GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

MONDAY, SEPTEMBER 13, 2021

- **Debt ceiling uncertainty may impact the US Treasury market** (link)
- **UK expected to announce a new Covid strategy** (link)
- **EM bond and equity funds saw strong inflows last week** (link)
- **Chinese equities underperform on additional regulatory tightening** (link)
- **Interest rate hikes in Latin America struggle to contain inflation** (link)
- **SPECIAL FEATURE: Latest Update on the EM Capital Flows (PDF attached)**

Mature Markets | Emerging Markets | Market Tables

Markets start the week mixed ahead of US CPI

Asian equities fell but European bourses rose and US equity futures signaled a positive opening this morning as market participants await the release of US CPI tomorrow. Asian shares underperformed on news of a new round of regulatory tightening in China, targeting the tech sector. Energy companies led gains in European stocks as crude oil extended a rally to a six-week high. Industrial metals also rose as supply disruptions continued, with aluminum reaching $3,000 a ton in London for the first time in 13 years. US Treasury yields were modestly lower this morning with European sovereign bond yields little changed. In the week ahead, and in addition to US CPI, final figures for European inflation data for August will be released on Tuesday and Wednesday. Central banks of Egypt and Nigeria will announce policy rates on Thursday and Friday correspondingly, with analysts expecting no changes.

Key Global Financial Indicators

Last updated: 9/13/21 1:26 PM	Level: Last 12m	Level: Latest	Change from Market Close: 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		4459	-0.8	-2	0	33	19
Eurostoxx 50		4209	0.9	-1	0	27	18
Nikkei 225		30447	0.2	3	9	29	11
MSCI EM		52	-0.1	-1	1	19	2
Yields and Spreads					bps		
US 10y Yield		1.33	-1.0	1	5	67	42
Germany 10y Yield		-0.33	-0.3	3	13	15	24
EMBIG Sovereign Spread		339	-3	0	-9	-60	-11
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		56.8	0.1	-1	1	2	-2
Dollar index, (+) = $ appreciation		92.8	0.2	1	0	-1	3
Brent Crude Oil ($/barrel)		73.4	0.6	2	4	84	42
VIX Index (%, change in pp)		19.2	-1.8	3	4	-8	-4

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

Mature Markets

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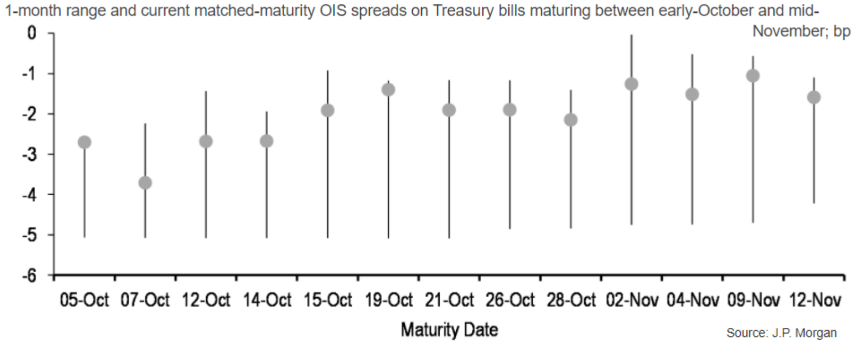
United States

On Friday, the S&P 500 index fell 0.8% amid investors' concerns about rising Covid cases, slowing growth, high current inflation, and uncertainty over the policy normalization path. The US Treasury 10-year yield rose by 4 bps, which was driven entirely to the change in real yields.

Investors are starting to price-in the possibility of a delayed congressional resolution for the debt ceiling. The US Congress is currently focused on other legislative topics (such as the infrastructure package and spending authorization for FY22) and may postpone the debt ceiling voting closer to the date of the actual depletion of Treasury's available resources, potentially causing a short-lived technical default. If it happens, such an event could lead to a sovereign rating downgrade by Fitch or Moody's and a reduction of foreign demand for US Treasury bonds. Currently, T-bills which mature in the second half of October, around the date for a potential technical default, have begun to underperform versus surrounding issues (chart below with US Treasury bills' OIS spreads) and there is still room for these tenors to underperform further, given the experience of previous debt ceiling episodes.

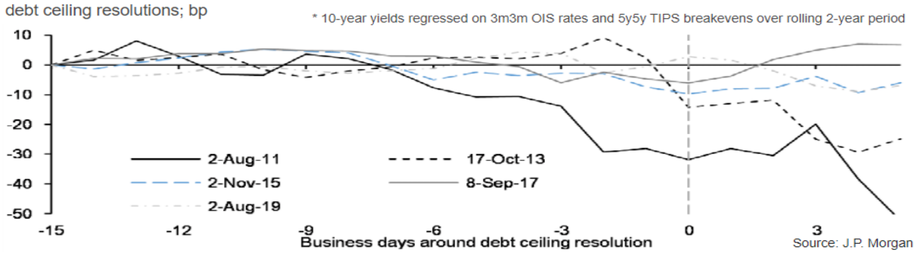
1-month range and current matched-maturity OIS spreads on Treasury bills maturing between early-October and mid-November; bp



Long-dated US Treasury yields may be impacted as well. Considering the last 5 major episodes of the debt ceiling resolution, the largest market impact was observed when the new legislation was passed only days before a potential technical default, with 2011 being the standout example. Long-dated yields are expected to decline in the event of a delay in congressional actions. As the short-lived technical default will not likely impact the long-term solvency of the sovereign, investors will be expected to switch to safe-haven long-dated Treasury bonds ahead of a potential market stress caused by the technical default. The exhibit below shows the cumulative change in 10-year Treasury yields, adjusting for the market's Fed policy and inflation expectations, in the weeks leading up to debt ceiling resolution in the previous years.

Exhibit 10: Treasury yields have tended to decline around more contentious debt ceiling debates, particularly 2011, 2013, and 2015

Cumulative change in 10-year Treasury yields, adjusted for Fed and inflation expectations*, in the business days around debt ceiling resolutions; bp

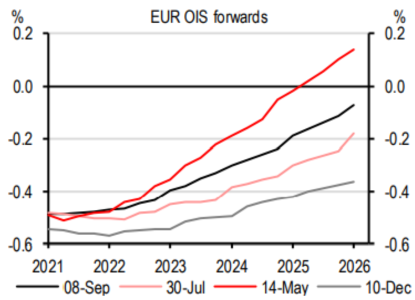


Euro-area

European stocks rose this morning with the main benchmark indices up around 1.0%. Energy shares were outperforming (+2%), benefiting from the oil price rise.

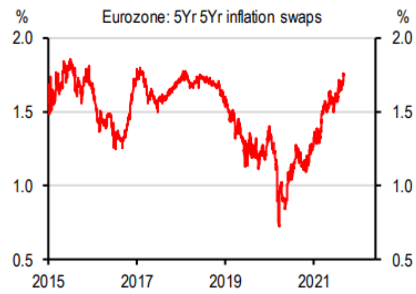
German bund yields were steady after reversing most of the post-ECB decline on Friday. By contrast, the post-ECB tightening has held in the Southern European spreads. Analysts at HSBC note that rate hike expectations rather than the pace of asset purchases programs are driving current bund valuations. The recent rise in yields comes as **markets have brought forward the first interest rate hike into 2023, as compared to 2024 after the ECB July meeting**. Analysts argue that the rise in long-term inflation expectations, measured by 5y5y inflation swaps, have been the main contributor to the market expectations shift, which now seem to be at odds with the ECB's latest forward guidance.

1. Market expectations for future rate rises have moved up again in recent weeks



Source: Bloomberg, HSBC.

2. 5yr 5yr forward inflation swap rates have risen markedly



Source: Bloomberg, HCB

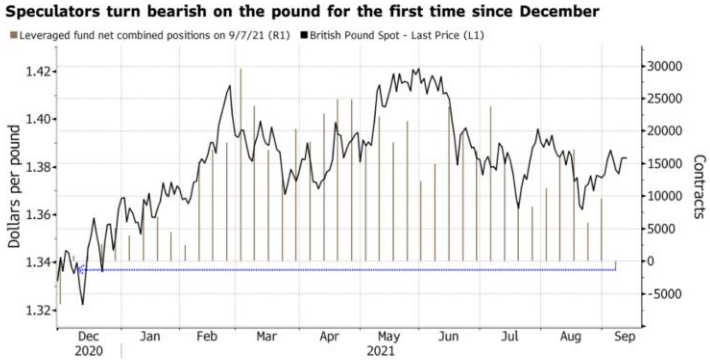
Further on fixed income, contacts note that demand for government bonds will be back in focus this week as a total of €30 bn in issuance is expected from Germany, Italy, France and Spain with also the EU looking to place common NGEU bonds after the summer break.

In Germany, **the second pre-election debate was held on Sunday**. The polls suggest that the SPD candidate and current **Finance Minister Scholz benefited with 41% of voters finding him more convincing**. The SPD has also managed to maintain its lead in the opinion polls with recent surveys putting it 4-6% ahead of the CDU/CSU union. Candidates will hold another debate on September 19.

United Kingdom

The UK is expected to announce a rehaul of its Covid-19 strategy this week. Media reports suggest that plans for mandatory vaccine passports for mass gatherings and the current traffic-light system for travel will be scrapped. Booster vaccine jabs, mandatory mask wearing indoors and guidance on working from home could be listed as main tools for managing a new Covid-19 outbreak as opposed to social distancing and lockdown measures. The UK FTSE 100 (+0.8%) was somewhat underperforming the Euro area benchmarks while the pound and UK gilts were steady. Interestingly, the latest Commodity Futures Trading Commission data suggest that **the net speculative positioning in the sterling futures has now flipped negative**, first time since December last year.

Speculators turn bearish on the pound for the first time since December



Japan

Japan's leadership rivals diverge on their views on post-pandemic economic policies. All candidates are in favor of fiscal stimulus to support the economic recovery during the pandemic, but their post-pandemic views vary. Taro Kono, who leads the poll, emphasized the need to accelerate the administrative reform and the digital transformation. In 2017, he urged the Bank of Japan to discuss about an exit strategy when inflation was around 1%. In contrast, Fumio Kishida back in 2018 advocated for the need to restore fiscal health, while Sanae Takaichi appears as the biggest proponent of aggressive monetary easing. **Producer prices remained flat m/m in August.** PPI inflation moderated to 5.5% y/y from 5.6% in July, weaker than market consensus. **Equities gained** (NIKKEI: +0.2%), outperforming regional peers. The **Japanese yen depreciated** (-0.2%) and **long-end JGB yields were mixed** (10-year: +0.3 bp; 30-year: -0.8 bp).

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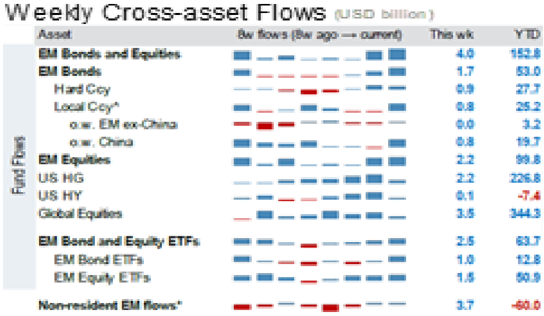
Asian equities generally declined, dropping 1.5% on net, led by Hong Kong equities (-1.5%). Asian currencies mostly depreciated, led by Thai baht (-0.7%) and Korean won (-0.6%). Long-end government bond yields rose, with 10-year yields rising in Korea (+4.6 bps), following the rise in U.S. treasury yields on Friday. China's additional regulatory tightening weighed on market sentiment, with analysts increasingly worrying about a slowdown that is partly induced by regulatory tightening (property and tech sectors). In Korea, the Korean won underperformed as North Korea successfully tested its cruise missiles over the weekend. In **EMEA, equities traded with a positive tone.** Turkish equities (+0.5%) and the lira (+0.2%) were higher after the current account deficit narrowed to $0.7 bn in July on higher tourist receipts (albeit less than expected). **The Nigerian naira fell to another record low in parallel markets**, as the central bank is investigating FX transactions of lenders operating in the country**.** Any lenders "found culpable with ongoing investigations" could have FX operating licenses suspended for at least a year. **EMEA primary markets remain active.** Nigeria plans to sell about $3 bn of Eurobonds in the second week of October. Egypt is reportedly planning to issue an inaugural-sukuk of a size of up to $1 bn in 2022H1. **Latin American equities and currencies were mixed last Friday.** Stocks rallied in Chile (1.3%) and Mexico (0.3%) but fell in Argentina (-1.6%) and Brazil (-0.9%). Meanwhile, currencies appreciated slightly in Chile (0.7%), Colombia (0.3%), and Mexico (0.2%), depreciated in Brazil (-0.8%), and remained essentially flat in Argentina.

EM Fund Flows

EM bond and equity funds saw strong inflows last week. EM bond inflows printed at $1.7 bn (the highest level in 10 weeks), split between hard currency bond inflows ($0.9 bn) and local currency bond funds ($0.8 bn) Within local currency bond funds, inflows were almost entirely into China-related bond funds (+$768 mn), which had their largest inflow in six weeks, as EM ex-China bond fund flows were flat (+$17mn). On the other hand, EM equity funds inflows reached $2.2 bn, breaching the $2 bn threshold for the first time since early June. Within regional equity funds, Asia ex-Japan saw significant inflows ($1.7 bn) while EMEA had outflows (-$35mn) and Latam had modest inflows (+$137mn).


Weekly Cross-asset Flows (USD billion)

	Asset	8w flows (8w ago → current)	This wk	YTD
Fund Flows	**EM Bonds and Equities**		4.0	152.8
	EM Bonds		1.7	53.0
	Hard Ccy		0.9	27.7
	Local Ccy*		0.8	25.2
	o.w. EM ex-China		0.0	3.2
	o.w. China		0.8	19.7
	EM Equities		2.2	99.8
	US HG		2.2	226.8
	US HY		0.1	-7.4
	Global Equities		3.5	344.3
	EM Bond and Equity ETFs		2.5	63.7
	EM Bond ETFs		1.0	12.8
	EM Equity ETFs		1.5	50.9
	Non-resident EM flows*		3.7	-60.0

*High frequency non-resident EM portfolio flow data

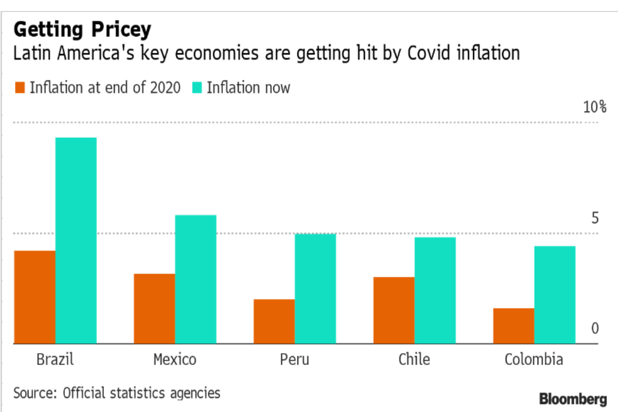
Source: JP Morgan

China

Chinese equities declined on additional regulatory tightening (CSI 300: -0.4%; Hang Seng China Enterprises: -1.8%). According to the *FT*, Beijing looks to break up Ant Group and create a separate app for its loan business. Regulators also called for platform operators to review the working conditions of workers and warned internet companies against blocking links to their rivals' services. The RMB depreciated (-0.2%); CGB yields increased (10-year: +2.0 bps; 30-year: +1.4 bps). In other news, **Evergrande remains under intense market pressures,** with its share price continuing to drop (today: -6.9%; past week: -12.9%). Last week, Evergrande said that it plans to suspend interest payments to two banks, following reported news that the Financial Stability and Development Committee signed off on Evergrande's proposal to renegotiate payment deadlines with its lenders.

Latin America

Central banks in Latin America are struggling to slow inflation despite a series of rate hikes. High inflation threatens the region as the annualized inflation approaches 10% in Brazil and has almost doubled in Mexico since the end of 2020. The threat is causing alarm because of the region's history of price instability, and central banks are consequently raising interest rates. The Central Bank in Chile doubled its key lending rate two weeks ago, and its Brazil peer has already raised its reference rate four times since March 2021. According to analysts, these tightening measures pose a threat to the economic recovery. As a result, analysts are revising their economic growth projections lower, with JP Morgan expecting the region's economic growth to slow to 2.4% next year, down from 6.4% in 2021.



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Global Financial Indicators

Last updated: 9/13/21 1:27 PM	Level Last 12m	Latest	Change 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		4468	-0.8	-1	0	34	19
Europe		4209	0.9	-1	0	27	18
Japan		30447	0.2	3	9	29	11
China		3715	0.3	3	6	13	7
Asia Ex Japan		89	0.0	-1	2	16	0
Emerging Markets		52	-0.1	-1	1	19	2
Interest Rates					basis points		
US 10y Yield		1.33	-1.2	1	5	66	42
Germany 10y Yield		-0.33	-0.3	3	13	15	24
Japan 10y Yield		0.05	0.1	0	2	2	3
UK 10y Yield		0.75	-1.1	5	17	57	55
Credit Spreads					basis points		
US Investment Grade		88	-0.3	-3	-5	-42	-7
US High Yield		315	-1.2	-4	-27	-206	-65
Europe IG		45	0.0	0	-1	-10	-3
Europe HY		227	0.0	1	-5	-91	-15
Exchange Rates					%		
USD/Majors		92.81	0.2	1	0	-1	3
EUR/USD		1.18	-0.3	-1	0	-1	-4
USD/JPY		110.1	0.1	0	0	4	7
EM/USD		56.8	0.1	-1	1	2	-2
Commodities					%		
Brent Crude Oil ($/barrel)		73	0.7	2	4	84	42
Industrials Metals (index)		169	-0.3	4	5	43	27
Agriculture (index)		55	-0.7	-3	-7	42	15
Implied Volatility					%		
VIX Index (%, change in pp)		19.2	-1.8	2.8	3.7	-7.7	-3.6
US 10y Swaption Volatility		65.8	2.0	-0.2	-2.4	13.0	2.5
Global FX Volatility		6.5	0.0	0.0	0.0	-3.0	-1.5
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		111	-1.9	-8	9	-49	-9
Italy		102	-1.2	-4	1	-44	-9
Portugal		56	-0.3	-1	-2	-25	-4
Spain		66	-0.3	-2	-3	-13	4

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

Emerging Market Financial Indicators

Last updated: 13/09/2021 1:29 PM	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		6.46	-0.2	0.0	0	5	1		3.0	0.0	3	0	-25	-25
Indonesia		14253	-0.4	-0.2	1	4	-1		6.1	-2.2	1	-16	-78	4
India		74	-0.2	-0.8	1	0	-1		6.3	0.0	0	-15	17	39
Philippines		50	-0.2	-0.1	1	-3	-4		4.3	-0.1	0	-3	67	67
Thailand		33	-0.5	-1.3	1	-5	-9		1.7	-0.4	6	17	23	41
Malaysia		4.15	-0.4	-0.1	2	0	-3		3.3	0.1	2	1	79	75
Argentina		98	0.0	-0.2	-1	-24	-14		47.8	7.1	111	302	392	-835
Brazil		5.21	0.6	-0.9	1	1	0		10.3	15.2	31	105	463	469
Chile		785	0.4	-1.6	-1	-3	-10		5.3	0.0	37	73	275	259
Colombia		3840	-0.2	-1.1	3	-3	-11		7.0	0.8	13	3	201	191
Mexico		19.86	0.2	0.3	0	6	0		7.0	1.4	-1	-11	103	140
Peru		4.1	-0.1	-0.2	-1	-14	-12		6.5	4.3	15	20	243	293
Uruguay		43	-0.1	-0.2	2	0	-1		7.9	0.0	2	0	10	67
Hungary		297	-0.1	-1.3	1	2	0		2.6	-0.2	2	35	90	111
Poland		3.86	-0.3	-1.3	0	-3	-3		1.3	0.3	-5	12	49	67
Romania		4.2	-0.3	-0.7	-1	-2	-5		3.6	-1.5	5	41	23	87
Russia		72.9	0.4	0.2	1	3	2		6.9	-2.4	2	4	119	121
South Africa		14.2	0.2	0.4	4	18	4		9.7	0.7	4	-15	-47	2
Turkey		8.45	0.2	-2.0	1	-11	-12		16.9	-7.7	7	-57	382	380
US (DXY; 5y UST)		93	0.3	0.9	0	-1	3		0.81	-0.5	3	4	56	45

	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		4992	1.3	1	1	7	-4		213	-3	-6	-24	-16
Indonesia		6088	-1.0	-1	-1	18	2		172	-2	-8	-66	-28
India		58178	1.1	0	5	50	22		144	-4	-9	-75	-7
Philippines		6968	1.6	1	10	16	-2		105	-2	-8	-37	-7
Malaysia		1570	-2.0	-1	4	4	-4		127	-4	-13	-47	-8
Argentina		75895	-1.6	2	9	66	48		1522	51	-27	426	166
Brazil		114286	-0.9	-2	-6	16	-4		290	4	6	-21	31
Chile		4464	0.0	0	1	20	7		144	2	1	-38	-12
Colombia		1321	-0.2	0	4	9	-8		276	2	-4	18	61
Mexico		51522	0.2	-1	0	42	17		340	-5	-16	-121	-17
Peru		17715	0.9	0	6	-2	-15		169	-2	-10	6	40
Hungary		52722	1.4	0	5	51	25		132	-2	3	-22	-17
Poland		71531	0.8	-1	3	41	25		24	-2	-11	-7	-4
Romania		12337	1.3	0	2	33	26		191	3	11	-63	-12
Russia		4021	2.6	0	4	38	22		161	-3	-4	-64	-18
South Africa		64645	-4.1	-2	-7	15	9		340	2	0	-158	-44
Turkey		1445	-1.9	-2	0	31	-2		456	-1	-23	-143	9
Ukraine		526	0.0	0	0	5	5		482	8	-29	-155	-11
EM total		52	-0.1	-1	1	19	2		351	4	-9	-30	13

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

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