Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Thursday, November 1, 2018

- **Sterling and UK bank stocks jump on reports of Brexit financial services deal (link)**
- **Fed proposes an easing in rules for smaller banks (link)**
- **US administration says additional tariffs on Chinese goods not 'set in stone' (link)**
- **Fitch affirms Mexico's BBB+ rating, but changes outlook to negative, citing increasing policy uncertainty (link)**

US | Europe | Emerging Markets | Market Tables

November kicks off with stronger risk appetite

Global risk markets generally traded with a stronger tone, supported by signs of progress on Brexit discussions, prospects of additional China stimulus, and upside surprises in US earnings reports. Global equities gained around 1-2% (though the Nikkei bucked the trend, down 1.1%). Implied equity volatility edged lower, with the VIX at 20.4, though the term structure is still inverted. In the UK, the pound and bank stocks gained on reports of a tentative agreement that would give UK financial services companies continued access to European markets after Brexit, though the agreement has not been confirmed and was dismissed as "misleading" by the EU's chief negotiator. The pound and gilt yields also extended gains following a slightly 'hawkish hold' by the Bank of England. The US dollar was broadly but modestly weaker against most currencies after reaching a 16-month high. Notably, the yuan strengthened by 0.4% to 6.9492 against the dollar, posting its largest gain in three weeks on expectations of further stimulus. US Treasury yields rose marginally across the curve, with the 10-year up 2 bps to 3.16%. Other major sovereign bond yields were mixed.

Key Global Financial Indicators

Last updated: 11/1/18 8:40 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		2712	1.1	2	-7	5	1
Eurostoxx 50		3209	0.3	1	-6	-13	-8
Nikkei 225		21688	-1.1	2	-11	-3	-5
MSCI EM		39	2.0	2	-9	-16	-17
Yields and Spreads			bps				
US 10y Yield		3.16	2.1	4	8	79	75
Germany 10y Yield		0.41	2.1	1	-7	3	-2
EMBIG Sovereign Spread		366	1.0	4	30	83	81
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		61.9	0.6	0	-1	-10	-11
Dollar index, (+) = $ appreciation		96.4	-0.8	0	1	5	5
Brent Crude Oil ($/barrel)		74.6	-0.6	-3	-12	23	12
VIX Index (%, change in pp)		20.6	-0.6	-4	9	10	10

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

United States

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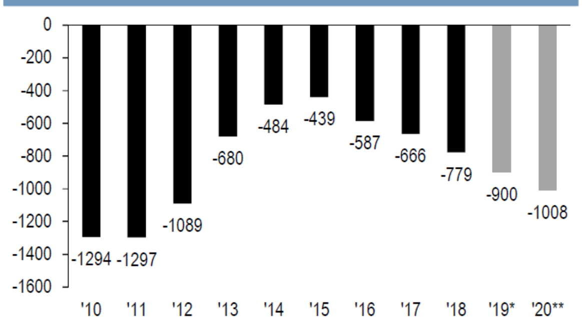
Stocks advanced Wednesday, paced by the tech-heavy Nasdaq (+2.0%). After recent losses, tech stocks surged (2.4%), while defensive sectors, such as consumer staples (-0.9%) and utilities (-1.2%) underperformed. Markets got a lift from earlier gains in Asia and Europe, and from better-than-expected earnings reports from Facebook (+3.8%) and General Motors (+9.1%). Risk-on behavior was also evident in the treasury market, where the 2-year yield rose 2 bps to 2.87% and the 10-year +2 bps to 3.14%. Strong data provided additional support. The ADP report showed private payroll gains of 227k in October. Employment costs rose 0.8% in Q3, and are up 2.8% yoy, matching the prior quarter as the biggest gain since 2008. Citi's economic surprise index extended its recent gains, with the index now above zero, reflecting stronger-than-expected data releases.

With stimulus spending pushing budget deficits wider and the Fed reducing the pace of reinvestments, **Treasury issuance is poised to continue to increase** going forward. For the fourth quarter, the Treasury intends to increase by $1 bn its 2-, 3- and 5-year note auctions for the next two months. There will also be $1 bn increases for 7-, 10- and 30-year maturities from November through January. The November 2-year floating-rate note auction will also be increased by $1 bn.

Annual budget balance by fiscal year*; $bn



*JPM forecast
Source: CBO, US Treasury, J.P. Morgan

The regulatory burden is set to ease on mid-sized banks. The Fed released a Notice of Proposed Rulemaking aimed at simplifying regulatory requirements for banks with assets of $100-$700 bn. Fed chair Powell advised the changes would "prescribe materially less stringent requirements on firms with less risk, while maintaining the most stringent requirements for firms that pose the greatest risks," and would translate into an estimated $8 bn less in overall capital for the sector.

Category	Revised Framework
$100-200 bn in Total Assets	No longer subject to standardized liquidity requirments. Two-year cycle for stress tests
>$250 bn in Total Assets	Subject to standards tailored to the risk profile of these firms. Those that aren't systemically important would see their liquidity requirment fall - to as little as 70% of current levels
Global giants	Threshold for identifying such banks raised considerably - from $250 bn in assets or $10 bn in foreign exposure to $700 bn and $75 bn. Subject to more stringent prudential standards appropriate to very large or internationally active banking organizations
GSIBs	Remain subject to the most stringent standards
Foreign Banks	Not included in the proposals, but regulators intend to follow up "in the newar future" with a new system for them

Sources: Bloomberg, Federal Reserve

WTI crude oil prices extended recent losses after registering a 9% decline last month on continued supply concerns and a stronger US dollar. US crude inventories rose for a sixth straight week, according to government data released yesterday. Domestic crude is relatively cheap, with the WTI benchmark trading $10 barrel lower than Brent.

Europe

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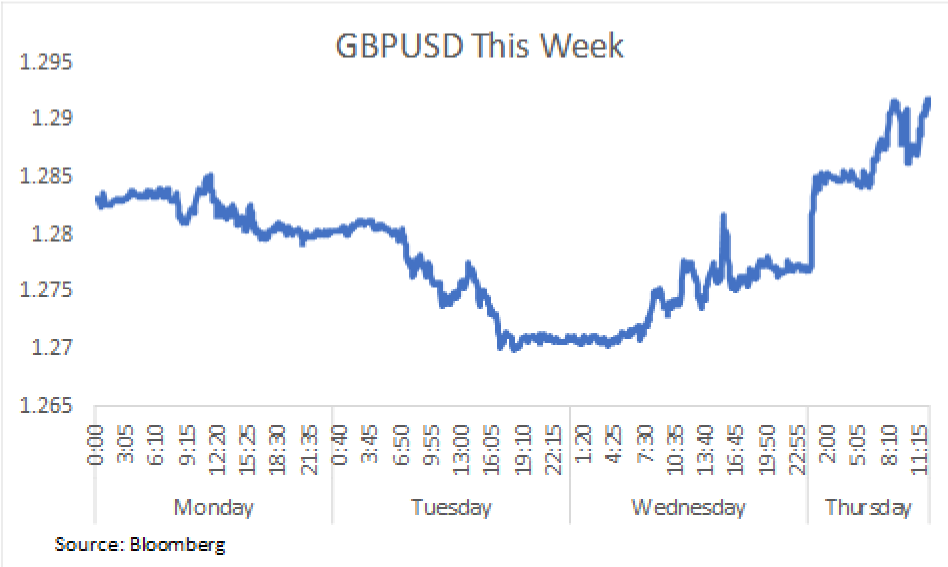
Equities rose this morning, adding slightly to yesterday's rally. The Euro Stoxx 600 was up 0.8% as the vast majority of sectors continued to bounce back. Banks outperformed, rising 1.4% as Danske Bank (+4.6%) had a rare positive day. The bank, facing compliance and AML issues, saw its largest gain since February 2016 after releasing better-than-expected Q3 earnings. ING (+6%) also soared on solid earnings while Credit Suisse (-1.9%) underperformed after a disappointing Q3 earnings report. **Sovereign yields were mixed again**. France and Germany saw yields rise 2-3 bps while Italian 10-year yields declined by 7 bps. The BTP spread to Bunds dipped below 300 again this morning after reaching a high of 327 last month.

Sterling and UK bank stocks jumped on news of progress in Brexit negotiations. Media reports that a prelimnary deal on financial services has been reached between the EU and the UK boosted sentiment in UK assets. According to the reports, negotiators have agreed to a deal which would see firms in the UK recognized by the EU as equivalent with disagreements going through some form of arbitration. The agreement has not been confirmed and has been dismissed as "misleading" by EU chief negotiator Barnier, but saw sterling gain 1.1% against the dollar this morning before retreating slightly on subsequently weak PMI data. The gains added to a 0.5% strengthening yesterday after Brexit secretary Raab suggested that a deal may be reached before November 21 although later reports cast doubts over the significance of the date. UK bank stocks outperformed the FTSE 100 and Euro Stoxx index, led by Barclays (+2.7%), Lloyds (+2.3%), and RBS (1.9%). Such bouts of optimism have previously been dashed, so market participants nonetheless remain cautious.

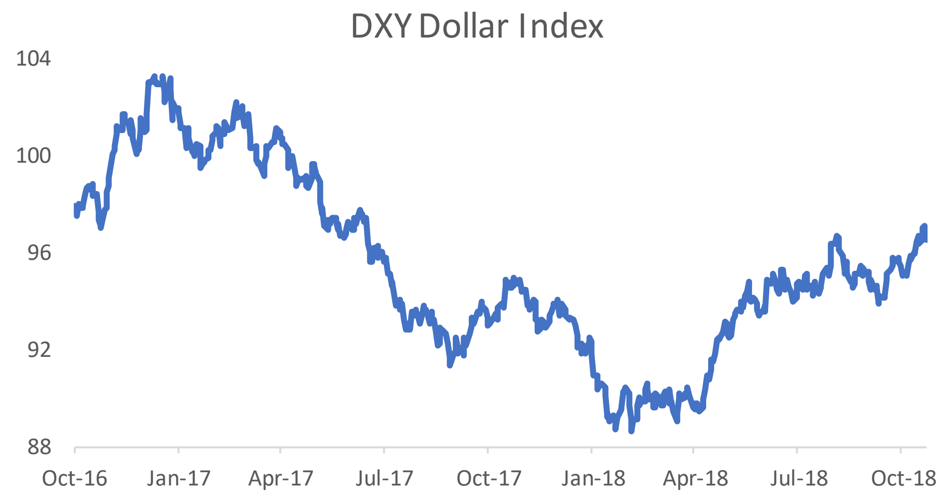
Sterling and gilt yields rose further after a slightly hawkish hold by the Bank of England. The decision to keep rates was unanimous among the MPC, members but it was accompanied by new forecasts suggesting the output gap has closed and that inflation will stay above 2%. Analysts took the announcement as firmer evidence that rates may rise at a faster pace than previously excepted if a disorderly Brexit is avoided. Brexit remains the main monetary policy challenge according to the statement, while global economic growth was described as uneven and downside risks were viewed as higher. 10-year Gilt yields were up 3 bps on the day following the announcement while sterling was up 0.4% against the euro and 1.2% against the dollar.



EU ambassadors yesterday approved the EC's NPL proposals. The proposals have slightly different parameters than the initial draft, requiring a 100% coverage level after three years for unsecured exposures and seven to nine years for secured exposures. The proposals have also been changed so that they cover only new exposures and not the outstanding stock. The EBA also published its final guidelines on management of non-performing exposures, including an NPE threshold of 5%, above which banks are required to develop a strategy to increase asset quality. Separately, ECB supervisory board chair Nouy said that risks had declined enough in the banking sector for a European deposit insurance scheme to be viable. She also claimed that greater consolidation in the sector could help banks deal with low profitability and that the creation of "European champions" via cross-border mergers could help banks compete on the global stage.

Major Currency Markets

The US dollar retreated 0.6% after registering solid gains in October that drove the trade-weighted index to its its highest level since June last year. Sterling gained 1.1% on positive Brexit news (see above) while the euro (+0.6%) also firmed. The Swedish krona was among the strongest performers, gaining 1.2% against the dollar and 0.6% against the euro after the release of strong manufacturing data for October. The yen was flat at just under ¥113 with little movement following yesterday's uneventful BoJ meeting.



Source: Bloomberg

Emerging Markets

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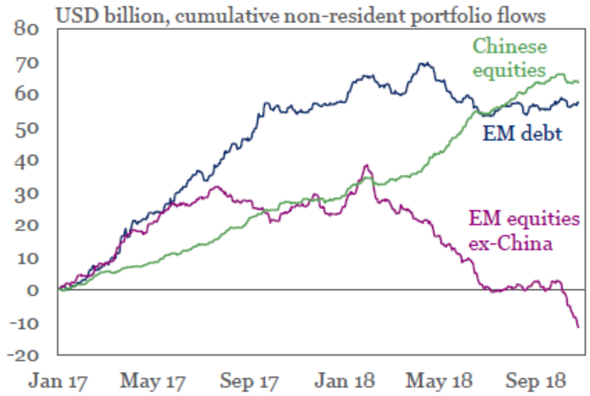
Key Emerging Market Financial Indicators

Last updated:	Level		Change				
11/1/18 8:14 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		39.16	2.0	2	-9	-16	-17
MSCI Frontier Equities		27.07	0.6	2	-5	-15	-18
EMBIG Sovereign Spread (in bps)		366	1.0	4	30	83	81
EM FX vs. USD		61.84	0.5	0	-1	-10	-11
Major EM FX vs. USD					%, (+) = EM currency appreciation		
China Renminbi		6.95	0.4	0	-1	-5	-6
Indonesian Rupiah		15128	0.5	0	-1	-10	-10
Indian Rupee		73.45	0.7	0	-1	-12	-13
Argentine Peso		35.91	2.3	3	10	-51	-48
Brazil Real		3.72	-0.7	0	8	-12	-11
Mexican Peso		20.17	0.8	-3	-7	-5	-3
Russian Ruble		65.65	0.3	0	-1	-11	-12
South African Rand		14.55	1.6	0	-2	-3	-15
Turkish Lira		5.55	0.6	2	7	-31	-32
EM FX volatility		10.25	0.0	0.3	0.2	2.2	2.4

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

Stocks traded mixed this morning across various regions. In **Asia**, equities in the Philippines (+1.8%) were the only gainers, while Vietnam (-0.7%), South Korea (-0.3%), and India (-0.1%) saw losses. In **EMEA**, most bourses advanced by about 0.7-2.0%. **Currencies in emerging Asia and EMEA strengthened versus the US dollar by roughly 1% in most countries**. The South African Rand, widely considered an EM proxy currency, was the main outperformer, gaining 1.8% on a broader improvement in risk appetite. **Latin American** markets closed mixed yesterday. The Mexbol gained 1%, recovering the prior session's loss, but the peso depreciated a further 1.3% after Fitch Ratings downwardly revised Mexico's sovereign debt outlook. The Ibovespa rose 0.6% and the real weakened by 0.6% against the dollar after the Brazilian central bank left the policy rate unchanged at 6.5%. The post meeting statement was little changed, but the committee now sees an improved balance of risks for inflation compared to the previous meeting. Argentina's peso strengthened by 2.3%. The central bank implements its new intervention zone today, at 35 – 45 (versus previously 34-44).

IIF data show that non-resident portfolio equity inflows to China (which have been supported by MSCI index inclusion) have re-trenched in recent weeks, though equity flows to EM ex-China have been far weaker.



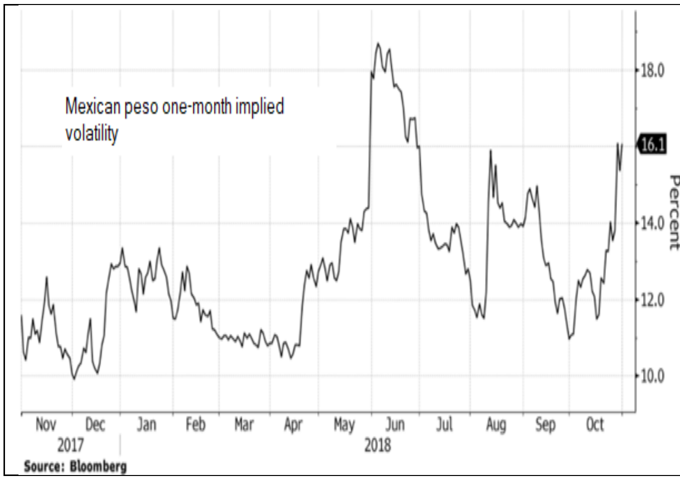
**IN, ID, KO, TH, PH, ZA, BR, HU, CN, TW, VN. Partial data through October 25, 2018Source: IIF, National sources*

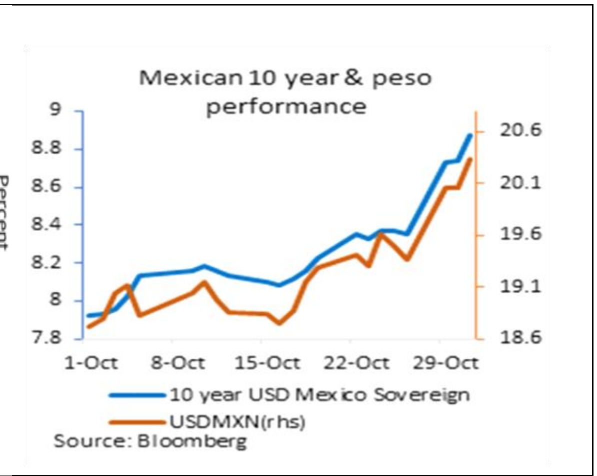
China

The yuan strengthened by 0.3% to 6.9496 per dollar, after touching an intra-day low of 6.9699. The gains come following a 1.4% weakening for the month as a whole in October, marking the currency's seventh straight monthly decline and its longest losing streak on record. The People's Bank of China on Wednesday said it will issue central bank bills in Hong Kong for the first time, which would allow it to absorb excess yuan liquidity in the offshore market and guide market expectations. The Shanghai and Shenzhen A-share Indices climbed 0.1% and 0.9% respectively, while Hong Kong's Hang Seng Index rose 1.8%. Sentiment was boosted by signals of additional policy support by the authorities. Separately, **US economic advisor Larry Kudlow indicated that more US tariffs on Chinese goods are not 'set in stone'.** He said that president Trump has not made any decision on escalating tariffs on Chinese goods, and may even withdraw some duties if there are promising policy discussions with the Chinese president. Trump and Xi are meeting at the end of November.

Mexico

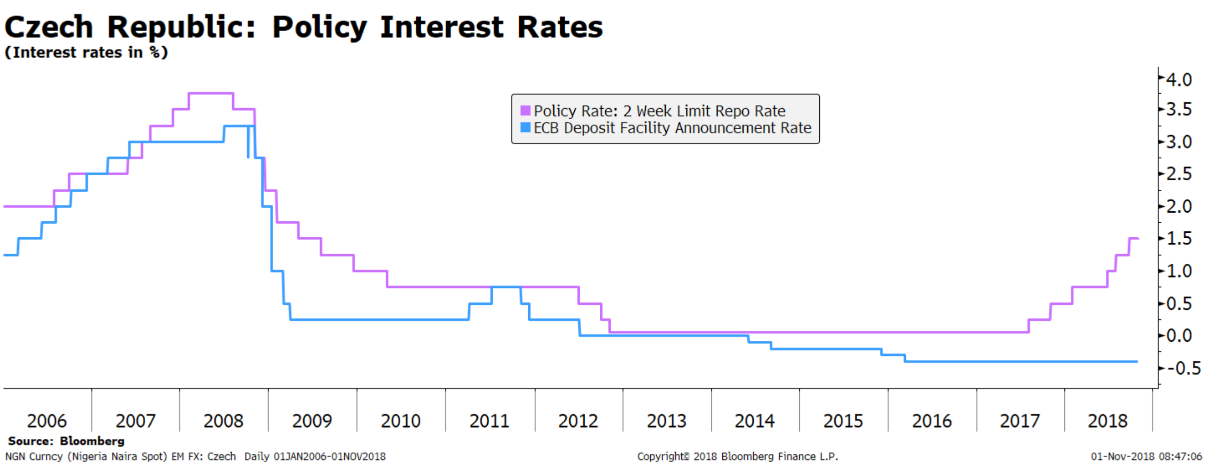
Fitch Ratings revised its outlook for Mexico's sovereign debt from stable to negative, but kept the country's credit rating at BBB+. Fitch attributed its decision to the increased risk of policy uncertainty under the incoming administration, highlighting the decision to cancel the current Mexico City airport project. This is the first major rating agency reaction to the airport cancellation. S&P and Moody's both maintain stable outlooks at BBB+ and A-, respectively. The AMLO government has given mixed messages on how it will deal with airport creditors, which has contributed to market anxiety. Earlier in the week, the peso underwent its largest 3-day depreciation in almost 2 years and bond yields rose sharply. Analysts expect risk premium in local assets to continue to increase, given concerns about a higher probability of a policy mistake.





Czech Republic

The Czech central bank is expected to raise rates to 1.75% from 1.50% later today. The rate hike would be the fourth consecutive tightening in an effort to counter a weakening koruna and tame inflation. It would also lead to a further divergence of the monetary policy stances in the eurozone and the Czech Republic.



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Global Financial Indicators

Last updated: 11/1/18 8:41 AM	Level Last 12m	Latest	Change 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		2712	1.1	2	-7	5	1
Europe		3209	0.3	1	-6	-13	-8
Japan		21688	-1.1	2	-11	-3	-5
China		2606	0.1	0	-8	-23	-21
Asia Ex Japan		63	1.3	2	-11	-17	-17
Emerging Markets		39	2.0	2	-9	-16	-17
Interest Rates					basis points		
US 10y Yield		3.16	2.1	4	8	79	75
Germany 10y Yield		0.41	2.1	1	-7	3	-2
Japan 10y Yield		0.12	-0.4	1	-1	6	8
UK 10y Yield		1.46	2.2	2	-13	12	27
Credit Spreads					basis points		
US Investment Grade		108	-0.2	3	11	14	16
US High Yield		375	-1.1	6	51	8	0
Europe IG		73	-1.2	-2	6	23	28
Europe HY		294	-4.0	-6	20	70	61
EMBIG Sovereign Spread		366	1.0	4	30	83	81
Exchange Rates					%		
Dollar Index (DXY)		96.40	-0.8	0	1	2	5
USDEUR		1.14	0.7	0	-2	-2	-5
USDJPY		112.8	0.1	0	1	1	0
EM FX vs. USD		61.9	0.6	0	-1	-10	-11
Commodities					%		
Brent Crude Oil ($/barrel)		75	-0.6	-3	-12	23	12
Industrials Metals (index)		115	1.0	-3	-5	-15	-17
Agriculture (index)		43	0.2	-1	1	-12	-10
Implied Volatility					%		
VIX Index (%, change in pp)		20.6	-0.6	-3.6	8.6	10.4	9.6
10y Treasury Volatility Index		4.4	-0.1	0.1	0.9	0.4	0.8
Global FX Volatility		8.4	0.0	0.2	0.3	0.9	1.1
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		382	-3.4	-3	7	-108	13
Italy		295	-9.4	-15	12	152	136
Portugal		145	-3.7	-9	2	-28	-6
Spain		113	-3.1	-6	7	3	-1

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

Emerging Market Financial Indicators

Last updated:	Exchange Rates								Local Currency Bond Yields (GBI EM)						
11/1/2018	Level		Change (in %)						Level		Change (in basis points)				
8:42 AM	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		6.94	0.5	0.1	-1	-5	-6			3.5	-0.4	-6	-14	-47	-48
Indonesia		15128	0.5	0.4	-1	-10	-10			8.6	-5.2	-7	46	156	199
India		73	0.7	-0.2	-1	-12	-13			8.0	-0.6	-5	-21	82	49
Philippines		53	0.4	1.0	2	-3	-6			6.6	2.7	3	18	180	178
Thailand		33	0.5	-0.1	-2	1	-1			2.9	-0.7	-1	7	64	61
Malaysia		4.18	0.2	-0.2	-1	1	-3			4.1	-1.5	2	6	13	23
Argentina		36	2.3	3.2	10	-51	-48			21.3	52.8	97	-254	575	524
Brazil		3.70	0.6	0.1	9	-12	-11			8.7	4.7	-18	-141	-13	-35
Chile		690	1.0	-0.4	-5	-8	-11			4.8	-3.2	-2	-1	14	2
Colombia		3220	-0.4	-1.7	-7	-6	-7			6.9	0.9	5	27	44	61
Mexico		20.20	0.7	-3.5	-7	-6	-3			8.9	14.1	47	92	157	118
Peru		3.4	-0.3	-0.9	-2	-4	-4			6.0	2.4	8	29	51	74
Uruguay		33	-0.2	0.0	1	-11	-13			10.8	3.1	15	37		225
Hungary		283	1.2	0.5	-2	-6	-9			2.7	12.8	2	11	130	147
Poland		3.80	1.1	-0.2	-3	-4	-8			2.6	4.7	5	-3	-21	-11
Romania		4.1	0.7	0.1	-2	-3	-5			4.6	-1.0	-7	22	114	73
Russia		65.7	0.2	-0.2	-1	-11	-12			8.4	-0.5	1	10	88	106
South Africa		14.6	1.4	0.3	-2	-4	-15			10.0	10.9	1	36	27	66
Turkey		5.55	0.5	1.5	7	-31	-32			19.4	42.3	-96	-62	762	747
US (DXY; 5y UST)		96	-0.7	-0.3	1	2	5			2.99	1.0	3	2	97	78

	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		2606	0.1	0	-8	-23	-21		182	1	-5	4	45	30
Indonesia		5836	0.1	1	-2	-3	-8		215	0	-1	37	50	49
India		34432	0.0	2	-6	2	1		169	0	2	6	56	59
Philippines		7140	1.8	0	-1	-15	-17		111	-2	-3	21	18	16
Malaysia		1707	-0.1	1	-5	-2	-5		132	0	5	5	24	22
Argentina		29491	0.2	5	-9	5	-2		639	-11	-32	9	273	289
Brazil		87424	0.6	5	11	18	14		255	-2	-8	-37	18	21
Chile		5104	1.8	-1	-4	-9	-8		139	0	1	19	21	20
Colombia		1392	0.0	0	-8	-3	-8		184	-1	-1	16	-3	10
Mexico		43943	0.9	-4	-12	-9	-11		306	-1	26	49	58	61
Peru		18909	1.4	1	-3	-5	-5		153	-1	-1	22	15	16
Hungary		37155	1.9	2	1	-6	-6		122	-1	-2	14	27	34
Poland		55313	1.3	0	-6	-15	-13		61	0	-2	16	14	14
Romania		8543	0.3	1	1	10	10		194	0	1	26	66	80
Russia		2341	-0.5	0	-5	12	11		219	-2	-8	11	37	41
South Africa		53036	1.2	3	-5	-11	-11		342	7	20	47	54	88
Turkey		91034	0.9	-2	-8	-19	-21		441	4	-20	8	134	152
Ukraine		565	0.1	1	5	88	79		612	9	20	59	147	157
EM total		23	1.3	2	-8	-12	-12		366	1	4	30	83	81

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