GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

MONDAY, SEPTEMBER 9, 2024
LEAD EDITOR: JOHANNES S. KRAMER

- **The 2y-10y US Treasury yield spread closed positive for the first time in 26 months** (link)
- **BoE expected to keep annual pace of QT unchanged** (link)
- **Japanese stocks inch lower following on weaker yen after downward Q2 GDP revision** (link)
- **Fund flows into EM hard currency bond funds have been contracting** (link)
- **Weaker activity data could compel Türkiye's central bank to front-load easing** (link)
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Jumbo pushback following payrolls data

Markets reacted cautiously to Fed policy guidance. Friday's labor market statistics painted a somewhat mixed picture of the US job market, with weaker employment numbers for the second consecutive month but a slight decline in the unemployment rate. In his Friday speech, Fed Governor Waller downplayed the likelihood of a jumbo rate cut in September, though he expressed some openness to front-loading rate cuts if necessary. Following his remarks, forward markets priced out the possibility of a jumbo rate cut at the September meeting, instead leaning towards cuts of larger magnitude in November and December. The stock market reacted cautiously to this pushback, with the S&P 500 and Nasdaq notably contracting as the Treasury yield curve disinverted for the first time in two years. Alongside this, market participants are closely watching upcoming US inflation data and the ECB meeting later this week. Attention is also on Tuesday's first televised debate between Harris and Trump. Elsewhere, Hungary's Prime Minister Orbán is expected to announce significant spending measures ahead of the upcoming elections, while former People's Bank of China Governor Yi Gang urged policymakers to immediately address deflationary pressures.

Key Global Financial Indicators

Last updated: 9/9/24 8:47 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
S&P 500		5408	-1.7	-3	1	21	13.39
Eurostoxx 50		4765	0.6	-4	2	12	5
Nikkei 225		36216	-0.5	-6	3	11	8
MSCI EM		42	-1.8	-3	-1	8	4
Yields and Spreads				bps			
US 10y Yield		3.74	3.0	-17	-20	-53	-14
Germany 10y Yield		2.21	3.5	-13	-2	-40	18
EMBIG Sovereign Spread		388	1	0	-34	-33	5
FX / Commodities / Volatility				%			
EM FX vs. USD, (+) = appreciation		45.6	-0.2	-1	-1	-3	-5
Dollar index, (+) = $ appreciation		101.6	0.4	0	-2	-3	0
Brent Crude Oil ($/barrel)		71.7	0.9	-8	-10	-21	-7
VIX Index (%, change in pp)		21.4	-1.0	6	1	8	9

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

Mature Markets

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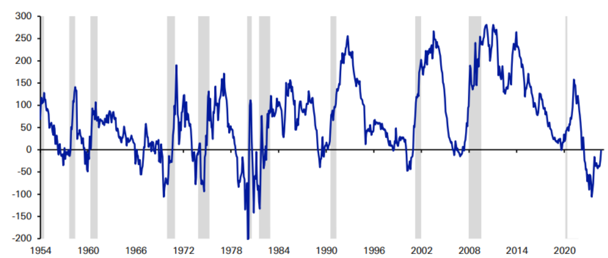
United States

This week will deliver the last batch of economic data for the U.S. economy before the FOMC meeting on September 17–18, including the CPI on Wednesday, the PPI and weekly jobless claims on Thursday, and the preliminary release of Michigan Consumer Survey results on Friday. The ECB is holding a policy meeting on Thursday and is almost certain to cut its policy rate by 25 basis points. The July figures for the UK's GDP and industrial production will be released on Wednesday.

Figure 1: US 2s10s Yield Curve (bps) with recessions shaded. Recessions only happen when the yield curve has steepened back up, and often only when the curve is back in positive territory...

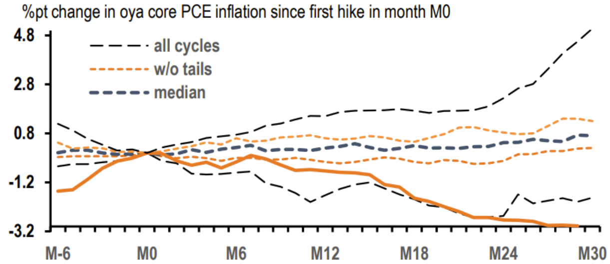


Source: GFD, Bloomberg Finance LP, Deutsche Bank

The last four recessions began following a yield curve disinversion. This week, the 2y to 10y Treasury yield spread turned positive after 26 months of inversion—the longest in four decades—rising by +6 bps on Friday, approaching 5 bps. This shift has triggered debate on whether the yield curve's reliability in predicting recessions has weakened, or if the US economy has managed to avoid a hard landing. Some market contacts point out that the term premium compression brought about by the Fed's large-scale asset purchases presents a confounding factor. Others, including analysts at Deutsche Bank, emphasize that the last four recessions began only after the 2y-10y yield spread disinverted, not at its most negative point. That said, the NY Fed recession model, which relies on the 3m to 10y yield spread to assess recession probabilities, provides a more comprehensive view, accounting for the delays in officially recognizing recessions identified by the National Bureau of Economic Research. With the 3m-10y spread remaining at -130 bps, it suggests a degree of caution in declaring that the yield curve's predictive power has diminished, especially when considering longer-term trends.

Figure 3: PCE inflation around policy tightening cycles

%pt change in oya core PCE inflation since first hike in month M0



Source: BEA, J.P. Morgan

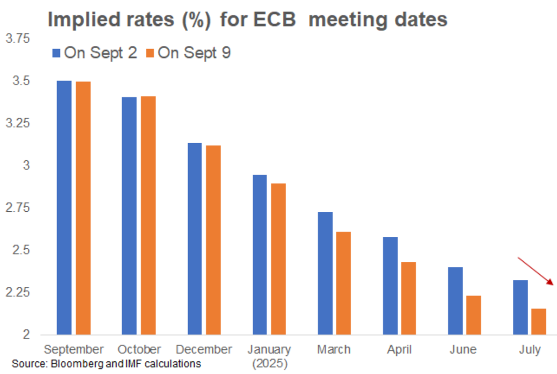
This Fed tightening cycle coincided with better disinflation than most previous ones. JP Morgan analysts assessed the last 11 Fed tightening cycles since the 1960s to gauge the cumulative change in core PCE inflation, starting 6 months before the first hike until 30 months after. While not accounting for exogenous factors, such analysis gives indications that the latest tightening cycle has led to one of the sharpest drops in core inflation. The trajectory of core PCE inflation during the latest cycle exemplifies this, having peaked at 5.6% before the tightening in early 2022, while falling to 2.6% in the latest July 2024 reading. Other market contacts acknowledge that such analysis might be overly simplistic, as it does not account for broader economic shifts, such as the normalization of supply and demand disruptions after the Covid pandemic that coincided with the latest tightening cycle. Taking these factors into account suggests that the Fed's policy tightening alone might not fully explain the decline in core inflation. External factors, such as the easing of supply chain bottlenecks and shifts in consumer demand also played a key role in the disinflation.

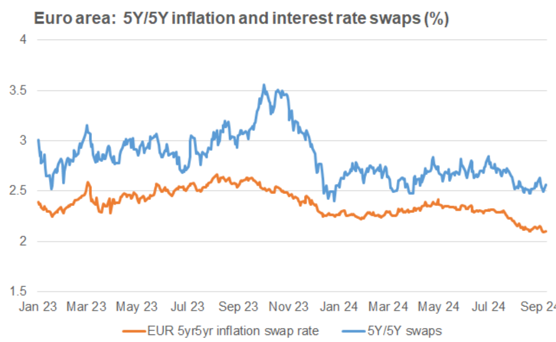
Euro Area

This morning, European equities rose, bund yields climbed, and the euro weakened. The Stoxx 600 index retracing some of last week's losses (+0.5%), lifted by gains in the technology and banking sector that gained +1.2% each. 10y bund yields rose this morning (+5bps) to approach 2.22% while remaining about 10bps lower than at the start of the month. The euro depreciated versus the dollar (-0.4%) to

$1.1043/€. In terms of data, the eurozone Sentix Investor Confidence index disappointed in September, falling to -15.4 (exp. -12.2 from -13.9).

A weaker outlook and slowing wage growth fuels expectation of faster ECB rate cuts. According to a recent Bloomberg survey mentioned in Friday's GMM, the ECB is expected to cut rates by -25bps per quarter until the deposit rate reaches 2.5% by September 2025. Goldman Sachs analysts, which have previously forecasted cuts until the rate hit 2.25% by December 2025, have revised its view, now predicting cuts will continue until the deposit rate reaches 2% by July 2025. Despite stubbornly high services inflation, they still expect a -25bps cut in September, followed by a pause in October and another -25bps cut in December. They argue that a weakening economic outlook, with data falling short of the ECB's June projections, and the prospect of slower services inflation next year due to easing wage pressures support a faster pace of cuts. HSBC analysts also suggest that sluggish economic growth and weaker consumer demand could lead the ECB to adopt a more cautious, dovish approach. Money markets have responded by pricing in -62bps of easing by the end of 2024 (unchanged from a week ago) and -160bps by July 2025 (compared to -142bps a week ago). A -25bps rate cut remains fully priced for Thursday's ECB meeting.

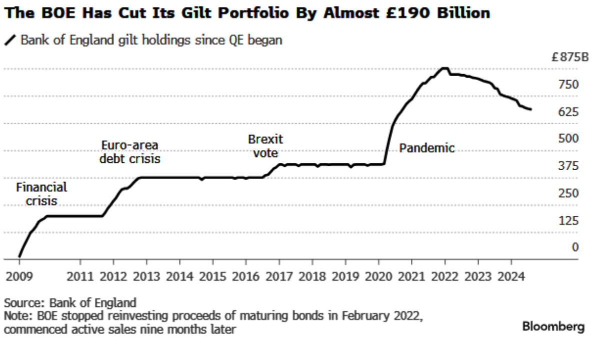


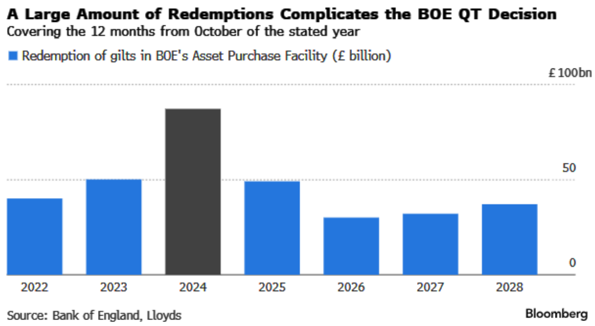


United Kingdom

The pound was weaker against the dollar this morning (-0.4% at 1.3077) but little changed against the euro, while 10y gilts yields were higher (+4bps at 3.92%). Contacts are focused on the jobs data due tomorrow, with some contacts arguing that weakening UK labor market data could see the market price in two BoE interest rate cuts this year (markets are currently pricing in -44bps of easing by end-2024).

The Bank of England (BoE) is expected to maintain the pace of quantitative tightening next year. The BoE's role in the Gilt market has become a key focus for market participants, particularly as the BoE is seen to provide guidance on the pace of reducing its Asset Purchase Facility (APF) at its meeting on September 19, ahead of the Autumn Budget presentation to Parliament on October 30. To recall, the BoE has reduced its gilt holdings by £190bn to £688bn through a combination of not reinvesting maturing securities and active gilt sales. Over the past 12 months, the BoE's gilt holdings declined by £100bn, with active sales and maturing gilts contributing equal amounts. However, in the coming year, maturing gilts will amount to £87bn. Most respondents in the BoE's recent market survey expect the annual reduction in gilts held in the APF to remain unchanged at £100bn, implying that active sales would total £13bn. Some analysts, however, expect the BoE to accelerate the pace of active sales to maintain continuity. Deutsche Bank, for instance, projects £40bn in active sales over the next 12 months, while Citibank analysts foresee the BoE increasing the total quantitative tightening (QT) envelope between £120bn and £140bn. On the other hand, some analysts believe the BoE could halt active sales, citing concerns that certain BoE repo facilities may not be "*effective and attractive*" enough, as highlighted by BoE officials.



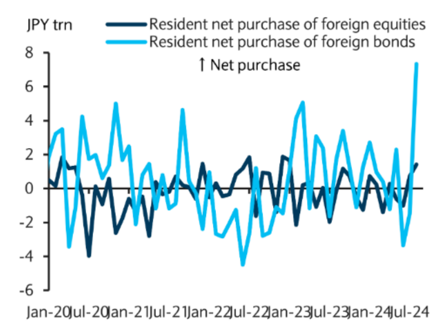


Japan

The yen weakened and Japanese stocks slipped as Q2 growth estimates were revised down. Growth for Q2 GDP was revised to +2.9% annualized q/q, down from the preliminary reading of +3.1% (exp. +3.2%). Japanese stocks ended -0.5% lower, after dropping up to -3.1% in the morning session, led by tech and exporter stocks. The yen similarly depreciated (-0.6%) to ¥143.64/$, snapping a four-session rally. Although some analysts believe the modest GDP revision does not alter the fundamental outlook for the economy or the Bank of Japan's rate path, Bloomberg analysts suggest the disappointing revision, combined with uncertainty over US interest rates, might have prompted some levered funds to unwind short dollar-yen positions, which were initially based on a risk-off sentiment expected to drive yen strength. This unwinding is seen to have contributed to the yen's weakness today.

Japanese purchases of foreign bonds notably climbed in August. Latest data from the Ministry of Finance in international security transactions for August indicate that domestic investors turned net buyers of foreign medium-long term bonds for the first time in three months in August, at +¥7.34tn (from -¥1.48 tn in July). Net buying reaching a record, surpassing the previous monthly peak of +¥5.45tn observed in July 2016, which Barclays analysts attribute to global risk aversion and the positive momentum brought about by the decline in yields. Excluding net buying by banks' banking accounts, which appear volatile and mostly foreign currency-funded (+¥2.66 tn), net buying still reflected a record at +¥4.68 tn (July: +¥242.3 bn), as Goldman Sachs analysts point out. Domestic investors were also large net buyers of foreign equities, at +¥1.41tn (from +¥724.2 bn in July). Conversely, foreign investors sold Japanese equities on net for the third consecutive month in August (-¥1.0 trn), with accelerated selling towards the end of the month, as Barclays analysts point out.

Figure 1. Japanese investment in foreign securities



Source: MoF, Barclays Research

Emerging Markets

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This morning, EMEA equities and currencies lacked clear trend. Ahead of key regional inflation data due this week, CEE currencies were mostly unchanged against the euro, although the Hungarian forint was weaker (-0.2%) against the euro to trade at 394.4/€. According to Bloomberg, Prime Minister Orbán is expected to introduce a wave of spending ahead of upcoming elections in 2026, news of which led the currency to erase earlier gains. The Turkish lira was weaker (-0.2%) against the dollar to trade at 34.05/$. Separately, Bloomberg reports that the Egyptian government is considering issuing green sukuk bonds—which are sharia-compliant instruments where proceeds are fully used to fund or refinance green projects—to diversify the country's investment base.

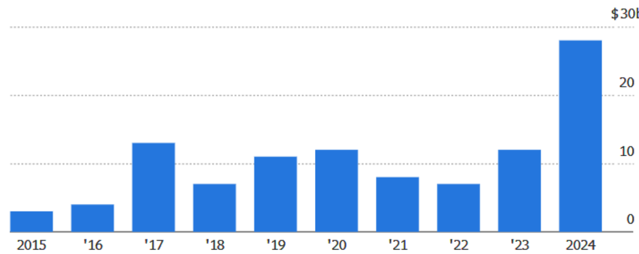
Asian equities and currencies are weaker. In aggregate, EM Asian stock markets fell (-1.5%), with market sentiment undermined following the release of US payrolls data on Friday. Asian currencies depreciated and government bond prices similarly fell, exemplified by the underperformance of the Philippine peso (-1.0%).

On Friday, Latin American assets declined. Stocks declined in Brazil (-1.4%), Mexico (-1.1%), Colombia (-1.0%), Chile (-1.8%), and Peru (-0.8%). Against the dollar, currencies depreciated in Brazil (-0.5%), Mexico (-0.6%), Chile (-0.3%), and Colombia (-0.3%).

EM Bond Issuance

Emerging market (EM) bond issuance surged notably during the first week of September. Last week, issuance volumes reached $28bn, more than double the amount seen during the same period last year. Concerns about potential market volatility—such as the upcoming US presidential election and the August market panic, which could drive up borrowing costs—are cited by market contacts as factors prompting issuers to frontload their funding needs. For now, EM issuers continue to benefit from relatively low yields compared to the last two years, averaging 6.5%. US dollar bond sales accounted for 86% of the new issuance last week. Year-to-date dollar bond sales by EM issuers have surged 54% to $349bn, as issuers seek liquidity and favorable borrowing terms.

Record Start to September
Emerging market borrowers sell $28 billion worth of Eurobonds in a week



Source: Bloomberg

EM Bond and Equity Flows

Fund flows into EM bond funds have been contracting, driven by those from hard currency funds. Last week's EPFR data shows that bond funds witnessed outflows in the magnitude of -$429mn (from +$265mn). These came predominantly from hard currency funds, which saw outflows of -$364mn (from +$453mn). Conversely, outflows seen from local currency funds decreased to -$65mn (from -$188mn). Bond ETFs turned to outflows of -$264mn (from +$293mn). EM equity fund outflows decreased to -$59mn (from -$136mn). Equity ETFs saw decreased inflows of +$260mn (from +$797mn), while non-ETF outflows decreased (-$318mn, from -$933mn). Across regional equity funds, there were outflows in the Asia ex-Japan (-$715mn) and Latam (-$111mn) regions, while the EMEA region saw inflows (+$10mn). Year-to-date, flows stand at -$15.2bn and -$17.9bn for bonds and equities.

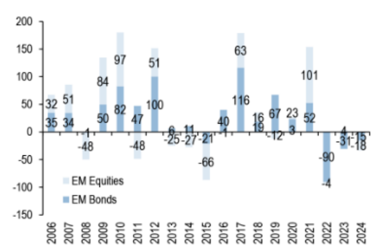
Figure 1: Weekly cross-asset flows

USD billion

	Asset	8w flows (8w ago → current)	This wk	YTD
Fund Flows	**EM Bonds and Equities**		-0.5	-33.2
	EM Bonds		-0.4	-15.2
	Hard Ccy		-0.4	-5.0
	Local Ccy^		-0.1	-10.2
	o.w. EM ex-China		0.0	-8.9
	o.w. China		0.0	-1.7
	EM Equities		-0.1	-17.9
	US HG		5.7	246.7
	US HY		0.6	17.9
	Global Equities		-4.9	113.8
	EM Bond and Equity ETFs		0.0	9.0
	EM Bond ETFs		-0.3	-2.3
	EM Equity ETFs		0.3	11.3
	Non-resident EM flows*		-1.3	7.7

Figure 2: EM bond and equity fund flows

USD billion

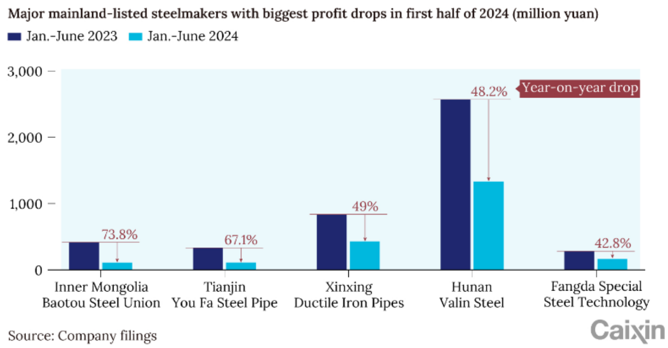


*High-frequency non-resident EM portfolio flow data where available. ^Local ccy split is retail only. *Source for all charts and data in this report: J.P. Morgan, EPFR Global, Bloomberg Finance L.P.*

China

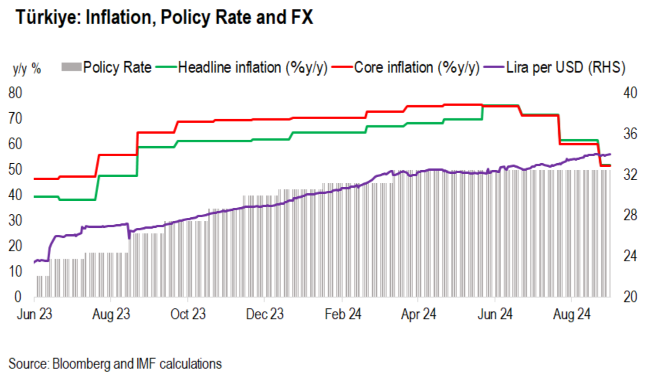
Disappointing August CPI and PPI readings point to lingering deflation risk. China's consumer and producer price inflation in August missed estimates. While CPI inflation edged up slightly to +0.6% y/y (exp. +0.7% from +0.5%), higher food prices due to bad weather have driven the gain. Meanwhile, PPI inflation dipped deeper into deflation, printing at -1.8% y/y (exp. -1.5% from -0.8%). Chinese stocks declined (CSI 300: -1.2%), with continued correction in high dividend stocks. Energy (-2.5%) and bank (-1.8%) stocks led the losses, down a total of 8.3% and 9.5% respectively in the past nine trading days. The RMB depreciated (-0.4%).

Falling prices and weaker demand have weighed heavily on the Chinese steel industry. A Caixin analysis highlights that profits among major mainland-listed steelmakers have come under pressure, comparing profits reported in H1 2024 to H1 2023. The analysis identifies Inner Mongolia BaoTou as the worst performer, with a net profit contraction of -74%. Commentary from market contacts and company officials suggests that the profit slump will deepen in Q3 due to delays in infrastructure projects and ongoing struggles in the property sector. Despite government efforts to revive the economy, steel consumption fell by -3.3% y/y in H1. Bloomberg analysts expect that steel demand in China could stabilize at 70–80% of its 2020 peak, as the country transitions to a more consumer-driven economy, similar to past experiences in the US and other major steel producers.



Türkiye

Weaker activity data could compel Türkiye's central bank to front-load easing, according to some analysts. HSBC analysts cite still high inflation, as well as recent weaker-than-expected activity and employment data, which could compel Türkiye's central bank to front-load rate cuts in the early part of 2025 while remaining on hold for the remainder of the current year. In such a scenario, the policy rate could reach 42.5% in Q1'25 and 36.5%. While monetary tightening and other measures implemented since June 2023 have put the Turkish economy on a stronger footing and investor sentiment is stronger than it has been in recent years, HSBC analysts note that the record-high inflation is adjusting only very gradually, prompting officials to maintain a restrictive policy stance for the rest of this year. Meanwhile, analysts at JP Morgan, citing downside risks to inflation, expect the policy rate to be cut by -250bps in November and December of this year, taking the policy rate to 45% by year-end.



This monitor is prepared under the guidance of Jason Wu (Assistant Director), Charles Cohen (Advisor), Nassira Abbas (Deputy Division Chief), Caio Ferreira (Deputy Division Chief) and Sheheryar Malik (Deputy Division Chief). Fabio Cortes (Senior Economist), Sanjay Hazarika (Senior Financial Sector Expert), Esti Kemp (Financial Sector Expert-London Representative), Johannes S Kramer (Senior Financial Sector Expert-New York Representative), Benjamin Mosk (Senior Financial Sector Expert), Patrick Schneider (Financial Sector Expert), and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Mustafa Oguz Caylan (Research Officer), Yingyuan Chen (Financial Sector Expert), Andrew Ferrante (Research Assistant), Deepali Gautam (Senior Research Officer), Harrison Kraus (Research Assistant), Yiran Li (Research Assistant), Xiang-Li Lim (Financial Sector Expert), Corrado Macchiarelli (Economist), Kleopatra Nikolaou (Senior Financial Sector Expert), Natalia Novikova (IMF Resident Representative in Singapore), Sonal Patel (Senior Financial Sector Expert-London Representative), Silvia Ramirez (Senior Financial Sector Expert), Francesco de Rossi (Senior Financial Sector Expert-London Representative), 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

9/9/24 8:48 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		5423	-1.7	-4	1	22	14
Europe		4765	0.6	-4	2	12	5
Japan		36216	-0.5	-6	3	11	8
China		3193	-1.2	-2	-4	-15	-7
Asia Ex Japan		70	-1.8	-4	-1	8	5
Emerging Markets		42	-1.8	-3	-1	8	4
Interest Rates			basis points				
US 10y Yield		3.74	3.0	-17	-20	-53	-14
Germany 10y Yield		2.21	3.5	-13	-2	-40	18
Japan 10y Yield		0.90	4.7	-1	5	25	29
UK 10y Yield		3.91	2.7	-14	-3	-51	38
Credit Spreads			basis points				
US Investment Grade		138	-0.3	4	-4	-8	4
US High Yield		383	-4.2	19	-8	-28	-2
Exchange Rates			%				
USD/Majors		101.56	0.4	0	-2	-3	0
EUR/USD		1.10	-0.4	0	1	3	0
USD/JPY		143.2	0.7	-3	-2	-2	2
EM/USD		45.6	-0.2	-1	-1	-3	-5
Commodities			%				
Brent Crude Oil ($/barrel)		71.7	0.9	-8	-9	-14	-5
Industrials Metals (index)		139	0.5	-4	0	-1	-3
Agriculture (index)		54	0.4	0	2	-18	-13
Implied Volatility			%				
VIX Index (%, change in pp)		21.4	-1.0	6.4	1.0	7.5	8.9
Global FX Volatility		8.7	0.0	0.1	-0.1	0.4	0.6
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		104	-0.1	2	-6	-31	1
Italy		146	0.6	2	4	-28	-22
Portugal		63	-0.5	3	-2	-11	0
Spain		83	0.2	2	-3	-21	-14

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

Emerging Market Financial Indicators

Last updated: 9/9/2024 8:48 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		7.12	-0.2	0.0	1	2	0		1.9	-1.8	-5	-14	-83	-63
Indonesia		15455	-0.6	0.5	3	-1	0		6.6	1.4	-3	-15	8	15
India		84	0.0	0.0	0	-1	-1		7.0	1.0	-11	4	(80.0)	-24
Philippines		56	-1.0	-0.2	1	0	-2		4.9	-3.6	-11	-34	-101	-71
Thailand		34	-1.3	0.8	4	5	1		2.4	3.0	-3	-6	-65	-28
Malaysia		4.37	-1.0	-0.3	1	7	5		3.8	1.1	-1	-1	-10	2
Argentina		956	-0.3	-0.5	-2	-63	-15		39.4	-82.6	-227	-525	-7845	-4696
Brazil		5.64	-0.6	-0.3	-2	-12	-14		11.8	11.2	-26	26	37	142
Chile		942	0.2	-2.6	-1	-5	-7		4.8	0.0	-19	-29	-49	-13
Colombia		4174	-0.4	0.1	-1	-2	-8		7.6	0.0	-19	-10	-94	0
Mexico		19.92	0.3	-0.5	-5	-13	-15		8.9	-0.2	-20	8	-30	46
Peru		3.8	-0.2	-1.3	-2	-2	-2		6.5	-0.5			-49	-19
Uruguay		40	0.0	-0.1	0	-6	-4		9.7	10.7	17	22	47	22
Hungary		358	-0.9	-1.0	1	0	-3		5.8	1.0	-14	-13	-105	7
Poland		3.87	-0.3	-0.4	2	11	2		4.5	-1.6	-24	-6	-8	-2
Romania		4.5	-0.4	-0.2	1	2	0		6.5	0.8	4	13	-8	31
Russia		90.6	-0.1	-1.0	-2	6	-1							
South Africa		17.9	-0.2	-0.3	3	6	3		8.6	4.3	-16	-22	-85	-55
Türkiye		34.05	-0.2	-0.5	-2	-21	-13		28.8	3.0	61	51	504	208
US (DXY; 5y UST)		102	0.4	-0.1	-2	-3	0		3.52	3.8	-18	-27	-88	-32

	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		3193	-1.2	-2	-4	-15	-7		125	1	-28	-56	-33
Indonesia		7703	-0.2	0	6	11	6		113	13	-5	-12	17
India		81560	0.5	-1	2	22	13		112	-1	-11	-26	-4
Philippines		6984	0.7	1	5	12	8		98	11	-2	-4	18
Thailand		1431	0.2	6	10	-8	1		0	0	0	0	0
Malaysia		1651	-0.1	-2	3	14	14		86	2	-15	-11	1
Argentina		1721668	-2.5	0	9	223	85		1487	49	-147	-690	-426
Brazil		134572	-1.4	-1	3	17	0		237	16	-9	6	22
Chile		6245	-1.8	-3	-1	6	1		128	11	-9	0	3
Colombia		1328	-1.0	-2	1	24	11		332	20	-6	-5	61
Mexico		51083	-1.1	-2	-4	-3	-11		335	15	-6	-30	1
Peru		28065	-0.8	-1	-2	23	8		149	12	-11	-4	5
Hungary		72021	-0.4	-1	0	27	19		161	13	-8	-34	12
Poland		81927	0.2	-5	3	23	4		111	10	-3	-5	14
Romania		17502	0.7	-3	-2	27	14		211	14	6	1	10
South Africa		81737	0.5	-2	1	11	6		311	19	-23	-74	3
Türkiye		9812	0.4	-3	-1	18	31		310	11	-23	-82	-4
EM total		42	0.3	-3	-1	8	4		414	14	-23	33	69

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

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