GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

MONDAY, SEPTEMBER 18, 2023

LEAD EDITOR: SANJAY HAZARIKA

- **US dollar at strongest in two years** (link)
- **Euro Area sovereign yields resume upward trend** (link)
- **High US Treasury yields attract foreign investors** (link)
- **Foreign ownership of Chinese government bonds falls below 8%** (link)
- **High yield US corporations face increasing refinancing risk** (link)
- **Russia surprises with 100 bps rate hike** (link)

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Markets in defensive mode ahead of key central bank meetings

Markets are cautious ahead of a week of key central bank meetings, including the Fed, the Bank of England, and the Bank of Japan. There is a growing gap between economic forecasters who expect another 25 bps hike from the Fed this year and market participants, who assign a probability of less than 50% to another Fed hike in 2023. Meanwhile, stocks in Europe are in the red across the board while US equity index futures are slightly higher. Investors are nervously eyeing the oil market, where Brent crude crossed $94/barrel to hit its highest level for the year, supported by production cuts from Saudi Arabia and Russia that are expected to last through December. Oil prices are up 24% since the June lows and worries about the impact of higher oil prices on inflation and the global economy are mounting. The price of Societe General shares fell as much as 11% after the leading French bank announced cuts in targets for profitability. Markets in Japan are closed for a national holiday.

Key Global Financial Indicators

Last updated: 9/18/23 8:01 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
S&P 500		4450	-1.2	0	2	15	16
Eurostoxx 50		4249	-1.1	0	1	21	12
Nikkei 225		33533	1.1	3	7	22	29
MSCI EM		39	-0.4	1	2	4	3
Yields and Spreads				bps			
US 10y Yield		4.34	0.8	5	9	89	47
Germany 10y Yield		2.69	1.8	6	7	94	12
EMBIG Sovereign Spread		415	-2	-4	-2	-78	-37
FX / Commodities / Volatility				%			
EM FX vs. USD, (+) = appreciation		47.5	-0.1	0	0	-4	-5
Dollar index, (+) = $ appreciation		105.3	0.0	1	2	-4	2
Brent Crude Oil ($/barrel)		94.4	0.5	4	11	3	10
VIX Index (%, change in pp)		14.6	0.9	1	-3	-12	-7

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

This will be a big week for central banks, with the FOMC meeting on Wednesday and the BOE meeting on Thursday the highlights of the week. The FOMC is expecting the Fed to stay on hold and markets assign a 70% probability for a rate hike of 25 bps by the BOE. Some analysts expect the People's Bank of China to announce further easing measures this week. The Bank of Japan is expected to stay on hold, but investors will be looking for clues about any future changes to its Yield Curve Control program. The Central Bank of Brazil is expected to cut the SELIC policy rate by 50 bps to 12.75% at its meeting on Wednesday. Other central banks in action this week include Taiwan POC, Norway, and Sweden. The US data calendar is light, with housing starts the only notable report due. In the euro area, inflation and PMIs are the main attraction, while the UK is due to release CPI and PPI data.

Mature Markets

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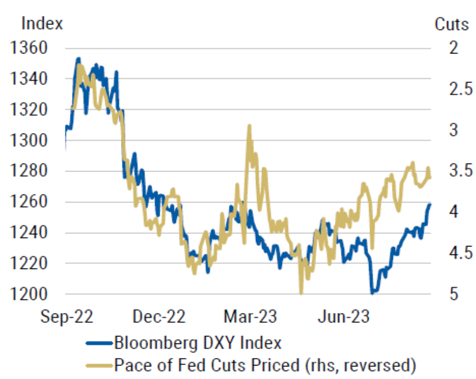
United States

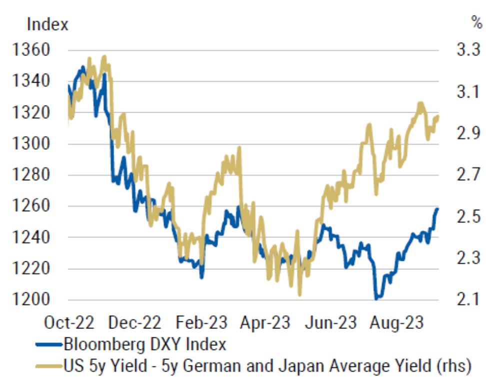
The US dollar index (DXY) is close to its strongest level in two years. According to Morgan Stanley, one key reason for the dollar's appreciation is the weakness in the Chinese economy and the renminbi, as well as the weakness of the yen. However, the dollar may have room to appreciate further. From a fundamental perspective, the dollar has risen less than would be expected based on market forecasts for future Fed policy (which have grown more bearish in recent days as investors reduce their expectations for Fed rate cuts in 2024.). If the market becomes convinced that the Fed will stay on hold for longer, dollar strength could pose further challenges, especially for emerging markets. Meanwhile, prospects for a stronger dollar could attract further inflows into US markets.

Exhibit 11: USD has risen less than Fed pricing...



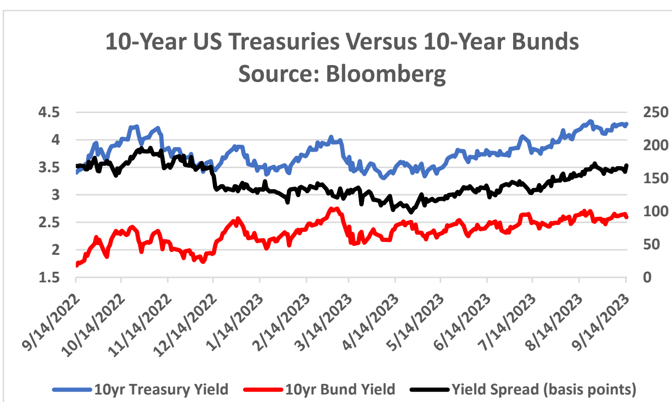
Source: Bloomberg, Morgan Stanley Research

Exhibit 12: ...or yield differentials would suggest

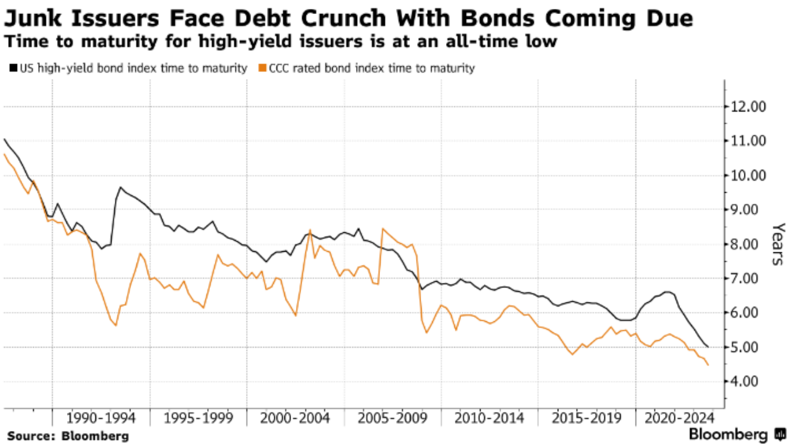


Source: Bloomberg, Morgan Stanley Research

The yield differential between the US Treasury markets and the German bund and Japanese Government Bond (JGB) markets has grown, making the US market even more attractive to foreign buyers. In fact, the latest Fed flow of funds data shows that both foreign buyers and US households have increased their purchase of US Treasuries, particularly for longer maturity bonds. The yield spread between 10-year Treasuries and 10-year bunds is at its widest in nine months. The wide yield spreads means that hedging cross-currency risk is still cheap despite the recent rally in the dollar. If the US economy continues to outperform the other major markets, yields could rise even more and further enhancing the attractiveness of US markets.



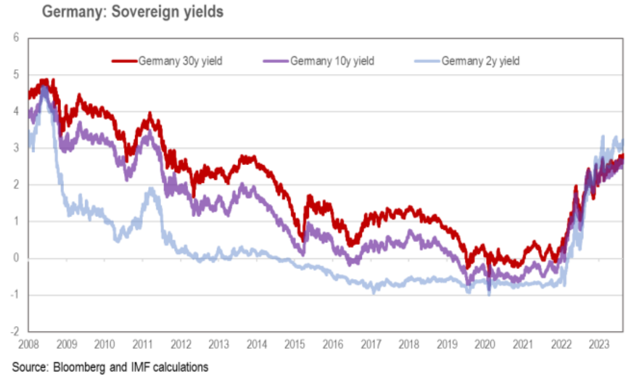
High yield (HY) US corporations are facing growing refinancing risk as higher interest rates become entrenched and debt maturities approach. The average time to maturity for HY issuers is at the lowest level in history, with the challenge particularly acute for the lowest (CCC) rated companies. Many HY companies loaded up on cheap financing in 2020–21 as central banks flooded global markets with liquidity to fight the pandemic, and they were able to stay out of the market for most of 2022 and 2023. Now, however, many of these companies will be forced to come back to refinance their debt at much higher cost and in the face of a possible recession further down the road. Some analysts predict higher defaults as a result.



Euro Area

European equities were mostly lower as markets brace for several central bank policy meetings this week—including the FOMC, the BoE, Japan, Norway, Sweden, and Switzerland. The Stoxx 600 Europe index was 0.6% lower, with most sectors trading in the red. From a sectoral perspective, the banking sector outperformed non-financial sectors last week (+4.2%), with contacts noting that the banking sector was supported by the ECB's rate hike and the lack of further changes to minimum reserve remuneration. Sovereign yields edged higher this morning (10y bund +2bps to 2.69%), while the euro was marginally stronger against the dollar (+0.1% to 1.067).

Sovereign yields have retraced post-ECB decision moves with 30y bund yields now back at levels last seen in 2011, despite ECB speakers broadly reiterating the September statement's forward guidance. 2y bund yields ended the week 13bps higher, while 10y bunds were up and 7bps and 30y bunds ended the week 8bps higher at 2.82%. Analysts note that ECB commentary in the aftermath of the ECB meeting last week has been largely in line with the ECB meeting statement, with some Governing Council members noting that it is too early to rule out further rate increases, and cautioned against bets that the ECB would cut rates in H1 2024. President Lagarde also reiterated that interest rate cuts were not yet on the table for policymakers. Moreover, some ECB Governing Council members have supported increasing the pace of quantitative tightening.

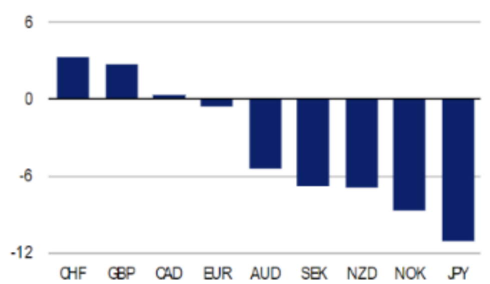


United Kingdom

The British pound has depreciated to a 15-week low against the dollar, with analysts seeing further downside risk. While the pound (GBP) has been among the top currency performers this year, it has depreciated by 2.4% against the dollar this quarter against a backdrop of a strong US economy and signs of weaker UK activity—which in turn has seen markets scale back BoE hiking expectations. BofA analysts see limited opportunities for the GBP to rally against the dollar in the near-term. In the meantime, the FTSE was little changed this morning after ending last week 3.1% higher, with analysts pointing to a weaker pound and higher commodity prices. Nevertheless, a recent Bloomberg survey showed expectations that the FTSE 100 would underperform global equities in 2024. Ahead of the BoE policy meeting this week, **UK residential rents saw the largest annual increase on record in August,** according to data from estate agent Hamptons. Residential rents increased by 12% y/y. Markets are now pricing in 20bps of tightening for the BoE meeting on Thursday (compared to 18bps last Friday), with roughly 36bps of tightening priced in by the end of this year.

Exhibit 1: G10 FX vs. USD year-to-date (percent)

GBP has been of the best-performing currencies this year

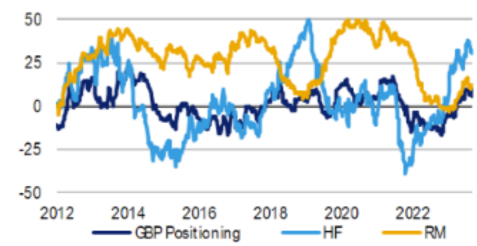


Source: Bloomberg. Data through Sep 14.

BofA GLOBAL RESEARCH

Exhibit 16: GBP positioning

GBP positioning long from neutral at the start of the year



Source: BofA Securities, Bloomberg. Note: +50 (-50) represents a max long (short) positioning level relative to Jan-2012. Aggregate positioning for G10 currencies takes into BofA Securities proprietary FX flows data as well as CFTC and BofA Global Research FX & Rates Sentiment Survey data. For details, please see the Liquid Cross Border Flows Primer.

Emerging Markets

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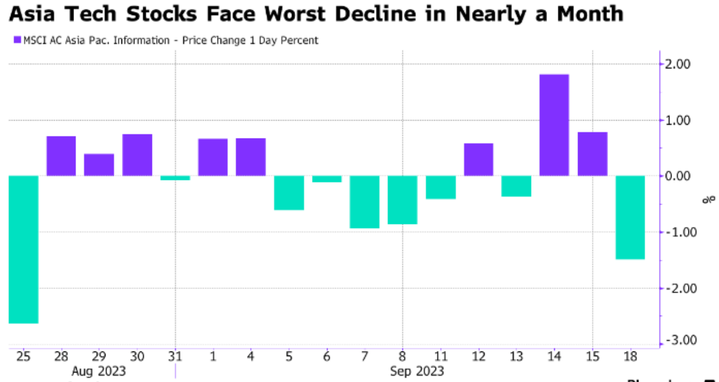
EMEA markets were mixed. This week there are central bank meetings taking place in Türkiye where consensus sees a 500bps hike, while central banks in Egypt and South Africa are expected to keep rates unchanged. **Asian equities declined -0.9%** on net. Tech stocks underperformed ahead of several important policy decisions this week. Hong Kong SAR equities declined -1.4%, followed by Taiwan POC and Vietnam (-1.3%). Mainland China's equities bucked the trend and eked out a gain of +0.5%. **Markets in Latin America were mixed, with Chile, Colombia and Mexico posting small gains while Brazil and Argentina were slightly lower.**

Asia Tech Stocks Face Worst Decline in Nearly a Month



Source: Bloomberg

Emerging Market Fund Flows

Emerging Markets bond funds outflow eased modestly (-$995mn, from -$1.1bn). ETFs saw outflows (-$21mn, from -$238mn) for the sixth week and non-ETFs outflows increased (-$975mn, from $844mn). EM equity funds outflows significantly increased (-$1.4bn, from -$484mn), mainly driven by increased non-ETF outflows (-$1.34bn, from -$476mn). ETFs outflows also increased (-$45mn, from -$8mn). The year-to-date flows currently stand at -$15.1bn and +$30.4bn for bonds and equities, respectively.

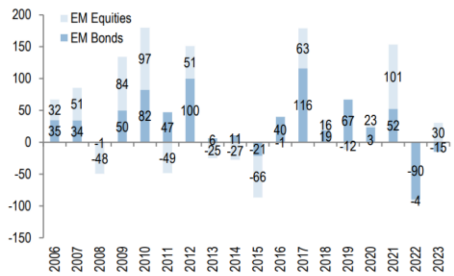
Figure 1: Weekly cross-asset flows

USD billion

	Asset	8w flows (8w ago → current)	This wk	YTD
Fund Flows	**EM Bonds and Equities**		-2.4	15.4
	EM Bonds		-1.0	-15.1
	Hard Ccy		-0.5	-12.5
	Local Ccy^		-0.5	-2.6
	o.w. EM ex-China		-0.5	1.0
	o.w. China		-0.1	-4.7
	EM Equities		-1.4	30.4
	US HG		2.3	222.4
	US HY		1.0	-0.2
	Global Equities		25.3	-21.4
	EM Bond and Equity ETFs		-0.1	35.9
	EM Bond ETFs		0.0	0.1
	EM Equity ETFs		0.0	35.9
	Non-resident EM flows*		-3.3	31.6

Figure 2: EM bond and equity fund flows

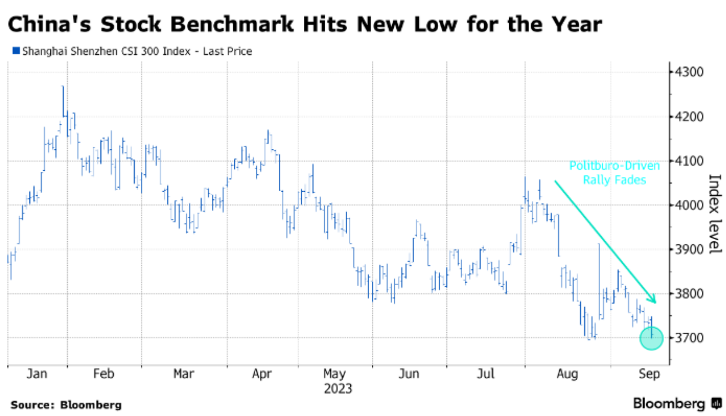
USD billion



*High frequency non-resident EM portfolio flow data where available. ^Local ccy split is retail only. All charts and data in this report: J.P. Morgan, EPFR Global, Bloomberg Finance L.P.

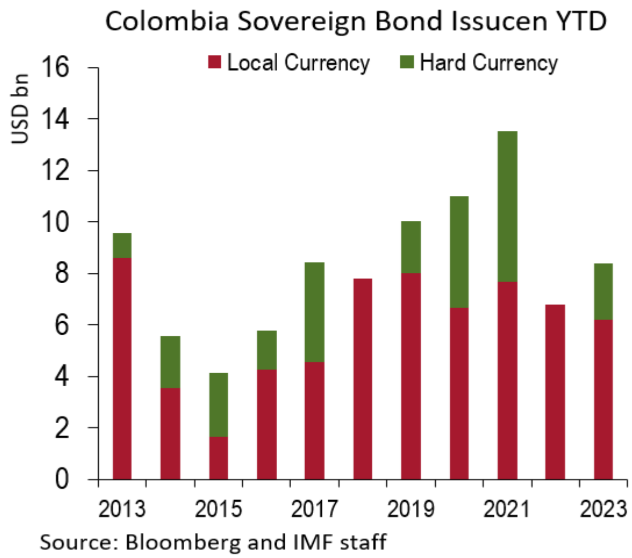
China

China equities recovered slightly +0.5%, after briefly touching the lowest level this year on Monday amid concerns over the property sector. The Heng Seng China Enterprise Index lost -0.9%, with tech stock sliding the most. Foreign funds have sold onshore Chinese stocks on a net basis for six straight weeks, Bloomberg estimated. On Friday, **Sino-Ocean announced it will suspend payments on all its offshore debt** (including $4bn dollar bonds). The state-linked builder, ranked 25th largest in China, will seek debt restructuring, citing a rapid decline in contracted sales and increased uncertainties in asset disposals. Separately, **the People's Bank of China (PBOC) kept adding liquidity ahead of the holidays and end of quarter**, with a net injection of 29bn yuan ($4bn) via open market operations on Monday. Meanwhile, the **share of foreign investors' ownership of Chinese government bonds fell below 8% for the first time since 2019**, Bloomberg calculated. Global funds sold a net 19.9bn yuan of Chinese government bonds and held 2.1tn yuan of these notes in August.



Colombia

Colombia insured $8.39 billion worth of bonds this year, 24% higher than same period last year, while the USD value of peso bond sales has decreased by 8.8%. Colombia also plans to issue 1 trillion pesos ($254.6 million) in green bonds by year-end while ending its 2023 auction program and redeeming a $791 million US-denominated bond due in February 2024. The Central Bank of Colombia published its monthly economist survey, showing a dip in both the 12-month and 24-month forecast inflation rates, while year-end inflation for 2023 and 2024 is expected to rise. Moreover, Colombia's industrial, retail, and manufacturing sectors experienced more significant declines in July than anticipated, impacting the country's economic landscape.



Russia

The central bank of Russia unexpectedly hiked its policy rate by 100bps to 13% on Friday, while most economists had expected rates to be left on hold. This follows an emergency 350bps hike in August. JPMorgan analysts highlight the absence of new macro news since the August hike, and think that the central bank might be erring on the side of caution as the August hike had seen the Russian ruble weakness subside somewhat. Bloomberg notes that the Russian ruble is one of the worst performing EM currencies this year, trading roughly 23% weaker against the dollar. JPMorgan analysts see further rate hikes in the remainder of the year as unlikely if there are no further large negative inflation or currency surprises. Goldman Sachs analysts, however, see material risks that the central bank will raise the policy rate to 14% at the next meeting.

This monitor is prepared under the guidance of Jason Wu (Assistant Director), Charles Cohen (Deputy Division Chief), Nassira Abbas (Deputy Division Chief), and Caio Ferreira (Deputy Division Chief). Fabio Cortes (Senior Economist), Sanjay Hazarika (Senior Financial Sector Expert), Esti Kemp (Financial Sector Expert-London Representative), Johannes S Kramer (New York Representative), Benjamin Mosk (Senior Financial Sector Expert), and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Yingyuan Chen (Financial Sector Expert), Andrew Ferrante (Research Assistant), Deepali Gautam (Research Officer), Phakawa Jeasakul (IMF Resident Representative in Hong Kong SAR), Harrison Kraus (Research Assistant), Yiran Li (Research Assistant), Xiang-Li Lim (Financial Sector Expert),Kleopatra Nikolaou (Senior Financial Sector Expert), Natalia Novikova (IMF Resident Representative in Singapore), Mustafa Oguz Caylan (Research Officer), Silvia Ramirez (Senior Financial Sector Expert), Patrick Schneider (Financial Sector Expert), Ying Xu (Economist), Dmitry Yakovlev (Senior Research Officer), and Akihiko Yokoyama (Senior Financial Sector Expert). Javier Chang (Senior Administrative Coordinator), Lauren Kao (Administrative Coordinator), and Srujana Sammeta (Administrative Coordinator) are responsible for the word processing and production of this monitor.

Global Financial Indicators

	Level		Change				
9/18/23 8:03 AM	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		4442	-1.2	-1	2	15	16
Europe		4249	-1.1	0	1	21	12
Japan		33533	1.1	3	7	22	29
China		3728	0.5	-1	-1	-5	-4
Asia Ex Japan		65	-0.4	1	2	3	1
Emerging Markets		39	-0.4	1	2	4	3
Interest Rates					basis points		
US 10y Yield		4.34	0.8	5	9	89	47
Germany 10y Yield		2.69	1.8	6	7	94	12
Japan 10y Yield		0.72	0.0	1	8	46	29
UK 10y Yield		4.39	3.5	-8	-28	126	72
Credit Spreads					basis points		
US Investment Grade		146	0.1	1	-1	-15	-12
US High Yield		407	0.6	-4	-24	-87	-74
Exchange Rates					%		
USD/Majors		105.29	0.0	1	2	-4	2
EUR/USD		1.07	0.1	-1	-2	6	0
USD/JPY		147.6	-0.1	1	2	3	13
EM/USD		47.5	-0.1	0	0	-4	-5
Commodities					%		
Brent Crude Oil ($/barrel)		94.4	0.5	4	12	17	15
Industrials Metals (index)		143	0.2	0	3	-7	-14
Agriculture (index)		67	0.0	0	1	-3	-3
Implied Volatility					%		
VIX Index (%, change in pp)		14.6	0.9	0.8	-2.7	-11.7	-7.0
Global FX Volatility		8.2	0.0	-0.1	-0.4	-3.2	-2.5
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		146	3.4	10	15	-106	-60
Italy		181	2.6	5	10	-46	-33
Portugal		74	-0.6	-1	0	-30	-28
Spain		107	0.2	2	2	-8	-2

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

Emerging Market Financial Indicators

Last updated: 9/18/2023 8:05 AM	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		7.30	-0.3	-0.1	0	-4	-5		2.7	3.0	1	16	-2	-32
Indonesia		15370	-0.1	-0.3	-1	-3	1		6.7	3.5	12	21	-49	-22
India		83	-0.1	-0.3	0	-4	-1		7.8	3.0	3	16	19.3	35
Philippines		57	-0.1	-0.3	-1	1	-2		5.8	-9.9	-13	-27	16	-19
Thailand		36	0.0	-0.6	-1	4	-3		3.2	4.0	10	23	17	53
Malaysia		4.69	-0.1	-0.3	-1	-3	-6		3.9	1.3	4	4	-24	-14
Argentina		350	0.0	0.0	0	-59	-49		115.6	-387.0	-688	1657	3509	2734
Brazil		4.87	-0.1	1.3	2	6	9		11.5	7.5	6	11	-32	-108
Chile		885	0.6	1.3	-3	4	-4		5.4	2.5	2	3	-124	2
Colombia		3928	-0.2	2.2	4	12	23		8.4	-12.0	-3	38	-135	-135
Mexico		17.09	-0.1	1.1	0	17	14		9.0	0.0	-1	27	18	28
Peru		3.7	-0.1	0.0	0	4	2		6.8	-4.7	-10	-18	-139	-117
Uruguay		38	0.2	0.1	0	7	5		9.3	0.4	2	25	-208	-135
Hungary		360	-0.2	-0.9	-2	10	4		6.8	0.0	-12	-63	-268	-283
Poland		4.35	0.2	-0.8	-6	8	1		4.6	-4.3	9	-43	-137	-153
Romania		4.7	0.1	-0.9	-2	6	-1		6.6	-1.0	-1	-4	-151	-112
Russia		96.6	0.1	-0.9	-3	-36	-23							
South Africa		19.0	-0.1	-0.8	0	-7	-10		9.6	4.4	14	-16	36	39
Turkey		27.02	-0.1	-0.6	0	-32	-31		27.2	0.0	234	519	1576	1741
US (DXY; 5y UST)		105	0.0	0.7	2	-4	2		4.48	1.8	7	10	85	48

	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		3728	0.5	-1	-1	-5	-4		183	1	2	-13	6
Indonesia		6936	-0.7	0	1	-4	1		129	0	4	-48	-11
India		67597	-0.4	1	4	14	11		139	-1	3	-19	-3
Philippines		6125	0.0	-2	-3	-5	-7		106	2	5	-21	9
Thailand		1528	-0.9	-1	1	-6	-8		0	0	0	0	0
Malaysia		1458	-0.1	0	1	0	-3		96	-1	3	0	-4
Argentina		567513	-0.7	7	-3	289	181		2174	11	-44	-172	-31
Brazil		118758	-0.5	3	3	9	8		227	-4	-7	-64	-47
Chile		6003	0.0	2	-2	9	14		124	-3	5	-51	-8
Colombia		1099	1.5	3	-3	-9	-15		332	-8	8	-66	-40
Mexico		51352	-0.8	-2	-3	10	6		358	2	-8	-59	-23
Peru		22956	0.0	1	1	19	8		156	1	4	-49	-24
Hungary		57759	-0.5	1	3	44	32		190	-5	-5	-54	-32
Poland		66927	-0.7	1	-2	36	16		124	-1	10	112	51
Romania		14173	0.3	1	11	21	22		206	-9	2	-83	-50
South Africa		73934	-0.9	0	1	11	1		373	-2	-14	-58	6
Turkey		7811	-1.9	-4	4	131	42		401	11	-6	-201	-39
Ukraine		507	0.0	0	0	-2	-2		3204	-121	-260	-142	-875
EM total		39	-0.5	1	2	4	3		377	-1	-3	-46	2

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

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