



Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Thursday, November 15, 2018


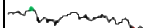
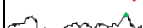


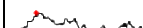


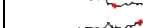


- **PM May passes Brexit deal through cabinet, but high-level resignations cast doubt about support for next steps ([link](#))**
- **US markets suffer a five-day losing streak ([link](#))**
- **China and US have resumed trade talks ahead of Trump-Xi meeting ([link](#))**
- **More signs of fading appetite for dollar bonds by Chinese issuers ([link](#))**
- **Indonesia's central bank surprises markets with another rate hike ([link](#))**

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Resignations over Brexit Weigh on European Markets

Brexit news dominate the headlines this morning, after several high-profile resignations in PM May's cabinet raised doubts that the draft agreement with the EU would be successful. Today's resignations of Brexit secretary Raab and Pensions secretary McVey also added to concerns about a potential challenge to PM May's leadership and occurred after May's cabinet approved the agreement yesterday. The pound slumped 1.7% to under \$1.28 on the resignations while Gilt yields fell 9-13 bps. UK equities are also lower, led by the banking sector (-1.9%), while European bank stocks are trading 1.2% lower. US equity futures point to a modestly higher opening, supported by news reports that China has signalled trade concessions ahead of the Trump-Xi summit in late November. The news also supported stock markets in China and other emerging markets, especially in Asia.

Key Global Financial Indicators

Last updated: 11/15/18 8:17 AM	Level		Change from Market Close				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
S&P 500		2702	-0.8	-4	-2	5	1
Eurostoxx 50		3204	-0.1	-1	0	-10	-9
Nikkei 225		21804	-0.2	-3	-2	-1	-4
MSCI EM		40	1.6	-4	0	-13	-15
Yields and Spreads			bps				
US 10y Yield		3.10	-1.5	-14	-6	78	69
Germany 10y Yield		0.37	-2.8	-9	-13	-1	-6
EMBIG Sovereign Spread		378	2	22	28	75	93
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		62.1	0.2	0	0	-8	-11
Dollar index, (+) = \$ appreciation		97.2	0.4	0	2	5	5
Brent Crude Oil (\$/barrel)		67.0	1.3	-5	-17	8	0
VIX Index (% change in pp)		21.1	-0.2	5	0	8	10

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

Commodities

The recent collapse in oil prices and a spike in natural gas has led the spread between the two commodities to narrow to its tightest level in 9 years. Oil futures are now worth just two times an equivalent unit of natural gas, compared with earlier in the year when oil was worth over four times the value of natural gas. News about colder weather coming to the northeast US sent natural gas prices soaring 18% on Wednesday, with prices up over 40% since the start of the month. Oil futures are slightly higher over the last couple of sessions but remain more than 10% lower this month and down about 25% since their October high.

United States

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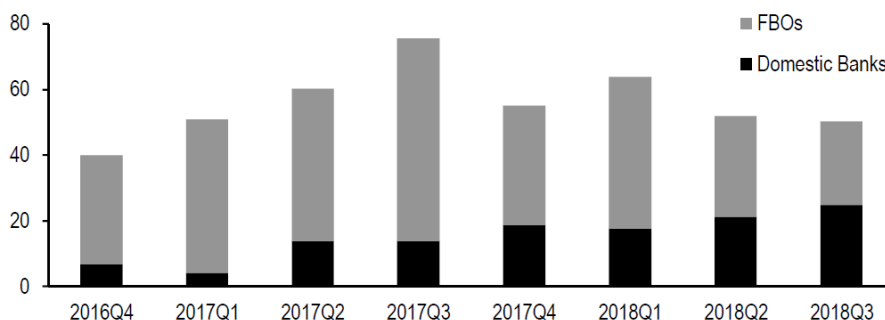
The S&P 500 was down for the fifth day in a row yesterday, having fallen by over 4% over the period. Technology stocks were among the main culprits as Apple lost ground again and earnings estimates for the sector continued to be marked lower. However, banks also had a bad day on comments by Democratic house member Waters that the easing of bank regulation would come to an end. The financial sector was already in the spotlight due to Goldman's connection with the 1MDB affair, and the Goldman stock price has fallen by over 15% during the past four days. Another Democratic member raised questions about the USMCA which will have to be approved by the new Congress next year, further weighing on sentiment. Treasury yields initially declined with equities, with the 10-year yield falling as low as 3.09% before ending little changed at 3.13%. The VIX rose back above 20.

In this morning's data, retail sales came in higher than expected at 0.8 versus the consensus forecast of a 0.5% gain. The closely followed ex-autos print was 0.7% versus the 0.5% forecast. The immediate market response was muted.

US banks have greatly increased their share of borrowing in the federal funds market relative to foreign banks. As of Q3 2018, they accounted for \$25 bn in borrowing (49% of the market), double the level of a year ago. Of these, the greatest increase in borrowing was by smaller regional banks in the \$100-250 bn balance sheet range. Foreign banking organizations (FBOs) are being slowly priced out of the market. Some analysts think the rise in federal funds borrowing by smaller regional US banks is due to liquidity-cost ratio (LCR) considerations, as federal funds financing from the Federal Home Loan Banks (FHLBs) receive better regulatory treatment than other unsecured debt markets such as the euro-dollar funding market. The FBOs and US G-SIBs have been more opportunistic in their tapping of the federal funds market, stepping in when market conditions are favorable. As smaller banks have a more structural reliance on this market they have been willing to pay up to gain access, causing a narrowing of the gap between IOER and the Fed Funds effective rate.

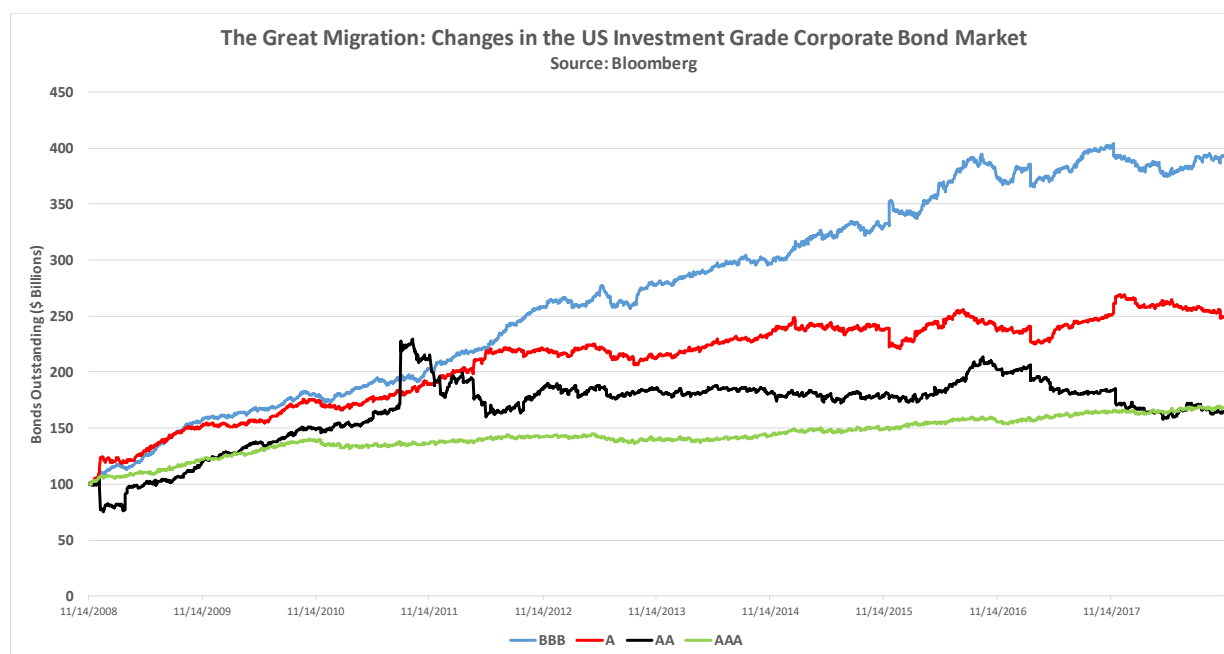
Exhibit 4: US banks are comprising a larger share of the FF market

Net Fed funds purchased (\$bn)



Source: FFIEC 002,031, 041, and 051, S&P Global Intelligence, J.P. Morgan

The lowest rated investment grade bonds (BBB) now account for roughly 50% of the US investment grade (IG) corporate bond market, raising fears among some analysts that credit downgrades could have destabilizing spillovers. The number of BBB-rated bonds outstanding has doubled since 2011. If many BBB-rated companies get downgraded to junk status, the corporate sector could face much higher funding costs or even lose access to funding altogether. This in turn could put their business models in jeopardy and lead to job layoffs and other adverse effects. Some market contacts think the recent collapse in the prices of GE bonds could be a harbinger of things to come. Others are more optimistic, pointing out that the growth of the BBB sector has levelled off since 2016 and that there are many junk-rated companies that are under review for upgrades to IG status due to their greatly improved credit quality and strong business performance. They point out that these “rising stars” could further increase the proportion of BBB-rated bonds outstanding while actually improving the overall credit profile of the BBB sector.



Credit conditions in the US high yield (HY) remained stable in Q3 2018 relative to Q2. Gross leverage, net leverage and debt/EBITDA across most of the HY universe held steady. Bond market liquidity improved although revenue and EBITDA growth slowed down. Although spending on buybacks remained high, more of these transactions were financed through internal cash generation rather than borrowing, another positive development for the sector. Gross debt levels for the sector were little changed.

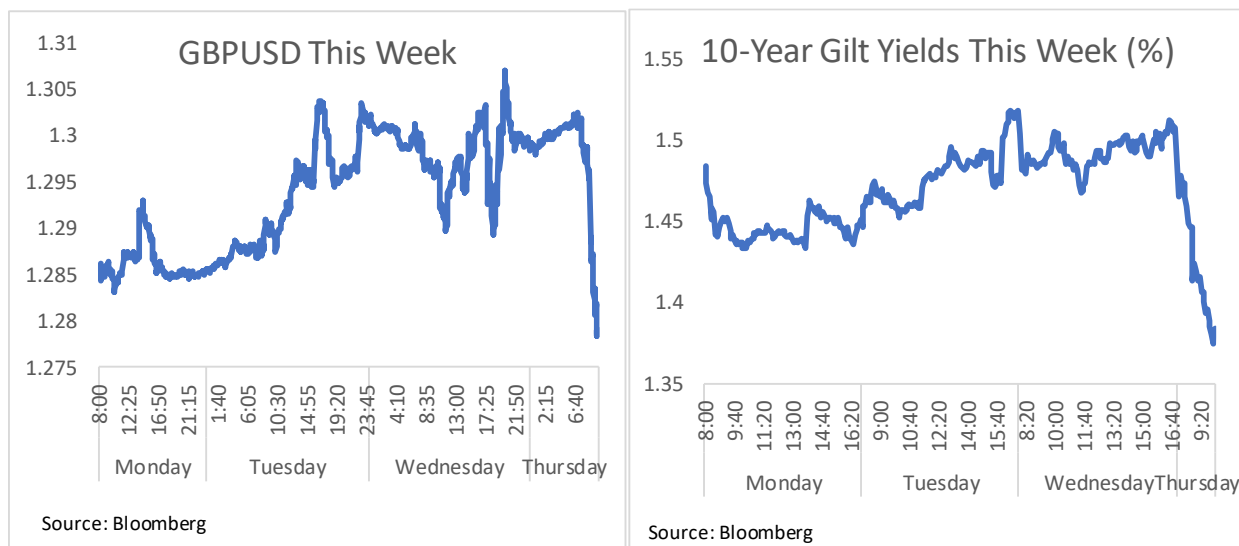
Europe

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United Kingdom

PM May's cabinet approved the Brexit deal but the pound and gilt yields sank after Brexit secretary Raab resigned from his post. In his resignation letter, Raab said he could not support the Brexit deal due to the “regulatory regime proposed for Northern Ireland” and “an indefinite backstop arrangement.” Esther McVey, the work and pensions secretary, handed in her resignation shortly after Raab while Northern Ireland minister Shailesh Vara also resigned. Earlier, European Council president Donald Tusk confirmed an EU summit on November 25 to discuss the deal. However, the unfolding political developments in the UK cast doubt on whether PM May will keep enough support within her government to reach the summit. Sterling weakened by 1.7% to under \$1.28 on the resignations while Gilt yields fell 9-13 bps. The drop in

10-year Gilt yields was the fourth largest decline since the referendum in 2016. Bank stocks were also heavily hit, falling 1.9% in aggregate with RBS plummeting by 7.3%.



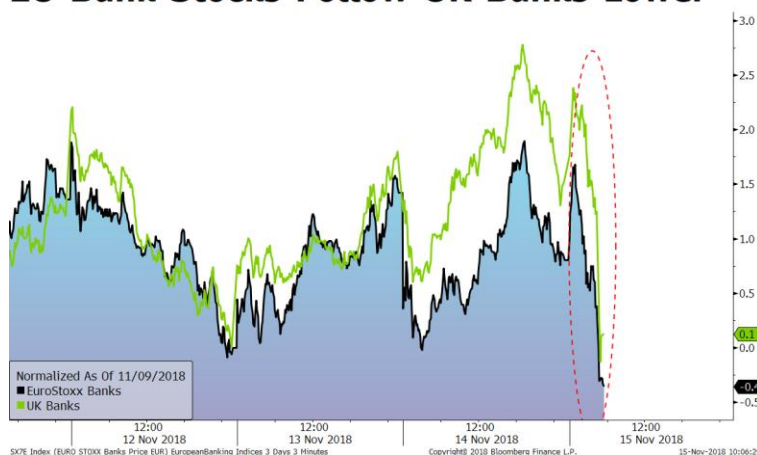
The draft Brexit withdrawal agreement and outline for the future relationship were released following yesterday's cabinet meeting. Coming in at 585 pages, the withdrawal agreement sets out the terms by which the UK would exit the European Union. This includes details of areas that have been known for some time, including the financial statement and citizens' rights. It also sets out the details of the transition period, which would run until the end of 2020, as previously announced, but the document also includes the possibility of an extension to the transition.

In short, the text lays out details of the so-called "backstop" which would keep the UK in a temporary "single customs territory." Northern Ireland would be in a deeper relationship with the EU to avoid a hard border in Ireland. The terms by which the UK could leave this agreement would need to be approved by a joint committee, with the EU and the UK having to decide jointly that the backstop would end. The document on the future relationship is a mere 7 pages and provides limited details on the precise arrangement that the two parties seek. On financial services, the goal is to commence "equivalence assessments" as soon as possible and conclude these assessments by June 2020. There is, however, no detail on the expected scope or depth of any equivalence regime.

Europe

The EuroStoxx 600 is down 0.5% with banking sector stocks falling 1.2%. German banks are leading declines with Commerzbank falling 3%. The fall in EU banks occurred in tandem with UK banks on the resignation of Brexit secretary Raab, though lower core yields have likely contributed to the move.

EU Bank Stocks Follow UK Banks Lower



German bund yields are down 3-4 bps across the curve. Yields are a few basis points higher across Southern Europe, leading to a modest widening of spreads. **Italian bonds are little changed despite some positive headlines in the local press suggesting that Italian PM Conte is taking a pro-active role in working with the EU to resolve the budget impasse.** Local media says Conte will try to focus negotiations on the excessive deficit, rather than on the high stock of debt.

Other Mature Markets [back to top](#)

Japan

Equities edged lower despite a generally positive session across Asia. The Topix (-0.1%) and Nikkei (-0.2%) were amongst a select few indices in negative territory, as energy stocks and financials continued to struggle. Both subsectors were down more than 1%. Sovereign yields were flat while the yen was moderately stronger against most major currencies.

Emerging Markets [back to top](#)

Latin American markets bounced back yesterday after falling in the prior session, reflecting a modest recovery in oil and other commodity prices. Equities rose notably in Argentina (+2.9%), Brazil (+1.2%), and Colombia (+1.0%). Most regional currencies modestly appreciated. Political uncertainty continues to weigh on Mexican markets, with the peso down 7.5% and local long-term yields up 95 bps on a monthly basis. Equity markets in Asia were mostly higher, notably China (+1.4%), while currencies were uniformly stronger against the dollar. The Indonesian rupiah (+0.8%) outperformed following the surprise hike by the central bank. In EMEA, equity and currency markets are mixed but in narrow ranges, with no major significant market developments in the region.

Key Emerging Market Financial Indicators

Last updated: 11/15/18 8:24 AM	Level		Change				YTD
	Last 12m	index	1 Day	7 Days	30 Days	12 M	
Major EM Benchmarks			%				%
MSCI EM Equities		39.93	1.7	-4	0	-13	-15
MSCI Frontier Equities		27.01	0.6	-2	-1	-14	-18
EMBIG Sovereign Spread (in bps)		378	2	22	28	75	93
EM FX vs. USD		62.05	0.2	0	-1	-8	-11
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.94	0.2	0	0	-5	-6
Indonesian Rupiah		14665	0.8	-1	4	-8	-7
Indian Rupee		71.98	0.5	1	3	-9	-11
Argentine Peso		35.90	0.0	-1	2	-51	-48
Brazil Real		3.78	0.7	-1	-1	-12	-13
Mexican Peso		20.41	0.0	-1	-8	-6	-4
Russian Ruble		66.61	0.6	0	-1	-10	-13
South African Rand		14.27	0.8	-1	1	1	-13
Turkish Lira		5.40	1.1	1	7	-28	-30
EM FX volatility		10.10	0.0	0.2	0.0	2.0	2.3

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

China

China and the US have resumed trade talks ahead of the Trump-Xi meeting at the upcoming G-20 summit in Argentina. According to reports from Reuters and Bloomberg, China has delivered a written

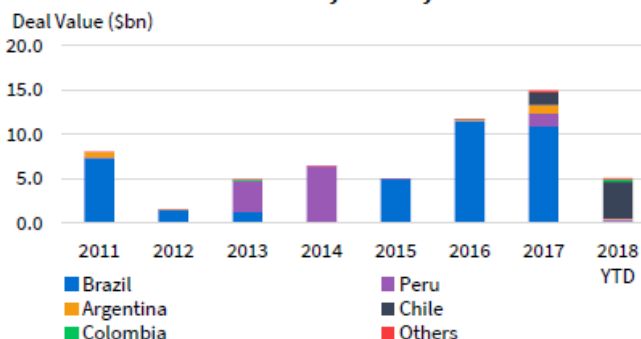
response to US demands for wide-ranging trade reforms, a move that could trigger negotiations to bring an end to the trade war between the world's two biggest economies. However, the commitments from China reportedly fall short of the type of major reforms that President Trump has been demanding, suggesting a long road ahead in negotiations. The news boosted Chinese equity markets, with the Shanghai A-share index gaining 1.4%. Stronger-than-expected earnings of the tech and telecommunication giant Tencent also supported equities. The renminbi strengthened 0.2% in the onshore market and 0.3% in the offshore market, reflecting general weakness of the US dollar against regional currencies.

There are more signs of fading appetite for dollar bonds offered by Chinese issuers. China's largest bank ICBC has pulled an offering of dollar bonds in the U.S. market, adding to concern that American investor demand for Chinese offerings is shrinking amid the trade tensions between the two nations. The bank decided on Wednesday not to proceed with marketing of its three-year and five-year floating-rate notes through its New York branch. The move came on a day when four other Chinese issuers, including a junk-rated firm, successfully priced dollar notes in Asia. However, slowdown in the Chinese economy and higher US interest rates have pushed up the yields of Asian dollar bonds.

Latin America

China's M&A activity in the region dropped sharply this year, mainly due to political risks. Over almost a decade, China's investments in Latin American companies supported their efforts to overcome domestic overcapacity and to globalize operations. China's investments in the region declined to \$5.1 bn this year, down from record high levels of \$11.7 bn and \$14.9 bn in 2016 and 2017, respectively, according to Dealogic's data. During the boom years, Brazil accounted for 85% of all the Chinese M&A activity in Latin America. As a result of the political uncertainty around the Brazilian elections, China's investments in Brazil fell to low levels this year, which was only partially offset by investments in Chile. Analysts expect that Chinese M&A activity will grow next year, helped by reduced political uncertainty, and will expand across sectors.

China - LATAM Cross Border by Country

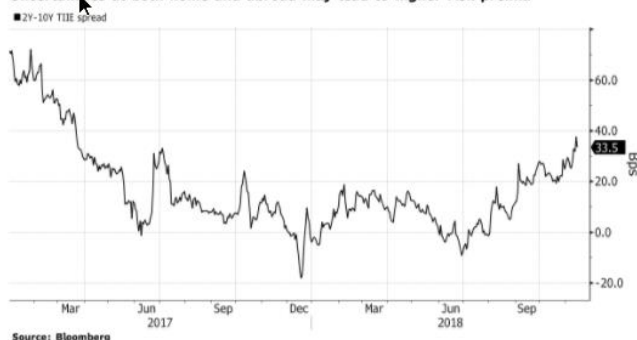


Mexico

Long-term yields keep climbing higher and the yield curve is steepening on continued policy uncertainty. President-elect Lopez Obrador announced this week that he plans to hold a new referendum on a new refinery, a tourist train, and pensions. Analysts are concerned that the use of popular votes for policy making will generate more uncertainty for markets. Separately, in the US, a senior House Democrat challenged the new USCM trade agreement, which may signal risks of a delay of the deal's approval. Mexico had expected an approval from the US Congress by 2019H2. The country's long-term bond yields rose by 95 bps on a monthly basis, compared to an 8 bp yield increase of its regional peers. The 2-10 year term spread has surpassed a 20-month high this week (chart).

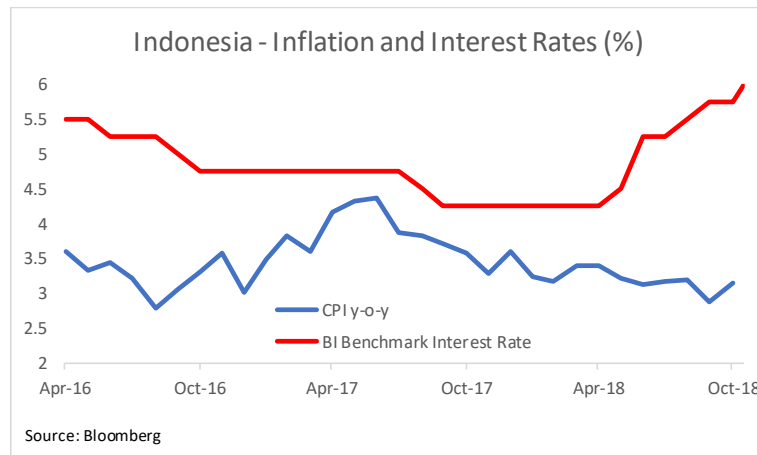
TIIE Curve Set to Steepen Further

Uncertainties at both home and abroad may lead to higher risk premia



Indonesia

The central bank surprised markets with a 25-bps interest rate hike. Analysts had expected no change in the benchmark rate, which now stands at 6%. The move takes the bank's cumulative hiking to 175 bps since May. The bank's forecast remained broadly unchanged, however, with expectations of a 5.1% growth rate this year and 3.2% inflation. Some attributed the surprise move to disappointing trade figures which increased concerns over the country's current account deficit. Alongside the interest rate decision, the central bank also relaxed macro-prudential measures to provide banks flexibility in liquidity management. The rupiah strengthened on the news and ended up 0.8% higher against the dollar while bond yields saw a smaller reaction.









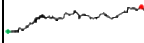

















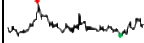




Philippines

The central bank raised interest rates for its fifth-consecutive meeting. The 25-bps move takes the overnight reverse repo rate to 4.75%, a decision that was expected by 11 of 19 analysts surveyed by Bloomberg. The decision still leaves real interest rates firmly in negative territory as inflation came in at 6.7% in October. In its statement, the bank said that prospects for the domestic economy "remain generally favorable" and that the move will help temper risks to the inflation outlook. The bank expects inflation to come down to 3.5% next year and 3.3% in 2020.

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Global Financial Indicators

Last updated: 11/15/18 8:17 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
United States		2702	-0.8	-4	-2	5	1
Europe		3204	-0.1	-1	0	-10	-9
Japan		21804	-0.2	-3	-2	-1	-4
China		2668	1.4	1	4	-22	-19
Asia Ex Japan		65	0.4	-3	1	-14	-15
Emerging Markets		40	1.6	-4	0	-13	-15
Interest Rates			basis points				
US 10y Yield		3.10	-1.5	-14	-6	78	69
Germany 10y Yield		0.37	-2.8	-9	-13	-1	-6
Japan 10y Yield		0.11	-0.2	-1	-4	6	6
UK 10y Yield		1.40	-10.8	-17	-21	11	21
Credit Spreads			basis points				
US Investment Grade		113	0.7	7	11	10	21
US High Yield		394	1.5	42	46	-13	19
Europe IG		75	2.2	7	0	22	30
Europe HY		308	7.6	26	13	56	74
EMBIG Sovereign Spread		378	2.0	22	28	75	93
Exchange Rates			%				
Dollar Index (DXY)		97.16	0.4	0	2	4	5
USDEUR		1.13	-0.1	-1	-2	-4	-6
USDJPY		113.4	0.2	1	-1	0	-1
EM FX vs. USD		62.1	0.2	0	0	-8	-11
Commodities			%				
Brent Crude Oil (\$/barrel)		67	1.3	-5	-17	8	0
Industrials Metals (index)		115	0.9	-1	-4	-11	-17
Agriculture (index)		43	0.5	-1	-4	-11	-10
Implied Volatility			%				
VIX Index (% change in pp)		21.1	-0.2	4.7	-0.2	8.0	10.0
10y Treasury Volatility Index		4.2	0.0	0.2	0.3	0.3	0.7
Global FX Volatility		8.5	0.0	0.4	0.2	0.7	1.1
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		419	8.5	31	30	-53	50
Italy		312	3.0	18	8	166	153
Portugal		159	2.7	11	9	-3	8
Spain		126	3.9	11	8	8	12

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: 11/15/2018 8:24 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		6.94	0.2	-0.1	0	-5	-6		3.4	-3.5	-8	-17	-62	-57
Indonesia		14665	0.8	-0.9	4	-8	-7		8.3	-3.9	6	-50	136	166
India		72	0.5	1.4	3	-9	-11		7.8	-3.5	-8	-31	53	32
Philippines		53	0.6	-0.4	2	-3	-5		6.7	0.4	3	16	186	188
Thailand		33	0.0	-0.3	-1	0	-1		2.9	1.3	4	-2	62	61
Malaysia		4.19	0.1	-0.7	-1	0	-3		4.2	0.2	1	8	9	27
Argentina		36	0.0	-1.2	2	-51	-48		24.0	15.3	22	144	788	800
Brazil		3.78	0.7	-1.2	-1	-12	-13		8.7	-8.0	4	-54	-42	-29
Chile		679	0.5	-0.5	0	-7	-9		4.8	-1.4	-2	-12	10	-1
Colombia		3206	-0.1	-1.9	-3	-6	-7		6.8	-0.8	5	6	30	57
Mexico		20.41	0.0	-1.0	-8	-6	-4		9.1	3.4	36	93	171	140
Peru		3.4	-0.2	-0.7	-2	-4	-4		5.9	0.2	5	6	51	65
Uruguay		33	0.2	-0.1	1	-10	-12		10.8	12.2	16	31		221
Hungary		285	0.0	-0.9	-2	-7	-9		2.7	-5.9	6	-21	137	145
Poland		3.80	-0.1	-0.8	-2	-5	-8		2.6	2.2	2	0	-18	-9
Romania		4.1	-0.2	-0.8	-2	-5	-6		4.4	6.0	5	-20	53	59
Russia		66.6	0.6	0.4	-1	-10	-13		8.4	-25.7	1	-4	89	116
South Africa		14.3	0.8	-1.0	1	1	-13		9.8	-5.5	9	-11	-25	44
Turkey		5.40	1.1	1.1	7	-28	-30		17.1	-12.7	-34	-354	467	520
US (DXY; 5y UST)		97	0.4	0.5	2	4	5		2.93	-3.1	-17	-8	89	72

	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		2668	1.4	1	4	-22	-19		186	2	7	2	43	34
Indonesia		5956	1.7	0	4	0	-6		224	6	17	25	44	58
India		35261	0.3	0	1	8	4		172	3	6	6	52	62
Philippines		6953	0.4	-1	0	-16	-19		113	3	14	6	10	18
Malaysia		1694	0	-2	-2	-2	-6		142	3	11	16	30	32
Argentina		29373	2.9	-6	-1	12	-2		644	1	37	6	258	294
Brazil		85973	1.2	-2	3	21	13		259	0	11	2	7	25
Chile		5139	0.1	-2	0	-3	-8		146	3	12	21	13	27
Colombia		1402	1.0	-2	-4	-2	-7		204	3	16	23	8	30
Mexico		42344	-0.2	-10	-11	-11	-14		333	3	30	72	78	88
Peru		18990	0	-1	-2	-2	-5		161	2	12	18	16	24
Hungary		39031	-0.2	1	7	1	-1		136	3	18	21	38	48
Poland		56732	-0.2	-2	1	-9	-11		67	4	16	3	18	20
Romania		8552	0.0	0	1	11	10		198	3	13	15	61	84
Russia		2391	0.5	-2	0	12	13		237	-2	18	17	47	59
South Africa		51898	-0.2	-4	-1	-12	-13		342	3	21	13	31	88
Turkey		93812	0.5	0	-5	-13	-19		436	3	26	-11	106	147
Ukraine		607	-0.1	2	10	101	93		626	-14	25	58	148	171
EM total		24	0.0	-3	0	-10	-10		378	2	22	28	75	93

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