

Market Comment | Disappointing economic data encourage investors' demand for bonds

Global Financial Markets Unit
19 Jul 2016

- **Financial markets extended yesterday's cautious mood** (gold +0.3%, JYP +0.03%), **underpinned by the disappointing July German ZEW Economic Sentiment expectations** (-6.8; consensus 9; previous 19.2), at their lowest level since 2012, dragged down by the uncertainty about Brexit. Furthermore, **the IMF trimmed (-0.1pp) its forecast for 2016 and 2017 global GDP growth**, with UK and Germany accounting for the main part of the revision for 2017 forecast (-0.9pp UK and -0.4pp Germany) due to the Brexit effect ([see](#)). The UK's new finance minister, Philip Hammond, said he would support further fiscal measures if post-referendum economic data showed weakness, but in the meantime he stated that "the response to this kind of a shock must be a monetary response". In fact he said he would detail new fiscal plans in the latter part of the year, with possible budget measures.
- On the other hand, low interest rates boosted US housing starts in June, but the data had only a mild effect on expectations of an interest rate hike. The Atlanta Fed GDPNow model forecast for real 2Q16 GDP growth remained unchanged at 2.4%
- In this context, **investors kept purchasing bonds, with yields decreasing across the board**. 10Y safe-haven yields inched down (-2 bps Germany and -3 bps US), while European peripheral yields declined significantly (-6 bps Spain, -5 bps Portugal, and renewed falls in Italian bank stocks no doubt weighed on Italian sovereign bonds (-2 bps).
- Weak economic data in Germany dragged down equity markets in Europe (Euro Stoxx, -0.5%; Dax, -0.8%, Ibex35, -0.4%). **Italian banks resumed their falls** (UniCredit -0.6%, Monte dei Paschi -3.29%, Intesa Sanpaolo -0.8%) coinciding with the release of the decision of the European Court of Justice of European Union, supporting the bail-in rules within the EU ([see](#)). The rally in the US equity index faded today, as investors took profits, but indices are close to historical highs. On the other hand, the Japanese index bucked the trend (Nikkei, +1.4%), underscoring expectations of further easing in economic policy later this month.
- The dollar reached the highest US Dollar Index in 4 months, but later in the session inched down against its major peers (-0.5%). The Chinese yuan hit its 5-year record low against the USD at 6.7 yuan per dollar. EM currencies experienced depreciation across the board against the USD (COP -0.3%, MXN -0.9%, CLP -0.5%, PLN -0.9%).
- **Turkish assets were very volatile today**. Equity and bond markets started the session rebounding after yesterday's sell-off, followed by the Central Bank's decision to cut interest rates today, but ended the day lower (BIST100 -1%), dragged down by the political uncertainty. The pressure on the Turkish lira caused it to depreciate against the USD (-1.6%), and Turkey's 10Y yield rose (+30 bps).

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Table 1

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

Debt markets (changes in bp)

US 91 9.8 (0.1) (1.58)
 US 91 1.1 (2.0) (1.44)
 US 10yr 1.9 (0.1) (0.41) (2)

Japan 10yr 2.2 (0.1) (0.17) (46)

OECD 5yr 4.6 (0.1) (1.4) (20)
 OECD 5yr 4.7 (0.1) (1.7) (25)
 OECD 5yr 4.5 (0.1) (0.4) (46)

Belgium 10yr 6.2 (1.0) (1.20) (24)
 Finland 10yr 5.1 (1.1) (1.22) (27)
 France 10yr 3.7 (0.1) (0.28) (33)
 Germany 10yr 4.0 (0.1) (1.1)

Italy 10yr 5.7 (1.1) (1.26) (37)
 Netherlands 10yr 3.9 (0.1) (0.19) (13)
 Portugal 10yr 5.0 (0.1) (1.2) (26)
 Spain 10yr 4.1 (0.1) (0.50) (46)

Issuance (billion)

Finland 10yr 4.6 (0.1) (1.17) (46)
 China 10yr 4.3 (0.1) (2.28) (28)
 Canada 10yr 3.7 (0.1) (2.28)

France 10yr 3.1 (0.1) (1.70) (20)
 France 10yr 3.1 (0.1) (1.41) (18)

France 10yr 2.0 (0.1) (1.24) (3)
 Russia 5yr 0.7 (0.1) (1.1) (46)
 Russia 10yr 0.1 (0.1) (1.61) (180)

Turkey 10yr 0.8 (0.1) (0.18) (81)
 India 10yr 0.1 (0.1) (0.2) (4)

Russia 10yr 0.2 (0.1) (1.4) (56) (18)

Country risk (changes in bp)

US 10yr sovereign spread (against Germany)
 France 24 (1.4) (1.0) (45)
 Finland 24 (1.0) (1.17) (2)

Germany 28 (0.2) (1.0) (20)
 Ireland 42 (1.6) (2.1) (4)

Italy 26 (0.1) (0.25) (0.9)
 Netherlands 12 (1.1) (1.1) (18)
 Portugal 31 (1.4) (1.0) (12)

Spain 12 (1.4) (1.0) (12)

US 10yr sovereign spread (against Germany)
 France 14 (1.1) (1.1) (12) (6)
 Finland 18 (0.1) (1.1) (2)

Germany 17 (0.1) (1.1) (2)
 Ireland 14 (0.1) (1.1) (2) (3)
 Italy 20 (1.1) (1.1) (18)

Netherlands 14 (0.1) (1.1) (12) (3)
 Portugal 20 (1.1) (1.1) (18)

Spain 12 (1.1) (1.1) (12) (3)

US 10yr sovereign spread (against Germany)
 France 12 (1.1) (1.1) (12) (6)
 Ireland 23 (1.1) (1.1) (12) (6)

Italy 23 (1.1) (1.1) (12) (6)
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 Portugal 13 (1.1) (1.1) (12) (6)

Spain 5 (1.1) (1.1) (12) (6)

Credit risk

US 10yr sovereign spread (against Germany)
 France 10 (1.1) (1.1) (12) (6)
 Ireland 23 (1.1) (1.1) (12) (6)

Italy 23 (1.1) (1.1) (12) (6)
 Netherlands 7 (1.1) (1.1) (12) (6)
 Portugal 13 (1.1) (1.1) (12) (6)

Spain 5 (1.1) (1.1) (12) (6)

Stock markets (changes in percentage)

US 10yr sovereign spread (against Germany)
 France 10 (1.1) (1.1) (12) (6)
 Ireland 23 (1.1) (1.1) (12) (6)

Italy 23 (1.1) (1.1) (12) (6)
 Netherlands 7 (1.1) (1.1) (12) (6)
 Portugal 13 (1.1) (1.1) (12) (6)

Spain 5 (1.1) (1.1) (12) (6)

CDS, EMBI & MSCI indices with one day delay

**Credit spread (BAA) with two days delay

***S&P GSCI with one day delay

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