GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

MONDAY, NOVEMBER 11, 2019

- **US stocks prices hit record highs on trade optimism** (link)
- **Spanish elections do not resolve political deadlock** (link)
- **Emerging markets continue to see strong inflows for a second week running** (link)
- **Global manufacturing may be near an inflection point** (link)
- **Credit quality of smaller leveraged loan issuers deteriorates sharply** (link)
- **MSCI's planned increase in the weighting of China A-shares is announced** (link)

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

Trade uncertainty continues to drive markets

Price action in global financial markets continues to be dominated by the ebbs and flows of US-China trade negotiations. News headlines were generally positive during the earlier part of last week, with increasing signs of a potential agreement on a "phase one" trade deal that would incorporate some reversal of tariffs along with other concessions on both sides. Consensus expectations seemed to converge on a potential rollback of the September tariffs and a suspension of the upcoming December 15 tariffs contingent on achieving the phase one deal. However, investor expectations were tempered on Friday following indications by the US administration that there was no agreement yet on the full roll back of tariffs. After last week's general rally in risk assets—global equities were up by about 1%—the price action today has been less buoyant, with most developed and emerging market equities trading in negative territory, and US futures pointing to a weak start.

Key Global Financial Indicators

Last updated: 11/11/19 8:35 AM	Level: Last 12m	Level: Latest	Change from Market Close: 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		3093	0.3	1	4	11	23
Eurostoxx 50		3690	-0.3	1	3	14	23
Nikkei 225		23332	-0.3	2	7	5	17
MSCI EM		44	-0.9	1	5	10	12
Yields and Spreads					bps		
US 10y Yield		1.94	2.4	16	21	-124	-74
Germany 10y Yield		-0.26	0.0	9	18	-67	-51
EMBIG Sovereign Spread		314	1	-3	-22	-48	-100
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		60.6	-0.2	-1	0	-2	-3
Dollar index, (+) = $ appreciation		98.2	-0.2	1	0	1	2
Brent Crude Oil ($/barrel)		62.1	-0.7	0	3	-12	15
VIX Index (%, change in pp)		13.3	1.2	0	-2	-4	-12

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

Wednesday will be an important day to watch, with several risk events. The Thrift Investment Board meeting will be closely watched for any potential decision to prevent allocating funds to Chinese companies. President Trump is expected to delay a decision on the imposition of auto tariffs on the EU and Japan (Section 232 investigation). Chair Powell will deliver his Congressional testimony on the US economic outlook. Lastly, the House starts its public impeachment hearings, with a second hearing scheduled on Friday. Elsewhere, central bank meetings are scheduled in New Zealand (Wed, hold), Philippines (Thu, hold), and Mexico (Thu, 25 bps cut). Key data reports this week include: CPI (Wed) and retail sales (Fri) in the US; GDP in the UK (Mon), Japan (Wed) and Euro area (Thu); and industrial production, retail sales and fixed asset investment in China (Thu).

United States back to top

US equity indices set new records on Friday. A weak morning session, dampened by President Trump's statement that he did not yet agree to rolling back import tariffs, was followed by an afternoon rally that lifted all three main indices to record highs, also marking the 5th and 6th weekly gains for S&P 500 and NASDAQ, respectively. Conversely, trading in Treasuries was soft, with yields closing modestly higher across the curve. The positive trade headlines in the past week has driven Treasury yields sharply higher, with 2-year yield up 11 bps to 1.677% and 10-year yield up 23 bps to 1.943%. Similarly, markets have pared back policy easing expectations with Fed funds futures pricing in less than 1 rate cut by end-2020.

The slowdown in global manufacturing activities seems to have reached an inflection point. Global PMIs have stabilized in the 45-50 range, with new orders showing nascent uptick. Global trade volume has bounced off from its recent trough, with trade data from China surprising on the upside. Given that spillover from the manufacturing downturn to the broader economy proves to be limited so far, stabilization in global manufacturing sector could reduce recession risks and imply upside to global growth. While global monetary policy easing is supportive of this cautious optimism, it also relies on the de-escalation of trade war to stimulate confidence and investment.

Signs of stabilisation in global manufacturing and trade…

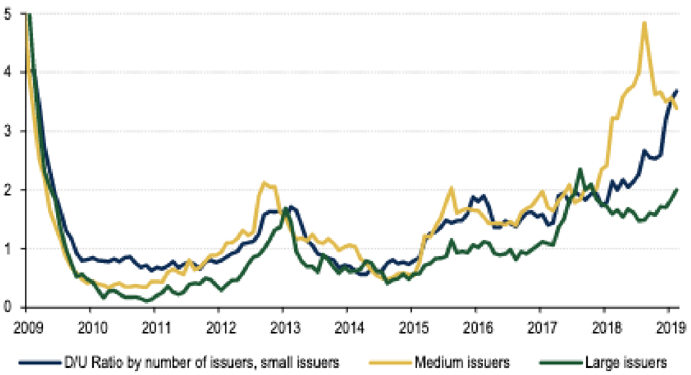
Source: CPB, IHS Markit, Haver Analytics, Barclays Research

…as the long decline in export orders may have bottomed

Source: ISM, IHS Markit, Haver Analytics, Barclays Research

Credit quality of smaller issuers in the leveraged loan market has deteriorated sharply this year. The downgrade to update ratio of this group jumped to 3.7, led by cyclical sectors such as retail, energy and materials. The downgrades concentrated in the single B rated issuers.

Chart 3: Recent downgrades have been driven by small issuers



Source: BofA Merrill Lynch Global Research, S&P LCD

Europe [back to top]

Capital Markets

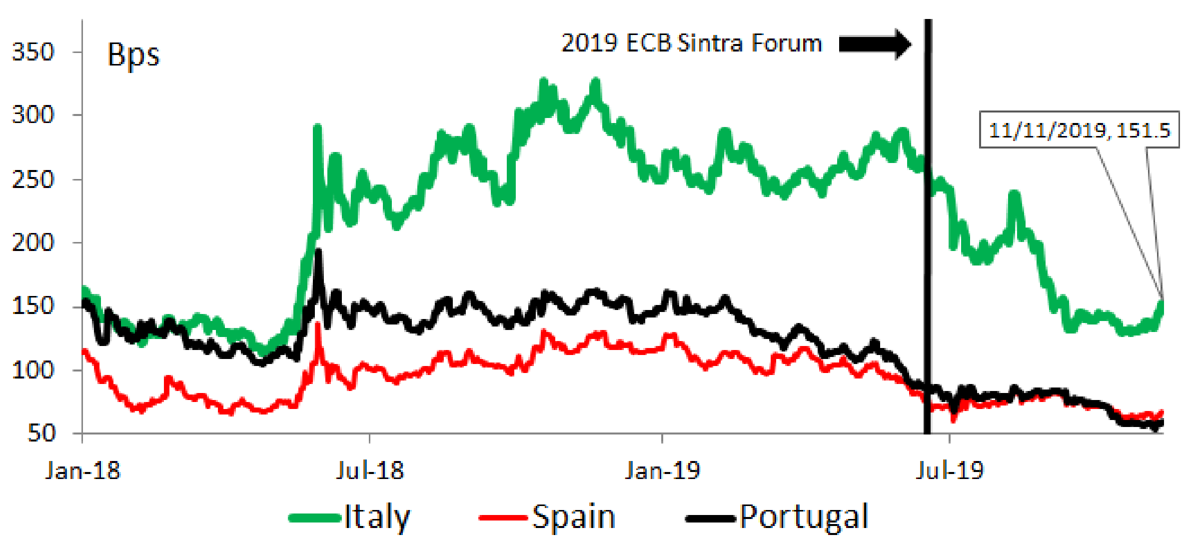
Bund yields are little changed. German 10-yr bund yields trade at -0.27%, and 10-yr OAT yields are at 0.03%. The euro is up +0.1% at 1.103. **European equities** (-0.3%) fell, with bank shares down 1%.

Euro Area

Spanish elections did not resolve political uncertainty, as expected. The Socialist party PSOE remains the biggest party at 120 seats (-3 from April) out of 350. Conservative PP rose to 88 seats (+22) while Podemos fell to 35 seats (-7). Nationalist Vox obtained 52 seats (+28). **Analysts see only two likely outcomes, either a coalition with left-wing and regional parties, or a grand coalition between PSOE and PP.**

Spanish 10-yr spreads over bunds edged 3 bps higher but more noteworthy is that Italian bonds have continued to underperform. Today, Italian 10-yr spreads rose 5 bps to 151 bps.

Euro area: 10-year spread over German bunds (bps)



Source: Bloomberg and IMF staff

The US administration will likely decide on tariffs on EU and Japanese cars by Thursday, but analysts expect no tariffs on European cars given last week's comments from policymakers.

Several ECB Governing Council (GC) members plan to propose changes to decision making at the ECB at President Lagarde's first GC meeting on Wednesday. Proposed changes reportedly include regular votes on monetary policy and ending the pre-announcement of policy plans by the ECB President.

United Kingdom

10-yr gilt yields are little changed at 78 bps but **stocks are 1% lower after Q3 GDP growth slightly disappointed at 0.3% qoq** (0.4% expected) or 1.0% yoy (1.1% expected).

Moody's left the U.K.'s rating unchanged (at Aa2) but downgraded the outlook from stable to negative on fears that political gridlock will persist post-Brexit. Fitch and S&P moved the U.K. to negative watch earlier.

Other Mature Markets back to top

Japan

The yen appreciated while equities were little changed as optimism regarding a potential U.S.-China trade deal proved short lived. President Trump dialed back expectations for a trade agreement. Meanwhile, worsening social tensions in Hong Kong SAR also boosted demand for safe-haven assets. The yen gained 0.3% against the dollar while the Topix held steady. **JGB yields fell on the day**, led by the short-end; the 2-year note fell 2 bps to -02% and the 10-year note fell 1 bp to -0.08%. Over the past 10 weeks, the yield on the benchmark 10- year note swung from -0.30%, a 3-year low, to -0.04%, its highest level in more than 5 months. Analysts noted that BOJ's reduced debt purchases helped lift yields higher. However, its decision to leave the policy rate unchanged at the end of October was accompanied by expectations that rates could still move lower, introducing some uncertainty to the direction of JGB yields. In its statement from October 31st, the BOJ pledged to keep interest rates low or lower as long as downside risks to inflation remained; it also dropped a time frame for keeping policy loose, making its easing stance more data dependent.

Emerging Markets back to top

Asian equities and currencies fell as investors await greater clarity on US-China trade negotiations after President Trump noted that the U.S. has not yet agreed to roll back tariffs. Escalating social tension in Hong Kong SAR also dented risk appetite. The won paced losses (-0.8%) on renewed trade uncertainty. The cautious tone also persisted in **EMEA**, with equities underperforming in South Africa (-1%) and generally 0.5-1% weaker. EMEA currencies also edged lower. In **Latin America**, equities closed lower on Friday. Equities in Argentina (-4.9%), Brazil (-1.8%), Peru (-1.4%), Colombia (-1.2%) and Mexico (-1.0%) fell sharply. Equities in Chile (0.4%) had a slight increase. Currency markets were similar. The Brazilian real (-1.5%) and the Chilean peso (-0.9%) saw sharp depreciations against the dollar. Government bond yields were relatively stable.

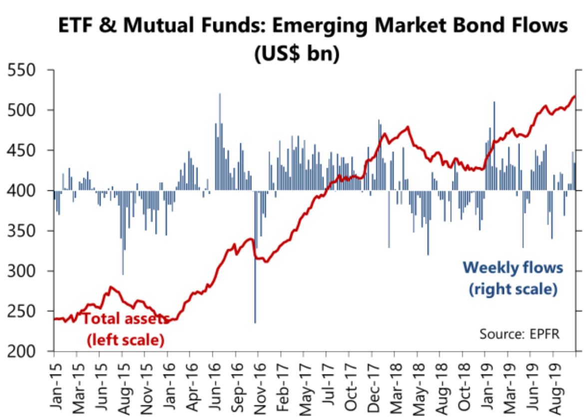
Key Emerging Market Financial Indicators

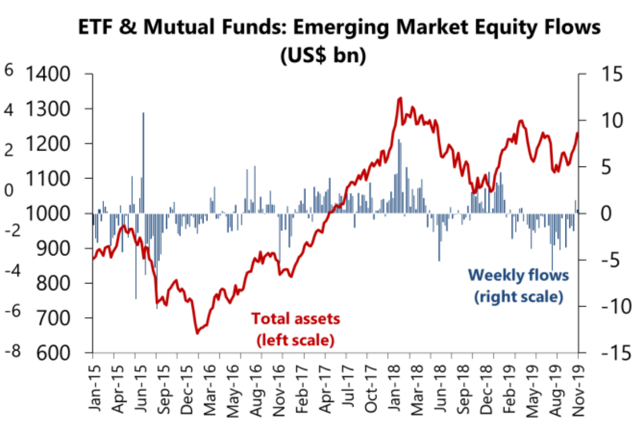
Last updated:	Level		Change				
11/11/19 8:39 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		43.68	-0.9	1	5	10	12
MSCI Frontier Equities		28.48	-0.2	-1	1	4	9
EMBIG Sovereign Spread (in bps)		314	1	-3	-22	-48	-100
EM FX vs. USD		60.56	-0.2	-1	0	-2	-3
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		7.01	-0.2	0	1	-1	-2
Indonesian Rupiah		14068	-0.4	0	0	5	2
Indian Rupee		71.47	-0.3	-1	-1	2	-2
Argentine Peso		59.60	-0.2	0	-3	-40	-37
Brazil Real		4.16	0.2	-3	-1	-9	-7
Mexican Peso		19.12	-0.1	0	1	7	3
Russian Ruble		63.90	-0.2	-1	0	6	9
South African Rand		14.88	-0.2	0	-1	-3	-4
Turkish Lira		5.77	-0.1	-1	2	-5	-8
EM FX volatility		7.24	1.3	0.0	-0.9	-2.8	-2.5

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

Flows to Emerging Markets

Emerging market funds received strong inflows last week, though the amounts were somewhat lower than the preceding week,. Bond flows (+$1.4 bn) saw the second highest value since the end of July. Equity flows (+$0.5 bn) were positive for two consecutive weeks for the first time since April, and after a long period of negative flows. After negative or small positive flows in early and mid-October, emerging markets experienced large positive flows in last two weeks.





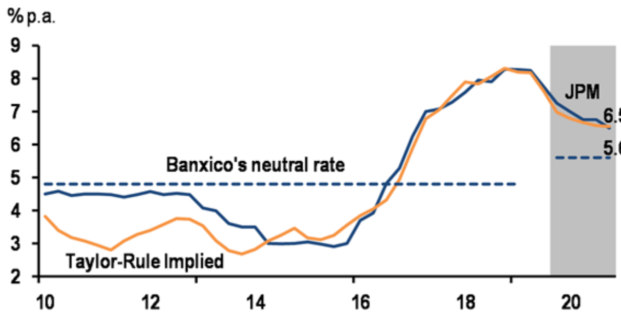
China

MSCI announced it will increase weighting of China A shares to 20%, as planned. MSCI will raise the inclusion factor of China A shares – RMB-denominated large cap shares traded on the Shanghai and Shenzhen Exchange - in some of its indexes from 15% to 20% on November 26th. MSCI indicated earlier this year that it would implement its phase in of China A shares in three stages, lifting the inclusion factor from 5% to 10% in May, to 15% in August, and to 20% in November. The RMB weakened a touch on the day following recent appreciation. The onshore CNY lost 0.2% and the offshore depreciated by 0.3%, with both hovering around the 7.00/dollar level.

Mexico

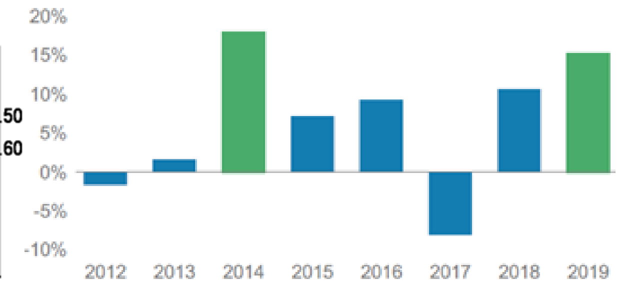
**At the Banxico`s monetary policy meeting on November 14th, markets expect a 25bps cut in the reference rate to 7.5%.** The bank can signal future cuts, given the negative output gap and well-behaved inflation. Looking ahead to 2020, the size of the effect of the Banxico`s decisions on the Mexican peso is likely to change based on the core yields. 2019 was a good year for the Mexican peso partly due to the carry trade, which generally performs well while core yields are falling globally. Morgan Stanley Research's carry strategy, which includes the Mexican peso in the its basket, had its best performance since 2014. A driver of this was falling US Treasury yields during 2019. However, the fact that it is unlikely for core rates to decrease at a similar pace in 2020 may put pressure on the Mexican peso in the near-term.

Monetary policy - Expected path and neutral rate



Source: J.P. Morgan with data from INEGI and Banxico. J.P. Morgan forecasts shaded.

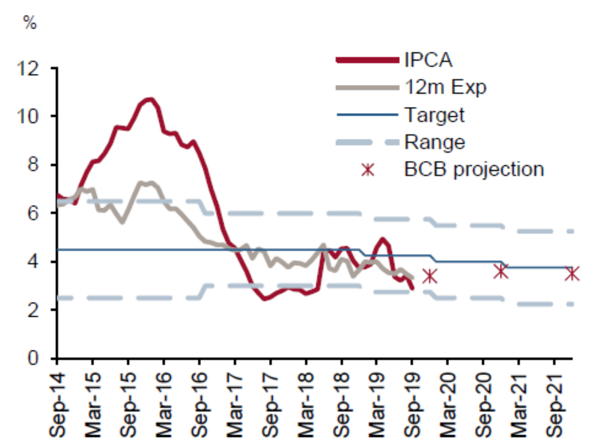
Carry Strategy: annualized excess returns (8% target vol)



Source: Morgan Stanley Research

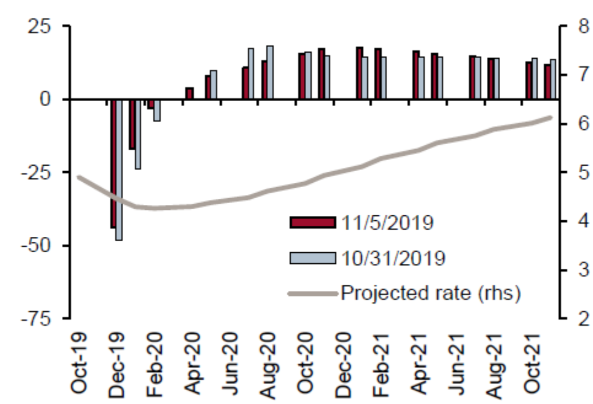
Brazil

The Central Bank of Brazil released its COPOM minutes last week, which signaled another 50bps cut on 11 December. According the meeting minutes, weak economic conditions were the main reason for the accommodative monetary policy stance, as inflation is forecast to remain below its target range for the coming years. The minutes also hinted that the central bank will be closely watching the lagged effect of monetary policy on the economic activity. The interbank deposit futures rate (DI) curve flattened following the release of the minutes. The curve now follows a path close to the policy signal, i.e. 50bps cut in December.



Source: IBGE, BCB, Credit Suisse

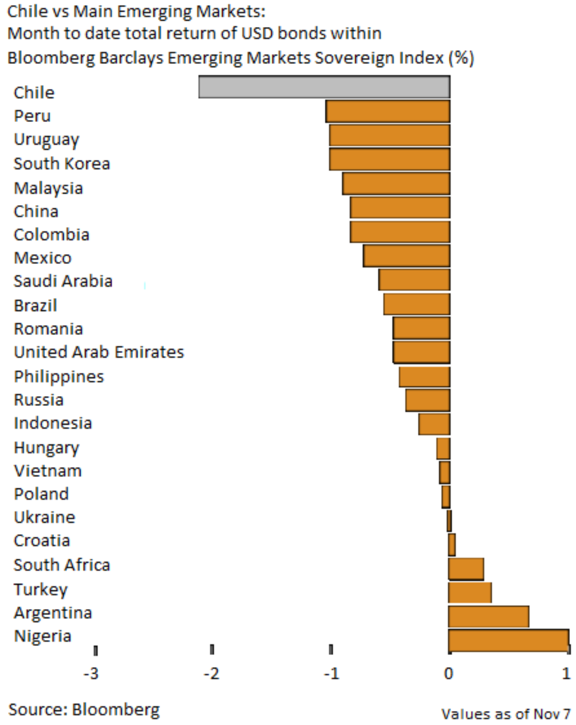
Cuts/hikes priced in bps; Projected rate in % (rhs). As of 5 Nov, 2019

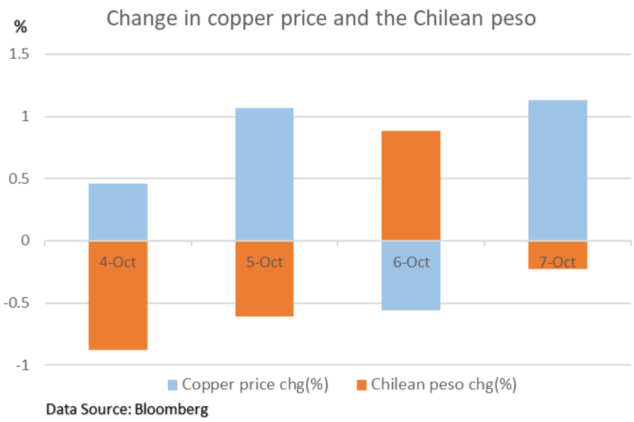


Source: Credit Suisse, the BLOOMBERG PROFESSIONAL™ service

Chile

The civil unrest in Chile has adversely affected the country's currency and dollar-denominated bonds in recent weeks. Chilean bonds have lost 3.1% in value during the first 7 days of November. The sovereign dollar notes due in 2047 and 2050 had the third and first worst returns among 74 emerging and frontier markets in the Bloomberg Barclays Emerging Markets Sovereign Index. Despite the fact that Chile exports around one third of the world's copper, the correlation between copper prices and the Chilean peso seems to have broken down last week.





EMEA

In today's data releases, monthly inflation was slightly higher than expected at 0.5% mom (+0.4% expected) in **the Czech Republic** with yoy CPI unchanged at 2.7% yoy. Analyst are now waiting for Q3 GDP on Thursday to assess the likelihood of further hikes by the Czech central bank. **Turkey** will report current account data on Tuesday and industrial production on Thursday. **South African** retail sales on Wednesday will also be followed closely ahead of the next SARB meeting on 21 Nov. In **Saudi Arabia**, the national oil company (Aramco) released its IPO prospectus on Saturday. However, investors are waiting for more information on the number of shares to be sold and the target price range, which will reportedly be released on November 17.

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Global Financial Indicators

Last updated: 11/11/19 8:36 AM	Level Last 12m	Level Latest	Change 1 Day	Change 7 Days	Change 30 Days	Change 12 M	YTD
Equities					%		%
United States		3093	0.3	1	4	11	23
Europe		3690	-0.3	1	3	14	23
Japan		23332	-0.3	2	7	5	17
China		2910	-1.8	-2	-2	12	17
Asia Ex Japan		72	-0.5	2	6	12	13
Emerging Markets		44	-0.9	1	5	10	12
Interest Rates					basis points		
US 10y Yield		1.94	2.4	16	21	-124	-74
Germany 10y Yield		-0.26	0.0	9	18	-67	-51
Japan 10y Yield		-0.06	-1.3	11	12	-19	-7
UK 10y Yield		0.78	-0.5	6	8	-71	-49
Credit Spreads					basis points		
US Investment Grade		116	0.1	-4	-16	11	-31
US High Yield		446	0.7	-15	-41	94	-75
Europe IG		49	0.3	0	-5	-23	-38
Europe HY		231	0.8	5	-9	-63	-121
EMBIG Sovereign Spread		314	1.0	-3	-22	-48	-100
Exchange Rates					%		
USD/Majors		98.16	-0.2	1	0	1	2
EUR/USD		1.10	0.2	-1	0	-2	-4
USD/JPY		108.9	0.3	0	-1	4	1
EM/USD		60.6	-0.2	-1	0	-2	-3
Commodities					%		
Brent Crude Oil ($/barrel)		62	-0.7	0	3	-12	15
Industrials Metals (index)		117	-1.0	-2	0	2	7
Agriculture (index)		39	-0.7	-1	0	-8	-5
Implied Volatility					%		
VIX Index (%, change in pp)		13.3	1.2	0.5	-2.3	-4.1	-12.1
10y Treasury Volatility Index		4.8	0.1	0.6	-0.5	1.0	0.2
Global FX Volatility		6.4	0.1	-0.1	-0.6	-1.8	-2.6
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		163	3.7	9	-25	-235	-253
Italy		149	3.3	14	11	-151	-101
Portugal		59	0.1	0	-6	-95	-89
Spain		67	1.6	1	-1	-52	-51

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

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Emerging Market Financial Indicators

Last updated:	Exchange Rates								Local Currency Bond Yields (GBI EM)						
11/11/2019	Level		Change (in %)						Level		Change (in basis points)				
8:38 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		7.01	-0.2	0.3	1	-1	-2			3.3	0.7	-2	10	-17	10
Indonesia		14068	-0.4	-0.4	0	5	2			7.0	-2.6	-7	-30	-116	-112
India		71	-0.3	-1.0	-1	2	-2			6.8	1.5	5	6	-103	-60
Philippines		51	-0.7	-0.7	1	5	3			4.3	0.3	0	-1	-238	-198
Thailand		30	0.1	-0.5	0	9	7			1.7	6.3	15	21	-116	-91
Malaysia		4.14	-0.2	0.2	1	1	0			3.4	-2.8	-2	-1	-74	-70
Argentina		60	-0.2	0.2	-3	-40	-37			62.6	5.1	571	345	3879	3955
Brazil		4.16	0.3	-3.4	-1	-9	-7			6.0	4.2	26	-30	-278	-214
Chile		755	-1.0	-2.0	-6	-9	-8			3.3	0.4	-12	54	-154	-120
Colombia		3339	-0.6	-0.4	3	-6	-3			5.9	3.5	14	24	-94	-65
Mexico		19.12	-0.1	0.3	1	6	3			7.0	3.2	11	10	-187	-175
Peru		3.4	-0.6	-0.5	1	0	0			4.5	-0.1	-1	16	-139	-128
Uruguay		37	0.0	-0.5	-1	-13	-13			10.9	0.1	3	11	32	21
Hungary		303	0.0	-2.3	-1	-5	-8			1.2	3.8	9	21	-148	-98
Poland		3.87	0.0	-1.0	1	-1	-3			1.9	1.0	14	21	-70	-36
Romania		4.3	0.1	-1.0	0	-4	-6			3.9	2.0	7	11	-45	-33
Russia		63.9	-0.1	-0.6	1	6	9			6.2	3.4	-1	-48	-230	-217
South Africa		14.9	-0.2	-0.5	-1	-3	-4			9.6	1.9	-5	20	-15	0
Turkey		5.77	-0.1	-0.6	2	-5	-8			12.1	6.5	-9	-153	-563	-474
US (DXY; 5y UST)		98	-0.2	0.7	0	1	2			1.75	0.0	15	19	-129	-77

	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		2910	-1.8	-2	-2	12	17		175	-2	-2	-14	-4	-19
Indonesia		6149	-0.5	-1	1	5	-1		168	1	-7	-11	-43	-68
India		40345	0.1	0	6	15	12		130	8	2	-5	-37	-66
Philippines		8009	-0.7	-1	2	15	7		77	2	1	2	-26	-44
Malaysia		1608	-0.1	0	3	-6	-5		119	-5	-1	-6	-12	-43
Argentina		34131	-4.8	-2	7	14	13		2438	2	158	549	1823	1623
Brazil		107165	-1.8	-1	3	25	22		223	0	1	-11	-27	-50
Chile		4652	0.4	-3	-9	-10	-9		139	-9	-3	-3	5	-27
Colombia		1636	-1.2	0	3	15	23		171	-12	-10	-17	-17	-57
Mexico		43702	-0.9	0	1	-1	5		308	-8	-7	-18	5	-46
Peru		19854	-1.4	0	3	4	3		121	-9	-9	-11	-28	-47
Hungary		43157	-0.7	1	7	12	10		89	3	-6	-3	-33	-59
Poland		59192	0.0	2	4	4	3		23	3	-5	-6	-33	-62
Romania		9707	0.2	1	2	12	31		184	3	-9	-19	1	-37
Russia		2959	-0.5	1	9	23	25		163	-10	-14	-41	-56	-89
South Africa		55991	-1.1	-2	1	5	6		324	-6	-20	-20	3	-41
Turkey		103658	0.5	4	5	12	14		427	1	-20	-64	3	-2
Ukraine		518	0.0	-1	-2	-13	-7		450	1	-7	-45	-163	-337
EM total		44	-0.9	1	5	10	12		314	1	-3	-22	-48	-100

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

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