GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

TUESDAY, OCTOBER 12, 2021

- **Analysts expect Fed to taper in November after U.S. jobs reports** (link)
- **U.S. dollar trades at year-to-date highs** (link)
- **EU places its inaugural green bond amid strong investor demand** (link)
- **U.K. rate hike expectation reach cycle high** (link)
- **Forecasts for inflation and policy rate continue to shift higher in Brazil** (link)
- **Bank of Korea signals another hike is likely in November** (link)
- **Czech inflation accelerates more than expected in September** (link)

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Markets price in further tightening

U.S. yields and the U.S. dollar consolidated at higher levels after the U.S. jobs report. Analysts believe the Fed remains on track to taper in November even though the report's headline number disappointed. Inflation data everywhere remains in focus as traders are pricing in more tightening across the world. Traders are pricing in a full hike by the Fed in 2022Q4 and expect 20 bps of tightening by the Bank of England by the end of this year. The Bank of Korea left rates unchanged but signaled that another likely is likely in November. More hikes are also expected in the Czech Republic after inflation accelerated more than expected in September. The EU's inaugural common green bond under the NGEU program saw very strong demand.

Key Global Financial Indicators

Last updated: 10/12/21 12:28 PM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		4361	-0.7	1	-2	23	16
Eurostoxx 50		4058	-0.3	0	-3	23	14
Nikkei 225		28231	-0.9	1	-7	20	3
MSCI EM		51	-0.2	2	-3	10	-2
Yields and Spreads					bps		
US 10y Yield		1.59	-1.7	7	25	82	68
Germany 10y Yield		-0.13	-1.2	6	20	41	44
EMBIG Sovereign Spread		358	1	-4	19	-52	8
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		55.0	0.1	-1	-3	0	-5
Dollar index, (+) = $ appreciation		94.3	0.0	0	2	1	5
Brent Crude Oil ($/barrel)		84.0	0.4	2	15	101	62
VIX Index (%, change in pp)		19.7	-0.4	-2	-1	-5	-3

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

Inflation data will be watched closely this week, including the September U.S. CPI (Wednesday) and University of Michigan inflation expectations (Friday). Minutes from the September FOMC meeting will be released on Wednesday. The Bank of Korea meets on Tuesday (no change expected), and Chile is expected to hike by 75bps to 2.25% (Wednesday). Meanwhile, the US Q3 earnings season kicks off with the banks first to report.

Mature Markets

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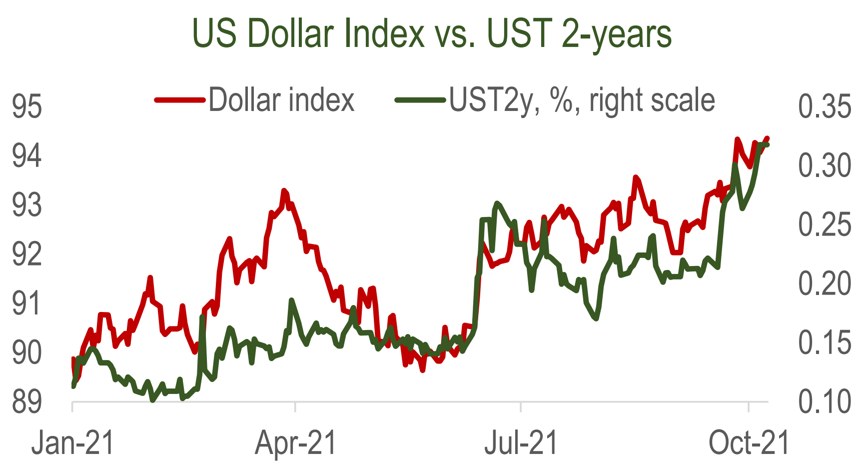
United States

Equities finished last week 0.8% despite higher energy prices and the weak job report headline. Lawmakers agreed to extend the debt ceiling until December 3 in the middle of the week to avoid a default for the next two months. Meanwhile, higher commodity prices fueled inflation fears, weighing on the markets: WTI oil futures were up 4.9% for the week. **On Monday, the futures price continued to rise to $82 a barrel, the highest since 2014. S&P 500 was down -0.7% for the day, and VIX rebounded to above 20.**

Most market participants expect the Fed to start tapering in November after Friday's job report. Market participants saw it as a strong report except for the headline: The August revision was significant; the unemployment rate fell to 4.8% (vs. 5.1% expected) on a fall in the participation rate; average hourly earnings were also above consensus. **Overall, analysts believe the Fed remains on track to taper at the November meeting, although some see that the headline net gain below 200k is at the low end of the range of what the FOMC could tolerate**. 10-yr rates closed higher on Friday at 1.61%. Eurodollar futures Dec 2023 contract implied yield initially fell by 4bps to 1.16% but then went up by 8bps to 1.24%. The Dec 2023 yield continued to go higher Monday, reaching 1.28%. Bond markets were closed Monday for the Columbus Day holiday.

U.S. dollar nears year-to-date high. Markets have been nervous about stagflation linked to Chinese growth concerns, supply constraints, rising energy prices, and a rapid move higher in US yields. Analysts see the key driver of the dollar in the near term will be U.S. yields. For the medium-term horizon, a focus is on China, where both the growth and credit outlook is in question.



Source: Bloomberg

Japan

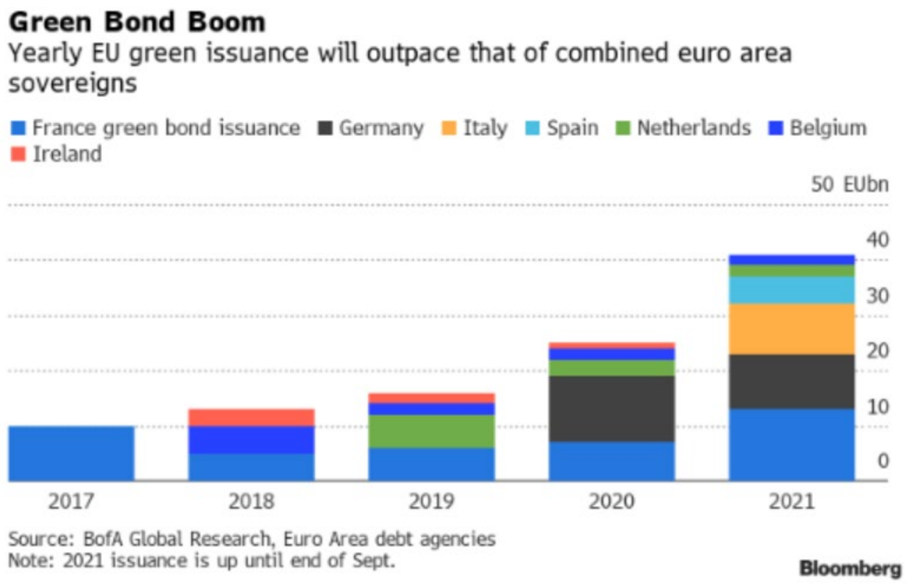
Producer prices increased more than expected in September. Producer price inflation edged up to 6.3% y/y from 5.5% in August (consensus: +5.8%). Analysts noted that corporate profit margins have narrowed as firms have been reluctant to pass their higher costs on to consumers, who are sensitive to price increases after years of deflation and stagnant wages; consumer prices largely remain flat. **PM Kishida vowed to narrow disparities in the society** by adopting policy measures that raise people's income. He wants to strengthen tax incentives for firms that raise wages (a policy introduced by Abe) and increase pay for public workers. Equities declined (NIKKEI: -0.9%); Japanese yen and long-end JGB yields were little changed after the yen depreciated 1% yesterday.

Europe

European equity markets have lacked cleared direction this week amid a bearish bias**.** Stock indices dropped by 1% this morning but managed to recover most of their losses with STOXX 600 trading nearly unchanged on the day. Energy shares (-1%) and metals (-1%) were underperforming today.

European sovereign bond yields are lower by 1 bps with Italian spreads 2 bps tighter. German bund yields are close to year-to-date highs with 10-year real yield rising about 10 bps in a week, despite the ongoing dovish communication by the central bank. ECB's Philipp Lane once again stressed the transitory nature of current price growth on Monday, noting that one-off wage rises would not constitute a sustained rise in inflation.

The EU placed its first common green bond under the NGEU program. The inaugural placement of €12 bn was well above analyst's expectation from few weeks ago and was met with more than €135 bn of investor interest. The 15-year security was placed 3 bps inside the initial guidance at mid-swap less 8 bps. **Contacts estimate the initial greenium (green bond premium) at around 1-2 bps** but expect an increase to around 5 bps or more in line with greenium seen for German securities.



On the data front, **German ZEW surprised to the downside** with both current assessment (-10 points) and expectations falling below consensus estimates with expectations indicator now back at Q2 2020 level.

United Kingdom

BoE rate hike expectations rose in response to hawkish comments of MPC members. The sterling curve is now pricing 50% chance of a November rate hike and a total of 20 bps of tightening by the end of this year, compared to 13 bps priced last week. The shift in expectations comes as the **Bank of England's MPC member Saunders suggested that markets are underpricing the size of the December move**. This followed Governor Bailey's remarks that there could be a damaging period of inflation if policy makers did not react. **Some contacts have pointed out that more dovish leaning MPC members are yet to speak this week and may counter Saunders's view. It is worth noting that the latest Deutsche Bank investors survey reveals that market participants are concerned with a hawkish policy mistake by the BoE.**

The UK labor market continued to recover in August. The unemployment rate edged lower to 4.5% in line with consensus, while wage growth was somewhat stronger at 7.2% 3m/yr. The payroll numbers have now returned to the pre-pandemic levels while job vacancies are about 30% above the pre-Covid levels. Analysts point out that labor market remains somewhat tighter than BoE's projections.

Emerging Markets back to top

Asian equities declined, -1.6% on net, led by Hong Kong (-1.4%), Korean (-1.4%) and Chinese (CSI 300: -1.1%) equities. Share prices rose in Malaysia (+0.8%) and Thailand (+0.6%). Investor sentiment was affected by concerns around elevated global inflation and a widening credit crunch in China's real estate sector. **Asian currencies generally depreciated**, led by Korean won (-0.3%) and Taiwan dollar (-0.3%). Thai baht appreciated (+1.3%) as the government unveiled a roadmap to revive tourism by gradually removing the mandatory quarantine for vaccinated visitors. Long-end government bond yields were mixed, with 10-year yields rising in Korea (+6.2 bps) while falling in Malaysia (-5.8 bps). **EMEA equities markets were mixed with markets underperforming in South Africa (-0.6%), Poland (-0.5%) and Russia (-0.3%). Currencies were mixed, trading in a narrow range.** The Turkish lira is little changed but fell to a record low of 9.0/$ yesterday, extending losses since the interest rate cut in September. The currency was also weighed down by increased regional tensions after President Erdogan's warned that Turkey will eliminate threats emanating from Syria. Romanian 10-yr bond yields (+2 bps) continue to head higher after inflation unexpectedly accelerated to 6.3% y/y (5.8% consensus) in September from 5.3% in August. **Latin American equities printed mixed while currencies depreciated.** Stocks rallied in Chile (0.4%) and Mexico (1.0%) and slumped in Brazil (-0.6%). Meanwhile, currencies depreciated in Brazil (-0.5%), Colombia (-0.1%), and Mexico (-0.8%).

EM Fund Flows

EM bond funds saw weekly outflows while EM equity reverted to inflows. EM bond outflows printed at -$1.3bn, mostly from hard currency bond funds (-$1.3bn) as local currency bond funds were essentially flat ($9mn), with China local currency bond funds printing at $0.1bn. On the other hand, EM equity funds inflows jumped to $1.2bn, from -$975mn last week. Within the regional equity funds, outflows were seen across Asia ex-Japan (-$127mn), Latin America (-$132mn), and EMEA (-$10mn).

China

Beijing wants Washington to stop restrictions and sanctions on Chinese firms. China's ambassador to Washington made the statement in response to U.S. Trade Representative Tai's outlining of Washington's demand for the trade discussion with China. Ambassador Qin also noted that restrictions due to national security are unfair and warned of serious consequences if this practice continues. **China starts an inspection of financial regulators and large state-owned banks, insurers and bad-debt managers** for the first time since 2015. The Central Commission for Discipline Inspection will carry out the inspection. Reportedly the inspection will focus on checking for gaps in political awareness among the party leaders of the organizations and problems that hinder the high-quality development of the financial industry. Some analysts noted that this inspection may bring about uncertainty and create a cloudy outlook for financial firms. **Evergrande reportedly missed interest payments due yesterday for its three offshore bonds.** Trading of its equities remains suspended; its bond prices were little changed. **Equities declined (CSI 300: -1.1%); RMB was little changed. Interbank repo rates were mixed** (overnight: +4.8 bps; 7-day: -3.1 bps); the People's Bank of China withdrew net liquidity of 90 bn yuan ($14 bn).

Korea

The Bank of Korea (BOK) kept the policy rate at 0.75% as expected, as contacts expect a rate hike in November. The decision to hold rates at 0.75% was not unanimous, with two dissenting votes for a back-to-back increase following the liftoff in August. **Governor Lee Ju-yeol provided a strong signal for**

a rate hike in November as he flagged worsening financial imbalances, growing inflationary pressures and solid recovery momentum. He also commented financial conditions remain accommodative and that businesses and households should be able to withstand another rise to 1%. The BOK also maintains a relatively upbeat growth forecast of 4% for 2021 while expecting CPI inflation at mid-2% (exceeding the BOK's target) for a period of time. Government bond yields rose (1-year: +2.3 bps; 10-year: +6.2 bps) as markets expect another rate hike in November. The Korean won depreciated (-0.3%); equities declined (-1.4%).

Czech Republic

Bond yields reached their highest level since 2012 after inflation unexpectedly accelerated to 4.9% y/y in September (4.6% consensus, from 4.1%). While price increased were broad-based, utilities such as housing and transportation costs were the main driver. Inflation rates have remained above the central bank's target for 33 months. Markets expect that the benchmark rate will increase by another 50 bps this year. On the political front, centre-right opposition group Together beat the ANO party of PM Babis in a surprise parliamentary election result on Saturday.

Czech Republic: Yields and exchange rate

Source: Bloomberg and IMF calculations

Poland

The Polish banking lobby ZBP expressed concern over banks' sovereign exposure following the recent increase in yields. Polish 10-yr yields rose 27 bps to 2.54% after the central unexpectedly hiked interest rates 40 bps last week. Polish banks hold roughly a third of the country's sovereign bonds, amounting to a fifth of banks' assets.

Egypt

Headline inflation increased to a 20-month high (6.6% y/y) in September, primarily driven by higher food inflation (+10.6% y/y). Core inflation accelerated to 4.8% y/y from 4.5% in August. The central bank meets on 28 October and has kept its deposit rate unchanged at 8.25% and its lending rate at 9.25% as inflation continue to be within the 5-9% inflation target zone. **Contacts expect the central bank to deliver a first hike in 2022Q1 if inflation accelerates further. Relatively high real rates have supported elevated foreign investor positioning in local markets.**

Brazil

Analysts expect higher inflation and key rate in 2022, according to a central bank survey. Inflation continues to gain ground in Brazil, as the annualized inflation reached 10.25% in September, breaching the double-digit threshold for the first time since 2016. **Pushed by rising fuel costs and rising demand for services, inflation and key interest rate are now expected to reach 4.14% and 8.75% at the end of 2022, up from the previous forecasts of 4.12% and 8.5%, respectively.** Since March 2021, the cumulated 425bps rate hikes have not been able to slow down inflation.

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Global Financial Indicators

Last updated: 10/12/21 12:28 PM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		4361	-0.7	1	-2	23	16
Europe		4058	-0.3	0	-3	23	14
Japan		28231	-0.9	1	-7	20	3
China		3547	-1.2	-2	-5	6	2
Asia Ex Japan		85	-0.4	2	-4	5	-5
Emerging Markets		51	-0.2	2	-3	10	-2
Interest Rates					basis points		
US 10y Yield		1.59	-1.7	7	25	82	68
Germany 10y Yield		-0.13	-1.2	6	20	41	44
Japan 10y Yield		0.09	0.2	3	5	6	7
UK 10y Yield		1.16	-2.5	8	41	89	97
Credit Spreads					basis points		
US Investment Grade		93	0.1	6	2	-35	-2
US High Yield		328	0.8	6	10	-180	-52
Europe IG		53	0.2	2	8	2	5
Europe HY		271	2.5	13	44	-36	29
Exchange Rates					%		
USD/Majors		94.33	0.0	0	2	1	5
EUR/USD		1.16	0.0	0	-2	-2	-5
USD/JPY		113.3	0.0	2	3	8	10
EM/USD		55.0	0.1	-1	-3	0	-5
Commodities					%		
Brent Crude Oil ($/barrel)		84	0.4	2	15	101	62
Industrials Metals (index)		171	0.1	5	1	43	29
Agriculture (index)		58	-0.1	0	4	43	20
Implied Volatility					%		
VIX Index (%, change in pp)		19.7	-0.4	-1.6	-1.3	-5.4	-3.1
US 10y Swaption Volatility		76.2	2.8	-0.4	10.4	5.6	12.9
Global FX Volatility		6.9	0.0	0.1	0.4	-1.7	-1.2
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		105	0.6	-2	-8	-31	-14
Italy		102	-1.4	-2	-1	-20	-9
Portugal		51	-0.9	-4	-5	-19	-9
Spain		63	-0.6	-2	-4	-6	1

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

Emerging Market Financial Indicators

Last updated:	Exchange Rates							Local Currency Bond Yields (GBI EM)					
12/10/2021	Level		Change (in %)					Level		Change (in basis points)			
12:33 PM	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	Last 12m	Latest	7 Days	30 Days	12 M	YTD
		vs. USD	(+) = EM appreciation						% p.a.				
China		6.45	0.0	-0.1	0	5	1		3.1	6	4	-25	-21
Indonesia		14218	-0.1	0.2	0	3	-1		6.3	6	19	-54	23
India		76	-0.2	-1.4	-2	-3	-3		6.4	8	10	35	49
Philippines		51	-0.1	-0.4	-2	-5	-6		4.3	-3	-2	70	65
Thailand		33	1.1	1.5	-1	-6	-10		2.0	11	25	50	66
Malaysia		4.16	0.1	0.3	0	0	-3		3.7	23	41	121	116
Argentina		99	0.0	-0.2	-1	-22	-15		48.9	-88	112	717	-723
Brazil		5.54	-0.5	-1.5	-6	0	-6		10.2	-14	-8	394	461
Chile		822	0.3	-1.3	-5	-3	-14		6.4	76	107	366	366
Colombia		3767	0.0	0.7	2	2	-9		7.3	-1	37	216	227
Mexico		20.78	0.4	-1.0	-4	2	-4		7.5	3	47	144	187
Peru		4.1	0.4	1.5	1	-12	-11		6.2	-14	-30	222	263
Uruguay		43	0.0	-1.1	-2	-2	-3		7.9	2	-2	56	65
Hungary		311	-0.2	-1.0	-5	-3	-5		3.1	6	49	148	160
Poland		3.96	0.3	0.3	-3	-5	-6		2.1	43	77	137	144
Romania		4.3	0.0	-0.5	-2	-4	-7		4.2	23	61	96	148
Russia		71.8	-0.1	0.7	1	7	3		7.4	2	44	172	166
South Africa		14.9	0.9	0.4	-5	11	-2		10.2	4	55	-12	56
Turkey		9.00	0.0	-1.5	-6	-12	-17		18.2	42	125	496	506
US (DXY; 5y UST)		94	0.0	0.4	2	1	5		1.07	9	25	73	71

	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		4884	-1.1	0	-2	1	-6		211	-2	-3	-30	-18
Indonesia		6486	0.4	3	7	26	8		184	3	11	-44	-16
India		60284	0.2	1	4	48	26		150	2	4	-57	-1
Philippines		7108	-0.2	2	2	20	0		126	6	17	-8	14
Malaysia		1584	0.8	3	1	4	-3		133	-1	5	-36	-2
Argentina		77553	0.1	0	0	71	51		1584	-9	95	227	228
Brazil		112181	-0.6	2	-2	15	-6		301	-9	8	-16	42
Chile		4146	0.0	-2	-7	13	-1		156	-2	13	-22	0
Colombia		1406	0.4	2	6	18	-2		287	-16	11	39	72
Mexico		51647	1.0	2	0	35	17		349	-7	12	-118	-8
Peru		19586	1.1	8	11	9	-6		167	-14	-3	7	38
Hungary		54645	0.4	2	4	65	30		114	-5	-19	-41	-35
Poland		74138	-0.4	3	4	51	30		24	-5	-2	-4	-4
Romania		12783	-0.1	1	3	44	30		201	-6	6	-41	-2
Russia		4264	-0.4	1	7	50	30		162	-4	-2	-55	-17
South Africa		65765	-0.5	2	2	18	11		360	-14	19	-140	-24
Turkey		1419	0.2	2	-1	20	-4		496	-13	38	-132	49
Ukraine		526	0.0	0	0	3	5		516	-14	36	-177	23
EM total		51	-0.5	2	-3	10	-2		375	-4	24	-25	36

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

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