GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

THURSDAY, OCTOBER 10, 2019

- **China-US trade negotiations continue to fuel market volatility** (link)
- **Possible disagreements within the ECB Governing Council are in focus** (link)
- **Inflows into US money market assets continue** (link)
- **Bank of Thailand set to relax capital flow rules** (link)
- **Vietnam's credit rating under review for possible downgrade** (link)
- **EM high-yield corporate defaults on track to be lowest in a decade** (link)

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Anxiousness Regarding Trade Negotiations Add to Market Jitters

Market action continues to be driven mainly by news surrounding China-US trade negotiations. Overnight announcements downplaying expectations regarding the meetings in Washington that start today were soon replaced by news of a potential interim agreement on less-contentious issues. One that paves the way for a more comprehensive agreement on core issues down the road. There were also reports of a possible currency pact between the two countries, although details remain sketchy. Markets were whipsawed by the news flow, with US equity futures dropping by as much as 1.5% in early trading before retracing most their losses. Action in Asia has been mixed, with Chinese equities posting slight gains today (around 1%) while markets in Korea and Taiwan have traded on the weaker side. On the aggregate however, risk assets have mostly traded sideways, with investors' attention clearly focused on developments in Washington over the next two days.

Key Global Financial Indicators

Last updated: 10/10/19 9:10 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		2919	0.9	1	-2	5	16
Eurostoxx 50		3461	0.0	1	-1	6	15
Nikkei 225		21552	0.4	1	1	-8	8
MSCI EM		41	0.3	1	-2	3	4
Yields and Spreads					bps		
US 10y Yield		1.60	5.5	7	-13	-156	-108
Germany 10y Yield		-0.51	4.3	9	4	-106	-75
EMBIG Sovereign Spread		346	-4	-6	14	-8	-68
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		60.3	-0.1	0	-1	-2	-3
Dollar index, (+) = $ appreciation		98.8	-0.3	0	0	3	3
Brent Crude Oil ($/barrel)		58.8	0.8	2	-6	-29	9
VIX Index (%, change in pp)		19.2	0.5	0	4	-4	-6

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

United States

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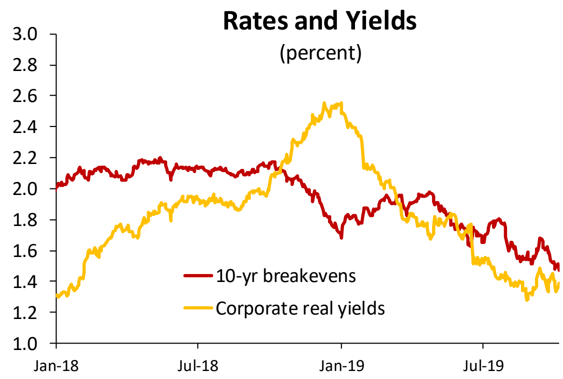
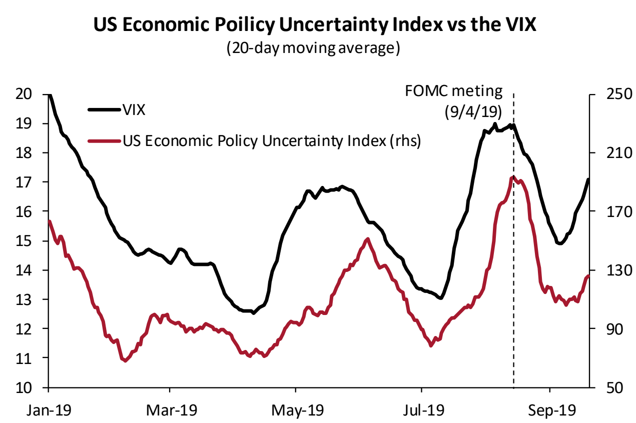
Trade headlines continue to provide market guidance. US stock markets recovered somewhat from recent losses Wednesday, rising throughout most of the session on optimism a partial trade deal between China and the US might be in the offing. But there was some late selling after Reuters reported that Chinese leaders had lowered expectations of significant progress this week. Tech markets (+1%) outperformed. And the luster was off safe havens today, as the 10-year Treasury yield rose 5 bps to 1.58%, but is down 30 bps since September 13th. Inflation expectations as measured by the 10-year breakeven remain below 1.5%. In the investment-grade corporate bond universe, CreditSights finds that real yields have been falling steadily all year, from 2.54% at the start of 2019 to 1.39% currently. It notes the post-crisis yields have been averaging 1.50%.



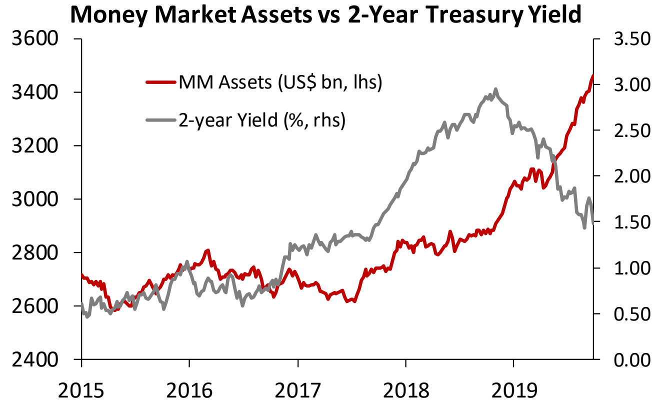
Source: Bloomberg; ICE Data Indices

FOMC minutes out yesterday provided that "downside risks to the outlook for economic activity had increased somewhat since the July meeting, particularly those stemming from trade policy uncertainty and conditions abroad." St. Louis president Bullard voted for a steeper rate cut of 50 bps, while two others voted to keep rates unchanged. Projections on the most favorable rate path evidence that policy makers were almost evenly divided between those advising it was a mistake to cut rates (5) that the reduction was enough for the year (5), and that a decrease before December was warranted (7). Market expectations of an October rate cut were little changed at 78% in reaction, but the ebb and flow of trade tensions and policy uncertainty have been driving market volatility.



Source: Bloomberg

Money market assets have been rising sharply this year. Assets outstanding now total $3,463 tn, and have added some $423 bn so far this year. This marks a 14.0% increase and is somewhat unusual given that short-term yields have been falling. The inflow into money market funds has been partly driven by investor and corporate flight to safety as rising global uncertainty—driven by escalating trade tensions, Brexit developments, US impeachment proceedings and other political developments—has dampened risk sentiment. Great risk aversiveness has also been reflected in the rally of US Treasuries, with 2-year and 3-year T-Bill yields falling by 42 bps and 75 bps, respectively, from their recent highs in May.



Source: Bloomberg, Investment Company Institute

CPI data out this morning came in a little below expectations for September. Headline CPI was flat (vs +0.1% expected) while core CPI was up 0.1% (vs +0.2% expected). This should give more cushion to a prospective rate cut in October. A 1.6% m/m drop in used car prices weighed on the releases.

Europe

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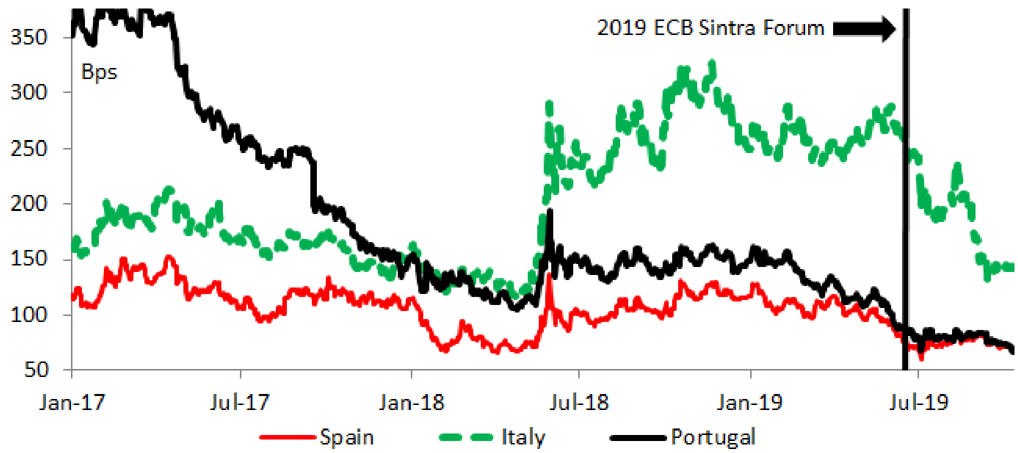
European Central Bank

Core sovereign debt yields backed up 2-3 bps and the euro (+0.5%) firmed against the USD as potential disagreements within the ECB Governing Council on the September package remain a focal point. Three members of the ECB Governing Council (so three national central bankers) confirmed to the FT that **the ECB's monetary policy committee, staffed with technocrats of the national banks, advised against resuming QE ahead of the September meeting**. The committee's opinion is non-binding, and the ECB Governing Council has decided differently at least 4 times during the tenure of President Draghi. The FT also reported that the **ECB's legal committee** warned that it could be harder for the ECB to defend itself from EU rules prohibiting monetary financing if the ECB was forced to raise the self-imposed limits on its QE program. **Finnish central bank governor Rehn** called the FT article "greatly exaggerated," adding that the ECB still has some time before hitting the limits on its QE program. He did admit that the split on recent decisions has some effect on policy. Governor Rehn also reiterated that tiering provides more space for rate cuts if needed. German 10-year yields are -0.52% (+3 bps); French 10-yr OAT yields traded at -0.19% (+3 bps); Italian 10-yr BTP yield at 0.91% (+2 bps).

Portugal

Demand for Portuguese bonds has been strong as PM Costa indicated that the formation of a stable government is very likely. Yesterday Portugal sold €750 mn of 15-yr bonds at 0.50% (compared to 0.68% on 11 Sep for the same bonds). Contacts also point to strong demand following that auction. Portugal 10-Year bonds trade at a spread of 67 bps over Bunds, compared to a spread of 70 bps for Spain and 143 bps for Italy.

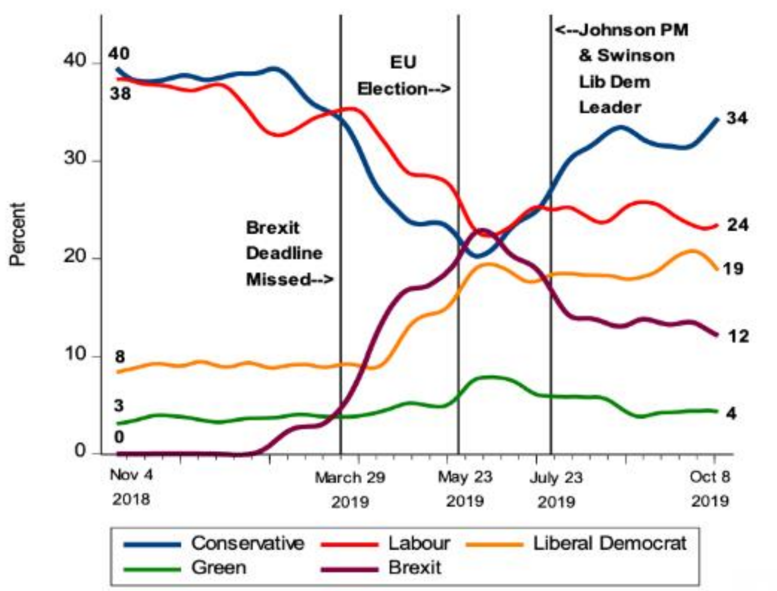
Euro area: 10-year spread over German bunds (bps)



Source: Bloomberg and IMF staff

United Kingdom

The British pound gained +0.4% against the USD ahead of a meeting between PM Johnson and PM Varadkar as UK parties prepare for elections. Labour will support a general election on November 26 if Brexit is not delivered in October. **A UK poll of polls g**ives the Conservatives a 34% voting share, Labour 24%, the Liberal Democrats 19%, the Brexit Party 12% and the Greens 4%. Analysts believe that such numbers would likely deliver a small conservative majority. UK stocks were little changed.



Italy

Yesterday's Eurogroup recommended Bank of Italy's deputy governor Fabio Panetta to replace outgoing ECB board member Benoit Coeuré. There were no indications of a potential replacement for Sabine Lautenschlager.

Other Mature Markets

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Japan

The yen held steady while equities recovered most of their losses amid conflicting headlines on the U.S.-China trade negotiation. The TOPIX ended the day unchanged while the Nikkei rose 0.5%. Meanwhile, a sharp decline in machinery orders in August, the largest in nearly 5 years, added to concerns that Japan's growth momentum could be faltering. Core machinery orders fell 14.5% y/y, suggesting growing caution about future investment plans among corporates.

Emerging Markets

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EMEA markets were mixed, with small moves in equities. Currencies mostly appreciated to the dollar, by about 0.2%-0.4%. **Latin American** markets were mixed on Tuesday, with Brazil (+1.3%) likely benefitting from expectations of significant further policy easing. In **Latin America**, Peruvian equities dropped 0.9%, while other markets were fairly flat on the day. The Brazilian real (-0.4%) weakened after a soft inflation print, while Mexico's peso gained 0.3% despite weak inflation data as well, perhaps due to increased market optimism about eventual passage of the USMCA. Bond yields across the region were mixed with little movement, though Ecuador's benchmark 2029 dollar bond yield eased around 12 bps, after President Moreno announced he was returning to the capital, Quito, after previously leaving over reported fears about a potential coup. In **Asia**, assets traded in a volatile session and ended the day mixed, buffeted by contrasting headlines on progress in the U.S.-China trade negotiations. In the currencies space, the offshore CNH appreciated 0.15% and the onshore CNY gained 0.07%, whereas the Philippine peso paced gains (+0.3%) and the South Korean won (-0.2%) underperformed. In equities, Chinese bourses outperformed (Shanghai Composite: +0.8%; Shenzhen: +1.4%) while most other Asian bourses suffered modest losses.

Key Emerging Market Financial Indicators

Last updated:	Level		Change				
10/10/19 9:08 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		40.65	0.3	1	-2	3	4
MSCI Frontier Equities		28.01	0.3	0	-1	2	7
EMBIG Sovereign Spread (in bps)		345	-5	-7	13	-9	-69
EM FX vs. USD		60.33	-0.1	0	-1	-2	-3
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		7.13	0.1	0	0	-3	-3
Indonesian Rupiah		14152	0.2	0	-1	7	2
Indian Rupee		71.07	0.0	0	1	4	-2
Argentine Peso		58.53	-0.9	-1	-4	-36	-36
Brazil Real		4.13	-0.4	-1	-1	-9	-6
Mexican Peso		19.56	0.1	0	0	-2	0
Russian Ruble		64.73	0.3	1	1	3	8
South African Rand		15.16	0.1	0	-3	-3	-5
Turkish Lira		5.89	-0.4	-3	-2	3	-10
EM FX volatility		8.21	0.0	0.1	-0.1	-2.5	-1.6

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

Trade Tensions

China-US trade negotiations continue to fuel market volatility as reports that the U.S. is considering a currency pact with China and allowing some U.S. companies to supply non-sensitive goods to Huawei lifted sentiment late in the session. But this positive development contrasted with earlier reports about a lack of progress in deputy-level trade negotiations between the U.S. and China before the principal discussion and that Vice Premier Liu He could cut short his visit by a day. That said, any interim deal would also delay a tariff increase set for next week. The U.S. is slated to raise tariffs from 25% to 30% on about $250 bn of Chinese exports on October 15th; additional increases are set to take place on December 15th.

EM corporates

Emerging market high-yield corporate defaults are on track to be the lowest in a decade, based on research from analysts at JP Morgan. HY default rates among companies in the JP Morgan CEMBI index are only 0.8% YTD, and 1.1% among the broader EM universe. This is significantly lower than forecasts from earlier in the year. The largest increase in default rates from 2018 came in the Middle East & Africa, which is tied with Latin America in 2019 at 1.6% as the region with the highest default rates. The largest default events in 2019 have been Digicel from Jamaica ($2.9 billion), and Etihad Partners ($1.2 billion) from the United Arab Emirates, where several smaller subsidiary airlines have struggled in recent times. However, analysts believe the outlook for 2020 may be a bit gloomier, given a material pickup in low rated maturities, and heightened concern for various Chinese and Argentine issuers.

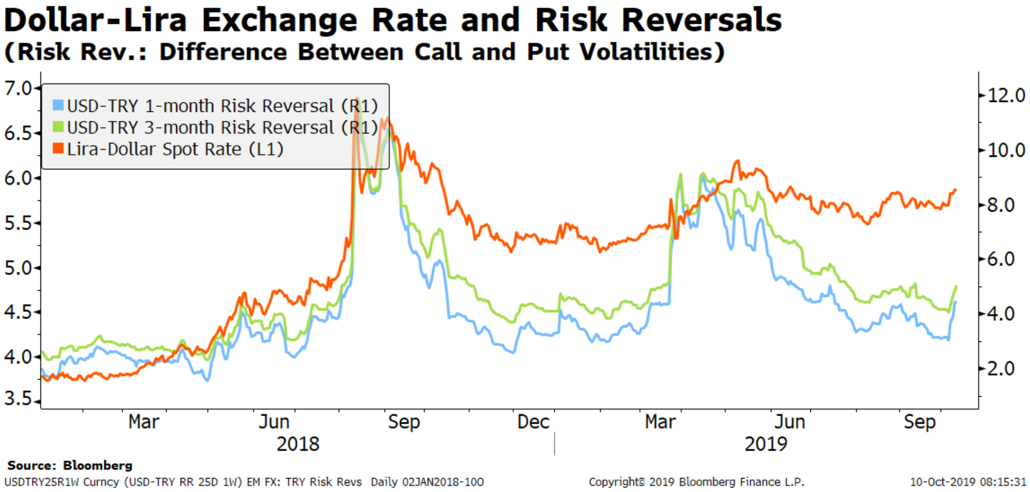
Modest default activity YTD2019

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019YTD
Asia	1.7%	0.0%	2.7%	1.2%	1.5%	3.1%	1.0%	1.0%	2.5%	1.0%
EM Europe	1.7%	0.7%	5.2%	2.3%	4.0%	2.5%	3.6%	4.0%	0.0%	0.0%
Latin America	1.8%	1.1%	3.6%	10.6%	6.5%	5.7%	9.2%	2.0%	2.1%	1.6%
ME&A	0.4%	0.0%	0.2%	0.0%	4.6%	4.0%	5.7%	3.2%	0.0%	1.6%
% EM HY	**1.6%**	**0.6%**	**3.5%**	**4.3%**	**3.8%**	**3.8%**	**5.1%**	**2.3%**	**1.6%**	**1.1%**

Source: J.P. Morgan. Based on par value of defaulted bonds and excluding 100% quasi-sovereigns.

Turkey

Turkish assets traded amid increased volatility as the nation's military incursion into Syria continues. Stocks zigzaged today and were 0.1% higher at the time of writing, amid changing investor sentiment. The lira was flat but has reportedly been propped by FX sales by Turkish state owned banks. Risk-reversals point to mounting bearishness against the lira in coming weeks.



Romania

The Romanian PM may face a no-confidence vote today. Socialist premier Viorica Dancila could be subject to a no-confidence motion as the opposition Liberal Party has garnered 237 signatures to present the motion today in parliament. To succeed the motion will require 233 actual votes. Most analysts expect the current government to succumb to the no-confidence motion. Separately, Q4 GDP data came in matching expectations, with growth at 4.4% y-o-y. **The Romanian leu traded 0.3% stronger to the dollar today**, in line with peers in the region.

Thailand

The Bank of Thailand will relax capital flow rules to blunt the baht's appreciation. Over the next month or so, the central bank will allow greater leeway for Thais to invest abroad and permit exporters to park money overseas. The Bank of Thailand had lowered interest rates by 25 bps to 1.5% in August as it sought to slow the baht ascent. Deputy Governor Supapongse noted on Thursday that the central bank could cut interest rates further if necessary. The baht lost 0.3%, pulling back from its strongest level against the dollar reached earlier in the day. The currency has gained 7.3% so far this year, making it the best performing currency among its Asian peers.

Vietnam

Moody's Investors Service placed Vietnam's credit rating under review for downgrade, citing "institutional deficiencies." The country's current Ba3 rating for its local and foreign currency issues is to be reviewed within 3 months. Moody's cited delayed payments on a government obligation as a concern and will assess "practices and systems the government has or is instituting, to ensure reliable, timely, and smooth payment of all obligations." Moreover, Moody's noted that although Vietnam's credit profile is supported by its strong growth potential, it is also exposed to climate change risks and has limited fiscal buffer against these risks. The Vietnamese dong was unchanged at VND 23,201/dollar on the day.

Brazil

Brazilian consumer price inflation moderated to 2.9% y/y and -0.04% m/m, likely clearing the way for further policy easing. Analysts had expected inflation to print 3.0%, but the weaker than expected September figure, below the midpoint of the inflation target (3.5%), alongside still sluggish domestic demand should help confirm expectations of a substantial rate cut. After a 50 bp cut in September, interest rate futures are pricing in 100 bps of easing over the next 6 months, with analysts suggesting a 50 bp cut at the October 30th meeting as close to a foregone conclusion. The real weakened close to 0.4 % against the dollar on the day, while Brazilian stocks were up over 1%.

Mexico

Mexican inflation slows to slowest annual rate since 2016 in September at 3.0% y/y, 0.3% m/m. Core inflation remained fairly steady at 3.8% y/y, while energy prices dropped -3.1% y/y and food prices rose 3.0% y/y. The central bank lowered the policy rate by 25 bps in consecutive meetings in August and September, and analysts expect another cut at the November meeting given stagnating economic growth (0.5% in 2019).

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Global Financial Indicators

Last updated: 10/10/19 9:11 AM	Level Last 12m	Level Latest	Change 1 Day	Change 7 Days	Change 30 Days	Change 12 M	YTD
Equities					%		%
United States		2919	0.9	1	-2	5	16
Europe		3461	0.0	1	-1	6	15
Japan		21552	0.4	1	1	-8	8
China		2948	0.8	1	-2	8	18
Asia Ex Japan		66	0.7	1	-2	3	4
Emerging Markets		41	0.3	1	-2	3	4
Interest Rates					basis points		
US 10y Yield		1.60	5.5	7	-13	-156	-108
Germany 10y Yield		-0.51	4.3	9	4	-106	-75
Japan 10y Yield		-0.20	-0.3	-1	2	-36	-21
UK 10y Yield		0.51	5.2	4	-13	-122	-77
Credit Spreads					basis points		
US Investment Grade		131	-0.1	0	-3	30	-17
US High Yield		478	-1.5	-19	27	125	-43
Europe IG		57	-0.3	-2	8	-14	-30
Europe HY		249	-3.1	-4	6	-40	-103
EMBIG Sovereign Spread		346	-4.0	-6	14	-8	-68
Exchange Rates					%		
USD/Majors		98.77	-0.3	0	0	3	3
EUR/USD		1.10	0.5	1	0	-4	-4
USD/JPY		107.6	-0.1	-1	0	4	2
EM/USD		60.3	-0.1	0	-1	-2	-3
Commodities					%		
Brent Crude Oil ($/barrel)		59	0.8	2	-6	-29	9
Industrials Metals (index)		116	1.0	1	-2	-3	6
Agriculture (index)		39	0.1	0	5	-9	-6
Implied Volatility					%		
VIX Index (%, change in pp)		19.2	0.5	0.0	4.0	-3.8	-6.3
10y Treasury Volatility Index		5.2	0.0	-0.2	0.0	0.7	0.6
Global FX Volatility		7.0	0.0	-0.2	0.0	-1.3	-1.9
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		196	-1.5	1	-24	-196	-220
Italy		143	1.1	1	-14	-153	-107
Portugal		66	-2.1	-7	-17	-75	-82
Spain		70	-0.3	-2	-11	-36	-48

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: 10/10/2019 9:09 AM	Exchange Rates: Level, Last 12m	Level, Latest	Change (in %), 1 Day	7 Days	30 Days	12 M	YTD	Local Currency Bond Yields (GBI EM): Level, Last 12m	Level, Latest	Change (in basis points), 1 Day	7 Days	30 Days	12 M	YTD
		vs. USD	(+) = EM appreciation						% p.a.					
China		7.13	0.1	0.3	0	-3	-3		3.2	-1.1	-1	11	-43	-1
Indonesia		14152	0.2	0.1	-1	7	2		7.4	2.4	2	-2	-127	-79
India		71	0.0	-0.3	1	4	-2		6.8	-0.6	-4	8	-139	-67
Philippines		52	0.3	0.3	1	5	2		4.3	-1.3	-3	-5	-225	-198
Thailand		30	-0.2	0.5	1	8	7		1.5	-1.3	-3	-15	-146	-114
Malaysia		4.19	0.2	-0.1	0	-1	-1		3.4	0.5	1	5	-69	-69
Argentina		59	-0.9	-1.3	-4	-36	-36		57.4	-174.6	-894	-835	3411	3436
Brazil		4.13	-0.4	-1.1	-1	-9	-6		6.2	-11.6	-18	-48	-292	-196
Chile		722	0.3	-0.7	-1	-5	-4		2.7	0.7	-10	7	-209	-173
Colombia		3468	0.0	-0.5	-3	-11	-6		5.6	0.4	-3	-10	-103	-89
Mexico		19.56	0.1	0.5	0	-2	0		6.8	-4.0	-14	-31	-130	-188
Peru		3.4	0.4	0.6	-1	-1	0		4.2	-8.0	-23	-10	-153	-152
Uruguay		37	-0.1	-0.3	-2	-11	-13		10.9	10.5	23	-1	44	21
Hungary		303	0.7	0.2	-1	-7	-7		1.0	1.3	-7	-22	-178	-117
Poland		3.92	0.6	0.9	0	-4	-5		1.7	1.4	-8	-17	-94	-56
Romania		4.3	0.4	0.4	-1	-6	-6		3.8	1.0	2	7	-80	-43
Russia		64.7	0.3	0.6	1	3	8		6.7	-2.6	-18	-18	-184	-172
South Africa		15.2	0.1	-0.1	-3	-3	-5		9.3	-4.4	-4	6	-44	-25
Turkey		5.89	-0.4	-3.4	-2	3	-10		14.1	44.7	70	-106	-782	-277
US (DXY; 5y UST)		99	-0.3	-0.1	0	3	3		1.41	0.8	6	-18	-159	-110

	Equity Markets: Level, Last 12m	Level, Latest	Change (in %), 1 Day	7 Days	30 Days	12 M	YTD	Bond Spreads on USD Debt (EMBIG): Level, Last 12m	Level, Latest	Change (in basis points), 1 Day	7 Days	30 Days	12 M	YTD
									basis points					
China		2948	0.8	1	-2	8	18		191	-3	2	4	3	-3
Indonesia		6024	-0.1	0	-5	3	-3		185	-4	-10	16	-13	-51
India		37880	-0.8	-1	2	9	5		135	0	0	-1	-30	-61
Philippines		7765	1.1	3	-2	11	4		81	-3	-7	16	-26	-40
Malaysia		1552	0.0	-1	-3	-11	-8		127	-4	-1	4	-2	-35
Argentina		30338	0.3	-1	7	6	0		1979	-33	-213	-115	1278	1164
Brazil		101249	1.3	0	-2	21	15		246	-1	-9	22	-25	-27
Chile		5035	-0.2	1	3	-4	-1		138	-1	-10	12	14	-28
Colombia		1589	0.0	0	1	7	20		187	2	-7	10	6	-41
Mexico		42502	-0.1	1	0	-12	2		319	-3	-8	-10	54	-35
Peru		19060	-0.9	0	-1	-1	-2		129	-2	-9	21	-14	-39
Hungary		39382	-0.4	0	-1	7	1		105	2	-8	25	-12	-43
Poland		55925	-0.6	1	-3	-2	-3		40	1	-12	24	-23	-45
Romania		9500	-0.2	1	3	12	29		198	-4	-4	7	24	-23
Russia		2710	-0.1	0	-3	12	14		201	1	-5	15	-23	-51
South Africa		54616	0.5	2	-1	3	4		338	-1	-10	38	8	-27
Turkey		98546	-1.1	-4	-3	4	8		509	14	24	5	31	80
Ukraine		527	0.1	0	0	-4	-6		514	2	-25	64	-48	-273
EM total		41	0.3	1	-2	3	4		345	-5	-7	13	-9	-69

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

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