GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

FRIDAY, SEPTEMBER 6, 2024

LEAD EDITOR: JOHANNES S. KRAMER

- **Bets on a jumbo-sized rate cut at the September Fed meeting are resurfacing** (link)
- **Implied volatility in the Dollar Index surged to its highest level since March 2023** (link)
- **France's sovereign spread narrows slightly after new Prime Minister announcement** (link)
- **ECB natural rate is seen between 2.25% and 2.5% according to Bloomberg survey** (link)
- **Extent of easing priced for National Bank of Hungary appears aspirational to some** (link)
- **Special Feature: August 2024 EM local currency bond holdings monitor** (attached)

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Expectation for a September jumbo Fed rate is on the rise

Treasuries continued their rally overnight ahead of payrolls data, following through on the release. Today's release of the August jobs report shows payrolls slightly below expectations with the average hourly earnings data and the household survey challenging the narrative of a deterioration in the labor market that could warrant larger rate cuts. Notwithstanding this, bond markets continued their rally following the release with expectations of jumbo rate cuts having resurfaced after the job openings released on Wednesday have reached a level that some market contacts associated with an inflection point towards a steeper curve of the Beveridge Curve although the latest unemployment rate that was released today declined compared to July. With that backdrop, market contacts are attentive to remarks from Governor Waller and NY Fed President Williams just before the blackout period starts ahead of the Fed's September meeting, providing a final opportunity to steer expectations. Elsewhere, the French sovereign spread slightly declined following the appointment of the new Prime Minister while the National Bank of Egypt maintained its deposit rate unchanged.

Key Global Financial Indicators

Last updated:	Level		Change from Market Close				
9/6/24 9:01 AM	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		5503	-0.3	-2	5	23	15.38
Eurostoxx 50		4801	-0.3	-3	5	13	6
Nikkei 225		36391	-0.7	-6	4	12	9
MSCI EM		43	0.1	-2	5	9	6
Yields and Spreads					bps		
US 10y Yield		3.70	-2.6	-20	-19	-58	-18
Germany 10y Yield		2.18	-3.0	-12	-2	-48	15
EMBIG Sovereign Spread		387	-16	-5	-43	-29	4
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		45.9	0.1	0	1	-3	-5
Dollar index, (+) = $ appreciation		100.8	-0.3	-1	-2	-4	-1
Brent Crude Oil ($/barrel)		73.0	0.5	-7	-5	-19	-5
VIX Index (%, change in pp)		20.2	0.3	5	-7	6	8

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

Mature Markets [back to top]

United States

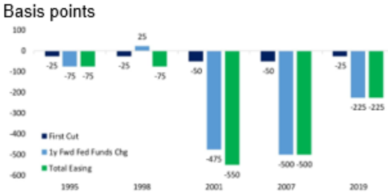
Today's August jobs report release show mixed results. Nonfarm payrolls printed at 142k, slightly below consensus (exp. 165k from 114k) while the unemployment rate slightly declined, in line with expectations at 4.2% (exp. 4.2% from 4.3%). However, wage growth was a tick higher than expected with average hourly earnings accelerating more than expected at 0.4% m/m (exp. 0.3% from 0.2%).

	Actual	Consensus	Prior	Revised
Nonfarm payrolls	142k	165k	114k	89k
Private payrolls	118k	140k	97k	
Average hourly earnings m/m	0.4%	0.3%	0.2%	
Average hourly earnings y/y	3.8%	3.7%	3.6%	
Unemployment rate	4.2%	4.2%	4.3%	
Participation rate	62.7%	62.7%	62.7%	

The initial market response was to treat the report as bullish for US interest rates especially at the short end, with the 2y rallying sharply. Initial analyst reports seem to lean towards a 25 bps rather than a 50 bps rate cut at the upcoming FOMC meeting on September 18, but Fed Funds futures markets now assign a 50% chance of a 50 bps move on that date, higher than the level before the jobs data.

Market Variable	Level at 8.10 am	Level at 8.40 am
10yr Treasury	**3.70%**	**3.68%**
2yr Treasury	**3.73%**	**3.65%**
10/2 Slope	**-3 bps**	**-3 bps**
September 18 Fed Funds Prediction	**1.425 rate cuts**	**1.52 rate cuts**
December 18 Fed Funds Prediction	**4.45 rate cuts**	**4.71 rate cuts**
S&P 500 Futures	**5484 (-0.5%)**	**5495 (-0.3%)**
USDJPY	**143.15**	**142.52**
EURUSD	**1.1103**	**1.1135**

Fed Funds rate changes during past easing cycles
Basis points

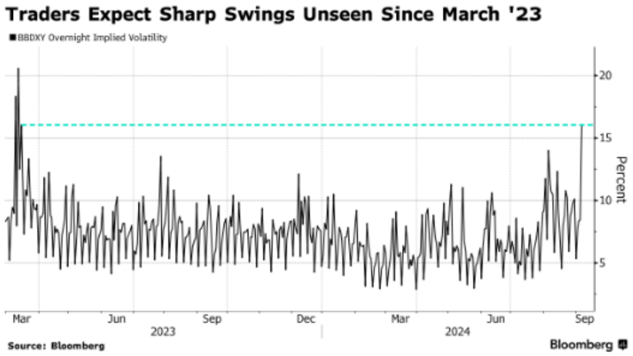


Source: Bespoke Investment Group.

Fed Funds rate trajectory around US elections, 1984-2016
pp. deviation from November

Source: JP Morgan.
Note: 1996, 2012 elections not shown as no change.

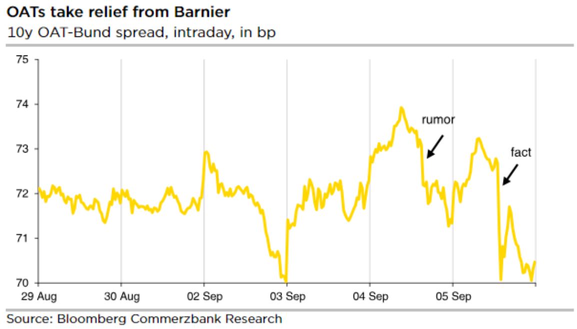
Following the release of JOLTS data on Wednesday, bets on a jumbo-sized rate cut resurface. The drop in the openings rate of the July Job Openings and Labor Turnover Survey (JOLT) release on Wednesday to a new post-Covid low of 4.6% shows that the relationship between that series and the unemployment rate seems to be normalizing after spending the better part of the past two years on the steep part of the Beveridge Curve. Notable in this regard is that Governor Waller—who has researched the relationships and inflection points of deteriorations in job vacancies that can lead to a faster rise in the unemployment rate—is scheduled to speak this morning after the release of the August unemployment rate with market contacts expecting him to take a dovish stance citing a speech from January where he stated that "*History has shown that unemployment would rise significantly from a tightening of monetary policy, particularly when the job vacancy rate is below 4.5 percent.*" Accordingly, bets on a -50bps jumbo-sized rate cut are resurfacing, reaching a probability of 43% for the imminent September meeting, which would be consistent with the magnitude of the first cuts during the easing cycles of 2001 and 2007 (left chart). From then on, market pricing is for a rate cut at every meeting between now and the end of next year, which would imply a cumulative easing of -250bps, bringing the Fed Funds rate down to less 2.8% by early 2026. Meanwhile, JP Morgan analysts point out that empirical regularities observed during past easing cycles provide little evidence that political considerations are affecting the interest rate setting decisions of the Fed (right chart).



Overnight, volatility in the Dollar Index surged to its highest level since the banking turmoil of March 2023. Investors are preparing for big swings in currency markets, expecting a broader trading range following this morning's key data release. According to Jefferies market contacts, sentiment around the dollar is bearish, with many traders heavily betting against it. This pessimism could backfire if the upcoming job creation and unemployment data do not confirm the expected cooling in the labor market. In that case, traders might rush to buy back their short positions, potentially sparking a dollar rally as investors adjust expectations for a shallower rate-cutting cycle and higher short-term U.S. yields.

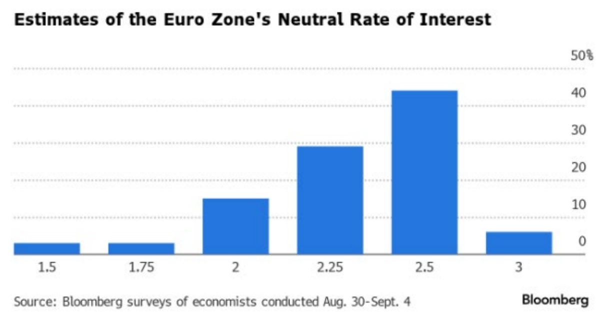
Euro Area

European equity markets were weaker this morning and sovereign bond yields were lower ahead of the US labor market data. The Stoxx 600 index inched lower this morning (-0.3%) with most sectors trading in the red, following yesterday's contraction (-0.5%) that market the fourth consecutive daily decline. Interest rates trended lower this morning with 10y bund yields rallying (-5bps) to 2.16%. The euro flat again the dollar this morning, trading at around $1.11/€.

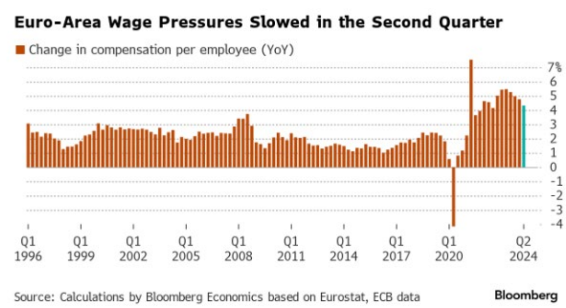


The French sovereign spread declines slightly following the appointment of France's new Prime Minister. French President Macron yesterday named Michel Barnier as prime minister, a move that Bloomberg analysts see as the first step toward resolving political uncertainty after the July 7 legislative election. The spread between 10y French (OAT) government bond yields and German bund yields narrowed marginally yesterday to around 70bps. Citi analysts suggest that market optimism remained muted as the new government will need support from both the far-right RN party and centrist factions to gain confidence in the Assembly. This raises concerns about government stability and the potential influence of far-right policies. Citi analysts see the upcoming budget, to be presented by October 1, as a critical test for the new government. Absent a clear path towards an improved government debt trajectory, the analysts expect medium-pressure France's sovereign credit rating, which currently stands at a AA first-best rating to persist. Hence, Citi analysts maintain their view for 10yr OAT-Bund spreads to remain rangebound between 65–75bps, with risks tilted towards more widening.

Economists expect quarterly rate cuts from the ECB following a recent Bloomberg survey. Results from a recent survey among polled economists ahead of the ECB policy meeting next week anticipate that the ECB will conduct a -25bps rate cut, consistent with market pricing. Median expectations expect quarterly rate cuts to continue until the deposit rate reaches a terminal rate of 2.5% in September 2025 to approach the neutral rate, which is seen in the range of 2.25% and 2.5%. As for the economic projections, survey respondents expect minor changes to the ECB forecasts, apart from a downward revision of 2024 growth.

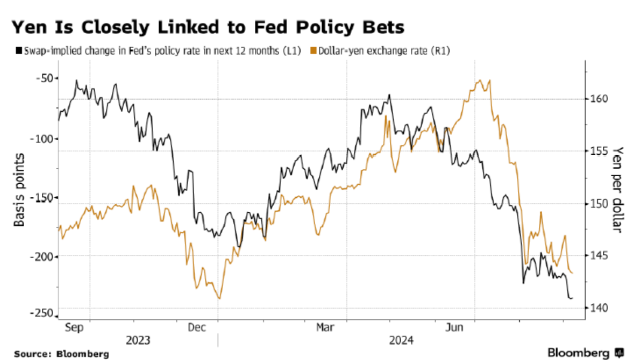


Euro area wage growth slows during the second quarter. Bloomberg economics estimate that euro area compensation per employee eased to 4.3%y/y in Q2, from 4.8% in Q1. Separate data releases this morning showed Germany's July industrial production disappointed and a downward revision in the euro area's final Q2 growth (to +0.2%q/q from previously estimated +0.3%). Bloomberg analysts note that the wage data paints a reassuring picture for the ECB ahead of the policy meeting next week, while the downward revision to Q2 euro area growth creates further motivation to ease. Markets continue to price in -65bps of ECB easing by the end of 2024, similar to yesterday.



Japan

The yen appreciated to its strongest level since early January. Today, the yen appreciated by +0.8% against the US dollar, touching ¥142.06/$, which reflects a cumulative appreciation of +3% during the past four days. Former Bank of Japan (BoJ) official Watanabe's remarks today further supported the yen. Watanabe stated that the pace of rate hikes could exceed market expectations with a possibility for the BoJ to hike two more times this year. He called for better communication from the BoJ to prevent market panic, suggesting the creation of a "dot plot" similar to the one that the Fed publishes. His comments followed remarks from BoJ Board Member Takata yesterday, who reiterated the need for higher interest rates if inflation aligns with the BoJ's economic outlook. In that context, Bloomberg analysts point out that market pricing is not sufficiently reflecting the possibility of further hikes from the BoJ, pointing out that the disconnect between the central bank's messaging and market expectations could be a source of future volatility. Japanese equities extended losses (Nikkei 225: -0.7%) amid the stronger yen.



Emerging Markets

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EMEA equities and currencies lacked clear trend ahead of the US payrolls data. CEE currencies depreciated against the euro, while only the Polish zloty marginally appreciated against the euro (+0.1%) to 4.28/€. Elsewhere, the Turkish lira was weaker (-0.1%) against the dollar to trade at 33.99/$ with Bloomberg reporting that investors remain cautious ahead of a rating announcement from Fitch. On the monetary policy front, in line with expectations, the National Bank of Egypt maintained its deposit rate at

27.25% at yesterday's meeting. In the accompanying statement, the MPC noted that "*current policy rates remain appropriate to maintain the prevailing tight monetary stance until a significant and sustained decline in inflation is realized*."

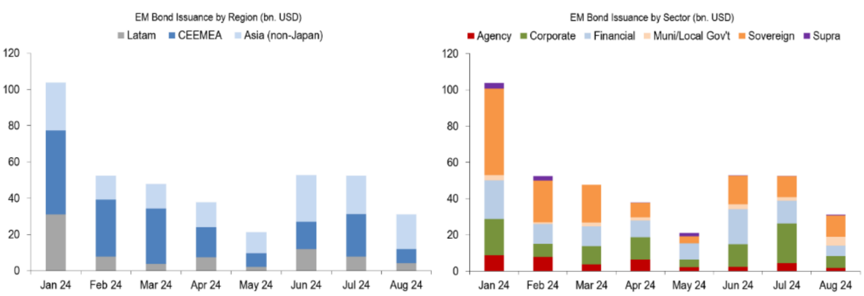
Asian equities and currencies posted muted gains. The aggregate EM Asia index slightly rose (+0.6%). Within currencies, the Philippine peso (+0.6%) led the way. The Indonesian rupiah appreciated less (+0.2%) amid the contry's foreign reserves having reached a record high. Long-term government bond yields fell further, mirroring the decline in US Treasury yields.

Yesterday, Latin American currencies strengthened while stock markets remained flat. In currencies the Brazilian real (+1.2%) and the Colombian peso (+0.4%) led the gains. The peso's rebound was supported by a recovery in copper prices (+1.5%), though the exchange rate remains below key resistance levels. Meanwhile, the Mexican peso recovered slightly (+0.1%) from an intraday low of 20.15/$, as investors reconsidered carry trades amid discussions of a controversial judicial reform. In stock markets, Colombia (+0.4%) and Brazil (+0.3%) posted modest gains, while Chile (-0.4%) and Mexico saw slight declines.

EM Bond Issuance

EM bond issuance reached $31 bn in August, bringing the year-to-date issuance to $399.5 bn. Bulgaria was the largest issuer last month with a volume of $4.8 bn in investment grade euro and dollar denominated sovereign bonds. Other notable sovereign issuance volumes include $2.9 bn in Peruvian dollar bonds, $2.5 bn in Philippine dollar bonds, and $1 bn samurai bonds from Mexico. In terms of issuer sectors, sovereigns (33%) contribute the lion's share, followed by corporates (23%), municipal bonds (21%), financials (17%), agencies (5%), and supranationals (1%). In terms of seasonality, last month's issuance volume was double the amount observed in August a year ago ($14.9 bn).

Largest Issuers: China and Sovereigns



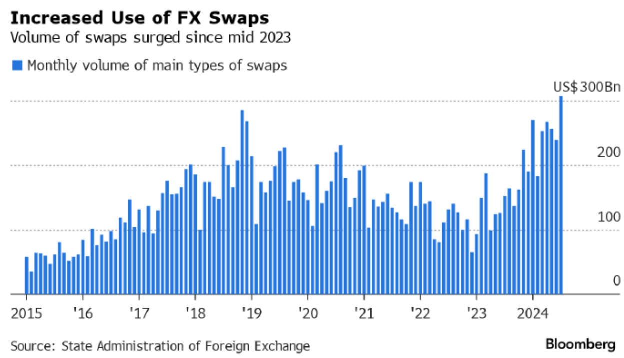
Sources: Bond Radar and IMF staff calculations

China

The RMB appreciated to its strongest level since June 2023. The currency appreciated on the day (+0.2%) to 7.0849/$ supported by the PBC's stronger fix and a softer US dollar. Chinese equities declined (CSI 300: -0.8%) while share prices of brokers outperformed (+0.5%) on company specific news of the two major state-owned brokers Guotai Junan Securities and Haitong Securities. The two companies are planning to merge, which, pending approval, could create the largest brokerage in China with RMB 1.68 trn (US$237 bn) in total assets. The plan has sparked speculation about further consolidation in the brokerage industry amid a global expansion push.

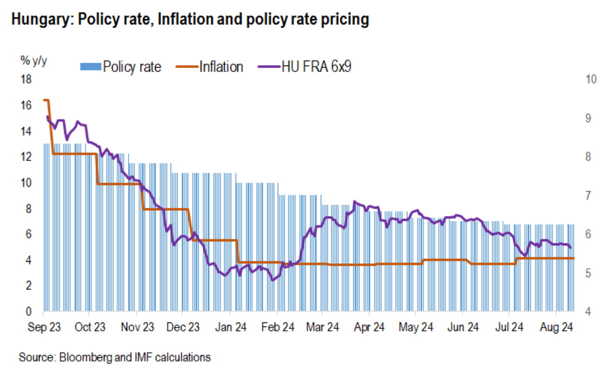
The People's Bank of China (PBC) may further reduce the required reserve ratio (RRR) for banks, currently around 7%, according to a top official. Zou Lan, head of the PBC's monetary policy department, stated that there is still room for more RRR cuts, although the effects of previous cuts are still unfolding. However, he noted that additional interest rate cuts may be limited due to narrowing profit margins for banks and the movement of deposits into asset management products. Zou also highlighted the PBC's goal to create a market-driven interest rate system by narrowing the gap between policy rates and market rates. This includes using the PBC's seven-day repo rate as China's main policy rate, signaling a shift to make short-term rates a more prominent tool for guiding market behavior. Zou also addressed rumors about whether the PBC's trading of treasury notes could flood the market with liquidity, clarifying that these operations are mainly aimed at managing liquidity and keeping the supply of base money balanced.

China's use of FX swaps to manage the RMB is reportedly exposing its banks to potential losses. According to a Bloomberg article, state-owned banks have used FX swaps to build short positions in the US dollar, exceeding US$100 bn, aiming to support the RMB during heavy selling pressure. This strategy allows China to stabilize the RMB without depleting foreign reserves but has led to mark-to-market losses for banks in the magnitude of billions when the RMB weakened. Some traders believe that these banks can delay booking the losses by initiating new swaps, hoping for Fed rate cuts to strengthen the RMB and reduce losses.



Hungary

The extent of easing priced for National Bank of Hungary (NBH) appears aspirational to some. Comments from Deputy Governor Virag coupled with the monetary policy committee's priority on stabilizing the forint and to anchor inflation seem to suggest that the NBH is in no rush cutting rates given inflation is expected to reaccelerate towards 4% by year-end, largely on base effects. Furthermore, the monetary policy outlook is seen uncertain after February 2025 given that the NBH will likely have a new Governor in Q1 2025. Against this backdrop, Bank of America analysts expect the NBH to deliver two -25bps rate cuts to take the policy rate to 6.25% by year-end, with rates then remaining on hold until the end of February 2025. This appears at odds with market pricing, which is for a -100bps cumulative amount of easing by the end of February 2025. Separately, July industrial production data released this morning contracted more than expected at -6.4% y/y (exp. -5.9%). Following the release, the forint slightly depreciated (-0.2%) against the euro, trading at 393.99/€.



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Global Financial Indicators

9/6/24 9:01 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities				%			%
United States		5506	-0.3	-2	5	23	15
Europe		4801	-0.3	-3	5	13	6
Japan		36391	-0.7	-6	4	12	9
China		3231	-0.8	-3	-3	-14	-6
Asia Ex Japan		72	0.2	-1	5	9	7
Emerging Markets		43	0.1	-2	5	9	6
Interest Rates				basis points			
US 10y Yield		3.70	-2.6	-20	-19	-58	-18
Germany 10y Yield		2.18	-3.0	-12	-2	-48	15
Japan 10y Yield		0.85	-2.6	-4	-5	19	24
UK 10y Yield		3.88	-3.9	-14	-4	-66	34
Credit Spreads				basis points			
US Investment Grade		136	0.0	2	-7	-12	2
US High Yield		382	3.6	18	-25	-32	-3
Exchange Rates				%			
USD/Majors		100.81	-0.3	-1	-2	-4	-1
EUR/USD		1.11	0.1	1	2	4	1
USD/JPY		142.9	-0.4	-2	-1	-3	1
EM/USD		45.9	0.1	0	1	-3	-5
Commodities				%			
Brent Crude Oil ($/barrel)		73.0	0.5	-5	-4	-12	-3
Industrials Metals (index)		140	0.3	-3	2	-2	-2
Agriculture (index)		55	0.0	2	2	-18	-11
Implied Volatility				%			
VIX Index (%, change in pp)		20.2	0.3	4.6	-7.5	5.8	7.8
Global FX Volatility		8.7	0.0	0.0	-0.2	0.4	0.6
EA Sovereign Spreads				10-Year spread vs. Germany (bps)			
Greece		102	-1.2	-4	-10	-35	-2
Italy		143	-0.7	2	-3	-33	-25
Portugal		61	1.0	0	-5	-14	-2
Spain		81	-0.3	-3	-6	-24	-16

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

Emerging Market Financial Indicators

Last updated: 9/6/2024 9:02 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		7.08	0.1	0.1	1	3	0		1.9	-0.3	-8	-7	-83	-61
Indonesia		15365	0.2	0.6	5	0	0		6.6	-2.3	-2	-21	8	13
India		84	0.0	-0.1	0	-1	-1		7.0	-1.9	-7	5	(65.7)	-25
Philippines		56	0.6	0.4	3	2	-1		5.0	-12.0	-17	-29	-97	-67
Thailand		34	0.4	1.0	6	6	2		2.4	-0.8	-2	-3	-66	-31
Malaysia		4.33	0.2	-0.2	3	8	6		3.7	-1.1	-2	-1	-12	0
Argentina		954	0.0	-0.3	-2	-63	-15		40.2	-112.2	-97	-433	-7731	-4614
Brazil		5.55	0.4	1.0	2	-10	-12		11.7	-10.7	-36	-18	15	126
Chile		938	0.5	-2.9	1	-7	-6		4.9	-1.5	-11	-20	-61	-6
Colombia		4130	0.7	1.1	0	-1	-7		7.9	0.0	4	-3	-60	23
Mexico		19.84	0.1	-0.6	-1	-11	-14		9.0	0.4	-15	-13	-13	50
Peru		3.8	0.1	-1.1	-2	-3	-2		6.5	-0.3	-2	-19	#VALUE!	-15
Uruguay		40	0.0	-0.1	0	-6	-4		9.6	4.8	7	8	28	11
Hungary		354	-0.1	0.4	3	2	-2		5.8	-2.0	-19	6	-126	-1
Poland		3.84	0.3	0.9	3	11	2		4.5	-9.6	-17	8	-34	-1
Romania		4.5	0.1	0.7	2	3	1		6.5	0.4	3	14	-12	31
Russia		89.9	-1.8	0.6	-5	9	-1							
South Africa		17.7	0.3	0.9	5	9	4		8.5	-7.0	-25	-28	-105	-65
Türkiye		33.96	0.0	0.3	-1	-21	-13		28.8	1.0	28	23	567	205
US (DXY; 5y UST)		101	-0.2	-0.5	-2	-4	0		3.51	-3.0	-20	-22	-91	-34

	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		3231	-0.8	-3	-3	-14	-6		126	-25	-29	-58	-32
Indonesia		7722	0.5	1	6	12	6		116	14	-11	-7	20
India		81184	-1.2	-1	2	22	12		112	-1	-11	-28	-4
Philippines		6936	0.4	1	4	11	8		101	11	-8	3	21
Thailand		1428	1.7	5	10	-8	1		0	0	0	0	0
Malaysia		1653	-0.7	-2	4	14	14		86	-3	-16	-10	1
Argentina		1765465	-1.8	6	21	202	90		1458	8	-201	-668	-455
Brazil		136502	0.3	0	8	18	2		236	15	-18	7	21
Chile		6362	-0.4	-2	3	8	3		128	7	-17	4	3
Colombia		1342	0.4	-2	3	28	12		328	11	-10	2	57
Mexico		51661	-0.3	-3	-1	-2	-10		332	9	-14	-25	-2
Peru		28304	1.0	0	1	23	9		150	6	-20	4	6
Hungary		72445	0.0	-1	3	30	20		164	11	-11	-28	15
Poland		83340	-0.1	-2	6	25	6		116	9	-9	5	19
Romania		17439	-1.6	-4	-2	29	13		214	13	2	11	13
South Africa		81918	-0.3	-2	3	10	7		310	12	-35	-68	2
Türkiye		9950	0.1	1	1	22	33		312	12	-30	-75	-2
EM total		43	-0.3	-2	5	9	6		414	7	-31	38	69

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

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