



- Chinese renminbi deepens run into its 16-year low versus the US dollar ([link](#))
- Markets price an ECB pause, but economists are divided on its rate decision next week ([link](#))
- Easing cycles in Hungary, Poland and the Czech Republic seen as justified ([link](#))
- US Treasury supply expected to reach a record high in 2024 in terms of duration ([link](#))
- Colombia's higher than expected August inflation may change expectations for easing ([link](#))

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Negative sentiment in stock markets continues on China-Europe pessimism

Major equity indices continued this week's declines on the back of concerns about growth in Europe and weakness in China. Today, stock prices in Europe and China continued to decline, extending losses from earlier this week, closing this week with losses of -1.2% and -1.4% respectively. In contrast with the aforementioned growth concerns, this week's declines in US stock prices may be partially explained by the relative resilience of the US economy. This relative resilience affects the outlook for the Fed, whereby a higher-for-longer scenario could lead to a sell-off in stocks over the next two months, according to Bank of America analysts. In addition, concerns about tensions between China and the US regarding microchips affected the technology sector's performance. The US dollar index remains close to its highest point since March 2023, even though it briefly dipped overnight, reportedly after dovish comments from Fed New York president Williams, who said that US monetary policy is in a good place. The renminbi continued to weaken, with the onshore renminbi continued to deepen its run into its 16-year low. Next week, the ECB will meet for its policy decisions; for this meeting, the market implied probability of a rate hike stands at 35%.

Key Global Financial Indicators

Last updated: 9/8/23 8:14 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		4451	-0.3	-1	-1	11	16
Eurostoxx 50		4185	-0.9	-2	-2	19	10
Nikkei 225		32607	-1.2	0	1	16	25
MSCI EM		39	-1.2	-3	-3	1	2
Yields and Spreads			bps				
US 10y Yield		4.24	-0.4	6	22	92	37
Germany 10y Yield		2.60	-1.3	5	13	88	3
EMBIG Sovereign Spread		425	3	3	16	-85	-27
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		47.2	0.1	-2	-1	-6	-5
Dollar index, (+) = \$ appreciation		105.0	-0.1	1	2	-4	1
Brent Crude Oil (\$/barrel)		90.5	0.6	2	5	1	5
VIX Index (% change in pp)		14.8	0.4	1	-1	-9	-7

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

Mature Markets

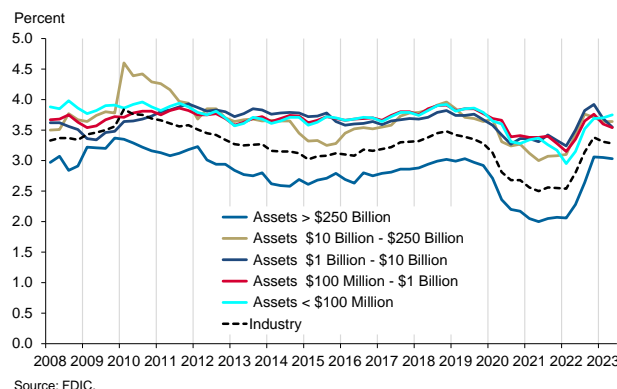
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United States

The technology sector was the main driver of the negative equity market performance on Thursday; Apple extended Wednesday's losses (-3.6%) by another 3.3%, following a headline that the Chinese government intends to extend the ban on using iPhones to government-backed agencies and state companies. Evercore ISI analysts argued that it would be difficult for China to take more substantive action against Apple without affecting the jobs in the country where most iPhones are assembled. Bank shares (-1.2%) also underperformed. According to the FDIC Q2 quarterly banking profile released Thursday, banks'

net interest margin declined for the second consecutive quarter, driven by rising funding costs for non-deposit liabilities, including FHLB and borrowings from the Fed's Bank Term Funding Program (BTFP).

Quarterly Net Interest Margin

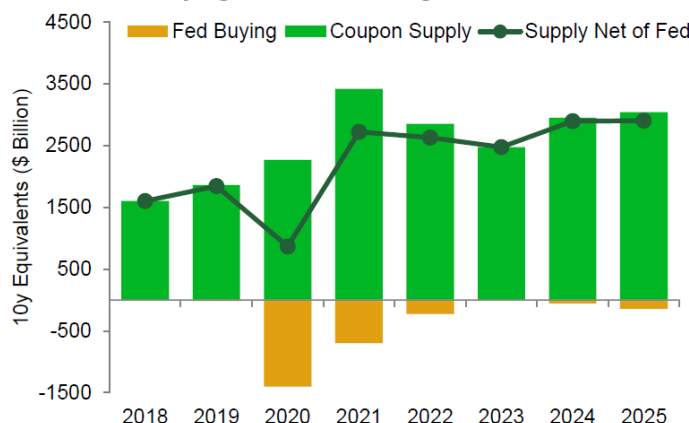


Source: FDIC.

The 2-year Treasury yield declined by 6.5bps on Thursday, with the yield curve steepening. Broader declines in global sovereign bond yields were attributed by analysts in part by spillovers from the UK: the 2-year gilt yield fell by more than 10bps after a survey found UK firms expect price raises at the slowest pace in two years.

Supply in the Treasury market will reach a record high in 2024 in terms of duration. At the August refunding meeting, the Treasury announced that it intends to gradually increase coupon auction sizes. TD Securities analysts expect coupon auction sizes to continue to increase at the November 2023 and February 2024 refunding meetings, likely resulting in the supply of coupon securities from \$1.04 tn in 2023 to \$1.46 tn in 2024. On a 10-year equivalent basis, the duration supply to markets, net of the Fed activity, will reach the highest levels on record. Concerns over future supply pressures could be one of the reasons behind increasing term premium.

Figure 4: 10y Equivalent Supply Net of Fed Buying to Hit Record High in FY2024

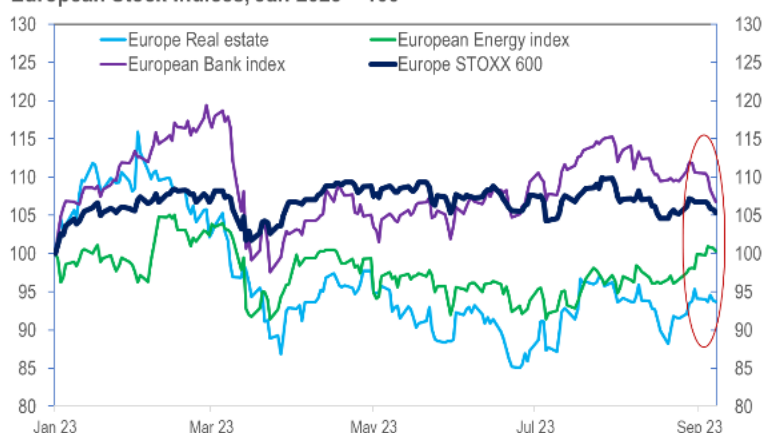


Note: Analysis uses US fiscal years.
Source: NY Fed, Treasury, TD Securities

Euro Area

European equities were trading in the red (Stoxx 600 Europe index -0.2%), on track for its eight consecutive daily decline. While the Stoxx 600 Europe index remains roughly 6.6% higher YTD, the index is now roughly 1.2% lower than at the start of the month, and is on track for its eight consecutive day of losses. Bloomberg notes that this would be the longest daily run of losses since 2016. Equities have been under pressure as data pointed to weakening momentum in the euro area economy, and also concerns about growth in China and focus on the policy outlook in the US. For example, Barclays analysts see yesterday's downward revision to Q2 euro area growth as consistent with stagnation in the euro area, against a backdrop of monetary tightening. Analysts expect activity to be weaker in the second half of this year. Moreover, while data released this morning showed industrial production data in France surprising on the upside in July, ING analysts highlight that the outlook for the French industry remains poor. Further adding to concern, this morning benchmark European gas prices increased on news of partial strikes in natural gas export sites in Australia. **The euro was marginally stronger against the dollar, trading at around 1.07/\$. Sovereign yields continued to edge lower (10y bund -1bps to 2.60%), while overnight index swaps continue to show a roughly 35% probability of a 25bps hike by the ECB next week.**

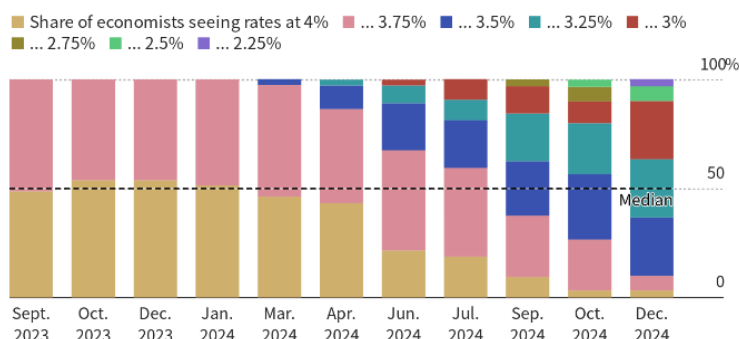
European Stock indices, Jan 2023 = 100



Source: Bloomberg and IMF calculations

Economists are close to evenly divided on whether the ECB will hike or pause next week, with a small majority of economists expecting the final hike in October and the first rate cut in March 2024. According to a recent Bloomberg poll, roughly 65% of economists expect the ECB to confirm by the end of this year that rates have peaked. As regards the ECB's balance sheet, 39% of respondents expect that the ECB could bring forward the end of PEPP reinvestments, roughly double the share of respondents that saw this as a possibility prior to the July ECB meeting, according to Bloomberg.

Views on ECB Rate Path Next Year Diverge Sharply



Source: Bloomberg survey of economists conducted Sept. 1-6

Bloomberg

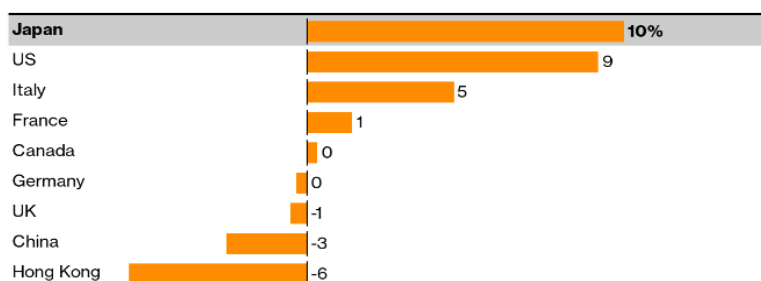
There is also now a slightly larger portion of economists that envisage that active APP sales could compliment APP roll-offs at some point in the future (43% of respondents versus 37% previously).

Japan

Japanese stocks declined -1%. By contrast, price targets for Japanese stocks had risen more than any other global peers over the past three months amid robust earnings results, Bloomberg reported. However, yesterday GDP growth for Q2 was revised down to +4.8% sa q/q (flash: +6%) on lower capex and consumption. In addition, labor cash earnings missed expectations and slowed to +1.3% y/y (consensus: 2.4%, previous: 2.3%). **The yen depreciated -0.1%, 10Y yields declined -0.8bps.**

Japan Optimism

Japan sees most price target hikes by analysts among global peers



Source: Bloomberg data

Note: data based on market cap weighted percentage change in price target over past three months of the Bloomberg World Large & Mid Cap Index

Bloomberg

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Equity markets in EMEA were mixed with most currencies trading in a tight range. The Hungarian forint was strengthening against the euro (+0.1% to 361.24/€) with data this morning showing Hungary's inflation easing marginally less than expected in August, but still declining to the lowest level in a year.

Asian equities were mixed, flat on net. India continued to outperform +0.5%. India's \$20.9bn net inflows from foreign equity funds in the last 12 months, is second only to Japan, sharp contrast to \$68bn outflows from China, Bloomberg reported. **Hong Kong SAR's** stock market was closed on Friday after city was shut down amid record rainfall in 140 years. **Asian currencies were mixed.** Offshore renminbi weakened towards the lowest on record, broke past 7.35 during the day, after a surprisingly weak yuan fixing by the People's Bank of China (PBC). Onshore renminbi tumbled to a 16-year low. Thai baht led the gains (+0.4%), followed by Philippine peso and Indian rupee (+0.3%). South Korea yields fell -7.1bps, followed by Indonesia (-4.9bps). **Philippines'** Bangko Sentral ng Pilipinas (BSP) conducted its first variable-rate auction of its overnight reverse repurchase facility. BSP said this auction format will allow more room for interbank market price discovery. **LATAM equities mostly showed declines in the range of -0.3 to -0.9% and currencies saw modest weakening.** However, markets in Colombia bucked this trend as both equities and currency gained 1.6% and 0.9%, respectively. **Colombia's August inflation number (released post market close) eased by less than expected** to 11.43% y/y, versus 11.78% in July and 11.19% surveyed. As per media reports, this could dampen the expectations of monetary policy easing, which as per a recent central bank survey, was anticipated to start in October.

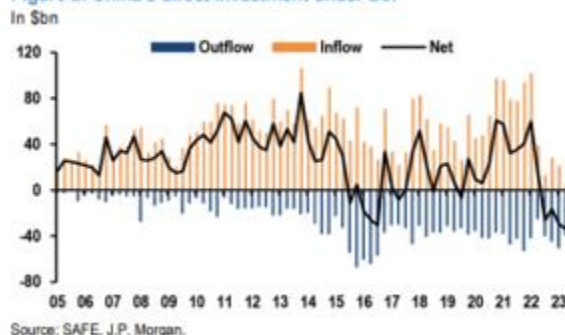
China

The offshore yuan weakened toward its lowest on record versus the US dollar. Offshore yuan broke past 7.35 during the day, after a surprisingly weak yuan fixing by the People's Bank of China (PBC). Onshore renminbi tumbled to a 16-year low. **While some analysts suggested yuan weakness reflects US dollar strengths as a dominant driver, others also pointed to shifts in external sector fundamentals.** JP Morgan noted a substantial deterioration in FDI inflows for China this year, with inflow down to \$4.9bn in 2Q, a 26-year low. Citi thought China's recent policies to help real estate demand isn't enough to sustainably form a bottom for sentiment. This shall further weigh on China's BoP dynamics, including narrower trade balance, wider services deficit, capital flows weighed by investor sentiment and rate differential, while FX tools deployment is more about containing the pace of moves. OCBC cautioned against sporadic liquidity tightening. **Chinese stocks fell -0.5%.** The US government began official probe into SMIC's Huawei chip. **10-year government bond yields were little changed.**

Offshore Yuan Declines After PBOC Set Weaker Fixing



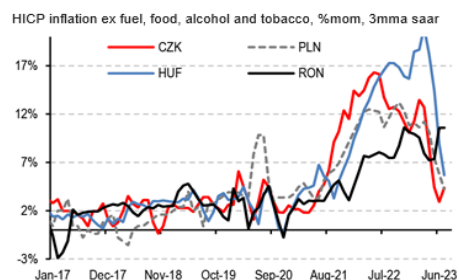
Figure 2: China's direct investment under BoP



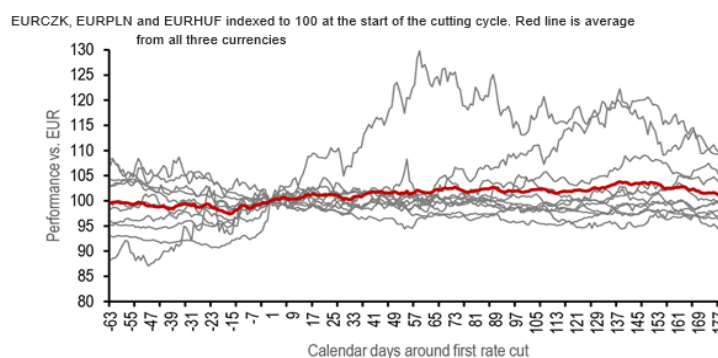
Central and Eastern Europe

Analysts think the start/continuation of easing cycles in the CE3—i.e., Hungary, Poland and the Czech Republic—is justified and see scope for markets to price lower terminal rates. Respective central banks of Hungary as well as Poland have started to cut policy rates and JPMorgan analysts argue that the dominant theme in the region is now likely to be the “delivery” phase of the easing cycle. With core inflation currently below policy rates in Hungary, Poland and the Czech Republic, JPMorgan analysts think that the start/continuation of easing cycles in the coming months is justified. Moreover, analysts also estimate that lower rates could still be priced in these three countries. As regards currencies, analysts expect CE3 exchange rates to weaken against a backdrop of high core yields but note that there is scope for total FX return differentiation. While JPMorgan analysts still forecast that the Czech National Bank would only start cutting rates in February 2024, they see a possibility that the central bank could already start easing rates in November.

Core inflation momentum is below policy rates



Performance of EUR-CE3 is not very consistent around cutting cycles

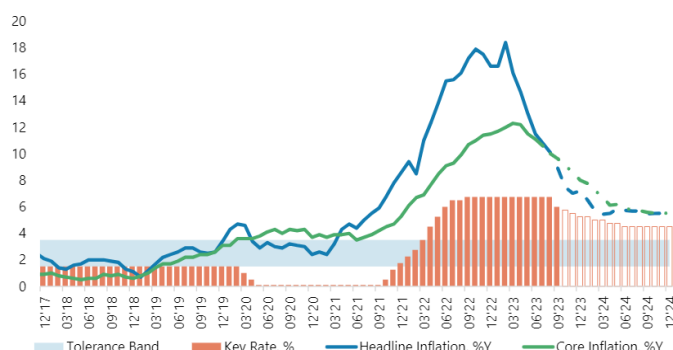


Poland

The polish zloty continued to weaken after Governor Glapinski's press conference yesterday was seen as dovish, with analysts now expecting more rate cuts. At the closely watched press conference the governor pushed back against views that the rate cut was politically motivated ahead of the October 15 parliamentary elections. He noted that the 75bps rate cut was justified given inflation has come down and that the deterioration in the economic situation was more severe than the council had expected. While he refrained from any clear forward guidance contacts noted strong signals about future rate easing. Morgan Stanley analysts now expect 25bps rate cuts at each of the policy meetings until the end of this year, and a further 75bps of rate cuts in 2024 with the policy rate expected to reach 4.5% (from 5% previously). Against this backdrop analysts have also revised their 2024 inflation forecasts higher. The polish zloty

weakened a further 1.2% yesterday but was trading stronger marginally against the euro this morning (+0.1% at 4.62/€).

Exhibit 1: We now see a lower policy rate but higher inflation path

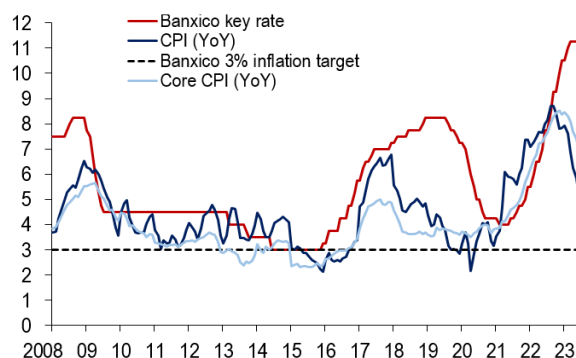


Source: Haver Analytics, Morgan Stanley Research forecasts; Note: Dashed line and unfilled bars represent Morgan Stanley forecasts.

Mexico

August inflation decelerated to 4.64% (-15bps sequentially) which was broadly in line with the consensus estimates. Core inflation too declined (56bps sequentially) to 6.08%. However, inflation has remained above the Bank of Mexico (Banxico) inflation target of 3% (+/- 1%) due to strong domestic demand. As a result, Banxico has left its policy rate unchanged at 11.25% since March 2023 while some of its regional peers have started cutting policy rates. As per a market survey, inflation expectations for 2023 and 2024 are at 4.7% and 4%, respectively, which implies the central bank is likely to maintain its hawkish stance.

Headline inflation and policy rate



Sources: Bloomberg, and IMF staff calculations

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), and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Benjamin Mosk (Senior Financial Sector Expert), 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.

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Global Financial Indicators

9/8/23 8:15 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		4451	-0.3	-1	-1	11	16
Europe		4185	-0.9	-2	-2	19	10
Japan		32607	-1.2	0	1	16	25
China		3740	-0.5	-1	-6	-7	-3
Asia Ex Japan		65	-1.2	-2	-3	0	0
Emerging Markets		39	-1.2	-3	-3	1	2
Interest Rates			basis points				
US 10y Yield		4.24	-0.4	6	22	92	37
Germany 10y Yield		2.60	-1.3	5	13	88	3
Japan 10y Yield		0.66	-0.2	2	5	40	23
UK 10y Yield		4.43	-2.1	1	5	129	76
Credit Spreads			basis points				
US Investment Grade		147	-0.6	2	2	-21	-11
US High Yield		416	1.7	0	-10	-87	-65
Exchange Rates			%				
USD/Majors		105.01	-0.1	1	2	-4	1
EUR/USD		1.07	0.1	-1	-2	7	0
USD/JPY		147.4	0.0	1	3	2	12
EM/USD		47.2	0.1	-2	-1	-6	-5
Commodities			%				
Brent Crude Oil (\$/barrel)		90.5	0.6	2	6	13	10
Industrials Metals (index)		141	-0.9	-1	-1	-6	-15
Agriculture (index)		66	-0.1	0	0	-1	-3
Implied Volatility			%				
VIX Index (%, change in pp)		14.8	0.4	1.2	-1.2	-8.9	-6.9
US 10y Swaption Volatility		104.6	0.0	-14.1	-17.8	-23.5	-21.1
Global FX Volatility		8.4	0.0	0.3	-0.2	-2.9	-2.3
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		136	0.3	6	3	-115	-69
Italy		174	1.3	5	9	-52	-40
Portugal		73	-1.2	0	-1	-28	-29
Spain		104	0.4	1	1	-9	-5

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

Emerging Market Financial Indicators

Last updated: 9/8/2023 8:16 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)						
	Level		Change (in %)				YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
	vs. USD		(+) = EM appreciation					% p.a.						
China		7.34	-0.1	-1.0	-2	-5	-6		2.7	0.5	7	4	4	-32
Indonesia		15325	0.0	-0.6	-1	-3	2		6.6	-3.7	16	21	-63	-39
India		83	0.3	-0.3	0	-4	0		7.6	1.0	9	10	19.0	18
Philippines		57	0.3	-0.1	-1	1	-2		5.9	-2.5	-2	-20	24	-9
Thailand		36	0.2	-1.5	-2	3	-3		3.0	-3.8	12	23	33	40
Malaysia		4.68	0.0	-0.7	-2	-4	-6		3.9	-0.4	2	0	-20	-19
Argentina		350	0.0	0.0	-19	-60	-49		118.8	91.2	-105	2757	3960	3057
Brazil		4.98	-0.2	-1.8	-2	5	6		11.5	5.0	39	46	-32	-108
Chile		885	-1.3	-3.7	-3	0	-4		5.5	-0.5	10	25	-127	11
Colombia		4039	0.9	1.4	1	9	20		8.4	0.0	17	44	-137	-139
Mexico		17.48	0.7	-2.2	-2	14	12		9.0	-7.5	25	34	23	28
Peru		3.7	-0.1	-0.5	0	5	3		7.0	#####	23	16	-125	-97
Uruguay		38	-0.5	-1.1	0	7	5		9.3	2.9	8	29	-199	-137
Hungary		361	0.2	-1.3	-2	10	3		7.1	2.0	29	-13	-271	-254
Poland		4.31	0.4	-3.8	-6	9	2		4.6	-11.3	-17	-22	-144	-157
Romania		4.6	0.1	-1.0	-3	5	0		6.6	-0.7	4	-1	-145	-110
Russia		97.8	0.5	-1.5	-1	-38	-24							
South Africa		19.1	0.5	-1.3	-1	-8	-11		9.4	-2.8	9	4	40	28
Turkey		26.85	0.0	-0.4	1	-32	-30		23.6	17.0	199	360	1225	1379
US (DXY; 5y UST)		105	-0.1	1.3	2	-4	1		4.36	-1.6	6	25	94	35

	Equity Markets							Bond Spreads on USD Debt (EMBIG)					
	Level		Change (in %)				YTD	Level		Change (in basis points)			YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		Last 12m	Latest	7 Days	30 Days	12 M	
								basis points					
China		3740	-0.5	-1	-6	-7	-3		184	-1	-3	-22	7
Indonesia		6925	-0.4	-1	1	-4	1		131	1	10	-56	-9
India		66599	0.5	2	1	12	9		142	2	3	-22	0
Philippines		6223	0.6	1	-4	-6	-5		107	3	9	-32	10
Thailand		1547	-0.2	-1	2	-6	-7		0	0	0	0	0
Malaysia		1455	-0.4	-1	0	-3	-3		98	1	5	0	-2
Argentina		548015	-6.2	-16	18	287	171		2150	41	126	-207	-55
Brazil		115985	-1.2	-1	-3	6	6		234	3	6	-68	-40
Chile		5886	-0.3	-2	-6	7	12		128	4	11	-52	-4
Colombia		1063	1.6	-2	-9	-12	-17		340	15	20	-84	-32
Mexico		52483	-0.9	-1	-2	13	8		360	-1	-1	-60	-21
Peru		22782	-0.7	-2	-4	19	7		154	6	6	-45	-26
Hungary		56193	-0.7	1	2	38	28		200	1	8	-51	-22
Poland		66156	0.3	-4	-5	35	15		126	3	10	84	53
Romania		13703	0.3	3	5	15	17		219	8	22	-92	-37
South Africa		73197	0.0	-2	-5	9	0		386	1	28	-62	19
Turkey		8356	0.2	4	13	143	52		398	3	-1	-243	-42
Ukraine		507	0.0	0	0	-2	-2		3405	-19	-203	-511	-674
EM total		39	0.2	-3	-3	1	2		382	6	11	-57	7

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

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