GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

THURSDAY, SEPTEMBER 9, 2021

- **ECB moderately lowers pace of pandemic QE purchases** (link)
- **EU central banks and regulators call for final implementation of Basel III** (link)
- **U.S. equity investors demand greater downside protection** (link)
- **China reports widening gap between producer and consumer price inflation** (link)
- **Central Bank of Brazil governor urges more action against inflation** (link)
- **Hungarian funding yields drop on liquidity imbalance** (link)

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ECB moderately lowers pace of its asset purchases

Global stocks traded with a cautious tone as several big financial institutions warned about a slowing recovery, upcoming central bank tapering and high valuations. Southern European spreads edged lower after the ECB removed the "significantly higher" PEPP purchase from its policy statement in favor of "a moderately lower pace" while delaying other decisions on its QE programs to a later meeting. In emerging markets, China reported a widening gap between producer and consumer price inflation. Hungarian funding yields were also in focus after yields fell sharply on a liquidity imbalance. The Brazilian real sold off as the central bank governor warned further action is needed to prevent inflation expectations from de-anchoring.

Key Global Financial Indicators

Last updated: 9/9/21 12:41 PM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		4514	-0.1	0	2	33	20
Eurostoxx 50		4163	-0.3	-2	0	25	17
Nikkei 225		30008	-0.6	5	8	29	9
MSCI EM		53	-1.5	0	1	19	2
Yields and Spreads					bps		
US 10y Yield		1.33	-1.0	4	0	63	41
Germany 10y Yield		-0.33	-0.6	6	13	13	24
EMBIG Sovereign Spread		339	3	-2	-9	-77	-11
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		56.7	0.2	-1	1	2	-2
Dollar index, (+) = $ appreciation		92.6	-0.1	0	0	-1	3
Brent Crude Oil ($/barrel)		73.1	0.7	0	6	79	41
VIX Index (%, change in pp)		18.9	0.9	3	2	-10	-4

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

Mature Markets

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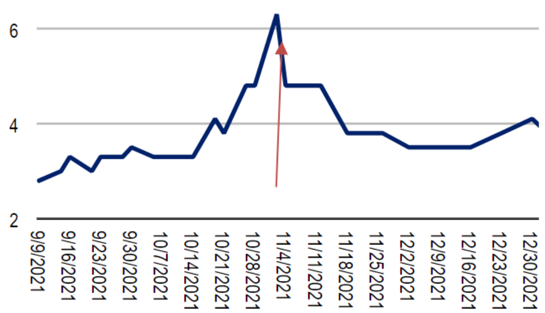
United States

Stocks traded with a cautious tone as several big financial institutions warned about a slowing recovery, upcoming central bank tapering and high valuations, when seasonality is typically unfavorable for stocks in September. Energy, materials and IT were the weakest sectors. The Treasury curve flattened and the 10-year yield fell 4 bps to 1.34%, with 5 bps drop in TIPS and 1 bp widening in breakevens. The 10-year note auction was well-received, awarded at 1.4bp through the when-issued rate with high indirect demand.

U.S.Treasury Secretary Yellen also said that cash and extraordinary measures will be exhausted in October to avoid breaching the debt limit, in line with market expectations. The bill market currently suggests the greatest risk of a government shutdown or technical default will be in late October.

Exhibit 2: UST bill curve shows debt limit concerns (bp)
Market believes debt limit risks concentrated in early Nov



Source: BofA Global Research

The post-Labor Day corporate borrowing spree continues. In high grade credit market, 21 companies issued $33bn on Tuesday, a record single day volume, followed by Wednesday's $27bn from 17 firms. This has lifted the total IG issuance to over $1tn this year. Investor appetite remains strong, with borrowers paying single digit concessions on deals that are 3 times oversubscribed. **The leveraged finance market is bracing for a surge in new deals as well, with $110bn expected in high yield bond and leveraged loan issuance.**

Investors continue to increase equity exposures but show greater demand for downside protections. Equity exposures at institutional investors such as asset managers and hedge funds hover around the YTD high, while retail investors have channeled $605bn into the US equity ETFs this year. This is accompanied by higher demand for downside protection as skew remain steep for both index and single stocks.

Japan

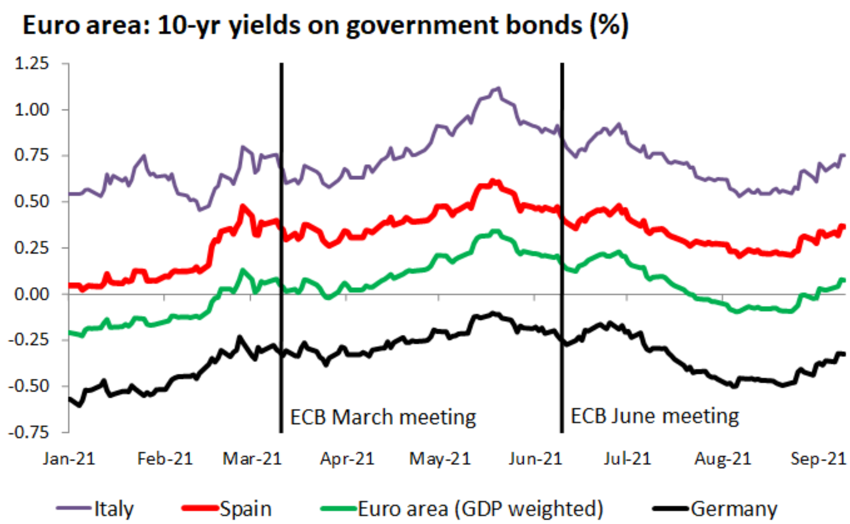
Equities (-0.7%) fell as the government extended virus emergency conditions in 19 areas including Tokyo and Osaka to 30 September. Separately, **Japanese funds boosted foreign bond buying to a five-months high of ¥1.04tn ($9.4bn) net last week.** They sold about ¥0.5tn of overseas stocks over the same period. This follows earlier reports that Japanese investors net sold foreign securities in August, the trend was led mainly by Japanese banks largely cutting positions in foreign long-term bonds. **10-yr yields and the yen were little changed.**

Euro area

Southern European spreads tightened 2-3 bps after the ECB removed the "significantly higher" PEPP purchase from its policy statement in favor of "a moderately lower pace" while delaying other decisions on its QE programs to a later meeting (as expected). Based on a joint assessment of financing conditions and the inflation outlook, the ECB Governing Council judged that favourable financing conditions can be maintained with a lower QE purchase pace. Contacts expect the ECB to reduce the pace of PEPP QE purchases from about €80 bn/m in Q3 to likely €60-70 bn/m in Q4 even though the ECB is not expected to provide precise numbers.

Equities (-0.1%) recovered from earlier losses whereas the euro (+0.1%) and 10-yr bund yields (-1 bps to 0.33%) were little changed after the ECB policy statement was released.

The ECB's outlook for medium-term inflation will be closely studied for signals on further tightening. In June, the ECB expected both HICP headline and core inflation to average 1.4% in 2023. ECB hawks in favor of tightening have pointed to still-favorable financing conditions as a justification to slow the pace of PEPP, especially as the inflation outlook has improved compared to March. Euro area GDP-weighted yields are trading slightly above levels in March when the ECB decided to "significantly" increase the pace of PEPP purchases.



Note: Euro area rates are GDP weighted average of Austria, Belgium, France, Netherland, Germany, Italy and Spain.
Source: Bloomberg and IMF staff

The ECB, national central banks and regulators across the EU have called for the bloc to full implement the final part of Basel III regulations. They called for the implementation of the "output floor", which limits large banks' discretion in setting their own capital requirement. Full implementation of the output floor could reportedly increase capital requirements by 18.5% for EU banks, leaving them with a capital shortfall of €52 bn ($62 bn) capital shortfall, based on EBA calculations. The central bankers also upheld a standardized approach to credit risk and said EU-specific deviations should be minimized. **EU legislation to implement the final part of rules known as Basel III is due soon after being delayed by the pandemic.**

Emerging Markets

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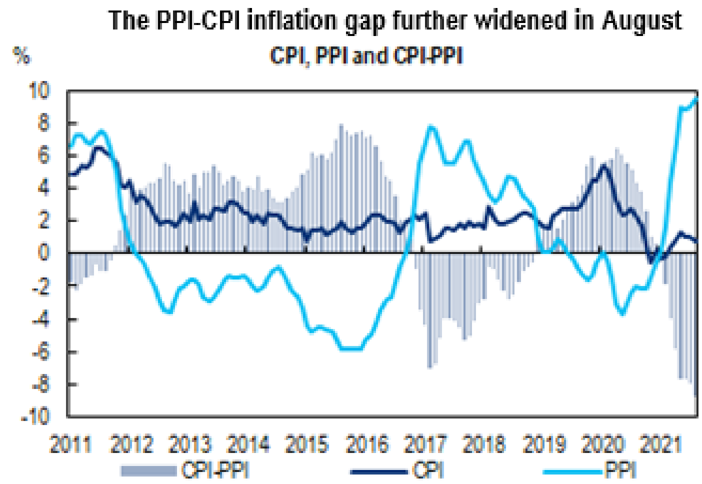
Asian equity markets (-1.2%) fell. Hong Kong underperformed (-2.3%) as Chinese tech stocks declined after the Chinese regulators summoned gaming companies' officials and warned them of the need for stricter oversight. China equity markets posted modest gains (Shanghai +0.5%, Shenzhen +0.1%), Indonesia was up (+0.7%). **Regional currencies were mixed.** The Philippines peso appreciated (+0.4%). The Korean won (-0.2%) weakened after the Bank of Korea (BOK) reiterated it will "gradually adjust" the pace of policy accommodation, based on virus developments, major economies' monetary policies and global inflation, financial markets, and household debt and property price trends. **EMEA equities were mostly trading lower with South Africa's JSE underperforming (-2.1%).** EMEA currencies were trading mixed with the South African rand (+0.4%) and the Russian ruble (+0.4%) appreciating while the Hungarian forint (-0.4%) and the Polish zloty (-0.4%) depreciated. In Poland, the central bank left its policy rate unchanged at 0.10% while maintaining a dovish communication against market expectation for a hawkish shift following the large inflation increase in August (5.4% in yoy). In Russia, headline inflation increased to 6.7% yoy in August, in line with consensus, while core came above consensus at 7.1% (6.9% expected). Analysts' expectations have been somewhat split between 25 bps and 50 bps rate increase at tomorrow's Central Bank of Russia meeting, but contacts note that the core inflation print makes 50 bps move more likely, which is roughly what is currently priced by the interest rate forwards market. **Equity markets in Latam posted large losses on Wednesday**. Stocks in Brazil (-3.5%) sank to the lowest in more than five months, due to increased political risks amid protests, while Argentina was down by 2%. **The Brazilian real fell 2.7%, making it the worst performing major currency**.

China

The gap between producer and consumer price inflation widened further in August. The producer price index (PPI) shot up to a higher-than-expected 9.5% y/y from 9.0% in July, record growth rate since August 2008. The rise in PPI inflation was led mainly by the mining sector and broadly based among upstream sectors. Consumer price index (CPI) fell to a lower-than-expected 0.8% y/y from 1.0% in July as food price deflation continued. Some analysts saw the divergence of PPI and CPI trends pointing to a worsening profit margin for manufacturers and services providers, which may exert extra downward pressure on activity growth in coming months. **China equity markets posted modest gains (Shanghai +0.5%, Shenzhen +0.1%), the renminbi and bond yields were little changed.**



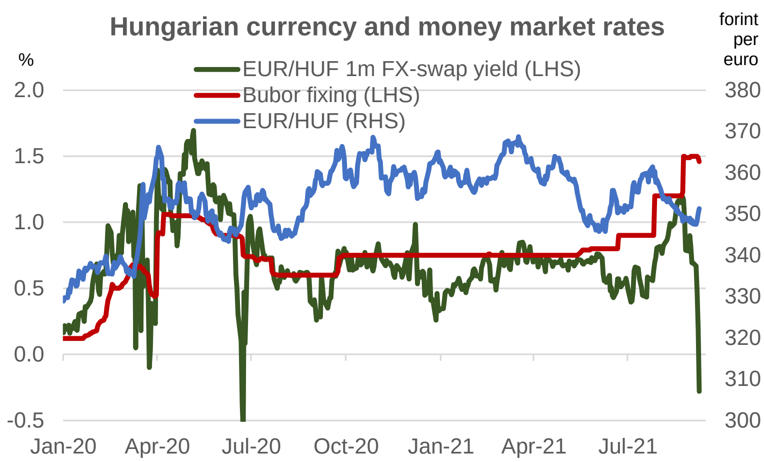
Source: NBS, Citi Research

Malaysia

Bank Negara Malaysia (BNM) held the overnight policy rate unchanged at 1.75%. The central bank thought the stance of monetary policy to be appropriate and accommodative. It projected that the gradual relaxation of containment measures, the rapid progress of the vaccination program and strong external demand will support growth recovery into 2022. BNM considered fiscal and financial measures will continue to cushion the economic impact on businesses and households and provide support to economic activity. It saw the recent spike in the headline inflation as transitory. The headline inflation is projected to average closer to the lower bound of 2.0%-3.0% range, core inflation is expected between 0.5% and 1.5% for the year. Separately, **Malaysia's Finance Minister projected the country is on track to fully vaccinate 80% of adults by end-Sepember**. Bloomberg reported, Tengku Zafrul Abdul Aziz stated during an online summit on Thursday that Malaysia is gradually relaxing curbs on movements. He also said the country will start the first phase of its 5G network rollout plan by end-2021, and targtes 100% national coverage by 2024. **Equities closed lower (-1.2%), the ringgit and yields were little changed.**

Hungary

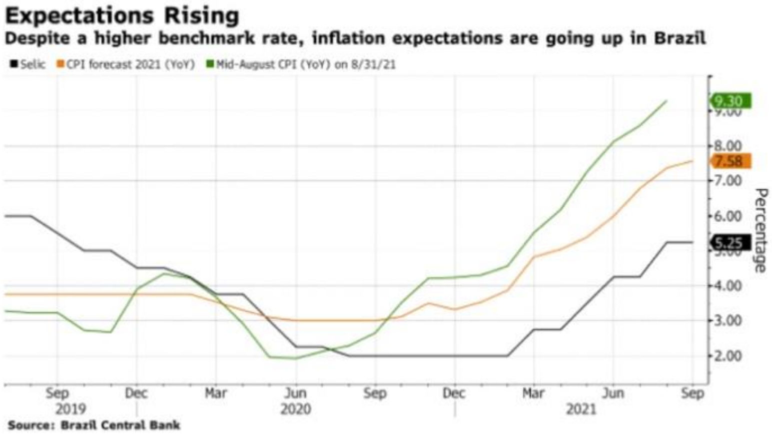
FX funding market rates dropped sharply on a liquidity imbalance. The 1-month implied yields fell by 160 bps to -0.40% and the spread to the policy rate in the 3-month tenor has now reached 100 bps. Contacts note that the FX swap market funding rates have been trading below the policy rate since June, largely due to a build-up in long forint exposure among international investors who positioned for the National Bank of Hungary (NBH) hiking cycle**. The latest drop comes due to the upcoming International Money Market position rollover as well as the quarter-end in September. Contacts also note that excess liquidity from the asset purchase program, counterparty limits and broader decrease in dealer activity have reduced markets capacity to deal with positioning build-up.** The FX-swap market got a temporary relief yesterday, following NBH promise to provide euro liquidity to the market at this month's FX-swap auction. However, contacts note that offshore market capacity constraints and limit issues are likely to remain until investor positioning is reduced.



Source: Bloomberg, IMF

Brazil

Central bank president Campos Neto said that the central bank will need to "act fast" to prevent a further deterioration of the country's inflation expectations. Despite successive rate hikes, inflation continues to rise and is now approaching 10% as a severe drought pushes electricity bills up, a faster rollout of its vaccination campaign is pressuring services prices, and the Brazilian real has slumped against its trading partners. **In Latin America, every major economy has now surpassed its central bank's inflation target.** One reason for that is the rapid increase in global food prices, which are now near their highest level in a decade, according to a closely watched UN index.



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Global Financial Indicators

Last updated: 9/9/21 12:50 PM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		4514	-0.1	0	2	33	20
Europe		4162	-0.4	-2	0	25	17
Japan		30008	-0.6	5	8	29	9
China		3693	0.5	3	5	14	6
Asia Ex Japan		90	-1.3	1	1	16	0
Emerging Markets		53	-1.5	0	1	19	2
Interest Rates					basis points		
US 10y Yield		1.33	-1.0	4	0	63	41
Germany 10y Yield		-0.33	-0.6	6	13	13	24
Japan 10y Yield		0.04	-0.2	1	3	1	2
UK 10y Yield		0.76	1.3	8	17	52	56
Credit Spreads					basis points		
US Investment Grade		91	-1.0	0	-1	-40	-4
US High Yield		318	0.3	-3	-19	-203	-62
Europe IG		45	-0.2	0	-2	-9	-3
Europe HY		228	-1.2	2	-5	-85	-14
Exchange Rates					%		
USD/Majors		92.57	-0.1	0	0	-1	3
EUR/USD		1.18	0.1	0	1	0	-3
USD/JPY		109.9	-0.3	0	0	4	6
EM/USD		56.7	0.2	-1	1	2	-2
Commodities					%		
Brent Crude Oil ($/barrel)		73	0.7	0	6	79	41
Industrials Metals (index)		165	1.2	3	5	40	24
Agriculture (index)		55	-1.2	-2	-3	45	15
Implied Volatility					%		
VIX Index (%, change in pp)		18.9	1.0	2.8	2.2	-9.9	-3.8
US 10y Swaption Volatility		67.3	-3.1	-1.6	-13.5	9.2	4.0
Global FX Volatility		6.6	0.0	0.1	-0.2	-2.9	-1.4
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		119	-1.2	5	18	-42	0
Italy		107	-1.0	1	5	-42	-5
Portugal		58	-0.4	-1	-1	-25	-2
Spain		68	-1.3	-2	-2	-13	6

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

Emerging Market Financial Indicators

Last updated: 09/09/2021 12:52 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	0.1	0.0	0	6	1		3.0	1.3	3	5	-30	-25
Indonesia		14253	0.0	0.1	1	4	-1		6.1	3.2	4	-8	-63	6
India		74	0.1	-0.6	1	0	-1		6.3	0.2	-3	-15	17	40
Philippines		50	0.4	-0.2	1	-3	-4		4.3	0.1	0	-5	68	67
Thailand		33	0.2	-0.7	2	-4	-8		1.7	4.4	11	20	22	43
Malaysia		4.15	0.1	0.2	2	1	-3		3.3	0.3	1	3	84	75
Argentina		98	0.0	-0.2	-1	-24	-14		47.3	39.6	93	272	273	-884
Brazil		5.32	-2.8	-2.5	-2	1	-2		10.1	20.8	39	90	464	456
Chile		787	0.0	-2.3	0	-2	-10		5.2	15.9	27	60	262	242
Colombia		3821	-0.3	-1.4	5	-2	-10		6.9	-0.2	12	4	192	185
Mexico		19.89	0.3	0.4	1	7	0		7.0	-3.7	2	-9	103	142
Peru		4.1	0.0	-0.2	0	-13	-12		6.5	9.3	15	25	235	287
Uruguay		43	-0.2	-0.5	2	0	-1		7.9	0.0	2	0	8	67
Hungary		297	-0.1	-1.0	1	2	0		2.7	0.3	8	39	94	113
Poland		3.83	-0.2	-0.8	2	-2	-3		1.4	0.4	12	19	53	72
Romania		4.2	0.2	-0.5	0	-2	-5		3.6	2.4	18	54	27	87
Russia		72.9	0.6	0.0	1	3	2		6.9	0.8	7	12	114	123
South Africa		14.1	0.5	2.4	5	18	4		9.7	-1.8	5	-18	-42	0
Turkey		8.45	0.2	-2.1	2	-11	-12		17.1	13.3	11	-53	373	396
US (DXY; 5y UST)		93	-0.1	0.1	0	-1	3		0.81	-0.3	4	1	52	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	1 Day	7 Days	30 Days	12 M	YTD
								basis points						
China		4970	0.0	2	-1	8	-5		199	0	-2	-9	30	-9
Indonesia		6068	0.7	0	0	24	1		158	0	-9	-25	-5	-29
India		58305	0.1	1	7	50	22		146	1	-2	-7	-69	-5
Philippines		6924	-0.4	1	5	17	-3		83	0	-9	-17	13	-22
Malaysia		1579	-1.2	0	5	6	-3		113	0	-2	-3	9	3
Argentina		77459	0.0	3	17	67	51		1459	0	19	8	-570	91
Brazil		113413	0.0	-5	-8	12	-5		253	0	0	-16	58	3
Chile		4378	0.0	-1	3	16	5		126	0	-6	-16	-14	-18
Colombia		1320	0.0	-1	7	6	-8		207	0	-4	-15	44	2
Mexico		51470	0.0	-1	1	42	17		348	0	-9	-34	55	-12
Peru		17410	0.0	-1	1	-5	-16		133	0	-4	-3	22	1
Hungary		52333	-0.3	1	5	49	24		65	0	-6	-15	-42	-31
Poland		70730	-0.3	-1	3	39	24		-22	0	-4	-11	-54	-21
Romania		12348	0.0	1	4	36	26		196	4	11	11	-56	-7
Russia		4005	-0.3	0	4	39	22		159	0	-5	-3	19	-7
South Africa		64239	-2.0	-4	-6	16	8		357	0	-4	-35	25	-23
Turkey		1442	0.6	-2	1	31	-2		421	0	-5	-47	34	-24
Ukraine		526	0.0	0	0	5	5		479	0	12	-21	127	-12
EM total		53	-0.8	0	1	19	2		421	0	17	-10	97	128

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

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