GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

THURSDAY, SEPTEMBER 19, 2019

- **FOMC cuts policy rate 25 bps; median policy rate forecast flat through 2020 (link)**
- **Bank of England keeps policy rate unchanged at 0.75% in unanimous vote (link)**
- **Norway's central bank hikes rate 25 bps and to remain stable in coming period (link)**
- **BoJ maintains policy stance and will further assess prices and economy in Oct (link)**
- **Bank Indonesia cuts benchmark rate 25 bps and eases loan terms to spur growth (link)**
- **Central Bank of Brazil cuts Selic rate 50 bps; inflation outlook signals more easing (link)**
- **SPECIAL FEATURE: G-SIB operating performance and balance sheet trends (attached)**

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Market sentiment gets boost amid central bank decisions

As broadly anticipated, the FOMC delivered a 25 bp policy rate cut, while markets interpreted the committees projections as slightly less accommodative. The updated median projected path for the policy rate showed no more changes in 2019 and 2020, although the meeting statement retained the pledge to act as appropriate to sustain the expansion. While US equities ended the day little changed, most of the market reaction could be seen in the sharp swing in US Treasury yields. After yields spent most of the session down 6 to 8 bps across the curve, they fully reversed as the press conference proceeded with the 2-year yield notably up to 1.76% and causing a flattening in the 2-year, 10-year yield curve. Money markets also remain on the periphery of investor focus with further open market operations planned for this morning to help curb the recent volatility in US funding markets. In other regions, central bank decisions also drove modest gains in risk assets with the BoJ, SNB, and BoE all maintaining their current policy stances, while the Norges Bank hiked rates, but signaled a near term pause. In EMs, central banks in Brazil and Indonesia eased policy, while oil prices are seeing some support this morning following the last two days of declines.

Key Global Financial Indicators

Last updated: 9/19/19 8:00 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		3007	0.0	0	3	3	20
Eurostoxx 50		3545	0.5	0	5	5	18
Nikkei 225		22044	0.4	2	7	-7	10
MSCI EM		42	-0.2	0	5	-2	7
Yields and Spreads					bps		
US 10y Yield		1.77	-0.5	-1	16	-130	-92
Germany 10y Yield		-0.50	1.4	2	15	-98	-74
EMBIG Sovereign Spread		335	2	6	-32	-18	-79
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		60.9	0.2	0	1	-1	-2
Dollar index, (+) = $ appreciation		98.3	-0.3	0	0	4	2
Brent Crude Oil ($/barrel)		65.0	2.2	8	9	-18	21
VIX Index (%, change in pp)		14.2	0.3	0	-3	2	-11

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

United States

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The market interpreted the FOMC meeting as mildly hawkish. Treasuries had rallied through the day but sold off over the course of the press conference. When asked if this was still a mid-cycle adjustment, Chair Powell called the cuts “insurance against risks.” That sounded like a mid-cycle adjustment to the Treasury market, which sold off further in response to his words. The details of the rate move were generally as predicted. In a 6-3 decision, the FOMC cut rates by 25 bps, setting the policy rate target at 1.75%-2.00%. The updated Summary of Economic Projections showed a median policy rate forecast with no further rate cuts from the current level over 2019-20 and a gradual upward convergence towards the longer-run estimate of 2.5% over 2021-22. The committee also cut the interest on excess reserves (IOER) by 30 bps to 1.80%. The reserve repo rate (RRP) was also cut by 30 bps to 1.70%. Governor Bullard dissented and called for a 50 bps cut and Governors George and Rosengren repeated their call from July 31 for no cut at all. The reduction of the RRP rate below the Fed Funds target was viewed by some as a disincentive to money market funds who had been using the facility and pulling reserves out of the system. This could be an indirect means of addressing recent funding market challenges. In the press conference, Chair Powell was asked if reserves in the system were too low. His response was that open market operations (OMOs) were adequate to address funding stresses but he seemed to agree that a larger balance sheet may be necessary under certain conditions.

FOMC Dot Plot Median Changes

Source: Bloomberg

	September	June	Change
2019 median	1.875%	2.375%	-50 bps
2020 median	1.875%	2.125%	-25 bps
2021 median	2.125%	2.375%	-25 bps
Long Run median	2.5%	2.5%	Unchanged

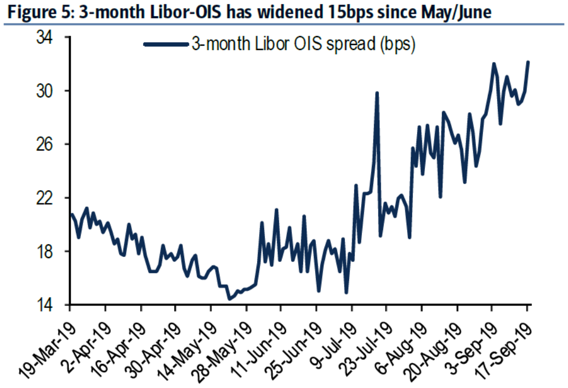
Stocks ended nearly flat with little response to the FOMC press conference although they did bounce back from moderate losses. US housing starts for August came in much stronger than expected (1364K versus 1250K) and 12.3% m/m (versus the 5% consensus forecast). The July numbers were also revised upwards. This is the fastest pace of new home construction seen in the current economic cycle. The National Association of Homebuilders index has also been on the rise, suggesting a constructive forecast for the US housing sector. The New York Fed’s second OMO of $75 bn attracted over $80 bn of bids and conditions in US money markets were calmer, with a third OMO scheduled for this morning. The Fed Funds (FF) and euro-dollar (EDF) futures curve adjusted in response to the perceived hawkishness by shifting higher, but the market is still more dovish than the Fed and is pricing in one more policy rate cut by year-end. This morning, US Treasury yields are down 2 to 3 bps and the S&P 500 futures point to a slight decline at the open.

Fed Funds Futures: Response to the FOMC (September 18, 2019)
Source: Bloomberg

	Before FOMC (1pm)	After FOMC	Change
October 2019 FF	1.870%	1.895%	+2.5 bps
December 2019 FF	1.715%	1.75%	+3.5 bps
June 2020 FF	1.39%	1.42%	+3 bps
December 2020 FF	1.24%	1.28%	+ 4 bps
December 2019 EDF	1.985%	2.05%	+ 6.5 bps
December 2020 EDF	1.49%	1.55%	+6 bps

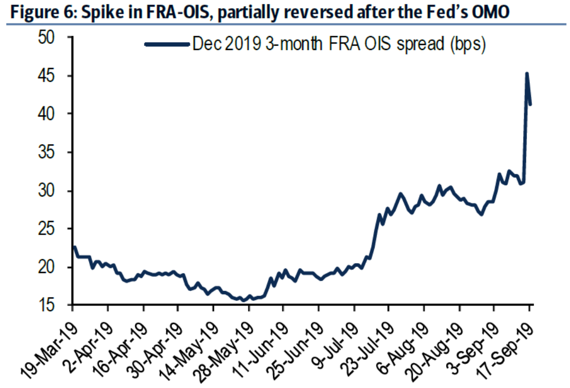
Volatility in US money markets could have spillover effects to the corporate bond market and other parts of the financial system. Contacts reported credit spread widening for corporate bonds over the past week as money market interest rates grew more volatile, culminating in the overnight repo rate spike on Monday and Tuesday. A modest amount of investor selling was also reported and new deal flow was slower than expected this week. Pressures in short term funding markets also cause overall funding costs to go up in various ways, especially via the pass-through to LIBOR, which gets pushed higher. The benchmark three-month LIBOR/OIS spread has widened by 15 bps over the past few months. Higher LIBOR rates translate into higher funding costs for foreign investors in the US bond market, many of whom hedge their currency exposure using the FX basis swap market. On a positive note, the Fed's open market operations did cause a narrowing of the FRA-OIS spread, lowering funding costs. Many market participants are worried about potential funding market volatility over quarter end when financing needs are especially high, and they are hoping that the recent Fed actions will restore a degree of calm to the money markets.

Figure 5: 3-month Libor-OIS has widened 15bps since May/June



Source: Bloomberg, BofA Merrill Lynch Global Research

Figure 6: Spike in FRA-OIS, partially reversed after the Fed's OMO



Source: Bloomberg

Europe

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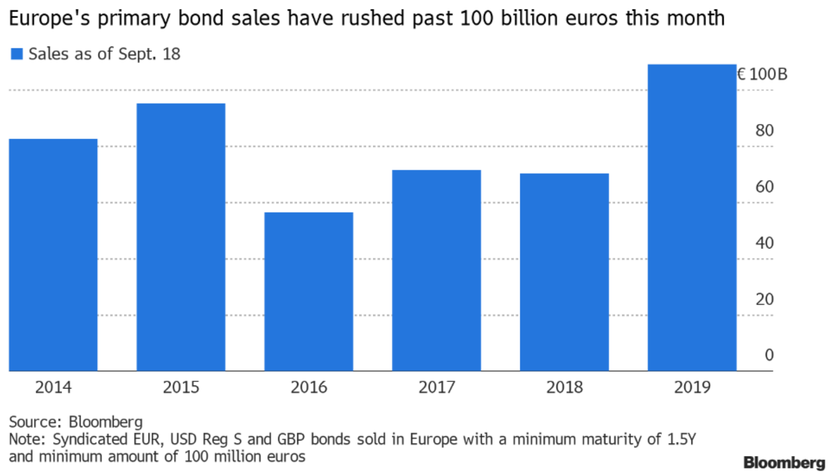
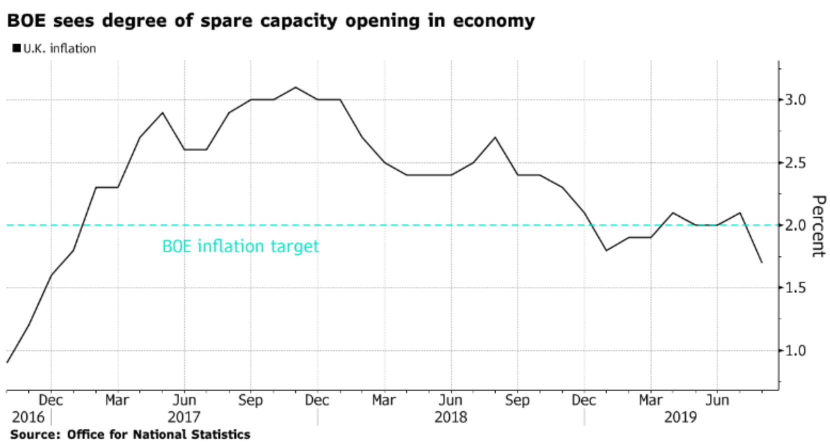
The EuroStoxx 600 is up 0.3%, back to the same level it ended last week. Banking sector stocks are outperforming, up 1.8%, recovering from three sessions of considerable losses. Yields are little changed across the region over the last couple of days, with no meaningful impact from the FOMC decision yesterday. **The still low-rate environment, more QE from the ECB, and Brexit-related uncertainty have prompted a rush of primary market issuance in September.** From the start of the month until yesterday, there have been €109 bn of debt sold. This amount has been considerably higher than the amount sold the last two years, closer to €70 bn.



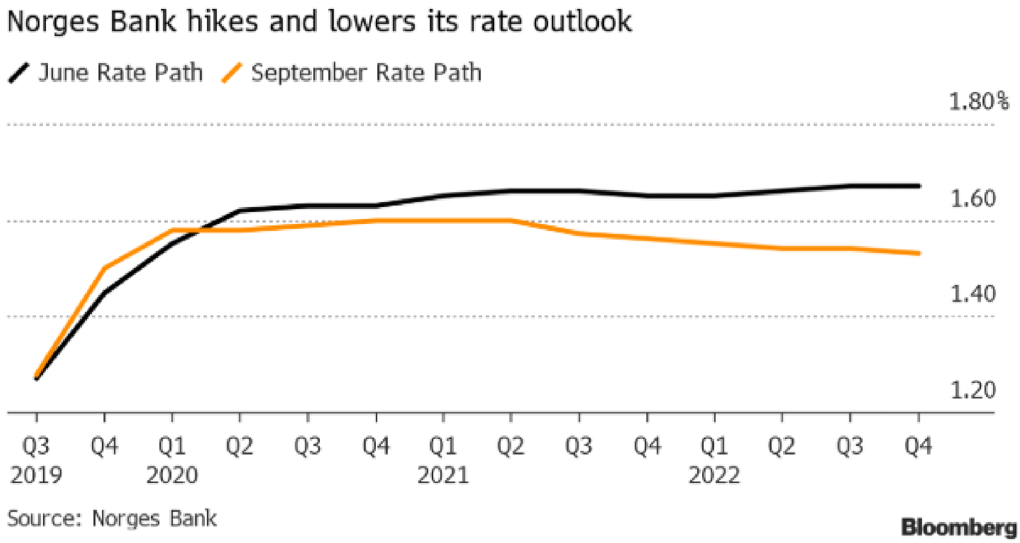
United Kingdom

The Bank of England kept the policy rate unchanged at 0.75% in a unanimous vote. The statement underscored the downside risks to inflation, noting that "political events could lead to a further period of entrenched uncertainty," impacting demand. Indeed, CPI continues to trend lower, reaching 1.7% y/y in August. The bank expects growth in Q2 at 0.2% from 0.3% previously. Implied rates suggest a 25% chance of a rate cut before the end of the year, and a 50% chance of cut by August of 2020. There was little market reaction to the decision.



Norway

The central bank delivered a 25 bp rate hike to 1.5% in today's meeting. Analysts were split going into the meeting, but most expected the Norges Bank to keep rates on hold. The new rate path is seen as peaking at 1.59% at the end of 2020, suggesting some chance of another hike given the uncertain global outlook. But Governor Olsen underscored that this is not the base case, noting that "the policy rate will most likely remain at this level in the coming period." **The krone appreciated sharply on the announcement but gave up most of its gains soon after, and yields are up a few basis points.**



Switzerland

The central bank kept interest rates unchanged at -0.75%, as expected, but cut its growth forecast. It also noted that the currency remained "highly valued," repeating its pledge to intervene if necessary. **The only policy change was in how the SNB will calculate the negative interest rates on sight deposits, offering banks some relief against negative rates.** It will now update its exemption threshold monthly, compared with its previous policy of granting an exemption worth 20 times a bank's minimum reserves. Officials also cut their 2019 growth forecast to 0.5%-1.0% from around 1.5% previously.

Other Mature Markets

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Japan

Equities (+0.6%) rose but pared earlier gains following the Bank of Japan (BoJ)'s decision to leave interest rates and asset purchases unchanged. The decision was in line with expectations. The BoJ said that it will review its assessment of prices and the economy at its October meeting. It mentioned that it needed to pay closer attention to the possibility of losing momentum toward its 2% inflation target amid the slowdown in overseas economies. Governor Kuroda said during the press conference that the central bank is more positive toward adding stimulus than it was at its last meeting. He also noted, however, that price momentum is not being lost and that there is no need for big changes in the policy framework for now. **The yen strengthened 0.4% while 10-year JGB yields fell 3bps to -0.23%.**

Emerging Markets

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The price action across EM assets has been mixed but relatively subdued following the FOMC decision yesterday. **Asian** equities (-0.5%) fell on net with wide dispersion across markets. India (-1.2%), Hong Kong (-1.1%), and Thailand (-0.8%) underperformed, while China (Shanghai +0.5%; Shenzhen +1.0%) and Korea (+0.5%) gained. Regional currencies were little changed. In **EMEA,** equity markets are mostly lower with Turkey (-1.4%) underperforming and Czech Republic (+0.5%) outperforming. Currencies are mostly strong albeit modestly, with the Turkish lira (-0.4%) the main exception. Stock indexes in **Latin America** saw a calm day without any major move, except for a 0.9% decrease in Mexico. The Brazilian real depreciated by 0.8%, while the region's other major currencies remained roughly flat. 10-year local currency benchmark rates and 5-year sovereign CDS spreads remained flat for the day. Argentina's US$ sovereign debt yields continued to edge lower with a similar speed as the day before, declining by 195 bps on the shorter 2-year end.

Key Emerging Market Financial Indicators

Last updated:	Level		Change				
9/19/19 8:05 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks			%				%
MSCI EM Equities		41.74	-0.1	0	5	-2	7
MSCI Frontier Equities		27.97	-1.1	0	-2	0	7
EMBIG Sovereign Spread (in bps)		335	2	6	-32	-18	-79
EM FX vs. USD		60.94	0.1	0	1	-1	-2
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		7.09	-0.1	0	-1	-3	-3
Indonesian Rupiah		14063	0.0	0	1	6	2
Indian Rupee		71.33	-0.1	0	0	1	-2
Argentine Peso		56.52	0.0	-1	-3	-30	-33
Brazil Real		4.11	-0.8	-1	-1	1	-6
Mexican Peso		19.40	0.0	0	2	-3	1
Russian Ruble		63.94	0.4	1	5	5	9
South African Rand		14.67	0.1	0	5	0	-2
Turkish Lira		5.70	-0.3	-1	-1	10	-7
EM FX volatility		8.18	0.0	0.0	-0.6	-3.5	-1.6

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

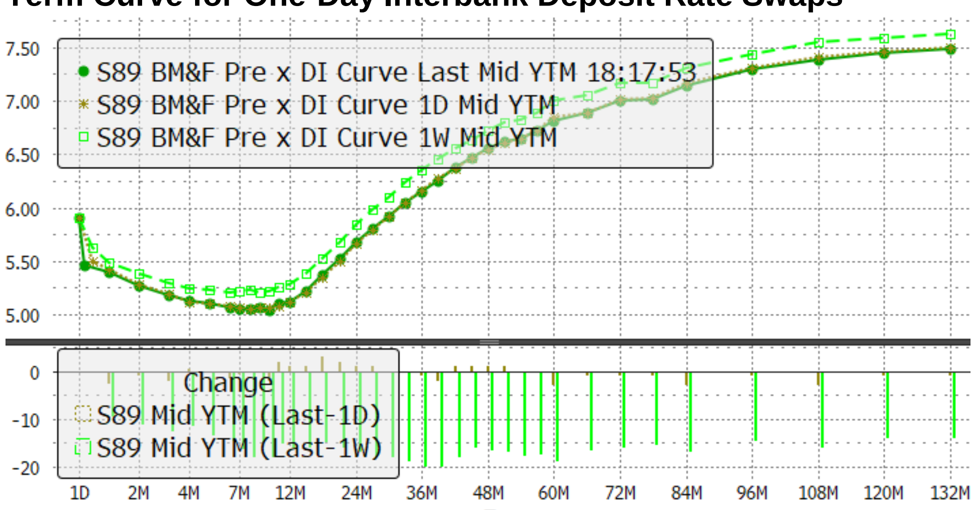
Indonesia

Bank Indonesia (BI) cut the seven-day reverse repurchase rate by 25 bps to 5.25%, in line with consensus expectations. This marked the third straight reduction as BI looks to bolster growth amid a slowing global growth environment. In addition, BI also relaxed loan-to-value ratios for property and environmentally-friendly vehicle loans to support domestic growth. BI forecasts growth to come in at 5.1% for the year, below the midpoint of its 5-5.4% range. Governor Perry Warjiyo said that BI will maintain an accommodative policy mix in line with low inflation forecasts and "the need to continue to drive economic growth momentum." **Equities fell -0.5% while the currency and 10-year bond yields were little changed.**

Brazil

Market reactions remained muted, as Brazil's central bank shifted its policy rate (SELIC) down to 5.5%. The 50 bps reduction was widely expected by market participants, with the Bloomberg consensus anticipating the move. Banco Central do Brasil's Monetary Policy Committee (COPOM) agreed unanimously on the decision. Analysts from Bloomberg and Goldman Sachs expected that the move would be motivated with inflation expectations staying below the target inflation and the presence of international risks. COPOM met these expectations, but also mentioned uncertainty around the continuation of domestic policy reforms. The Brazilian term curve for one-day interbank deposit rate swaps continued to edge lower during the day, indicating market expectations for continued cuts in the SELIC rate over the next months. These expectations match with COPOM's assumptions for its baseline scenario yielding a projected inflation of 3.3% at the of the year. The Brazilian real weakened 0.8% following the meeting decision.

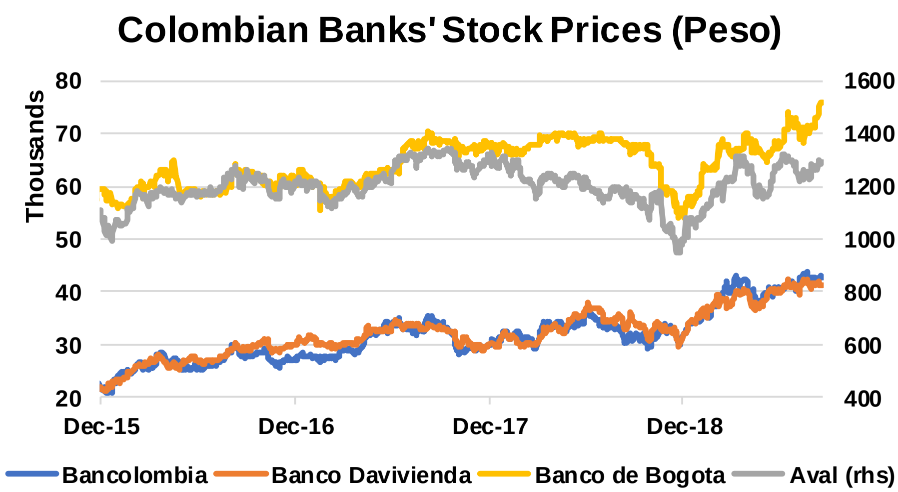
Term Curve for One-Day Interbank Deposit Rate Swaps



Source: Bloomberg

Colombia

Colombian banks have enjoyed robust growth, slightly improved asset quality and sound profitability expectations. According to JP Morgan the Colombian banking sector has shown robust growth with loan growth of 7.7% y/y and ongoing improvements in asset quality. The ratio of non-performing loans to assets declined y/y by 30 bps to 4.7% in July and the sector's costs of risks metric, typically measured as provisions over loans, declined q/q by 20 bps to 2.8%. Estimates for 2020 returns on equity stand well above 10%, and for most entities closer to 20%. Accordingly, stock price trends since the beginning of the year appear to signal some optimism in expectations.



Source: Bloomberg

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Global Financial Indicators

Last updated: 9/19/19 8:01 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		3007	0.0	0	3	3	20
Europe		3545	0.5	0	5	5	18
Japan		22044	0.4	2	7	-7	10
China		2999	0.5	0	4	10	20
Asia Ex Japan		68	-0.2	0	4	-3	7
Emerging Markets		42	-0.2	0	5	-2	7
Interest Rates					basis points		
US 10y Yield		1.77	-0.5	-1	16	-130	-92
Germany 10y Yield		-0.50	1.4	2	15	-98	-74
Japan 10y Yield		-0.21	-3.0	0	1	-34	-22
UK 10y Yield		0.62	-1.9	-5	15	-98	-65
Credit Spreads					basis points		
US Investment Grade		131	0.5	-2	-5	31	-16
US High Yield		443	0.5	-10	-62	116	-78
Europe IG		47	-0.8	2	-4	-13	-40
Europe HY		244	-4.3	9	-26	-36	-108
EMBIG Sovereign Spread		335	2.0	6	-32	-18	-79
Exchange Rates					%		
USD/Majors		98.28	-0.3	0	0	4	2
EUR/USD		1.11	0.3	0	0	-5	-3
USD/JPY		108.0	0.5	0	-1	4	2
EM/USD		60.9	0.2	0	1	-1	-2
Commodities					%		
Brent Crude Oil ($/barrel)		65	2.2	8	9	-18	21
Industrials Metals (index)		116	-0.2	-2	2	-1	6
Agriculture (index)		38	-0.2	0	1	-8	-9
Implied Volatility					%		
VIX Index (%, change in pp)		14.2	0.3	0.0	-2.7	2.5	-11.2
10y Treasury Volatility Index		5.7	-0.2	0.5	-0.1	2.1	1.1
Global FX Volatility		7.2	0.0	0.2	-0.8	-1.4	-1.8
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		190	-1.6	-17	-78	-172	-226
Italy		140	1.7	2	-68	-96	-110
Portugal		76	0.6	1	-5	-65	-72
Spain		74	0.2	0	-4	-30	-43

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: 9/19/2019 8:08 AM	Exchange Rates: Level, Last 12m	Exchange Rates: Level, Latest	Change (in %): 1 Day	Change (in %): 7 Days	Change (in %): 30 Days	Change (in %): 12 M	YTD	Local Currency Bond Yields (GBI EM): Level, Last 12m	Level, Latest	Change (in basis points): 1 Day	Change (in basis points): 7 Days	Change (in basis points): 30 Days	Change (in basis points): 12 M	YTD
		vs. USD	(+) = EM appreciation						% p.a.					
China		7.09	-0.1	-0.2	-1	-3	-3		3.1	1.1	4	6	-50	-7
Indonesia		14063	0.0	-0.5	1	6	2		7.3	0.6	-6	-11	-115	-82
India		71	-0.1	-0.3	0	1	-2		6.8	-5.3	3	2	-149	-68
Philippines		52	0.1	-0.4	0	3	1		4.4	-0.8	0	-18	-188	-193
Thailand		31	0.0	-0.3	1	6	7		1.6	-2.3	-10	5	-133	-107
Malaysia		4.19	-0.2	-0.6	0	-1	-1		3.4	0.1	2	11	-72	-71
Argentina		57	0.0	-0.6	-3	-30	-33		71.9	8.1	186	2688	4702	4886
Brazil		4.11	-0.8	-1.0	-1	1	-6		6.5	0.2	-15	-7	-382	-161
Chile		716	-0.2	0.0	0	-4	-3		2.8	0.0	9	10	-198	-167
Colombia		3374	0.3	0.0	2	-11	-4		5.7	-1.6	-4	9	-93	-83
Mexico		19.40	0.0	0.2	2	-3	1		7.2	-5.9	-11	13	-84	-150
Peru		3.4	-0.4	-0.4	1	-1	1		4.4	1.8	10	9	-122	-132
Uruguay		37	0.0	-0.6	-1	-10	-12		10.7	4.8	-18	-20		-4
Hungary		301	0.4	0.0	-2	-8	-7		1.1	-5.5	-12	18	-166	-114
Poland		3.92	0.4	0.0	1	-6	-5		1.9	-4.3	-2	24	-75	-42
Romania		4.3	0.3	-0.1	0	-7	-5		3.7	-1.0	-1	18	-57	-52
Russia		63.9	0.4	1.2	5	5	9		6.9	0.7	2	-25	-162	-152
South Africa		14.7	0.1	-0.5	5	0	-2		9.3	-4.4	2	-19	-47	-28
Turkey		5.70	-0.3	-0.7	-1	10	-7		14.4	-23.3	-63	-75	-685	-247
US (DXY; 5y UST)		98	-0.3	0.0	0	4	2		1.64	-3.2	1	17	-130	-87

	Equity Markets: Level, Last 12m	Equity Markets: Level, Latest	Change (in %): 1 Day	Change (in %): 7 Days	Change (in %): 30 Days	Change (in %): 12 M	YTD	Bond Spreads on USD Debt (EMBIG): Level, Last 12m	Level, Latest	Change (in basis points): 1 Day	Change (in basis points): 7 Days	Change (in basis points): 30 Days	Change (in basis points): 12 M	YTD
								basis points						
China		2999	0.5	0	4	10	20		183	-1	-2	-2	0	-11
Indonesia		6244	-0.5	-2	-1	6	1		168	3	2	-21	-26	-68
India		36093	-1.3	-3	-3	-3	0		131	-4	-5	-9	-32	-65
Philippines		7911	-0.1	0	0	10	6		68	5	6	-12	-26	-53
Malaysia		1596	-0.2	0	0	-11	-6		119	-1	-2	-7	-10	-43
Argentina		30071	-0.3	5	-1	-9	-1		2095	-1	-11	212	1470	1280
Brazil		104532	-0.1	1	5	34	19		221	1	2	-16	-101	-52
Chile		5073	0.0	4	6	-5	-1		131	0	5	-5	1	-35
Colombia		1597	0.0	1	4	6	20		177	0	5	-11	1	-51
Mexico		43070	-0.9	1	9	-13	3		318	1	2	-33	52	-36
Peru		19507	0.1	1	2	2	1		117	1	9	-7	-20	-51
Hungary		40788	-0.3	2	2	12	4		87	2	3	-16	-20	-61
Poland		58037	-0.4	0	4	0	1		23	3	6	-9	-19	-62
Romania		9345	0.3	1	3	13	27		183	-1	-3	-21	8	-39
Russia		2800	-0.6	0	6	16	18		185	4	5	-27	-50	-67
South Africa		56071	-0.3	-1	3	-1	6		306	4	4	-20	-23	-59
Turkey		100668	-1.2	-2	6	4	10		485	3	-1	-24	21	56
Ukraine		517	0.0	1	-3	-4	-8		472	12	32	-67	-79	-315
EM total		42	-0.1	0	5	-2	7		335	2	6	-32	-18	-79

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

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