

Trade tensions caught markets off-guard

■ Risk-off mood resurfaced in financial markets. Market volatility surged during the week (VIX surged to 19, although still below the 30 level high seen last December), reflecting underlying investor fears over the fallout of re-escalation in US-China trade tensions on global growth. Equity markets fell across the board this week led by cyclical sectors.

■ That said, market reaction was quite contained, even though the US hiked tariff from 10% to 25% on \$200bn worth of Chinese imports and threatened to impose tariff on remaining \$350bn in China imports, while China said it will take countermeasures. This behaviour suggests markets remain hopeful that US and China would eventually resolve their trade differences, even as the risk of a complete breakdown in talks has increased in recent days.

■ Elsewhere, economic data showed some resilience in Germany, amid rising prospects of a recovery in the manufacturing sector as industrial production, factory orders and exports improved in March. EZ Composite PMI was a little firmer than flash reading in April, allaying some concerns after the European Commission lowered Eurozone 2019 GDP growth projections (1.2%, -0.1pp) and projected a more moderate recovery in 2020 (1.5% - 0.1pp). In the US, headline CPI increased 0.3% MoM in April led by gasoline prices, while core prices increased modestly for the third consecutive month at 0.1% MoM, suggesting that the recent increases in energy prices are having only a modest impact on core components.

■ **Sovereign yields fell** (10Y yield declined -8bp and -6 bps in both US and Germany, respectively, with the latter returning to negative levels (-0.04%), **as investors sought shelter in government bonds amid trade tensions and muted inflation pressure.** Meanwhile, concerns about the impact of trade tension in the economy boosted market's implied probability of a Fed rate cut in 2019 (to 60% from 51%), although Fed Vice Chairman Clarida noted that he doesn't see a strong reason to move rates up or down, in turn pushing back against market speculation that the Fed would cut rates to boost inflation. **Italy's risk premium widened sharply** (with limited spillovers to Spain and Portugal), amid rising prospects of early elections, jointly with concerns about its public finances and US Fund manager BlackRock's decision to withdraw the rescue offer for Banca Carige. European Commission projects that Italy's public deficit will hit 3.5% of the GDP by 2020.

■ **In FX, USD lost some strength, whereas JPY acted as a real safe-haven currency,** attracting fresh flows. Positive economic data led a slight appreciation of the euro. Importantly, China's renminbi depreciated on the back of trade tensions coupled with weaker April credit outturns, that fueled market expectations of further policy easing by the PBoC. EM FX also depreciated across the board, while idiosyncratic factors weighed additionally on the TRY and ARS. Moreover, EM assets bore the brunt of markets concerns with risk premia increasing both for sovereigns and corporate bonds, whereas HY spreads also widened. EM equity fell sharply this week.

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Debt markets (10Y, %, changes in bp)					
Developed Markets	level	Daily	Week	Month	YTD
US (2-yr)	2.23	-2.9	-10.4	-9	-26
US	2.43	-1.1	-9.3	-3	-25
GER (2-yr)	-0.62	0.8	-3.0	-3	-1
Germany	-0.05	0.1	-7.1	-2	-29
France	0.35	0.1	-2.7	2	-36
Spain	0.98	-1.1	-0.6	-7	-54
Italy	2.68	0.0	12.2	12	-21
Portugal	1.12	-0.2	-0.5	-5	-75
Greece	3.51	-2.4	16.7	9	-89
Japan (2-yr)	-0.16	-0.2	-0.8	1	-2
Japan	-0.05	-0.1	-0.9	0	-5
Emerging Markets	level	Daily	Weekly	Monthly	YTD
Brazil	8.76	-3.1	-12.3	-15	-48
Chile	3.89	-1.0	-5.0	5	-36
Colombia	6.67	-4.3	-15.3	12	-8
Mexico	8.10	-2.1	1.0	15	-54
Peru	4.81	-2.7	0.7	-2	-55
Poland	2.90	-2.5	-13.5	0	8
Russia	8.28	5.1	4.2	1	-50
Turkey	20.15	-33.0	158.0	330	435
India	7.41	1.4	1.8	4	4
Indonesia	8.00	-6.5	11.5	32	-3
Country risk (bp, changes in bp)					
Developed Markets	level	Daily	Weekly	Monthly	YTD
10-yr sovereign spread vs Germany					
France	39	0.0	4.4	4	-2
Italy	273	-0.1	19.3	15	8
Portugal	116	-0.3	6.6	-3	-40
Spain	102	-1.2	6.5	-5	-20
2-yr sovereign spread vs Germany					
France	6	0.3	0.9	-1	-9
Italy	122	-1.3	18.9	41	13
Portugal	28	-1.5	2.6	3	2
Spain	28	-0.9	3.1	3	-9
Emerging Markets	level	Daily	Weekly	Monthly	YTD
5-yr sovereign CDS *					
Brazil	173	1.5	-1	4	-35
Chile	44	1.5	3	4	-19
Colombia	107	1.5	5	4	-51
Argentina	1154	23.3	-88	246	348
Mexico	119	2.5	4	3	-36
Peru	65	2.5	5	7	-30
Poland	66	0.0	0	-2	-2
Russia	131	1.5	1	-1	-23
Turkey	493	19.0	49	85	133
China	48	1.9	7	5	-19
India	82	1.5	3	-1	-32
Indonesia	106	3.2	10	8	-31
Risk indicators					
Volatility indicators	level	Daily	Weekly	Monthly	YTD
VIX	19	0.2	6	6	-6
VSTOXX	18	-1.7	5	4	-5
EMEFT volatility Index	23	-1.4	7	7	-2
Dollar/euro volatility	5	-0.3	0	0	-2
EM FX volatility index	9	0.4	1	1	0
Credit spread (BAA) (change in bps)	223	1.1	10	0	-23
US bonds volatility index	55	3.4	9	6	-12
Inflation expectations	level	Daily	Weekly	Monthly	YTD
US Inflation expectations (5Y5Y)	2.21	-	-4	-7	8
EZ Inflation expectations (5Y5Y)	1.37	-	-3	2	-24
Banking 5y CDS	level	Daily	Weekly	Monthly	YTD
US	59	0.6	2	0	-23
EZ	87	4.1	9	7	-33
UK	63	2.7	5	2	-32
Large Spanish	58	4.2	6	-2	-29
Medium Spanish	84	-1.5	-13	-20	-28
Corporate 5y CDS	level	Daily	Weekly	Monthly	YTD
US Non-financial	169	0.6	2	0	-23
EZ Non-financial	85	4.1	9	7	-33
UK Non-financial	108	1.5	4	3	-11
Interbank markets (% changes in bp)					
	level	Daily	Weekly	Monthly	YTD
EONIA Index	-0.36	0	-1	0	-1
Euribor 3m	-0.31	0	0	0	0
Euribor 12m	-0.12	0	0	-1	0
Libor 3m	2.54	-1	-3	-5	-26
Libor 12m	2.70	-1	-3	-5	-31
Stock markets (%)					
Main indices	level	Daily	Weekly	Monthly	YTD
S&P500	2,837	-1.2	-3.7	-1.8	13
Dow Jones	25,518	-1.2	-3.7	-2.4	9
Nikkei	21,345	-0.3	-4.1	-1.6	7
FTSE 100	7,216	0.1	-2.2	-2.8	7
EuroStoxx 50	3,368	0.5	-3.8	-1.7	12
IBEX	9,133	0.4	-2.9	-2.9	7
DAX	12,081	0.9	-2.7	1.5	14
CAC	5,337	0.4	-3.8	-2.1	13
MIIB	20,917	0.5	-3.9	-3.5	14
ASE Athens	736	1.0	-5.0	-2.6	20
MSCI Latam *	90,279	-0.8	-1.7	-3.7	5
Ibovespa (Brazil)	93,796	-1.1	-2.3	-2.2	7
Mexbol (Mexico)	42,680	-1.2	-3.6	-5.0	2
Merval (Argentina)	33,838	-0.8	4.4	5.2	12
MSCI EM Europe *	5,523	-0.7	-3.2	-4.4	4
Poland	2,192	0.6	-5.5	-8.4	-4
Micex 10 (Russia)	4,509	-1.1	-1.7	-2.4	8
Ise 100 (Turkey)	88,533	-0.2	-5.8	-8.7	-3
MSCI EM Asia *	851	-1.9	-4.8	-5.3	9
Shanghai Com (China)	2,939	3.1	-4.5	-9.3	18
Jakarta (Indonesia)	6,209	-1.0	-2.6	-4.2	0
Banking sector	level	Daily	Weekly	Monthly	YTD
US banks	137.7	-0.9	-4.2	2.6	19
JPM	111.4	-1.0	-4.1	5.7	14
Citi	67.2	-0.7	-4.9	2.5	29
BoA	29.4	-0.9	-4.2	1.2	19
MS	46.0	-0.9	-4.2	3.6	16
GS	200.0	-0.8	-3.6	-1.5	20
EZ banks	76.3	0.2	-6.9	-1.6	11
BNP	45.5	0.3	-5.6	3.0	15
Crédit Agricole	11.6	0.0	-6.5	1.7	23
Deutsche Bank	7.0	1.4	-5.3	-4.0	0
ING	10.5	0.6	-6.7	-6.7	11
Intesa	2.2	-0.1	-6.8	-2.6	12
SG	26.1	-0.6	-9.0	-0.6	-6
Unicredit	11.2	1.1	-8.0	-5.0	14
UK banks	78.0	0.4	-3.1	-2.6	7
HSBC	653.6	0.3	-4.0	0.1	1
RBS	232.8	0.3	-2.1	-8.1	7
Lloyds	158.0	0.7	-3.5	-2.6	5
Lloyds	61.2	0.5	-2.3	-2.0	18
Large Spanish banks	62.4	-0.2	-5.4	-4.7	7
Santander	4.1	-0.3	-6.2	-5.4	4
BBVA	5.1	-0.2	-4.8	-4.0	10
Medium Spanish banks	54.4	0.4	-2.9	0.5	-5
Caixabank	2.8	-0.2	-4.2	-4.1	-13
Sabadell	1.0	1.0	0.3	11.7	4
Bankinter	6.8	0.3	-3.3	-2.7	-3
Bankia	2.3	0.8	-4.2	2.8	-9
Currencies (% red for currency depreciation)					
Developed	level	Daily	Weekly	Monthly	YTD
EURUSD	1.124	0.2	0.4	-0.3	-2
GBPUSD	1.30	0.1	-1.1	-0.5	2
USDJPY	109.56	0.2	1.4	1.3	0
DXY	97.22	-0.2	-0.3	0.3	1
Emerging	level	Daily	Weekly	Monthly	YTD
USDARS (Argentina)	44.99	0.6	-1.2	-4.4	-16
USDBRL (Brazil)	3.97	-0.4	-0.7	-3.5	-2
USDCLP (Chile)	686.92	-0.3	-1.3	-3.6	1
USDCOP (Colombia)	3284	-0.2	-1.4	-6.1	-1
USDMXN (Mexico)	19.15	0.5	-1.2	-1.7	3
USDPEN (Peru)	3.32	-0.1	-0.5	-0.7	2
LACI	53.49	-0.5	-0.9	-3.0	-2
USDPLN (Poland)	3.82	0.2	-0.1	-0.7	-2
USDRUB (Russia)	65.27	1.0	-0.3	-1.5	6
USDTRY (Turkey)	6.08	1.9	-1.9	-6.5	-13
USDCNY (China)	6.83	0.0	-1.3	-1.6	1
USDINR (India)	69.91	0.1	-1.0	-1.1	0
USDIDR (Indonesia)	14327	0.2	-0.4	-1.2	0
ADXY	104.85	-0.1	-0.9	-1.4	-1
Commodities (%)					
	level	Daily	Weekly	Monthly	YTD
Brent	70.8	0.5	-0.1	-1	32
WTX	62	0.4	0.0	-4	36
Copper	277	-0.5	-1.9	-5	5
Gold	1288	0.3	0.7	-2	0
S&P Spot commodity *	434	-0.6	-1.6	-4	16
S&P Brent Spot *	594	-0.3	-1.4	-2	30
S&P Metals Spot *	321	-0.7	-2.0	-6	1
S&P Agricultural *	259	-1.8	-3.4	-7	-9

Source: Bloomberg, Datastream and Haver

* With one day delay