Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

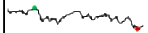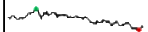**Thursday, November 8, 2018**
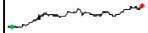
- **Divided congress raises concern over possible government shutdown (link)**
- **US mortgage applications hit lowest since 2014 (link)**
- **Italian yields rise as EC raises projected deficit for 2019 (link)**
- **China October exports surprisingly strong in race to avoid higher US tariffs (link)**
- **Turkey issues $1.5 bn eurobond (link)**

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Markets pull back slightly as post-election realities settle in

Equity markets are pulling back this morning following yesterday's strong rally as markets consider potential negative impacts of a divided US government. While US stocks rallied 2% on Wednesday after the midterm elections went mostly as expected, markets are slipping modestly so far this morning.European equities are down slightly, while US futures are pointing to a weak opening as investors are expressing some nervousness over the potential implications of a divided congress in terms of the debt ceiling, trade negotiations and Russia sanctions. Emerging markets are performing mixed this morning. While Wednesday's strong US session carried over into trading for most Asian markets with currencies largely gaining, CEEMEA currencies and equities are generally weaker so far today. China equities were a notable exception to the gains in Asia this morning, despite very strong trade data for October. Shares slipped modeestly over ongoing skepticism about whether a trade deal can be reached at the upcoming G20 summit.

Key Global Financial Indicators

Last updated: 11/8/18 7:50 AM	Level		Change from Market Close				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
S&P 500		2814	2.1	4	-2	8	5
Eurostoxx 50		3243	-0.1	1	-2	-11	-7
Nikkei 225		22487	1.8	4	-5	-2	-1
MSCI EM		42	-0.4	6	2	-11	-12
Yields and Spreads			bps				
US 10y Yield		3.22	0.8	9	-2	88	81
Germany 10y Yield		0.46	1.1	6	-7	13	3
EMBIG Sovereign Spread		355	-10	-12	12	53	70
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		62.6	-0.1	1	2	-8	-10
Dollar index, (+) = $ appreciation		96.2	0.2	0	0	4	4
Brent Crude Oil ($/barrel)		71.9	-0.2	-1	-14	13	8
VIX Index (%, change in pp)		16.5	0.1	-3	2	7	5

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

United States

Post-election relief sent risk asset prices higher. Equity indices climbed by 2% Wednesday with all sectors up led by consumer discretionary such as Amazon (+6.9%). Healthcare names were also well bid while banks underperformed as a reaction to Democrat's victory in the House. The High Yield corporate bond spread tightened by 9bp to 350bp. US Economic Policy Uncertainty Index declined below five-day moving average.

US Daily Economic Policy Uncertainty Index

Source: Economic Policy Uncertainty
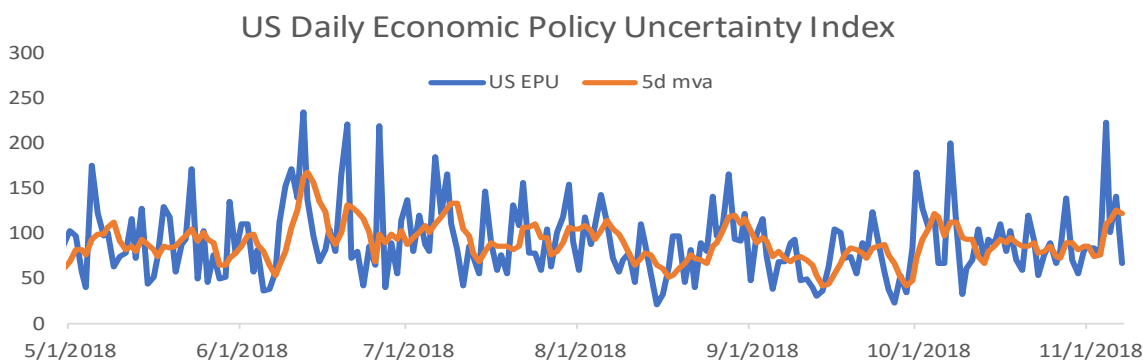
Divided Congress raises concerns over the government shutdown. The next spending deadline is December 7, but this is likely to be pushed into next year. Analysts argue that a divided Congress poses a substantial risk of a shutdown at the next spending deadline in 2019. "The debt limit will be reinstated March 1, 2019, and we expect Congress will need to raise it by August. We note that the two most disruptive debt limit debates in recent memory, in 2011 and 2013, both occurred in a divided Congress."

The treasury curve resumed its flattening trend, despite the weak result of the 30-year auction. With Congress firmly split, the likelihood of further fiscal stimulus has been reduced, analysts commented. 10-year treasury closed at 3.24% and 2-years at 2.96%. The $19bn 30-year auction was not received well, with the primary dealers share, a reverse indicator of investors' demand, coming in at 38.1%, the highest in more than three years.

Equity volatility declined. VIX went lower by 3 points to 16.3, a one-month low, with the term structure reverting to a positive slope. S&P 500 one-month option implied volatility is lower than model-based volatility forecast. Analysts expect realized volatility to decline as systematic investors, such as volatility targeters, will start rebuilding positions into year-end.

Mortgage applications hit lowest since 2014. The Mortgage Bankers Association's mortgage loan application index was down -4% in the week ending November 2, possibly due to the higher loan rates. The report also showed that 30-year home-loan rates rose to an eight-year high of 5.15%. Analysts pointed out that concern about mortgage and housing is one of the most important catalysts to explain the recent correction in stocks.

S&P500 implied volatility vs. model-based forecast %/year

Source: Bloomberg, staff calculations
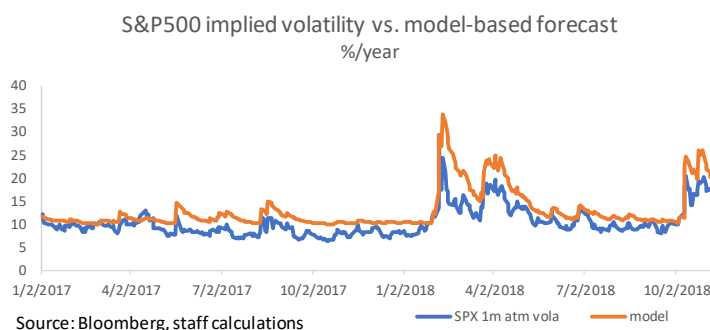
Housing Crunch
Rising borrowing costs push U.S. mortgage applications to almost four-year low

Source: Mortgage Bankers Association

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Yields are up 1-3 basis points across the region but rising 7 bps in Italy. The German 10-year is trading at 0.45% and the Italian at 3.41%. Higher Italian yields follow the release of the EC's latest economic forecasts in which it increased the country's projected deficit for next year from 2.4% to 2.9%, and to 3.1% in 2020. They assume 1.2% GDP growth for 2019, compared with the Italian forecast of 1.5%. Analysts are concerned that the commission is laying the ground to reject the budget and further escalate the conflict between Italy and the EC. Italy has until November 13 to resubmit its tax and spending proposals. For the region as a whole, the commission expects growth of 2.1% this year and 1.9% (from 2.0%) next year**.** The EC raised its 2018 inflation forecast to 1.8% and left the 2019 projection at 1.6%, roughly in line with those of the ECB.

European Commission sees slower growth in the coming years
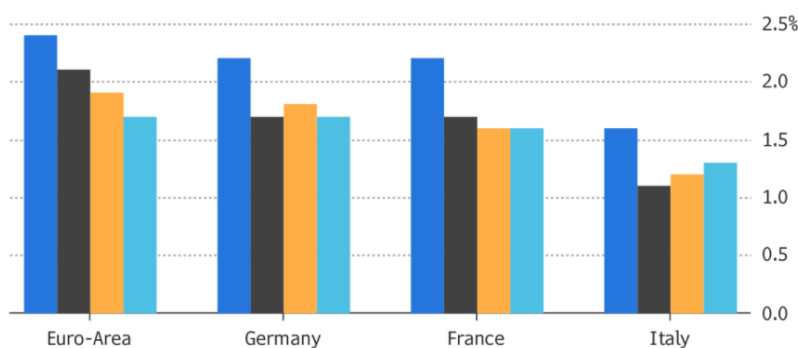
Source: European Commission

The EuroStoxx is down slightly by 0.2%, dragged lower by a 0.6% decline in Italian stocks. Of note, the banking sub-index is up 1.5% over the last two sessions, continuing its outperformance over the last few weeks on higher yields and in some cases supportive Q3 earnings. Still, EuroStoxx banks is down more than 20% over the last 6 months compared to a decline of 5% for the main index (chart). UniCredit (-4.0%) is the main underperformer after reporting Q3 net profit of €29 mn, well below the consensus of €759 mn. This was largely due to an impairment from its stake in the Turkish lender Yapi. Additionally, there were provisions relating to an upcoming settlement in the U.S. over sanctions violations also weighing on its results.

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European Bank Indices
(Last 6 Months)

Normalized As Of 05/08/2018
- ■ EuroStoxx Banks
- ■ Italy Banks
- ■ Germany Banks
- ■ Spain Banks
- ⬚ EuroStoxx 600

94.1
80.2
78.2
75.4
67.9

May Jun Jul Aug 2018 Sep Oct

SX7E Index (EURO STOXX Banks Price EUR) EuropeanBanking Indices Daily 08MAY2018   Copyright© 2018 Bloomberg Finance L.P.   08-Nov-2018 10:19:12
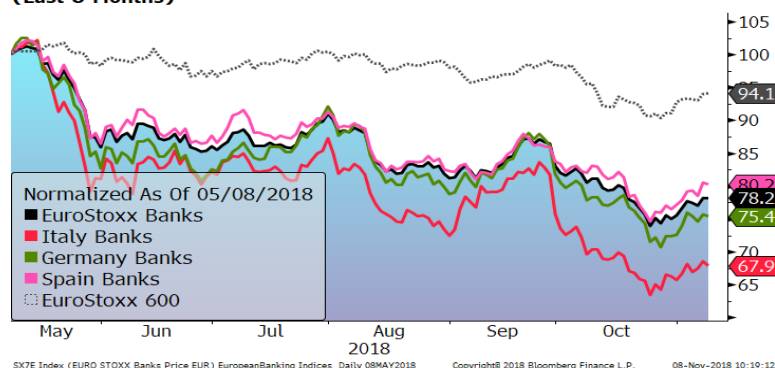
Italy

The government won the confidence vote yesterday linked to harsher restrictions on asylum seekers proposed by the Lega, quelling some concerns about a fracturing coalition and the risk of snap elections. The motion went through with 163 votes in favor of the government (5 above the absolute majority), 59 against, and 19 abstained. Five senators from the co-ruling M5S left the floor during voting in protest, but they will continue to support the government on other provisions. Yields fell 3-6 bps across the curve yesterday, in part helped by the news, but are up this morning on the aforementioned headlines about the larger projected deficit by the EC.

Separately, the ECB nominated Andrea Enria as head of the Single Supervisory Mechanism, which some interpreted as a victory for the Italian government. Analysts at Citibank argued that the appointment will have an indirect bearing on the composition of the executive board of the ECB by increasing the odds of the Irish CB governor Philip Lane succeeding Peter Praet in May.

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Key Emerging Market Financial Indicators

Last updated:	Level		Change				
11/8/18 7:52 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks			%				%
MSCI EM Equities		41.63	-0.3	6	2	-11	-12
MSCI Frontier Equities		27.70	0.7	2	-2	-12	-16
EMBIG Sovereign Spread (in bps)		355	-10	-12	12	53	70
EM FX vs. USD		62.58	-0.1	1	2	-8	-10
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.93	-0.2	0	0	-4	-6
Indonesian Rupiah		14539	0.4	4	5	-7	-7
Indian Rupee		73.00	0.2	1	1	-11	-13
Argentine Peso		35.67	-0.1	1	5	-51	-48
Brazil Real		3.73	0.2	-1	1	-13	-11
Mexican Peso		19.86	0.0	2	-5	-4	-1
Russian Ruble		66.39	-0.2	-1	0	-11	-13
South African Rand		13.98	-0.6	3	6	1	-11
Turkish Lira		5.42	-1.1	2	13	-29	-30
EM FX volatility		9.89	0.0	-0.2	-0.6	1.8	2.0

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

EM equities rallied on Wednesday (MSCI EM: +1.8%) boosted by the positive risk sentiment in US assets following the election results. In **LatAm,** the Mexican peso led losses (-0.7%) amid concern that a "split decision" election outcome in US could delay the ratification of a new North American trade deal. In Argentina the peso weakened vs the dollar (-0.1%) after Fitch affirmed the sovereign credit rating at B but lowered the outlook to "negative" citing weakness in economic activity and uncertainty about fiscal consolidation. **Asian** equity indices were mostly higher (+0.3-0.6%) but Chinese stocks closed slightly lower. Currencies are mixed across the region, with the Philippine peso (+0.7%) the notable mover. In **EMEA**, most currencies and equity indices are down against the dollar, notably the Turkish lira (-1.4%) and the BIST index falling 1.8% on poor Q3 earnings results.

China

China October exports surprisingly strong in race to avoid higher U.S. tariffs. The October figures came in stronger than expected 15.6% from a year ago, versus market consensus of 11.7%. The robust export figures could be partly driven by front loaded shipments by exporters to avoid another round of higher tariff rates due to kick in at the start of next year. Meanwhile, imports expanded by 21.4%, also defying forecasts for a slowdown in growth. Beijing's growth-boosting measures may also play a role. The upbeat trade readings from China offer good news for both those worried about global demand and for the country's policymakers. But analysts continue to warn of the risk of a sharp drop in U.S. demand for Chinese goods starting in 2019, saying that robust export readings won't last much longer as indicated by shrinking export orders from the recent PMI readings. An additional sign of a possible exports slowdown can be seen from shrinking US orders at the latest Canton fair, dropping more than 30% from a year earlier by value.

China Exports Continue to Show Resilience Amid Trade War

China's stock market slid despite stronger-than-expected trade figures, while the renminbi was little changed. Despite improved sentiments elsewhere in the region following the US midterm election results, which are largely in line with expectations, investors remained skeptical that a trade deal can be reached during the Trump-Xi talks at the upcoming G-20 Summit. The Shanghai and Shenzhen A share indices edged down 0.2% and 0.5% respectively at market close. The Chinese yuan was trading within a narrow range, closing at 6.9285 against the dollar and little changed from previous close. In the offshore market, the CNH weakened by 0.2% to 6.9242, as improved risk appetite supported the US dollar to strengthen against most regional currencies in Asia.

Russia had a disappointing bond auction as the changing political tide in the US weighs on sentiment. Investors are concerned that a Democrat-controlled House will be more aggressive in pushing for sections against Russia. The treasury sold RUB 10 bn ($150 mn) of local bonds due 2024 and 2029, but this was just over half of what was planned. According to Bloomberg, weakening demand due to sanctions risk led the Finance Ministry to cut its bond sales plans by 30% this year. Ten-year yields were up 10 bps to 8.8% following the weak auction result.

Russian Local Debt
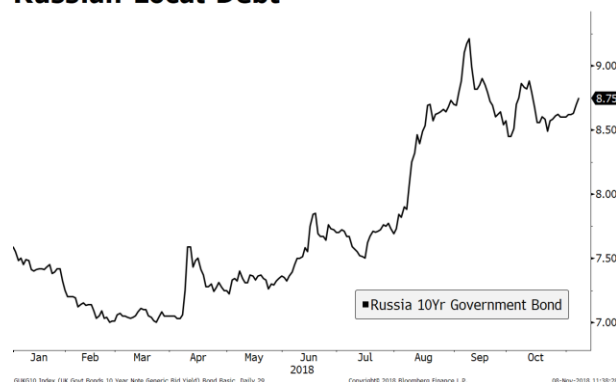
Turkey

The treasury has issued a €1.5 bn Eurobond due 2026 at 5.25%, compared with the initial guidance of 5.50%. The sale was more than three times oversubscribed. The bond brings the total amount the Turkish treasury has raised from international capital markets to $7.7 bn this year, compared with the original borrowing program of $6.5 bn. The Treasury did not comment on whether the funds will be used for pre-financing the 2019 external borrowing plan. The yield on the country's 2028 Eurobond issued in April is up 3 basis points over the last couple of sessions. The lira is down 1.4% today against the dollar and the country's stock index is falling 1.8% on poor Q3 earnings results, including of Turkish Airlines. Separately, Moody's updated its forecasts for Turkey and now expects GDP to contract by 2.0% in 2019, but then recover by 3% in 2020.

Turkey Eurobond and Lira
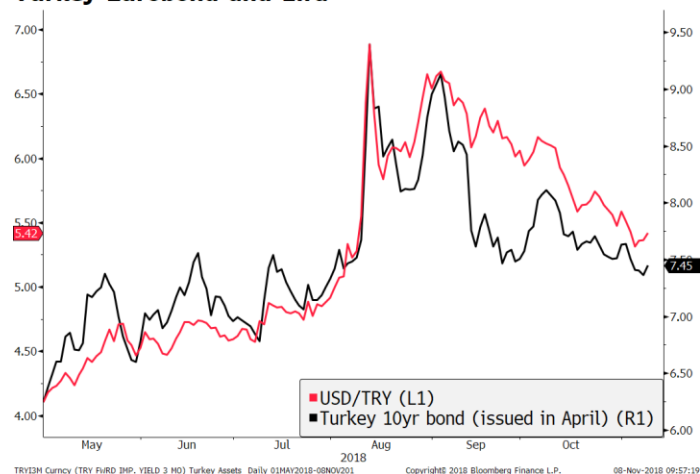
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Global Financial Indicators

Last updated: 11/8/18 7:51 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
United States		2814	2.1	4	-2	8	5
Europe		3243	-0.1	1	-2	-11	-7
Japan		22487	1.8	4	-5	-2	-1
China		2636	-0.2	1	-3	-23	-20
Asia Ex Japan		67	2.1	6	1	-13	-12
Emerging Markets		42	-0.4	6	2	-11	-12
Interest Rates			basis points				
US 10y Yield		3.22	0.8	9	-2	88	81
Germany 10y Yield		0.46	1.1	6	-7	13	3
Japan 10y Yield		0.12	-0.1	0	-3	10	7
UK 10y Yield		1.55	2.0	10	-12	33	36
Credit Spreads			basis points				
US Investment Grade		105	-1.5	-3	5	7	13
US High Yield		353	-8.0	-23	25	-24	-23
Europe IG		68	0.8	-4	-4	16	23
Europe HY		280	0.1	-10	-10	46	47
EMBIG Sovereign Spread		355	-10.0	-12	12	53	70
Exchange Rates			%				
Dollar Index (DXY)		96.21	0.2	0	0	1	4
USDEUR		1.14	0.0	0	-1	-1	-5
USDJPY		113.7	-0.1	-1	0	0	-1
EM FX vs. USD		62.6	-0.1	1	2	-8	-10
Commodities			%				
Brent Crude Oil ($/barrel)		72	-0.2	-1	-14	13	8
Industrials Metals (index)		115	-0.7	0	-4	-13	-17
Agriculture (index)		43	0.2	0	0	-11	-9
Implied Volatility			%				
VIX Index (%, change in pp)		16.5	0.1	-2.9	1.7	6.7	5.4
10y Treasury Volatility Index		4.0	-0.7	-0.4	-0.2	0.4	0.5
Global FX Volatility		8.1	0.0	-0.2	-0.3	0.8	0.7
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		385	-1.0	2	-26	-94	16
Italy		293	3.7	-5	-11	151	134
Portugal		146	-2.0	-2	2	-22	-5
Spain		114	-1.2	-3	8	-2	0

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

Emerging Market Financial Indicators

Last updated: 11/8/2018 7:53 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		6.93	-0.2	-0.1	0	-4	-6		3.5	-2.3	0	-15	-46	-49
Indonesia		14539	0.4	4.1	5	-7	-7		8.2	-12.0	-39	-25	132	160
India		73	0.2	0.9	1	-11	-13		7.9	0.0	-9	-31	70	40
Philippines		53	0.3	0.9	3	-3	-5		6.7	5.8	8	27	187	185
Thailand		33	-0.2	0.0	0	1	-1		2.9	-0.4	-4	-4	63	58
Malaysia		4.16	0.0	0.3	0	2	-3		4.2	0.4	3	6	12	26
Argentina		36	-0.1	0.7	5	-51	-48		23.8	26.5	254	60	802	778
Brazil		3.73	0.2	-0.8	1	-13	-11		8.7	2.1	2	-107	-25	-33
Chile		675	0.2	2.0	1	-6	-9		4.8	0.9	-1	-3	14	1
Colombia		3130	0.6	2.9	-3	-3	-5		6.8	-5.1	-9	9	27	52
Mexico		19.86	0.0	1.5	-5	-4	-1		8.7	9.8	-14	57	144	104
Peru		3.4	0.2	0.3	-1	-4	-4		5.8	-4.0	-13	8	49	60
Uruguay		33	0.1	0.4	1	-11	-12		10.6	-1.0	-20	24		205
Hungary		281	0.0	0.6	1	-4	-8		2.6	-1.0	-8	-7	128	139
Poland		3.76	-0.1	1.0	0	-3	-7		2.6	4.2	0	-7	-19	-10
Romania		4.1	0.0	0.2	0	-2	-5		4.4	0.0	-19	-13	92	54
Russia		66.4	-0.2	-1.1	0	-11	-13		8.4	7.4	9	0	97	115
South Africa		14.0	-0.6	3.0	6	1	-11		9.7	-6.1	-30	-18	-14	35
Turkey		5.42	-1.1	1.7	13	-29	-30		17.5	15.1	-193	-429	520	554
US (DXY; 5y UST)		96	0.2	-0.1	0	1	4		3.07	-0.9	11	0	106	86

	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		2636	-0.2	1	-3	-23	-20		178	-5	-6	-2	37	26
Indonesia		5977	0.6	2	4	-1	-6		209	-14	-13	22	38	43
India		35238	0.0	2	2	6	3		166	-2	-3	6	51	56
Philippines		7036	0.0	0	0	-17	-18		101	-12	-13	3	2	6
Malaysia		1721	0	1	-3	-1	-4		130	-13	-6	9	21	20
Argentina		31405	1.4	7	3	12	4		597	-7	-38	-76	214	247
Brazil		88375	-1.1	1	3	19	16		243	-12	-10	-25	-3	9
Chile		5232	0.0	4	-2	-5	-6		134	-18	-8	17	5	15
Colombia		1423	1.5	2	-4	-1	-6		183	-16	-3	13	-7	9
Mexico		46917	1.3	8	-2	-4	-5		294	-16	-13	37	43	49
Peru		19266	0	2	0	-3	-4		150	-16	-6	25	9	13
Hungary		38282	0.2	5	4	-5	-3		119	-5	-6	13	20	31
Poland		57671	-0.3	4	0	-11	-10		53	1	-11	4	0	6
Romania		8685	0.2	1	2	12	12		185	-3	-8	15	54	72
Russia		2437	-0.4	4	-1	13	15		220	-12	-2	6	32	42
South Africa		54301	-0.8	1	0	-10	-9		322	-17	-23	6	16	68
Turkey		93859	-1.8	2	-2	-16	-19		411	-16	-33	-64	76	122
Ukraine		589	0.5	3	7	95	87		602	2	-13	49	125	147
EM total		25	0.0	5	0	-9	-7		355	-10	-12	12	53	70

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