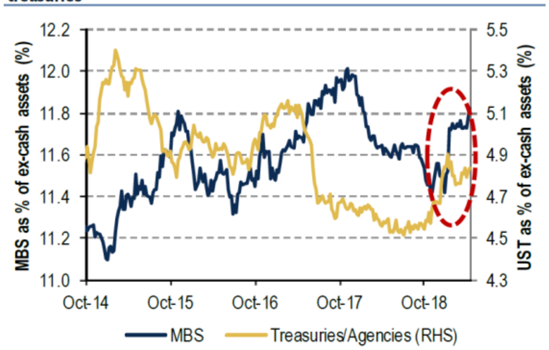
Weakness in bank lending so far in Q2 reinforces the belief among many analysts that the US economy is likely to slow down through the rest of the year. So far, loan growth has followed the same weak trend as 2017, but banks have not appreciably tightened their lending standards suggesting that companies are not actively looking for new bank funding, perhaps due to continued strong investor demand in the corporate bond market. The lack of demand for loans has led to speculation that banks are putting funds to work in other areas, such as increasing their holdings of mortgage-backed securities.

Chart 43: Loan growth during the seasonally strong Q2 has been lackluster, tracking 2017



Source: BofA Merrill Lynch Global Research, Fed H8

Chart 44: Bank allocation to MBS has risen, and not from rotation out of treasuries

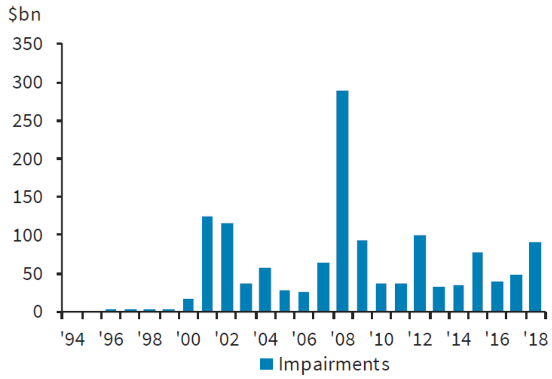


Source: BofA Merrill Lynch Global Research, Fed H8

Note: Holdings are not duration adjusted in this calculation

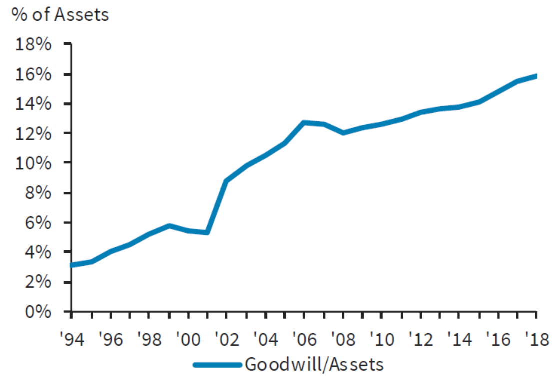
Rising values of goodwill impairments are a potential warning sign of credit problems for US non-financial corporates (NFCs). In 2018 US NFCs had their highest level of such impairments since 2012, and goodwill has grown steadily as a proportion of total NFC assets to the point where higher impairments could have a greater impact on the broader market. Goodwill is defined as the intangible part of a corporation's value, emerging from unquantifiable aspects such as the strength of customer relationships, brand loyalty, licenses, trademarks, strength of dealer networks, etc. Barclays found that goodwill impairments are widespread in companies that recently completed acquisitions of other companies. On average, large goodwill write-downs occurred 2 ½ years after the closing of the M&A transactions, and these write-downs were frequently followed by significant credit spread widening. In view of the large volume of M&A transactions that closed in 2017 and 2018, markets could be exposed to potential credit volatility this year if some of these companies run into trouble.

FIGURE 1
Goodwill Impairments for US Non-Financials



Source: Compustat, Barclays Research

FIGURE 2
Goodwill as a Percent of Assets for US Non-Financials



Source: Compustat, Barclays Research

US corporate bond maturities will rise over the next three years at a time when many believe the US will enter a recession. 67% of US corporate CEOs expect a recession by Q3 2020, according to a recent survey by Duke University, while 84% predict a recession by Q1 2021. The New York Fed recession model assigns a probability of 27.1% that there will be a recession in the next 12 months, compared to just 11% at the beginning of the year. Funding conditions are likely to become more difficult for US corporations as investors recalibrate their spread requirements as the downturn unfolds, especially for the more highly leveraged BBB issuers. If the recession turns out to be severe, these companies may face rollover risks.

Table 1. USD corporate bond maturities, 2019 - 2021, by asset class, USDbn

Debt maturing in:	Total	IG	HY	IG % of Total	HY % of Total
2019	1,130	851	280	75%	25%
2020	1,229	904	325	74%	26%
2021	1,249	922	326	74%	26%

Source: Dealogic, HSBC

Table 2. USD IG corporate bond maturities, 2019 - 2021, by rating category, USDbn

Debt maturing in:	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-
2019	14	11	47	120	94	119	133	107	86	70
2020	8	12	26	114	128	135	142	111	99	81
2021	12	10	30	120	120	141	148	121	104	80

Source: Dealogic, HSBC

Europe

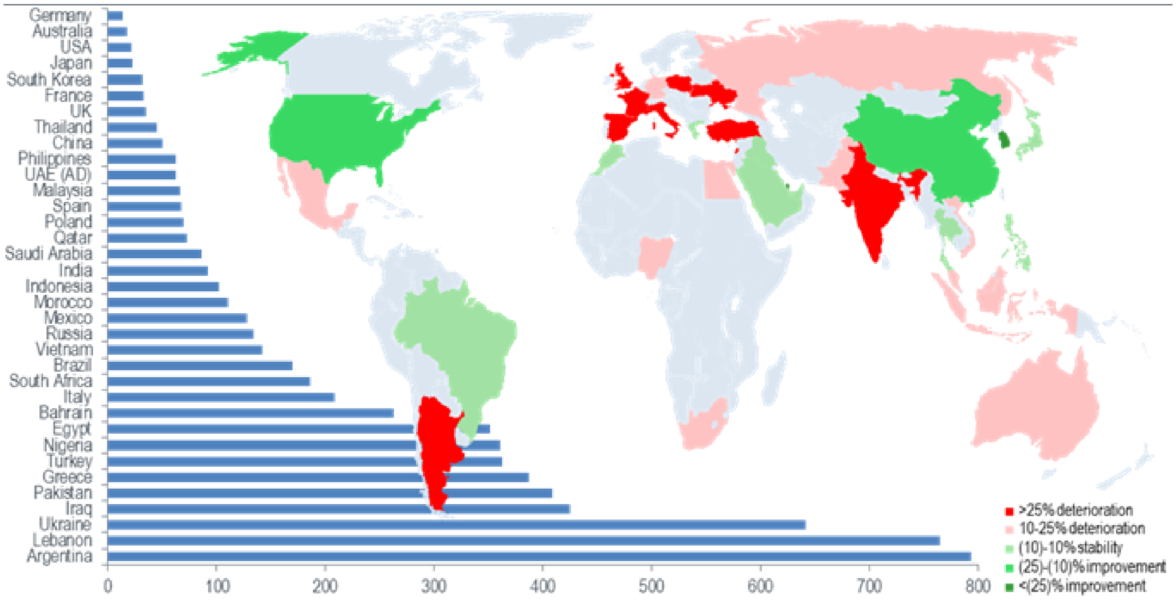
back to top

Trade war fears weighed on equity investors' sentiment, pushing the main indices down by about 0.4-0.5%: EuroStoxx 600 (-0.3%), DAX (-0.4%), and CAC 40 (-0.5%). **Sovereign bond markets were largely unaffected**, with 10-year German yields 2 bps lower at -0.01% and French at 0.34% (-1 bp).

Market perceptions of sovereign risk have deteriorated in some large European economies in the last 12 months, as highlighted by Standard Chartered research. Five-year CDS spreads have widened about 20% on average, with various European countries such as Poland, Spain, and France seeing their spreads revert to historical averages after tightening previously. For the UK, spreads widened 81% (or 30% wider than its five-year average).

Figure 1: 5Y CDS spreads (bps) ranked by country and spread change; March 2018 to April 2019

Broad-based – but mild – deterioration in risk perception across 70% of our sample (3M average)



Source: Bloomberg, Standard Chartered Research

A consortium of Italian banks and asset manager BlackRock are planning to launch a $800 mn-rescue of Banca Carige. The plan involves the conversion of over $300 mn of hybrid bonds held by the Italian banks into new equity, giving the lenders a 43% stake in Carige. BlackRock, in turn, will acquire most of the remainder of the new share issue and take operational control of Carige, which has been under special administration since early 2019. The plan is awaiting approval by Italy's Interbank Deposit Protection Fund (FITD) by May 14.

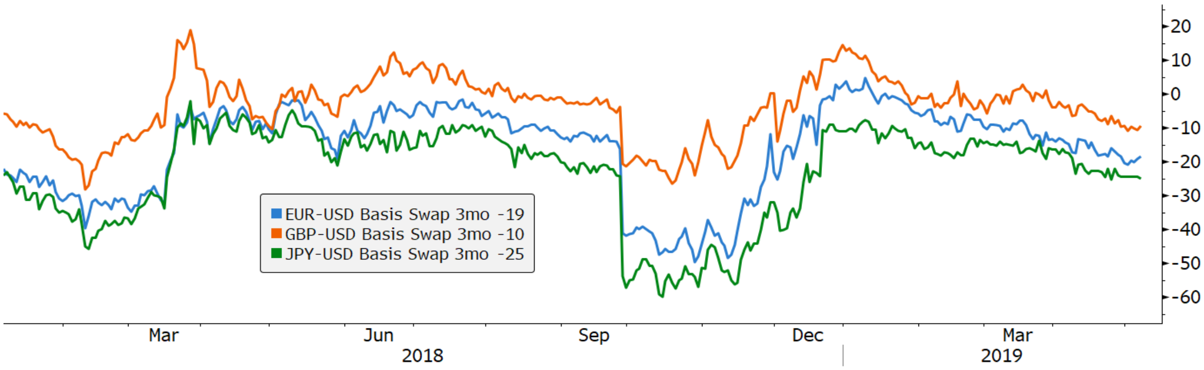
In **European credit markets**, the iTraxx indices have continued to trade sideways in recent weeks, thus breaking the downward trend from Q1. Investment grade spreads stood at 60 bps and high-yield at 259 bps. In money markets, dollar funding conditions have progressively tightened through 2019, although they remain at relatively liquid levels compared to 2018Q4.

European Corporate Credit Spreads

Source: Bloomberg
ITRXEXE Curncy (MARKIT ITRX EUR XOVER 06/24) Credit: Itraxx indices Daily 01JAN

07-May-2019 09:09:20

Cross-Currency Basis Swaps (3 mo)



Source: Bloomberg
EUBSC Curncy (EURUSD BS (3M VS 3M) 3M) Mon Mkt: XC Bsis Swp 3M Daily 05JAN2018-

07-May-2019 09:14:25

Other Mature Markets back to top

Australia

The Reserve Bank of Australia kept its target policy rate unchanged at 1.50%, defying market expectations for a 25-bps rate cut. Referencing the policy rate decision, which has held steady since September 2016, Governor Lowe noted that policy makers will pay close attention to developments in the jobs market, which needs to improve further to meet the central bank's inflation target. That said, the RBA's growth forecast remains intact. The Australia's dollar gained by as much as 0.8%, the most in 3 weeks following the policy decision before settling at AUD 0.7024/dollar (+0.5%). Government bond yields also rose; the 2-year note rose 9 bps to 1.36% and the 10-year note rose 5 bps to 1.78% as the yield curve flattened.

Japan

Japanese equities fell as investors digested implications of renewed US-China trade tensions following a 10-day Golden Week holiday. The Topix slid 1.1% and the Nikkei fell 1.5% with shares of electronics and machinery makers suffering the most. **The yen strengthened by 0.1%,** extending its gains for the past three sessions to ¥110.64/dollar, reaching its strongest level since March month end. Meanwhile, yields on longer-dated JGBs fell 1 to 1.5 bps, with the 10-year note down 1 bp to -0.06% and the 30-year note 1.5 bps lower at 0.54%.

Emerging Markets

back to top

Asian currencies and equities pared initial losses following news that the Chinese trade delegation will press ahead with its trip to Washington DC later this week. News that the US administration plans to raise tariffs on Chinese exports starting this Friday had cast the future of US-China trade negotiation in doubt. **China's announcement that the trade negotiation would continue this week – Vice Premier Liu He has been confirmed to visit Washington DC on May 9th and 10th - allayed some of the trade-related fears, though the negotiation outcome remains highly uncertain. Currencies were mostly little changed**. The Thai baht outperformed (+0.4%) in the currency space while equities were mixed. **Chinese bourses staged a modest rebound following yesterday's sharp losses** (Shanghai: +0.7%), but the Korean Kospi fell further (-0.9%), underperforming others. Contacts noted that market sentiment remains fragile amid the re-escalation in trade tension. Investors will await the next round of developments in the negotiations for trading direction. **EMEA** equity markets were mixed with Turkey (-2.0%) being the main mover on more negative political news (see below). Similarly in FX, the lira depreciated 1.3% on the day while most other currencies were little changed. Among **Latin American** equities, Brazil (-1%) saw the biggest losses, followed by Mexico (-0.4%), while Argentine equities gained by +2% for the fourth session and has strengthened nearly 14% this month. Among regional currencies, Brazilian real (-0.8%) weakened the most, followed by Argentine (-0.5%), Colombian (-0.5%) and Mexican (-0.3%) peso.

Key Emerging Market Financial Indicators

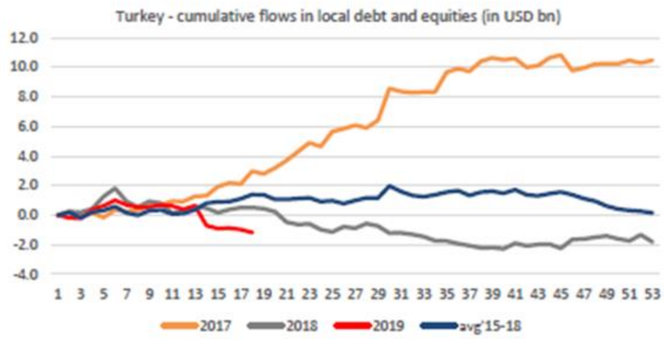
Last updated:	Level		Change				
5/7/19 8:13 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks				%			%
MSCI EM Equities		43.31	-2.5	-2	-2	-6	11
MSCI Frontier Equities		28.68	-0.2	2	0	-12	10
EMBIG Sovereign Spread (in bps)		347	2	2	7	15	-67
EM FX vs. USD		62.02	-0.1	-1	-2	-8	0
Major EM FX vs. USD				%, (+) = EM currency appreciation			
China Renminbi		6.77	0.0	-1	-1	-6	2
Indonesian Rupiah		14280	0.1	0	-1	-2	1
Indian Rupee		69.43	0.0	0	0	-3	0
Argentine Peso		44.67	-0.5	-1	-2	-51	-16
Brazil Real		3.97	0.0	-1	-3	-11	-2
Mexican Peso		19.02	-0.1	0	0	2	3
Russian Ruble		65.08	0.2	-1	0	-3	7
South African Rand		14.41	0.4	-1	-2	-13	0
Turkish Lira		6.15	-1.1	-3	-7	-31	-14
EM FX volatility		8.43	0.0	0.4	0.2	-0.3	-1.3

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

Turkey

Assets sold off on news that the Electoral High Commission authorized a re-run of the Istanbul elections, which the ruling AKP had narrowly lost. New elections will take place on June 23. Contacts said that the decision brings yet more political and economic uncertainty for Turkey by suggesting further institutional weakness and government interventionism. **The lira has depreciated more than 3% over the last two sessions** and is back above the TRY6.0 against the dollar for the first time since last October. Analysts at DB also note that outflows from domestic assets have continued, especially local bonds. Year to date, there has been some $1.2 bn of net outflows (-$2.05 bn from bonds and +$0.9 bn into equities), considerably more outflows than the average for the last few years (chart). Others have pointed out the negative impact of the weaker currency on local banks, which have some 40% ($460 bn) of loans denominated in foreign currencies, according to Bloomberg figures.

Figure 2:...dynamics are now significantly worse than in previous years...



Source : Deutsche Bank, CBT, Haver Analytics

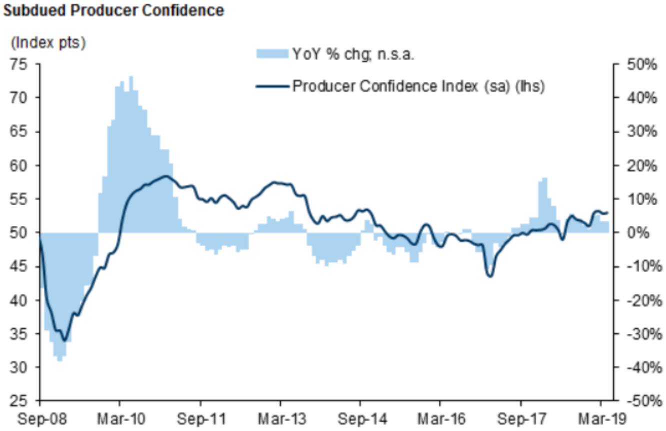
Malaysia

Bank Negara Malaysia (BNM) lowered its benchmark interest rate by 25 bps to 3%, its first cut since July 2016. In its policy statement, BNM noted "downside risks" to growth: GDP expansion is projected to be 4.3 to 4.8% this year, lower than earlier estimates of 4.9% as weaker global demand and rising trade tensions could weigh on the economy. That said, analysts noted that the rate cut is seen as insurance against dramatic headwinds to growth and is likely to be a one-off move for now. The Malaysian ringgit is little changed in reaction to the rate cut (-0.04%) while bond yields edged lower. The 3-year note fell 6 bps to 3.34% and the 10-year fell 2 bps to 3.76%.

Mexico

Mexico announced additional measures to help fund state oil company Pemex, including cuts to public servants' benefits. According to analyst reports, the amount of savings will not be substantial given Pemex's funding needs of $10-$15 bn annually. In other news, **Mexico's consumer confidence recorded a 1.9% mom sa decline in April, adding to the 3.1% mom sa decline in March**. Despite the March-April declines, consumer confidence has strengthened by 25.9% since the election of President Obrador in July 2018. Business sentiment has been noticeably more subdued as producers remain apprehensive with regards to policy direction under the AMLO administration. TIIE swap rates were up a few bps, in line with a weaker peso (-0.4%) against dollar. The TIIE curve prices in ~12 bps of easing in 6 months and about 45 bps of easing in 12 months.

Subdued Producer Confidence



Source: Haver Analytics, INEGI

Source: Goldman Sachs

List of GMM Contributors (Global Markets Analysis Division, MCM Department)

Anna Ilyina
Division Chief
Peter Breuer
Deputy Division Chief
Will Kerry
Deputy Division Chief
Evan Papageorgiou
Deputy Division Chief
Sergei Antoshin
Senior Economist
John Caparusso
Senior Financial Sector Expert
Sally Chen
Senior Economist
Fabio Cortés
Senior Economist
Mohamed Jaber
Senior Financial Sector Expert
David Jones
Senior Financial Sector Expert
Sanjay Hazarika
Senior Financial Sector Expert
Juan Solé
Senior Economist
Jeffrey Williams
Senior Financial Sector Expert
Akihiko Yokoyama
Senior Financial Sector Expert
Dimitris Drakopoulos
Financial Sector Expert
Tryggvi Gudmundsson
Economist
Henry Hoyle
Financial Sector Expert
Robin Koepke
Economist
Thomas Piontek
Financial Sector Expert
Rohit Goel
Financial Sector Expert
Jochen Schmittmann
Economist
Ilan Solot
Financial Sector Expert
Martin Edmonds
Senior Data Mgt Officer
Yingyuan Chen
Senior Research Officer
Piyusha Khot
Research Assistant
Xingmi Zheng
Research Assistant

Global Financial Indicators

Last updated: 5/7/19 8:10 AM	Level Last 12m	Latest	Change 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		2932	-0.4	0	1	10	17
Europe		3432	-0.9	-2	0	-4	14
Japan		21924	-1.5	-1	3	-2	10
China		2926	0.7	-6	-10	-7	17
Asia Ex Japan		71	-2.3	-1	-3	-5	12
Emerging Markets		43	-2.5	-2	-2	-6	11
Interest Rates					basis points		
US 10y Yield		2.47	-5.6	-3	-3	-48	-22
Germany 10y Yield		-0.03	-3.8	-5	-4	-56	-27
Japan 10y Yield		-0.05	-1.2	-1	-2	-10	-6
UK 10y Yield		1.17	-4.8	-1	6	-23	-11
Credit Spreads					basis points		
US Investment Grade		114	2.2	3	-3	12	-33
US High Yield		401	1.1	3	-6	60	-120
Europe IG		60	2.2	3	-1	4	-27
Europe HY		261	9.3	12	0	-13	-92
EMBIG Sovereign Spread		347	2.0	2	7	15	-67
Exchange Rates					%		
USD/Majors		97.68	0.2	0	0	5	2
EUR/USD		1.12	-0.1	0	-1	-6	-2
USD/JPY		110.6	0.2	1	1	-1	-1
EM/USD		62.0	-0.1	-1	-2	-8	0
Commodities					%		
Brent Crude Oil ($/barrel)		70	-1.3	-3	0	-8	31
Industrials Metals (index)		115	-1.1	-3	-5	-15	5
Agriculture (index)		38	0.0	-2	-6	-22	-9
Implied Volatility					%		
VIX Index (%, change in pp)		16.7	1.3	3.6	3.9	2.0	-8.7
10y Treasury Volatility Index		4.0	0.4	-0.1	0.4	0.3	-0.6
Global FX Volatility		6.7	0.0	0.2	-0.1	-1.0	-2.3
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		338	4.0	2	-15	-23	-78
Italy		261	3.9	7	14	138	11
Portugal		113	1.4	3	-12	-1	-35
Spain		99	1.2	0	-11	25	-18

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

back to top

Emerging Market Financial Indicators

Last updated: 5/7/2019 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		6.77	0.0	-0.5	-1	-6	2		3.4	-3.1	-1	14	-23	17
Indonesia		14280	0.1	-0.1	-1	-2	1		8.1	7.8	20	36	95	-9
India		69	0.0	0.2	0	-3	0		7.5	-0.1	-2	7	-36	7
Philippines		52	0.1	0.1	1	0	1		5.2	-1.9	-5	-13	-20	-113
Thailand		32	0.4	0.1	0	0	2		2.6	0.0	1	4	16	-2
Malaysia		4.15	0.0	-0.3	-1	-5	0		3.8	-1.5	1	6	-34	-25
Argentina		45	-0.5	-0.7	-2	-51	-16		26.8	20.5	27	315	720	382
Brazil		3.97	0.0	-1.2	-3	-11	-2		8.2	-1.1	-6	4	-20	0
Chile		678	-0.1	0.2	-2	-7	2		4.1	1.2	2	-3	-57	-34
Colombia		3254	-0.4	-0.2	-4	-13	0		6.4	1.8	2	17	21	-15
Mexico		19.02	-0.1	-0.4	0	2	3		8.2	2.4	0	14	63	-50
Peru		3.3	-0.3	0.1	-1	-1	2		5.3	1.7	2	4	1	-38
Uruguay		35	-0.5	-0.8	-4	-16	-8		11.0	4.6	14	49		24
Hungary		290	-0.3	-0.4	-2	-9	-3		2.2	0.1	9	24	53	-5
Poland		3.83	-0.2	-0.3	-1	-7	-2		2.4	-1.2	8	10	-9	16
Romania		4.3	-0.2	-0.3	-1	-8	-5		4.2	0.0	-2	3	7	-1
Russia		65.1	0.2	-0.7	0	-3	7		7.9	2.3	0	-10	82	-47
South Africa		14.4	0.4	-0.8	-2	-13	0		9.4	2.6	6	14	50	-17
Turkey		6.15	-1.1	-2.9	-7	-31	-14		20.8	0.6	-1	226	688	395
US (DXY; 5y UST)		97.6	0.1	0.2	0	5	2		2.26	0.0	-2	-4	-52	-25

	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		2926	0.7	-6	-10	-7	17		174	1	0	-1	-9	-20
Indonesia		6297	0.7	-2	-3	7	2		184	-1	3	-7	-18	-52
India		38277	-0.8	-2	-2	9	6		150	0	0	-9	8	-46
Philippines		7911	0.6	0	0	5	6		80	-2	2	-9	-30	-41
Malaysia		1639	0.4	0	0	-10	-3		122	0	-2	-5	-8	-40
Argentina		32989	1.8	10	1	20	9		921	6	-31	137	450	106
Brazil		95009	-1.0	-1	-2	15	8		245	0	-1	-1	-11	-28
Chile		5124	-0.2	-1	-2	-9	0		123	-1	-3	-6	-11	-43
Colombia		1549	-0.4	-3	-3	0	17		178	-1	3	-3	-12	-50
Mexico		44117	-0.4	-2	-2	-5	6		302	1	8	4	31	-52
Peru		20747	-0.3	-1	-3	-2	7		129	0	2	7	-28	-39
Hungary		41223	-0.8	-3	-1	10	5		100	1	-4	-6	-28	-48
Poland		58690	-0.7	-4	-3	0	2		44	2	-3	-5	-34	-41
Romania		8404	0.3	0	2	-5	14		182	1	-12	-21	24	-39
Russia		2570	-0.4	0	1	12	8		208	2	10	-8	-16	-44
South Africa		58294	-0.7	-1	1	1	11		307	-2	-1	13	35	-58
Turkey		91849	-1.3	-3	-7	-9	1		506	14	1	43	148	77
Ukraine		569	0.1	2	1	20	2		636	8	-5	42	119	-151
EM total		43	-2.5	-2	-2	-6	11		347	2	2	7	15	-67

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