GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

TUESDAY, NOVEMBER 7, 2023

LEAD EDITOR: JEFF WILLIAMS

- **Slope of the UST yield curve continues to dictate term premia** (link)
- **Italian spreads in limelight as rating reviews loom while issuance supply shrinks** (link)
- **Reserve Bank of Australia hiked cash rate by 25bps as expected** (link)
- **EM sovereign rating outlook appears stable though with differentiation** (link)
- **National Bank of Poland expected to cut policy rate** (link)
- **Special Feature: Emerging Markets Issuance Monitor for October (attached)**

Mature Markets | Emerging Markets | Market Tables

All good things must come to an end, including equity rallies

The S&P 500's streak of six consecutive days of positive returns is at risk today with futures showing a weaker opening. The move follows earlier declines seen in Asian equity markets overnight and European markets this morning, with the Stoxx 600 down 0.3% to start the day. The dip comes despite a decline in sovereign bond yields. The UK 10-year is 7 bp lower this morning after comments from the Bank of England's chief economist that there will be a "*sharp further fall*" in inflation for October. US Treasury yields are seeing a more modest decline, as the 10-year is down just 2 bp, with Minneapolis Fed president Kashkari saying in an interview that it is too soon for policy makers to declare a victory over inflation. Emerging market currencies are broadly negative this morning versus the dollar, with the South African rand leading losses, down 0.7% on weaker commodity prices.

Key Global Financial Indicators

Last updated: 11/7/23 8:34 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
S&P 500		4366	0.2	5	1	15	14
Eurostoxx 50		4143	-0.4	2	0	12	9
Nikkei 225		32272	-1.3	5	4	16	24
MSCI EM		39	0.8	5	2	7	2
Yields and Spreads				bps			
US 10y Yield		4.62	-2.5	-31	-18	40	74
Germany 10y Yield		2.69	-5.0	-12	-20	35	12
EMBIG Sovereign Spread		422	-1	-19	-30	-102	-30
FX / Commodities / Volatility				%			
EM FX vs. USD, (+) = appreciation		47.6	0.0	1	3	-4	-5
Dollar index, (+) = $ appreciation		105.6	0.4	-1	0	-4	2
Brent Crude Oil ($/barrel)		83.3	-2.2	-5	-2	-15	-3
VIX Index (%, change in pp)		15.0	0.1	-3	-2	-9	-7

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

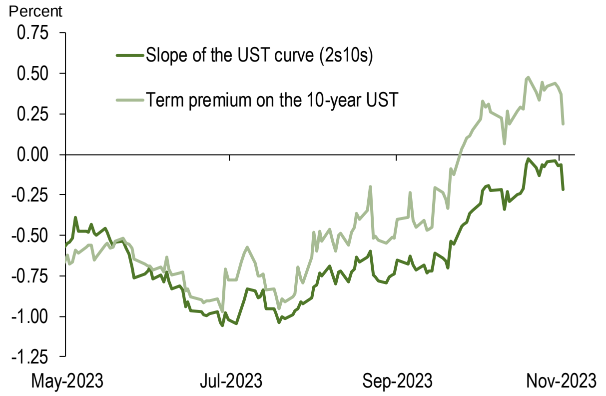
Mature Markets

back to top

United States

Slope of the yield curve continues to dictate term premia. Steepening of the yield curve since the summer has allowed term premia for long-dated bonds to decompress. This rise in excess returns demanded by investors has been the major driver of higher nominal yields over the same period. Even though the broader level of interest rates in the US economy had been rising throughout 2022, the subsequent inversion of the curve was proving to be a headwind against higher term premia. This highlights that last week's decrease in term premia at the 10-year tenor was likely to have been driven by the recent inversion of the 2s10s curve. Considering the US Treasury decided to issue a higher proportion of short-dated securities relative to expectations, the behavior of the slope of the yield curve may continue to be an important factor over the next few months.

Steepening of the yield curve had paved the way for term premia to decompress

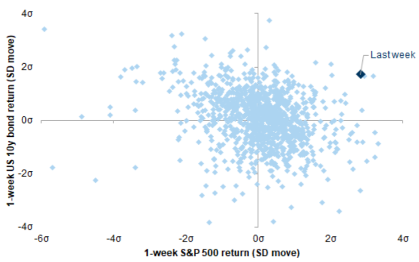


Source: Adrian, Crump & Moench (2013), Bloomberg, NYFRB, IMF Staff calculations

Last week's market rally stands out compared to recent history. The Federal Reserve's decision to hold interest rates steady was viewed by markets as the central bank finishing its tightening cycle. Markets are now pricing the first full cut to take place by the June meeting. The relief rally has been more than a two standard deviation move both for weekly equity and bond returns—large enough for the correlation between equities and bonds to turn positive again on a two-week basis. Goldman Sachs analysts continue to see some scope for yields to continue their richening with softening growth data throughout the rest of the quarter. While this may prove to be a headwind for the US dollar's performance in the near-term, the strategists think the structural reasons for a stronger dollar continue to be there. Firstly, Chair Powell's acknowledgement for a "persistent" shift in financial conditions as a substitute for further tightening might be able to provide favorable ground for the dollar to bounce back from its recent underperformance. Second, positive supply-side news should benefit the dollar when other central banks are revising their growth forecasts lower. Third, FX is a relative asset—its performance is dependent on its peers—lower growth forecasts among other regions could encourage markets to price in rate cuts earlier than for the US.

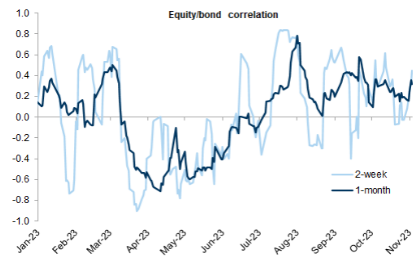
Exhibit 1 : A sharp move up for both equities and bonds

1-week return / 1-year standard deviation over the past 20 years



Source: Haver Analytics, Goldman Sachs Global Investment Research

Exhibit 2 : Equity/bond correlation is in positive territory again



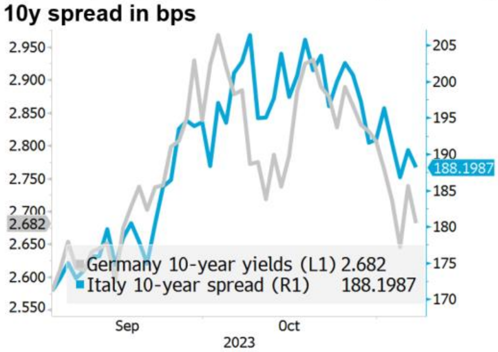
Source: Haver Analytics, Goldman Sachs Global Investment Research

Euro Area

European government bond yields retraced from yesterday's sharp selloff. For 10-year Italian government bond yields, yesterday's rise by 13bp to 4.64% reflected the largest daily rise since July 6. Today, Italian yields compressed by 6bp at 4.58% while those of Bunds declined by -4bp to 2.7%. Markets took solace in today's downbeat industrial production data out of Germany for September that printed extremely soft at -1.4% m/m (expected -0.1% from revised -0.1%), confirming the state of the country's troubled manufacturing sector and validating that the euro area might have more arguments in favor of lower rates than the US. Euro area producer prices for September validated expectations, printing at +0.5% m/m (expected 0.5% from revised 0.7%). Stock markets continued inching lower with the Stoxx 600 declining 0.2% lower during the beginning of today's trading session, led by basic resources and energy sectors that declined 1.5% and 1.3%. The euro fractionally weakened by 0.4% to 1.07/$.

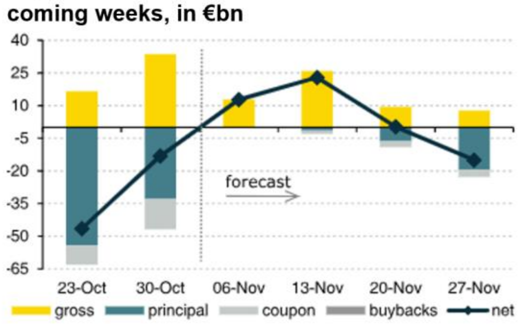
Italian bond spreads take center stage as rating reviews loom while issuance supply is dwindling. Italian spreads turn back into focus as rating jitters could increase again ahead of the scheduled reviews from Fitch on Friday and Moody's next week (left chart). Fitch affirmed its BBB/stable rating in May, which was before the budgetary plans for 2024 were published by the Italian government. Early October, Fitch stated that Italy's future deficit plans "*represent a significant loosening of fiscal policy*". While Fitch's slightly more optimistic assumption about Italy's trend growth could be supportive, with the risk tilted towards a negative rating outlook. Market contacts see scarcer euro-area sovereign issuance supply as a supportive factor. To that effect, Commerzbank Analysts estimate that auction supply drops to about €13bn this week vs. €33.7bn last week (right chart), with the lion share in maturities up to the 10y sector led by Italy (€7.5bn), followed by Germany (€4bn) and Austria (€1.3bn). On a duration weighted basis, Goldman Sachs analysts estimate the issuance supply this month to be 50% lower than in September and October on a duration weighted basis, falling to one of the lowest levels this year.

Germany 10y years in % and Italy-Germany 10y spread in bps



Source: Bloomberg, IMF Staff Calculations

Expected EGB gross and net issuance over the coming weeks, in €bn

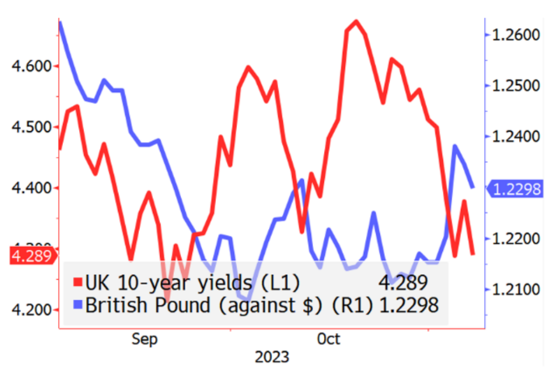


Source: Commerzbank

United Kingdom

Gilts rally on dovish remarks from Bank of England chief economist and softer grocery prices. Huw Pill stated that there will be a "*sharp further fall*" in inflation for October, a development which he hinted could afford interest rates to be cut by the middle of next year. Also October grocery price inflation as captured by Kantar data slowed to single digits to 9.7% y/y (from 11%), marking the eighth consecutive decline since the peak of 17.5% in March and the first time that the grocery price increase has fallen below 10% since July last year, which confirms a development already seen in data from the British Retail Consortium on Tuesday last week. The Kantar data further shows that British consumers have turned to both discount grocers and increasingly to own-label lines, which have grown ahead of their branded counterparts every month since February last year. In reaction, 10-year Gilt yields fell by 7bp to 4.3% while the pound softened by -0.5% to 1.23/$.

Gilt 10y yields in % and British Pound against $



Source: Bloomberg, IMF Staff Calculations

Japan

Equities declined 1.2%. Japan's labor cash earnings picked up 1.2% y/y (previous: +0.8%) in September, however, real cash earnings, adjusted for inflation, remained in contraction -2.4% y/y (previous: -2.8%). JPM found that wage growth continued to be disappointing in 3Q, dragged by weakness in wages of the manufacturing sector. Japan's Economy Minister Nishimura said the new economic stimulus package aims to support wage growth. He also indicated the government wishes to see wage growth of "5% plus alpha" to boost the economy. **10Y yields were little changed.** Some investors saw the next resistance level for 10Y yields will be at 1.1–1.2%. The 10Y inflation-index bond bid cover ratio fell to 2.73, the lowest since 2017, signaling poor investor appetite amid expectations of higher yields. **The yen weakened 0.2%.**

Source: Bloomberg, OCBC Research

Source: MHLW, J.P. Morgan

Australia

The Reserve Bank of Australia (RBA) raised its cash rate by 25bp to 4.35% as expected, to ensure inflation returns to target within a reasonable timeframe. Their inflation forecast for end-2024 was revised up to around 3.5% from 3.25%. RBA's forward guidance tempered tightening expectations as they adopted a data-dependent stance, a shift from October's further tightening warning. Analysts thought RBA's forward guidance had a dovish tilt but still expected another 25bp hike in December or early 2024. Separately, **PM Albanese met with China's President Xi**, amid improved relations between both countries. Albanese emphasized the need to remove Chinese restrictions on Australian exports. Both countries sought to strengthen cooperation, while managing differences**.** Equities fell by 0.3%. The Australian dollar weakened 1% and 10Y bond yields fell -2.7bp.

Emerging Markets back to top

Asian equities broadly declined, net -1.1% amid pullback from the recent rally. South Korea equities lost 2.3%, followed by Hong Kong SAR (-1.7%). **Hong Kong SAR**'s Financial Secretary Chan said in an interview that economic recovery is weaker than expected, however, GDP growth will likely exceed 3% in 2023. **Asian currencies weakened.** The South Korean won depreciated by 0.8%, followed by the Malaysian ringgit. **10Y bond yields were mixed.** Indonesian yields declined (-16bp). **Philippines**' CPI inflation was softer than expected at 4.9%y/y (previous: 6.1%), reaffirming a likely hold by BSP in November. Meanwhile, Taiwan's POC's inflation was stronger than expected rising to 3.1%y/y (previous: 2.9%) in October. **EMEA currencies and equities are mostly weaker.** Within Europe, the Polish zloty (-0.5%) and Romanian leu (-0.4%) led the decline while the Russian ruble fractionally gained (+0.1%). Ahead of the central bank decisions tomorrow, stock markets in Romania defeated the broader downward trend, rising 0.7%. In South Africa, stock markets declined by 1.7% and the rand depreciated (-0.5%) on weaker Chinese trade data and concerns raised by rating agency Fitch over South Africa's rolling power cuts, rail freight challenges, and its ability to meet the fiscal targets that were announced in the mid-term budget last week. **Equity markets in LATAM opened the week higher, however most regional currencies underperformed.** In Brazil, the finance minister reiterated the commitment toward zero fiscal deficit in 2024. Markets reacted positively with equities and currency gaining 0.2% and 0.3%, respectively, while the swap rate fell by 10–16bp in the short end of the curve.

EM sovereign ratings

EM sovereign ratings are seen to be stabilizing after enduring a long phase of downgrades. As per a market report, the average sovereign rating of EMs has declined from ~BB+ in 2013 to ~BB- in 2023. Using a statistical model, the report attributes the downgrades overtime to three key factors, firstly, external shocks in the form of declining commodity prices during 2014–16; secondly, deterioration in fiscal health due to the pandemic support related expenditures; and finally, the more recent rise in inflation amid slower global economic growth. Further, the report argues that while in 2023 the rate of downgrade seems to have stabilized at pre-covid level, EMs are now facing the additional challenge from the higher-for-longer rate regime in developed economies. Using IMF and consensus forecasts, the model projects stability in EM sovereign ratings in 2024, however with significant heterogeneity. Countries with better outlook on fiscal, inflation and economic growth trend show a higher probability of a rating upgrade.

Figure 1. Commodity exporting regions have seen the most substantial downgrades over the last 10 years

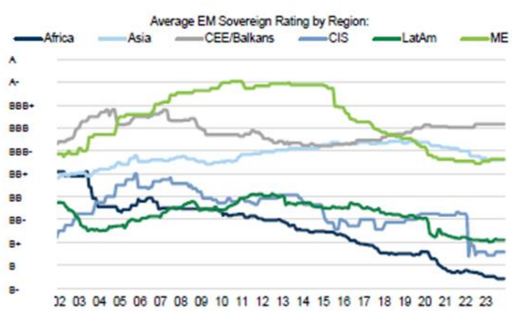
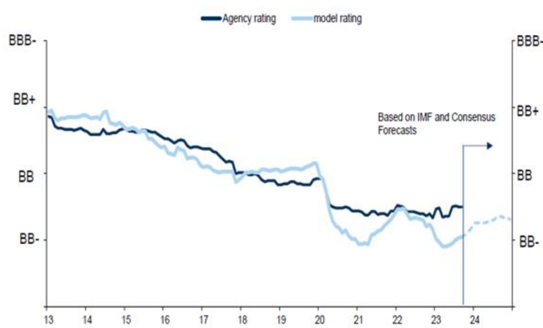


Figure 2. The average EM rating has declined since 2013, as is also estimated by the model.



Source: Bloomberg, Goldman Sachs Global Investment Research

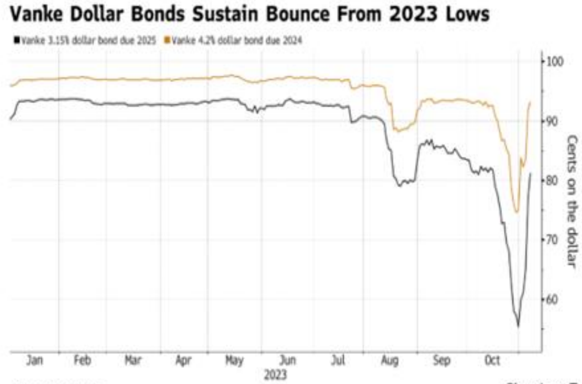
China

Chinese equities slipped 0.4%. China's exports slump worsened further in October to -6.4%y/y (previous: -6.2%), although imports rebounded to +3%y/y (previous: -6.3%). Barclays believes a quick turnaround in exports is unlikely due to declining FDI, slowing global growth and contracting new export orders. Separately, **China tightened rare earths export controls on Tuesday**, requiring exporters to report transaction details such as destination and rare earth types; effective through end October 2025. Separately, **Vanke, China's second largest builder received a strong signal of public support**. Shenzhen's State-owned Assets Supervision and Management Commission said it has confidence in Vanke and enough cash and tools to support the developer if required. Vanke's dollar bonds surged on the news, some notes, however, are still trading at distressed levels below 80 cents, Bloomberg reported. The offshore renminbi depreciated by 0.1%. 10Y bond yields were little changed.

Figure 3. Shipments to major destinations remain weak

Source: Wind, Barclays Research

Vanke Dollar Bonds Sustain Bounce From 2023 Lows



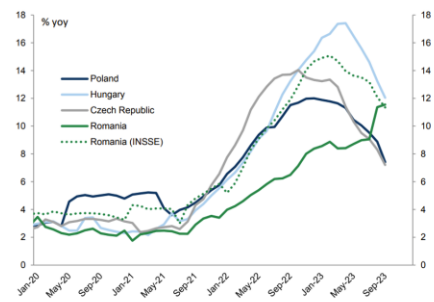
Source: Bloomberg

Bloomberg

Romania

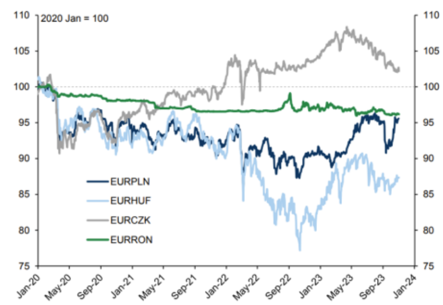
The Romanian National Bank (NBR) is expected to remain on hold. For the impending meeting tomorrow, consensus expects NBR to maintain 7% where it has kept policy rates since January. The latest inflation prints, supported by strong income growth and a new outlook for oil prices, continue to suggest that the disinflation process in Romania is not a given. While headline inflation has been fallen from one year ago on account of a combination of favorable base effects and underlying price pressures receding, the slowdown in sequential core inflation has been less marked in Romania than its CEE peers (left chart), leaving a longer way to go before approaching the NBR's 2.5% +/- 1pp. target range. ING analysts perceive that this background sets the stage for NBR to remain cautious—leading to the likely scenario of the NBR being the last CEE4 central bank to begin its cutting cycle. In addition to the slower disinflation relative to peers, Goldman Sachs analysts expect that a cautious cutting cycle in the first half of 2024 also allows the NBR to maintain RON stability (right chart).

Across CEE4 countries, core inflation appears stickiest in Romania



Source: Goldman Sachs
Note: INSSE CPI excluding vegetables, fruit, eggs, fuel, products whose prices are regulated and beverages & tobacco.

While volatility rose since mid-2022, the RON is the steadiest currency among CEE4 countries.

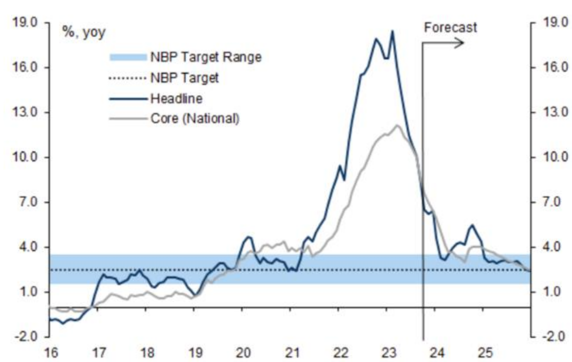


Source: Goldman Sachs

Poland

Market expectations and consensus expect the National Bank of Poland (NBP) to cut rates. To recall, NBP eased monetary policy by 100bp due to what market contacts described as an exceptionally dovish short-term reaction ahead of the election. Market pricing and consensus continue to expect the central bank delivering another 25bp rate cut at its meeting tomorrow. However, Goldman Sachs analysts highlight that Governor Glapinski's voting history used to be more hawkish during his time as a regular MPC member under the Civic Platform-led government. This might herald the NBP adopting a more cautious approach, leaving policy rates unchanged as headline inflation approaches the NBP's 2.5% +/- 1pp. target range in Q1 next year. From then onwards, base effects and the planned reintroduction of VAT on foods that is expected to happen gradually throughout 2024 are predicted to exert some upward pressure on inflation, keeping it within the upper band of the target range.

Poland Headline and core inflation vs. NBR target



Source: Goldman Sachs

This monitor is prepared under the guidance of Jason Wu (Assistant Director), Charles Cohen (Advisor), Nassira Abbas (Deputy Division Chief), and Caio Ferreira (Deputy Division Chief). Fabio Cortes (Senior Economist), Sanjay Hazarika (Senior Financial Sector Expert), Esti Kemp (Financial Sector Expert-London Representative), Johannes S Kramer (New York Representative), Benjamin Mosk (Senior Financial Sector Expert), and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Yingyuan Chen (Financial Sector Expert), Andrew Ferrante (Research Assistant), Deepali Gautam (Research Officer), Phakawa Jeasakul (IMF Resident Representative in Hong Kong SAR), Harrison Kraus (Research Assistant), Yiran Li (Research Assistant), Xiang-Li Lim (Financial Sector Expert), Corrado Macchiarelli (Economist), Kleopatra Nikolaou (Senior Financial Sector Expert), Natalia Novikova (IMF Resident Representative in Singapore), Mustafa Oguz Caylan (Research Officer), Silvia Ramirez (Senior Financial Sector Expert), Patrick Schneider (Financial Sector Expert), Ying Xu (Economist), Dmitry Yakovlev (Senior Research Officer), and Akihiko Yokoyama (Senior Financial Sector Expert). Javier Chang (Senior Administrative Coordinator), Lauren Kao (Administrative Coordinator), and Srujana Sammeta (Administrative Coordinator) are responsible for the word processing and production of this monitor.

Global Financial Indicators

11/7/23 8:34 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		4365	0.2	4	1	15	14
Europe		4143	-0.4	2	0	12	9
Japan		32272	-1.3	5	4	16	24
China		3620	-0.4	1	-2	-3	-7
Asia Ex Japan		65	0.9	4	2	9	0
Emerging Markets		39	0.8	5	2	7	2
Interest Rates					basis points		
US 10y Yield		4.62	-2.5	-31	-18	40	74
Germany 10y Yield		2.69	-5.0	-12	-20	35	12
Japan 10y Yield		0.88	0.1	-6	8	63	46
UK 10y Yield		4.31	-6.7	-20	-26	67	64
Credit Spreads					basis points		
US Investment Grade		159	0.8	-3	5	-18	0
US High Yield		433	4.3	-29	-20	-41	-47
Exchange Rates					%		
USD/Majors		105.63	0.4	-1	0	-4	2
EUR/USD		1.07	-0.4	1	1	7	0
USD/JPY		150.6	0.4	-1	1	3	15
EM/USD		47.6	0.0	1	3	-4	-5
Commodities					%		
Brent Crude Oil ($/barrel)		83.3	-2.2	-2	0	-3	3
Industrials Metals (index)		139	-1.4	1	0	-8	-16
Agriculture (index)		66	-0.5	2	3	-4	-5
Implied Volatility					%		
VIX Index (%, change in pp)		15.0	0.1	-3.1	-2.4	-9.3	-6.6
Global FX Volatility		7.6	0.0	-0.5	-0.6	-4.1	-3.1
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		130	-1.1	-8	-23	-113	-76
Italy		189	-1.1	-3	-13	-25	-25
Portugal		69	-2.2	-3	-8	-28	-33
Spain		106	-0.2	-2	-7	1	-4

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

Emerging Market Financial Indicators

Last updated: 11/7/2023 8:35 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		7.28	-0.2	0.5	0	-1	-5		2.7	1.5	-2	-3	-15	-37
Indonesia		15636	-0.6	1.6	0	0	0		6.7	-16.4	-42	-33	-77	-26
India		83	-0.1	0.0	0	-2	-1		7.5	-1.0	-15	-34	(8.1)	9
Philippines		56	-0.4	1.1	1	4	-1		5.9	0.1	2	16	3	-9
Thailand		36	-0.3	1.5	4	5	-3		3.1	-3.0	-16	-30	4	51
Malaysia		4.67	-0.7	2.0	1	2	-6		3.9	-2.5	-19	-20	-57	-16
Argentina		350	0.0	0.0	0	-54	-49		109.2	0.0	-3	131	1355	2101
Brazil		4.87	0.4	3.5	6	6	9		11.5	-13.9	-38	-35	-38	-108
Chile		883	-0.1	1.6	4	4	-4		5.7	1.0	-38	-11	-62	32
Colombia		3980	0.0	3.6	9	29	22		8.5	0.0	-61	-121	-315	-131
Mexico		17.53	0.1	3.0	4	11	11		9.3	0.0	-39	-21	-3	55
Peru		3.8	-0.4	2.0	2	5	1		7.3	-0.3	-39	-30	-66	-69
Uruguay		40	0.0	0.3	0	0	0		9.9	-2.7	1	5	-134	-83
Hungary		354	-0.1	2.1	4	13	5		7.2	-4.0	-32	-37	-352	-242
Poland		4.18	-0.5	0.8	3	12	5		4.8	-2.3	-20	-28	-245	-136
Romania		4.7	-0.4	0.9	1	5	-1		6.7	0.6	-18	-31	-233	-101
Russia		92.4	0.2	1.1	8	-33	-20							
South Africa		18.4	-0.7	1.2	5	-4	-8		9.6	0.5	-28	-38	25	42
Turkey		28.50	-0.2	-0.7	-3	-35	-34		31.8	98.0	245	512	1973	2193
US (DXY; 5y UST)		106	0.4	-1.0	0	-4	2		4.58	-1.1	-28	-18	19	57

	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	7 Days	30 Days	12 M	YTD
								basis points					
China		3620	-0.4	1	-2	-3	-7		166	-4	-7	-41	-11
Indonesia		6844	-0.5	1	-1	-3	0		119	-8	-10	-78	-21
India		64942	0.0	2	-2	6	7		130	-6	-17	-81	-12
Philippines		6131	0.9	2	-2	-3	-7		96	-9	-10	-58	-1
Thailand		1408	-0.6	2	-2	-14	-16		0	0	0	0	0
Malaysia		1463	-0.1	1	3	2	-2		94	0	-4	-25	-6
Argentina		637284	-2.6	-3	1	321	215		2531	-53	-148	-47	326
Brazil		118431	0.2	5	4	3	8		219	-1	-8	-56	-55
Chile		5612	-0.8	3	-1	6	7		143	1	7	-23	11
Colombia		1099	0.1	1	0	-12	-15		312	-17	-48	-141	-60
Mexico		51634	0.7	5	4	2	7		358	-13	-18	-44	-23
Peru		21569	0.5	-1	-3	-2	1		159	-1	0	-34	-21
Hungary		57214	-0.3	1	4	31	31		186	-11	-22	-82	-36
Poland		72211	-0.8	2	13	37	26		107	-4	-27	62	34
Romania		14678	0.7	3	5	33	26		186	-29	-38	-140	-70
South Africa		71743	-2.1	3	0	3	-2		356	-31	-47	-47	-11
Turkey		7856	-0.2	5	-7	81	43		364	-29	-36	-147	-76
Ukraine		507	0.0	0	0	-2	-2		3427	-184	-288	-1060	-652
EM total		39	-0.4	5	2	7	2		390	-15	-25	-48	14

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

back to top