BBVA Research

Market Comment | Markets waiting for the Fed's interest rate decision

Global Financial Markets Unit
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- **Mixed data in the US.** US housing starts rose in November more than expected (by 111K to 1173K; consensus: 1130K), while building permits increased against estimates of decreasing (by 128K to 1,289K: consensus: 1,150K). On another front, industrial production in November dropped more than expected (by -0.6% MoM; consensus: -0.2%).

- **Eurozone PMIs point to an acceleration of GDP despite the slight drop in December.** Eurozone PMI composite declined in December unexpectedly (by 0.2 points to 54.0; BBVAe and consensus: 54.2), due to the slowdown in services PMI (by 0.3 points to 53.9; consensus: 54.0), whereas manufacturing PMI improved, surprising expectations (by 0.3 to 53.1; consensus: 52.8). These data suggest that GDP growth would be consolidating or accelerating slightly in 4Q15 (after 0.3% QoQ in 3Q15), in line with our short-term MICA-BBVA model, which estimates an increase of around 0.4% QoQ. By country, activity moderated slightly in Germany, while in France the services weighed on the index. In the periphery, economies are moving at a robust pace. On another front, eurozone inflation in November was revised slightly upward by 0.1% to 0.2%YoY (BBVAe: 0.3%, consensus: 0.1%). (see)

- **Fitch withdraws Brazil's investment grade.** The ratings agency cut Brazil's sovereign rating by one notch, from BBB- to BB+, the highest step within the speculative grade zone. Moreover, it maintained the negative rating outlook, meaning that additional downgrades should not be ruled out. Even though a second downgrade was already expected, it happened some months before most had anticipated. This will force the exclusion of Brazil from investment grade indices, spurring some capital outflows. Even though this is likely to cause a further correction in local financial markets, this effect should be relatively small as it is to a large extent already priced in. It is worth noting that Fitch's decision follows moves by the Brazilian government in the last days to reduce the 2016 primary surplus target from 0.7% of GDP to something between 0.0% and 0.5% of GDP. As one of the goals of the ongoing fiscal adjustment was to prevent the country from losing its investment grade, today's announcement by Fitch also reinforces the view that fiscal consolidation in forthcoming years will be lower than expected and lower than needed to avoid a further fiscal deterioration (the gross public debt should converge to 75% of GDP in 2017 and almost 80% in 2020, in comparison to 57% in 2013). Finally, without an investment grade rating, and confronting significant political and economic problems, Brazil is not in a good position to face the consequences of the Fed's imminent increase in interest rates.

- **Markets waiting for the Fed's interest rate decision.** Financial markets generally expect that the Fed will raise the Fed Funds target rate to 0.50% today, which would be the first tightening in more than nine years. Against this background, equity markets continued yesterday's rebound across the board (S&P: +0.3%, Euro Stoxx: +0.4% CAC: +0.5% DAX: +0.5%). On Asian markets, the Nikkei rose (+2.6%) following yesterday's European and US recovery. On bond markets, US treasury yields rose slightly in all tenors (2Y and 10Y: +3bp), with the focus on today's Fed announcement. In the same vein, European yields increased, especially among the safe havens (GER 10Y: +3bp, FRA 10Y: +3bp, ITA 10Y: +1bp, SPA 10Y: +1bp, POR 10Y: +1bp). As a result, peripheral risk premia were narrowed (ITA: -2bp, SPA: -3bp, POR: -2bp). In FX markets, the US appreciated, mainly against major currencies linked to oil prices (Canadian dollar: -0.69%, Norwegian Krone: -0.46%), while the euro remained flattened. EM currencies showed a mixed performance against the US dollar (BRL: -1.9%, RUB: -0.7%, COP: +0.4%, CLP: +0.3%, MXN: -0.1%) despite the new falls in oil prices (Brent: -2.9%, WTI: -3.5%), dragged by the worse-than-expected crude inventories, which showed an increase in the supply. Meanwhile, the copper price rose (+0.7%) after yesterday's plunge, and gold also increased during the session (+1.3%).

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Table1

(Current level and changes at daily, weekly, monthly and annual frequencies)

Debt markets *(changes in bp)*
Developed Markets
US 2-yr 0,99 (3) (7) (14) (33)
US 5-yr 1,74 (4) (9) (8) (8)
US 10-yr 2,3 (3) (8) (3) (13)

Japan 10-yr 0,3 (0) (0) (0) (-3)

GER 2-yr -0,34 (0) (-2) (3) (-24)
GER 5-yr -0,03 (2) (4) (9) (-5)
GER 10-yr 0,67 (3) (7) (14) (13)

Belgium 10-yr 0,99 (3) (10) (16) (15)
France 10-yr 1,01 (3) (9) (16) (18)
Greece 10-yr 8,26 (-47) (-12) (112) (-148)
Ireland 10-yr 1,16 (3) (3) (8)
Italy 10-yr 1,7 (1) (13) (13) (-19)
Netherlands 10-yr 0,83 (3) (8) (14) (15)
Portugal 10-yr 2,58 (1) (12) (-10) (-11)
Spain 10-yr 1,77 (1) (14) (-3) (16)

Emerging Markets
Brazil 10-yr 16,22 (28) (60) (76) (386)
Chile 10-yr 4,64 (0) (2) (3) (65)
Colombia 10-yr 8,85 (-2) (26) (56) (175)
Mexico 10-yr 6,34 (0) (3) (25) (51)
Peru 10-yr 7,22 (-1) (21) (14) (177)

Poland 10-yr 3,13 (6) (15) (45) (61)
Russia 5-yr 10,07 (2) (11) (14) (-413)
Russia 10-yr 9,62 (0) (7) (-14) (-339)
Turkey 10-yr 10,54 (4) (41) (88) (267)

India 10-yr 7,74 (-5) (-4) (8) (-14)
Indonesia 10-yr 8,93 (-12) (40) (28) (111)

Country risk *(changes in bp)*
Developed Markets
10-yr sovereign spreads *(against Germany)*
Belgium 31 (0) (2) (2) (2)
France 33 (0) (2) (1) (5)
Greece 759 (-50) (-20) (97) (-162)
Ireland 48 (0) (-4) (-7) (-23)
Italy 102 (-2) (5) (-1) (-33)
Netherlands 16 (0) (1) (-1) (1)
Portugal 191 (-2) (5) (-24) (-24)
Spain 110 (-3) (7) (-17) (3)

5-yr sovereign spreads *(against Germany)*
Belgium 10 (0) (4,6) (-1) (-5)
France 15 (-1) (2) (0) (-1)
Greece 1605 (-2) (-4) (-9) (472)
Ireland 27 (0) (3) (-6) (-13)
Italy 62 (-2) (5) (4) (-32)
Netherlands 1 (0) (0,5) (-2) (-7)
Portugal 120 (-2) (4) (-32) (-23)
Spain 75 (-3) (6) (-4) (-12)

2-yr sovereign spreads *(against Germany)*
Belgium 7 (0) (0) (1) (2)
France 5 (-1) (-1,1) (-1) (-2)
Ireland 17 (0) (-1) (0) (5)
Italy 43 (0) (6) (5) (-20)
Netherlands 1 (0) (0) (-1) (-6)
Portugal 47 (0) (3) (-5) (-5)
Spain 44 (1) (8) (6) (-6)

5-yr sovereign CDS
5-yr CDS Belgium 33 (1) (-2) (-1) (-16)
5-yr CDS France 25 (0) (-1) (-2) (-21)
5-yr CDS Germany 13 (0) (0) (0) (-5)
5-yr CDS Greece 1066 (-23) (57) (12) (-215)
5-yr CDS Ireland 42 (0) (-1) (-1) (-9)
5-yr CDS Italy 99 (0) (8) (-8) (-36)
5-yr CDS Netherlands 16 (0) (0) (0) (-4)
5-yr CDS Portugal 176 (-3) (7) (-47) (-24)
5-yr CDS Spain 87 (0) (7) (-10) (-9)
5-yr CDS UK 19 (1) (0) (1) (-3)
5-yr CDS US 20 (0) (0) (-1) (3)

Emerging Markets
5-yr sovereign CDS
5-yr CDS Brazil 446 (-20) (-9) (18) (247)
5-yr CDS Chile 134 (-9) (1) (2) (40)
5-yr CDS Colombia 241 (-17) (0) (22) (102)
5-yr CDS Mexico 172 (-12) (4) (14) (69)
5-yr CDS Peru 191 (-11) (-3) (11) (76)
5-yr CDS Venezuela 5380 (-104) (980) (197) (875)

5-yr CDS Poland74 (-1) (-1) (0) (4)
5-yr CDS Russia 300 (-20) (7) (11) (-176)
5-yr CDS Turkey 272 (-14) (-5) (21) (90)

5-yr CDS China 110 (-6) (4) (8) (24)
5-yr CDS India 155 (-1) (5) (1) (-16)
5-yr CDS Indonesia 240 (-11) (9) (19) (84)

Credit risk
Risk indicators *(changes in percentage except for BAA spreads, bp)*
VIX 19,92 (-4,9) (1,6) (9,7) (0)
VSTOXX25,47 (-7,3) (4,8) (-1,5) (-2)
EM EFT volatility Index 27 (-5) (-3) (11) (20)
Dollar/euro volatility 10,2 (0) (2,4) (-15) (6)
EM FX volatility index 11 (0) (7) (6) (5)
Credit spread (BAA) 316,1 (-3,4) (-2,3) (-4,8) (67)
US bonds volatility index 80 (0) (10) (18) (15)

Bank risk *(changes in bp)*
US banks CDS 78 (-3) (1) (3) (8)
EMU banks CDS 83 (-5) (4) (-2) (-1)
UK banks CDS 79 (-4) (5) (-2) (20)

Large Spanish banks CDS 125 (-8) (10) (-6) (48)
Medium Spanish banks CDS 160 (4) (6) (0) (46)

Greek banks CDS 1631 (26) (128) (297) (747)
Russian banks CDS 400 (2) (25) (19) (-187)

Corporate risk *(changes in bps)*
US Non-financial CDS 0 (0) (0) (0) (-157)
EMU Non-financial CDS 0 (0) (0) (0) (-107)
UK Non-financial CDS 0 (0) (0) (0) (-113)

Interbank markets *(changes in bp)*
UEM OIS spread 3m 10 (0) (-2) (-5) (-1)
UEM OIS spread 12m 33 (0) (0) (-3) (-6)
UEM TED spread 3m 36 (0) (4,8) (6) (12)

US OIS spread 3m 19 (-1) (2) (7) (6)
US OIS spread 12m 55 (-1) (3) (6) (21)
US TED spread 3m 26 (-2) (2) (0) (4)

Spain Ted Spread 3m -9 (-2) (-17,5) (-21) (-15)

EONIA Index -0,24 (0) (-0,4) (-10) (-38)
Euribor 3m -0,13 (0) (-1,4) (-5) (-21)
Euribor 12m 0,06 (0) (-1) (-2) (-27)

Libor 3m 0,53 (0) (3) (16) (27)
Libor 12m 1,07 (0) (2) (14) (44)

Stock markets *(Changes in percentage)*
Developed Markets
Main equity indices
S&P500 2050 (0,3) (0,1) (-0,2) (0)
Dow Jones 17579,1 (0,3) (0,5) (0,5) (-1)
Nikkei 19049,9 (2,6) (-1,3) (-1,8) (9)
FTSE 100 6066,8 (0,8) (-1) (-1,3) (-8)
EuroStoxx 50 3253,3 (0,4) (-0,7) (-3,2) (3)
IBEX9714,6 (0) (-1,2) (-4) (-5)
DAX 10498,9 (0,5) (-0,9) (-2) (7)
CAC4637 (0,5) (0) (-3,5) (9)
MIB 21228,6 (-0,2) (-1,3) (-2,7) (12)
ASE Athens 601,2 (3,1) (7,4) (-6,6) (-27)

Bank stocks
US banks 95,9 (0,2) (0,5) (-2,1) (-4)
JPM 66,3 (0,3) (1,3) (-0,3) (6)
Citi 52,5 (-0,1) (-0,7) (-2,3) (-3)
BoA 17,4 (0,1) (1,9) (0) (-3)
MS 32,9 (0) (-1,6) (-3,5) (-15)
GS 182,9 (0,5) (1,2) (-4,8) (-6)

UK banks 85,1 (0,6) (-0,5) (-2,8) (-15)
HSBC 522,1 (2,1) (2,1) (2,1) (-14)
RBS 290,1 (0,5) (-0,1) (-5,9) (-26)
Barclays 215,1 (0,1) (-3,1) (-4,2) (-12)
Lloyds 70,3 (-0,1) (-0,6) (-3,3) (-7)

EMU banks 106,5 (-0,1) (-0,8) (-5,3) (6)
BNP 52,5 (0,1) (0,6) (-5,4) (7)
Crédit Agricole 10,5 (0,1) (-1,2) (-4,9) (-3)
Deutsche Bank 21,5 (0,3) (-3,9) (-9,3) (-14)
ING 12,2 (-1,2) (-0,9) (-7,2) (13)
Intesa 3,1 (-0,8) (-0,6) (-1,9) (27)
SG 42,1 (1,2) (0,6) (-3,1) (20)
Unicredito 5,1 (-0,7) (-1,2) (-6,9) (-4)

Large Spanish banks 77,8 (0,7) (-2,1) (-6,8) (-22)
Santander 4,7 (0,7) (-1,4) (-5,8) (-33)
BBVA 7 (0,8) (-2,6) (-7,6) (-11)

Medium Spanish banks 86,1 (-0,2) (-0,6) (-0,4) (-14)
Caixabank 3,5 (-0,6) (1,1) (3,5) (-19)
Popular 3,2 (-0,5) (-1,3) (-4,1) (-23)
Sabadell 1,7 (-0,1) (-0,8) (-1,3) (-17)
Bankinter 6,6 (-0,3) (-0,9) (1,5) (-1)
Bankia 1,1 (0,6) (-0,8) (-1,5) (-9)

Greek banks 4,4 (2,9) (12,2) (-71,2) (-96)
Alpha Bank2,4 (2,6) (24,9) (-24,7) (-90)
Pireus Bank0,3 (0,7) (-12,7) (-80,1) (-100)
National Central Bank0,3 (1,8) (-31,3) (-95,3) (-99)
Eurobank Ergasias1 (4) (9,7) (-61,9) (-84)

Emerging Markets
Main equity indices
MSCI Latam 60053 (1,15) (0,8) (-3,5) (-10,1)
Ibovespa (Brazil) 44571 (-0,7) (-3,3) (-4,9) (-10,9)
Mexbol 43288 (0,9) (2,1) (-0,8) (0,3)

MSCI EM Europe 4179 (1,98) (-0,3) (-5,8) (-5,7)
Poland 1805 (1,8) (1,8) (-8,5) (-22,1)
Micex (Russia) 1755 (0,7) (1,2) (0,9) (25,6)
Ise 100 (Turkey) 72832 (0,9) (-2,3) (-10,1) (-15)

MSCI EM Asia 648 (0,45) (-1,9) (-3,5) (-9,9)
Shanghai Composite (China) 3516 (0,17) (1,3) (-2,5) (8,7)
Jakarta Composite (Indonesia) 4483 (1,7) (0,4) (0,9) (-14)

Bank stocks
Turkish banks 76 (1,8) (-2,3) (-9,4) (-24,5)
Akbank T.A.S. 7 (1,9) (-2,3) (-10,5) (-20,9)
Garanti 7 (1,7) (-2,3) (-7,7) (-21,9)
Turkiye Is Bankasi 5 (1,7) (-2,3) (-10) (-30,7)

Russian banks 151 (2,2) (2,3) (5,1) (51,2)
Sberbank 102 (2,3) (1,6) (6,8) (86,3)
VTB Bank 0,1 (1,9) (3,5) (2,4) (16)

Currencies *(in percentage, positive for dollar depreciation)*
Developed Markets
EURUSD 1,094 (0,09) (-0,76) (2,4) (-9,6)
GBPUSD 1,5 (-0,27) (-1,2) (-1,3) (-3,8)
USDJPY 121,83 (-0,12) (-0,32) (1,1) (-1,7)
DXY 98,24 (0) (-0,9) (1,2) (-8,8)

Emerging Markets
USDARS (Argentina) 9,8 (0,1) (-0,6) (-1,7) (-15,7)
USDBRL (Brazil) 3,94 (-1,9) (-5,1) (-3,3) (-48,4)
USDCLP (Chile) 708,79 (0,3) (-0,7) (0,6) (-16,8)
USDCOP (Colombia) 3301,73 (0,4) (-0,5) (-7,3) (-38,9)
USDMXN (Mexico) 17,13 (-0,1) (-0,4) (-2,1) (-16,1)
USDPEN (Peru) 3,37 (0,1) (0,2) (-0,7) (-13,1)
LACI 64,43 (-0,5) (-1,9) (-2,3) (-21,6)

USDPLN (Poland) 3,93 (0,3) (0,3) (1) (-11,1)
USDRUB (Russia) 70,46 (-0,7) (-1,6) (-7,8) (-21,9)
USDTRY (Turkey) 2,96 (0,2) (-1,5) (-2,6) (-26,9)

USDCNY (China) 6,47 (-0,2) (-0,7) (-1,6) (-4,3)
USDINR (India) 66,73 (0,3) (0,2) (-1,1) (-5,3)
USDIDR (Indonesia) 14071 (-0,2) (-0,4) (-2,3) (-13,6)
ADXY 106,65 (-0,1) (-0,2) (-0,7) (-5,4)

Commodities *(change in percentage)*
Brent 37,35 (-2,9) (-6,9) (-16,2) (-34,9)
WTx 36,05 (-3,5) (-3) (-13,6) (-32,3)
Copper 206,5 (0,7) (0,2) (-2,5) (-27,3)
Gold 1075,14 (1,3) (0,2) (-0,7) (-9)
CRB Index 378,88 (0) (-1,6) (-1,2) (-13,4)
CRB (food) index 348,65 (0) (-3,9) (-2,7) (-5,6)
Baltic Dry Index 484 (0) (-11,4) (-12) (-38,1)

Source: Bloomberg, Datastream and Haver

*CDS, EMBI & MSCI indices with one day delay
**Credit spread (BAA) with two days delay