



Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Friday, October 5, 2018

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- **US payrolls softer than expected as jobless rate hits 48-year low** ([link](#))
- **Asian tech stocks slump on broadening US-China tensions** ([link](#))
- **Danske Bank stocks drop 9% amid worries of large legal fines** ([link](#))
- **Italian banks weaker on reports they could be tapped to help finance deficit** ([link](#))
- **India's central bank holds interest rates steady, surprising analysts** ([link](#))
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Risk assets sputter following increases in US yields

Global equities and EM currencies are faltering as this week's lift-off in US long-term yields causes indigestion among investors. The move in US Treasuries is reportedly causing anxiety among investors in risk assets, many of whom fear the pace of the increase in yields more than the level – now 3.2% at the benchmark 10-year tenor. Global equities are off 1.3% since Wednesday, while EM equities are down almost 4% and EM currencies are off 1%. Broadening US-China tensions are also fueling anxiety in Asian share prices, where reports of Chinese tech espionage and a confrontational speech by US VP Pence have chilled market sentiment. In Europe, banks remain in the spotlight as Italian shares weaken on concerns that they may be enlisted in financing the deficit, and Danske Bank shares plummet on regulator's concerns about its exposure to large legal penalties.

Key Global Financial Indicators

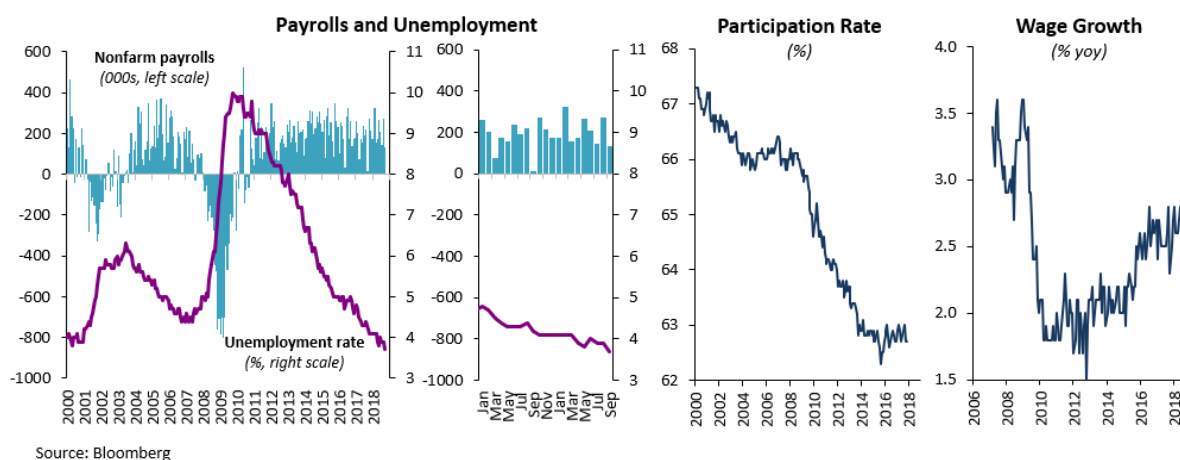
Last updated: 10/5/18 8:12 AM	Level		Change from Market Close				YTD
	Last 12m	Index	1 Day	7 Days	30 Days	12 M	
Equities			%				%
S&P 500		2900	-0.8	0	0	14	8
Eurostoxx 50		3363	-0.3	-1	1	-7	-4
Nikkei 225		23784	-0.8	-1	5	15	4
MSCI EM		41	-2.5	-5	-2	-11	-13
Interest Rates			bps				
US 10y Yield		3.20	1.7	14	30	86	80
Germany 10y Yield		0.55	1.8	8	17	9	12
Japan 10y Yield		0.16	-0.4	3	4	11	11
FX / Commodities / Volatility			%				
Dollar index, (+) = \$ appreciation		95.8	0.0	1	1	2	4
Brent Crude Oil (\$/barrel)		84.4	-0.2	2	9	48	26
VIX Index (% change in pp)		14.3	0.1	2	0	5	3

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

United States

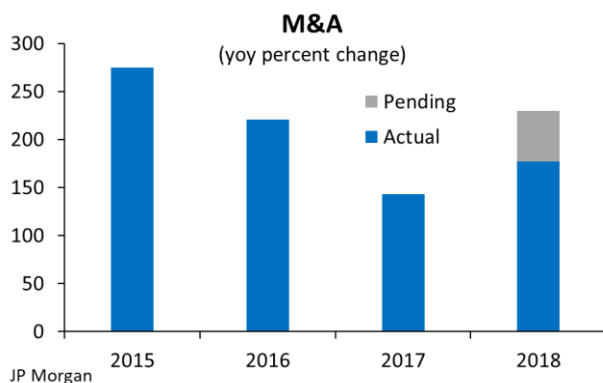
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Nonfarm payrolls came in at a low 134k compared to market expectations of a 185k increase. Hurricane activity likely skewed the report. On the upside, August numbers were revised 69k higher, and the headline unemployment rate fell to 3.7% from 3.9%. Hourly wages were up 0.3% mom (+2.8% yoy) in line with expectations. Treasury yields have been volatile on the news.

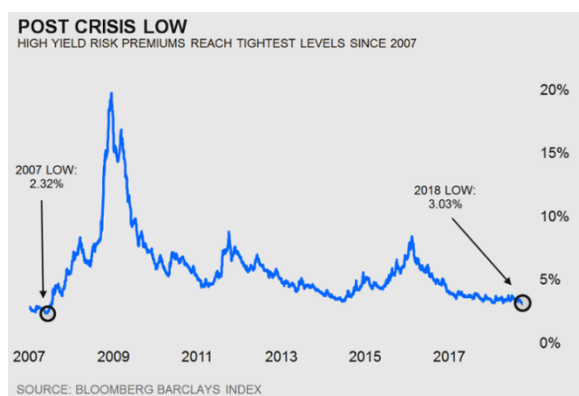


Stocks sold off Thursday, with the biggest losses in the tech sector (-1.7%). Financials (+0.7%) bucked the trend. The prices of major indices fell steadily through the morning and rallied somewhat in afternoon trade. Treasury yields ended flat after jumping 12 bps Wednesday. The dollar gave back most of Wednesday's gains yesterday. Initial jobless claims came in lower (207k) than expected (215k). Durable goods orders ex-transportation were flat in August, the slowest pace in over six months, while the headline number rose 4.4%.

Merger and acquisition (M&A) activity so far this year has exceeded last year, and is expected to surpass 2016's total as well. JP Morgan estimates that there will be a further \$53 bn in deals during the balance of the year, for a total of \$230 bn in 2018. This compares to just \$143 bn in M&A deals last year, when uncertainty surrounding tax reform legislation weighed on deal flow. But the firm expects M&A activity to taper off in a few quarters after the current backlog is worked through. Concerns over trade and tariffs should pressure dealmaking, and deal costs should rise as investment-grade bond yields move higher with Fed tightening.

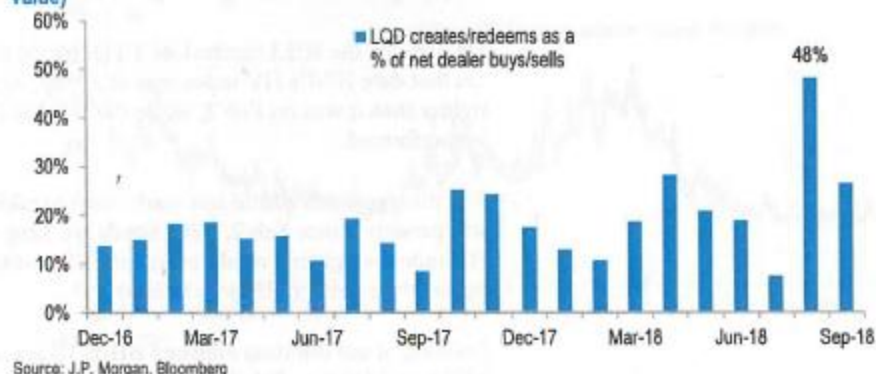


Bonds rated CCC have returned 6% so far this year, easily outperforming higher-rated bonds. By contrast the rest of the high-yield bond segment has increased just 2.2%, while investment-grade bonds have lost 3%. The yield pick-up from holding CCC bonds over the highest-rated high-yield debt however has fallen to 4.2 ppts from 4.5 ppts a year ago, making these bonds less attractive. As a whole, junk bond yields are also now about 3 ppts more than Treasuries, the narrowest since 2007. Moreover, issuance has been falling, as rising rates make refinancing more expensive. Bloomberg gauges that high-yield bond issuance is down 30% this year. That said, Fitch expects speculative-grade default rate to drop to 1.5% from 2.7% for the 12 months ending September.



Primary activity in high-grade credit exchange-traded funds (ETFs) is picking up, pointing to shifts in bond market structure. ETF share creations and redemptions have grown to record highs, with JPMorgan noting that this is true in both absolute terms and relative to net dealer buy/sell daily volumes (according to TRACE data). The median daily trading volume of the high-grade benchmark LQD ETF was \$209 mn/day over the last month through September 10th. The median in the US dollar high-grade cash market is \$371 mn/day. This suggests dealers and investors are creating and redeeming shares as a means of generating liquidity for the underlying bonds, rather than just to accommodate shifts in demand for exposure to the asset class.

Exhibit 17: Primary activity in LQD has grown recently. Create/redeems amounted to \$209mn/day from mid-August to mid-September, compared to \$371mn/day dealer buy/sell (both in absolute value)



Private equity funds raised \$121 bn of capital globally in Q3. This compares to \$96 bn in Q2 according to Preqin. It noted that 55% of the capital raised in Q3 was carried out by that 10 largest funds that closed during the period. Moreover, the amount of liquid assets that private equity funds had ready to invest (dry power) increased to \$1.14 tn in September. North American funds accounted for three-quarters of the total raised in Q3.

Europe

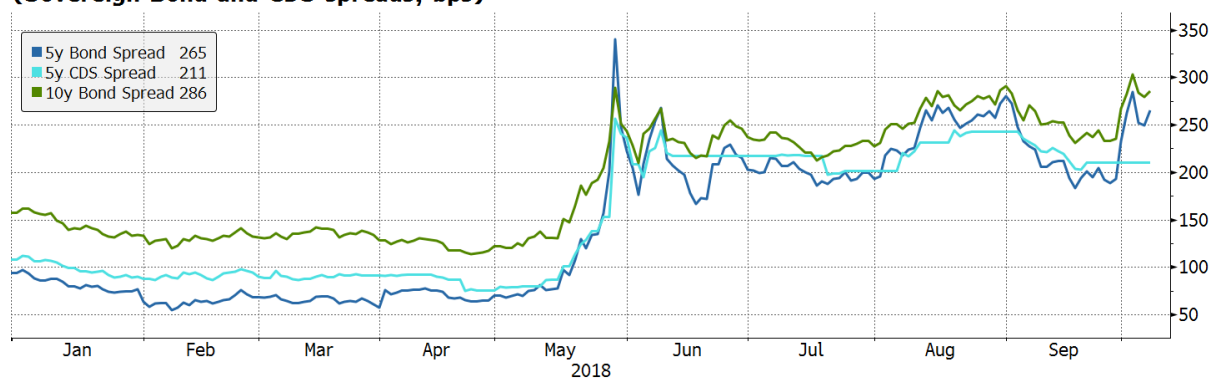
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The Italian government has unveiled details of its economic and public finance projections. According to the latest figure, the deficit targets have been downgraded to 2.4% of GDP for 2019, 2.1% for 2020, and 1.8% for 2021. Many analysts continue to see the real GDP growth projections as overly optimistic at 1.6%, 1.5% and 1.4% for 2019 to 2021.

Sovereign debt yields are mostly unchanged – German 10-yr bunds at 0.54% (+1 bp) and French OATs at 0.88% (+1 bp) – **except for Italian bonds:** 2-year yield is up 18 bps to 1.37% and 10-year is at 3.40% +8bps.

Italy-Germany Spreads

(Sovereign Bond and CDS spreads, bps)

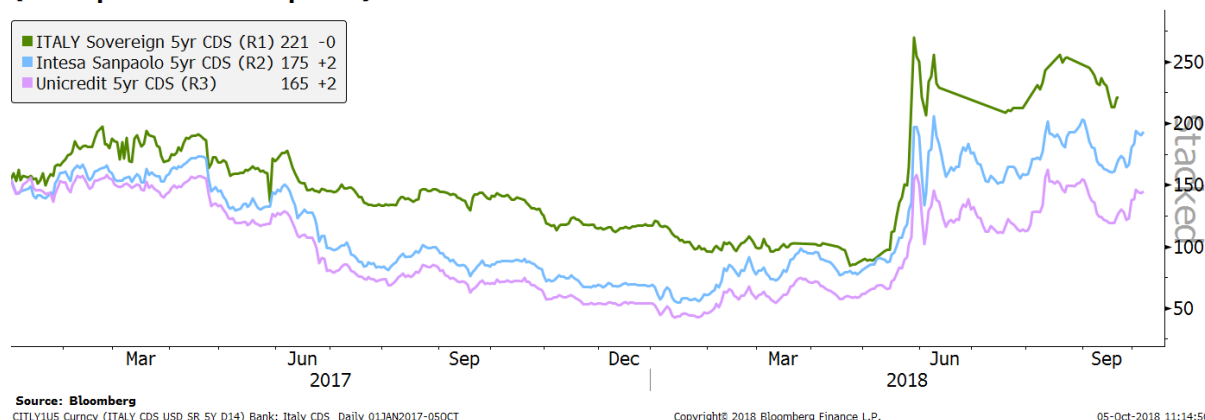


European equities are down about 0.6% today, dragged down by bank stocks (-1.0%). The downward move has been more pronounced in Italian equities.

Italian bank stocks (-2.5%) are heavily underperforming after local media reported that the new draft budget could be partially financed by banks. Details of the plan are not available but newspapers

note that a likely measure is the reduction the amount of interest payments and writedowns that banks can deduct from their taxable income. Unicredit (-2.9%), Intesa (-2.8%), MPS (-2.3%).

Italy: Credit Default Swaps (CDS spreads in basis points)



Stocks of Danske Bank fell a further 9.4% today. The bank's equity has fallen over 15% this week as the bank is embattled in an ongoing money laundering scandal in Estonia involving Russian clients. Today, the Danish Financial Supervisory Authority has requested a further capital increase for Danske in preparation for possible legal fines. Some analysts estimate potential fines of up to \$1.8bn.

UK house prices fell 1.4% in September, compared to an expected increase of 0.2% according to the Halifax House Price Index. Analysts attribute most of the contraction to the uncertainty caused by Brexit.

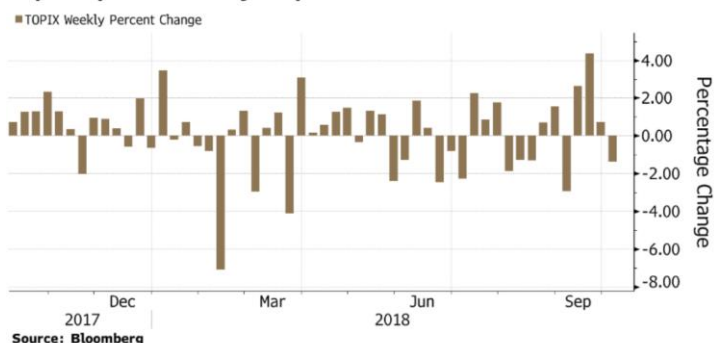
Other Mature Markets [back to top](#)

Japan

Equities fell in line with regional peers, while the yen was little changed. The Topix fell 0.4%, and the Nikkei closed 0.8% lower, after touching a 27-year high early this week. Technology shares sold off, following pressures on the sector in the US overnight. **Ten-year JGB yields were declined 0.4 bps to 0.145%.** In its regular operation today, the BoJ kept the magnitude of super-long government bond purchases unchanged even as yields remain near highs for the year, underscoring its commitment to allow yields to move within a wider range.

Retreat


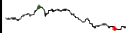

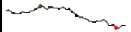



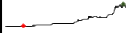

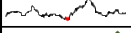



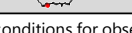
Topix caps first weekly drop in four



Emerging Markets

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Key Emerging Market Financial Indicators

Last updated: 10/5/18 9:29 AM	Level		Change				YTD
	Last 12m	index	1 Day	7 Days	30 Days	12 M	
Prices/Returns of Major EM Benchmarks			%				%
MSCI EM Equities		40.99	-2.5	-5	-2	-11	-13
MSCI Frontier Equities		28.27	-1.1	-1	2	-11	-15
Hard Currency Sovereign Debt		823.98	-0.1	0	1	-3	-4
Local Currency Sovereign Debt		16.10	-1.0	-2	2	-15	-15
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.87	0.0	0	-1	-3	-5
Indonesian Rupiah		15180	0.4	-2	-1	-11	-10
Indian Rupee		73.94	-0.2	-2	-3	-12	-14
Argentine Peso		38.34	0.7	8	1	-55	-51
Brazil Real		3.87	0.1	5	7	-19	-14
Mexican Peso		18.95	0.9	-1	2	-2	4
Russian Ruble		66.53	0.5	-1	3	-13	-13
South African Rand		14.71	1.1	-4	5	-7	-16
Turkish Lira		6.12	0.6	-1	8	-41	-38
Dollar vs. Mature FX (DXY index)		95.62	-0.1	1	0	2	4

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

Emerging market assets weakened on Thursday on investor concerns about rising US interest rates and renewed worries about US-China tensions. In Argentina, the peso dropped 1.8% and equities tumbled 4.0%. Brazilian and Mexican stocks declined 0.4% and 0.7%, respectively. EMEA assets were under pressure but the moves were in line with the broader negative risk sentiment: Russian equities are underperforming (-1.0%) and currencies are mixed in narrow ranges. In Asia, equities were down across the board with Taiwan (-1.9%) underperforming. The Thai baht is underperforming 0.7%, and equities were down across the board with Taiwan (-1.9%) underperforming.

Tech stocks sold off (-2.2%) across Asia on U.S.-China tensions. The regional MSCI tech index hit the lowest since July 2017 as investors digested a Bloomberg report that Beijing had hacked 30 US companies, including Apple and Amazon. The story came the same day Vice President Mike Pence criticized China across economic, commercial and diplomatic fronts in a keynote speech. Chinese tech stocks listed in Hong Kong SAR and tech companies from Taiwan POC were particularly hard hit. Notably, Chinese computer maker Lenovo which generates 30% of its revenue in the U.S. slumped as much as 23% for its biggest loss in almost a decade before paring some losses toward the close of the trading session; ZTE was also down about 10%. Markets in Shanghai and Shenzhen have been closed this week for a holiday.

Sleep Mode

Lenovo slumps on fears U.S. will slow down server imports

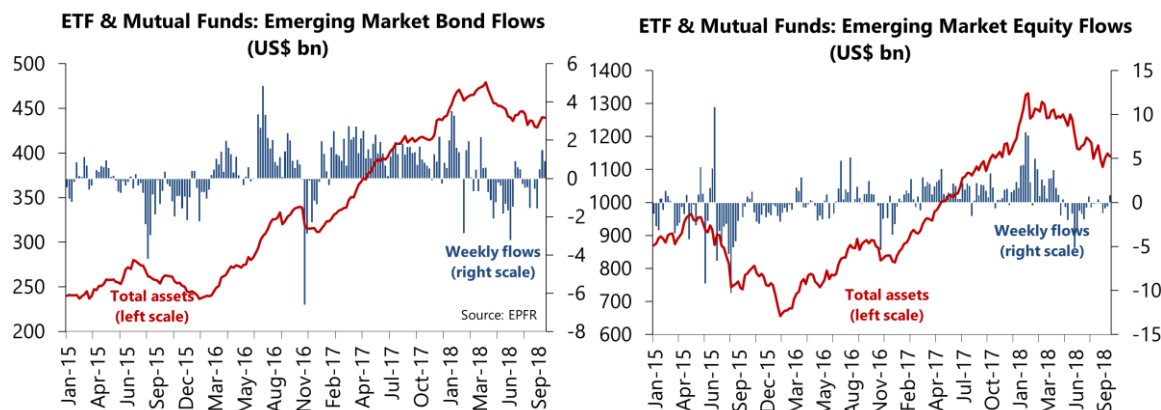
■ Lenovo Group Ltd



Source: Bloomberg

Bloomberg

EM fund flows continued to turn positive. Bond funds had net inflows (\$923 mn) for a third straight week according to EPFR, driven by hard currency funds. Equity funds witnessed inflows (\$848 mn) after three weeks of outflows. In the realm of non-resident EM portfolio flows, JP Morgan advised that equity outflows were led by India and Korea, while Brazil posted inflows.



Indonesia

The rupiah was little changed today, after breaking through the psychologically important 15000 level against the dollar earlier in the week. The rupiah's slump, including a decline of 1.9% this week, saw the government announce the rollout of domestic non-deliverable forwards (DNDF) settled in IDR starting November. The authorities hope that the new FX instrument will be a useful additional hedging tool, reduce dollar demand in the offshore NDF market, and also facilitate development of the onshore market. Most analysts, however, do not expect the DNDF to help stem depreciation pressures on the rupiah. Meanwhile, Bank Indonesia stated that it will continue to intervene in the markets and smooth IDR volatility. Ten-year bond yields fell 4 bps to 8.3%. Equities declined 0.4% bringing the weekly decline to 4%.

No Respite?

Rupiah heads for worst weekly loss since 2016



India

The Reserve Bank of India (RBI) kept the policy rate on hold at 6.5%, against consensus expectations of a 25 bps or even 50 bps hike. Five out of six MPC members voted in favor of a pause. In a second surprise, the RBI also lowered its CPI inflation forecasts for the next three quarters, indicating that it expects limited pass-through from higher oil prices and a weaker Indian rupee. In response to the unexpected announcement, the rupee depreciated 0.7%. Sovereign bond yields declined by 10-12 bps and the curve bull steepened.

Mexico

The central bank kept its policy rate steady but signaled its readiness to act. The monetary policy committee left the key rate unchanged at 7.75% yesterday, as expected. The central bank said that while it expects higher inflation to be transitory, it is prepared to act promptly to ensure price stability. The committee acknowledged that while the trilateral trade deal made on Sunday has diminished downside risks to the economy, Mexico continues to face tighter external financial conditions. The central bank will continue to monitor the exchange rate's passthrough to inflation, the Fed's monetary stance, and the economic slack, and, if necessary, will guide inflation towards the 3% target. Some commentators viewed the central bank's statement as more hawkish than before. Two- and 10-year yields rose 6 bps and 7 bps, respectively. The peso edged slightly lower. Equities declined in tandem with US stocks, down 0.7% yesterday.

Argentina

Markets weakened, as the potential for a further rise in US rates kept investors on edge. The peso was 1.8% weaker at 38.35 per dollar, while external bond spreads underperformed other EM credits at +32 bps, and equities were down 4.0%. The central bank sold ARS 97.7 bn in today's daily auction, with the average 7-day leliq rate up another 156 bps to an average rate of 72.8% (versus 60% before the new program went into effect). Commentators expect near-term FX volatility to persist.

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Global Financial Indicators

Last updated: 10/5/18 8:12 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		2900	-0.8	0	0	14	8
Europe		3363	-0.3	-1	1	-7	-4
Japan		23784	-0.8	-1	5	15	4
China		2821	1.1	3	4	-16	-15
Asia Ex Japan		67	-2.5	-6	-4	-9	-12
Emerging Markets		41	-2.5	-5	-2	-11	-13
Interest Rates			basis points				
US 10y Yield		3.20	1.7	14	30	86	80
Germany 10y Yield		0.55	1.8	8	17	9	12
Japan 10y Yield		0.16	-0.4	3	4	11	11
UK 10y Yield		1.69	1.6	11	24	30	50
Credit Spreads			basis points				
US Investment Grade		98	1.1	1	-6	1	6
US High Yield		323	-1.5	-5	-22	-41	-52
Europe IG		68	0.2	0	3	13	24
Europe HY		278	-0.1	3	-14	34	44
EMBIG Sovereign Spread		340	1.0	-3	-37	58	55
Exchange Rates			%				
Dollar Index (DXY)		95.76	0.0	1	1	2	4
USDEUR		1.15	0.0	-1	-1	-2	-4
USDJPY		113.9	0.0	0	-2	-1	-1
EM FX vs. USD		61.5	0.2	-1	2	-11	-12
Commodities			%				
Brent Crude Oil (\$/barrel)		84	-0.2	2	9	48	26
Industrials Metals (index)		121	-0.4	1	5	-6	-12
Agriculture (index)		43	0.4	3	2	-11	-9
Implied Volatility			%				
VIX Index (% change in pp)		14.3	0.1	2.2	0.4	5.1	3.2
10y Treasury Volatility Index		4.1	0.3	0.8	0.4	-0.2	0.6
Global FX Volatility		8.4	0.0	0.2	-0.5	0.7	1.1
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		400	3.1	28	-18	31	31
Italy		286	6.4	19	31	127	127
Portugal		138	-0.6	-3	-12	-14	-14
Spain		102	-1.2	-1	-5	-12	-12

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

Data source: Bloomberg.

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Emerging Market Financial Indicators

Last updated: 10/5/2018 8:19 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		6.87	0.0	0.0	-1	-3	-5		3.6	0.0	0	6	-10	-34
Indonesia		15182	0.4	-1.9	-1	-11	-10		8.5	16.1	17	2	167	186
India		74	-0.2	-1.9	-3	-12	-14		8.3	6.4	10	7	121	80
Philippines		54	0.2	-0.4	-1	-6	-8		6.5	1.9	1	54	161	161
Thailand		33	-0.2	-1.5	0	2	-1		2.9	6.0	5	10	67	60
Malaysia		4.15	-0.2	-0.3	0	2	-2		4.1	2.1	2	0	22	20
Argentina		38	-1.6	7.7	1	-55	-51		23.0	6.0	-74	-187	804	693
Brazil		3.84	0.8	5.4	8	-18	-14		9.7	-5.3	-23	-97	110	70
Chile		673	0.2	-2.3	2	-7	-9		4.8	1.4	-1	8	29	4
Colombia		3033	0.1	-2.3	2	-3	-2		6.7	2.4	9	11	36	42
Mexico		19.01	0.5	-1.6	2	-3	3		8.0	7.6	11	0	102	36
Peru		3.3	0.0	-0.7	0	-2	-3		5.8	3.8	6	22	39	52
Uruguay		33	0.3	1.0	-1	-11	-13		10.3	-9.2	-17	-113		176
Hungary		282	-0.1	-1.2	0	-6	-8		2.7	4.8	4	14	114	142
Poland		3.74	0.1	-1.4	-1	-2	-7		2.7	3.9	5	6	-13	-3
Romania		4.1	0.0	-1.4	-2	-4	-4		4.4	5.0	3	1	131	53
Russia		66.7	0.3	-1.6	2	-13	-13		8.4	15.3	11	-12	87	110
South Africa		14.7	0.8	-4.1	5	-7	-16		9.8	10.9	25	7	54	52
Turkey		6.17	-0.1	-1.8	7	-42	-39		21.6	85.5	157	-156	1068	968
US (DXY; 5y UST)		96	0.0	0.7	1	2	4		3.06	1.1	10	29	111	85

	Equity Markets							Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)					Level		Change (in basis points)				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
								basis points						
China		2821	0.0	3	4	-16	-15		182	3	-1	-5	38	30
Indonesia		5732	-0.4	-4	1	-3	-10		189	1	4	-18	24	23
India		34377	-2.3	-5	-10	9	1		160	4	-2	-1	37	50
Philippines		7078	-0.2	-3	-9	-15	-17		100	3	4	-11	11	5
Malaysia		1777	-0.7	-1	-1	1	-1		124	3	-5	-12	2	14
Argentina		30929	-4.0	-8	8	14	3		658	33	68	-126	287	308
Brazil		82953	-0.4	4	10	8	9		277	2	-9	-58	40	43
Chile		5326	0.0	1	4	-2	-4		120	2	-4	-22	-8	1
Colombia		1517	-0.5	1	1	2	0		170	1	3	-12	-13	-4
Mexico		48683	-0.7	-2	0	-4	-1		258	0	1	-27	24	13
Peru		19629	-1.0	0	4	0	-2		132	2	0	-16	-8	-5
Hungary		37075	-0.2	0	0	-2	-6		108	7	-2	-13	21	20
Poland		58545	-0.3	-1	0	-9	-8		47	5	0	-13	-2	0
Romania		8561	0.6	2	3	8	10		168	7	-3	-15	40	55
Russia		2462	-0.1	-1	6	18	17		214	1	-17	-24	30	36
South Africa		54512	-0.9	-2	-5	-4	-8		312	0	-9	-47	53	58
Turkey		94186	-0.3	-6	2	-10	-18		470	0	17	-130	189	181
Ukraine		544	-0.1	1	3	83	73		559	0	10	-59	104	104
EM total		25	-1.7	-4	-2	-7	-7		340	1	-3	-37	58	55

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