

Market Comment | Yields rose sharply ahead of today's US GDP figures and next week's FOMC

Global Financial Markets Unit
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- **Rating agency DBRS maintained Portugal's long-term sovereign debt rating at BBB low with a stable outlook.** The decision was crucial for Portugal's sovereign bond markets, as a downgrade would have prevented the ECB from purchasing Portuguese sovereign debt or accepting it as collateral. ([see](#))
- **Positive economic data in the EZ, led by Germany.** German PMI drove the EZ PMI improvement and its Ifo Business Climate Index surprised positively in October. Furthermore, supportive **GDP growth for Q3 2016 in the UK** (+0.5% QoQ, consensus +0.3% QoQ), confirmed that the UK economy slowed only slightly after the Brexit referendum. On another front, this week's **Eurogroup** meeting unsurprisingly approved the disbursement of €2.8 billion in funds to Greece as part of the country's third bailout after Athens completed the required reforms.
- Against this backdrop **sovereign yields increased, led by the UK (10YUK +17bps)**, which returned to pre-Brexit levels, and pushing up EZ sovereign yields (10YGER +16 bps) in the week. In the meantime, European peripheral risk premiums decreased, above all in Portugal (10YPOR +11 bps) due to the favourable decision by DBRS rating agency, and Spain (10YSPA +7 bps) due to the loosening of the political deadlock. US yields also increased, fuelled by increasing market expectations of a Fed interest rate hike in December (73%) **ahead of today's important 3Q 2016 US GDP figures. The focus is on the Fed's stance, as it will hold its next policy meeting next week.** Moreover, the increase in inflationary expectations across the board (US 5Y5Y inflation swap 2.18% and EZ 5Y5Y inflation swap 1.48%) also contributed to the recent yield rebound.
- **Equity markets were little changed and showed mixed performances across the board,** although equity volatility increased (VIX +14%, VSTOXX +15%) amid mixed corporate earnings reports both in Europe (Dax -0.1%, Euro Stoxx50 +0%, Ibex35 +0.7%) and the US (S&P500 -0.4%). Nonetheless, the higher yields along with the steeper yield curves pushed up banking stocks across the board (EZ banks +2.8%, UK banks +1.9%, US banks +1.3%).
- **In FX markets, the JPY and the GBP depreciated significantly against the USD (-1.4% and -0.8% respectively), while the EUR remained stable.** On the other hand, oil prices were around 3% lower on uncertainty over whether OPEC would be able to coordinate a global action to carry out a sufficient cut in oil production to eliminate the current supply glut. In this context, EM currencies depreciated across the board, especially the MXN (-1.2% against the USD) on the back of a recent uptick in the polls by Republican candidate Donald Trump in some US states.

FOMC preview

- At its 1-2 November meeting, the FOMC will be faced with the challenge of preparing markets for policy renormalisation in December and reconciling market expectations with a gradual — but still positive - tightening cycle. With markets looking to December for the next increase, and with the meeting falling only six days before the end of the U.S. presidential elections, there is a low probability of a rate hike at this meeting. That being said, broader macro conditions are consistent with levels that would imply a rate hike, suggesting that December remains the most likely time for a rate hike in 2016.

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Table 1

Debt markets (10Y, % change in bp)					
	level	Daily	Weekly	Monthly	YTD
Developed Markets					
US (2-yr)	0.88	0.6	5.7	12	-17
US	1.85	-0.5	11.4	28	-42
GER (2-yr)	0.61	1.0	4.7	8	-27
Germany	0.16	0.7	15.7	31	-47
France	0.46	0.3	17.0	30	-53
Spain	1.20	0.6	8.8	31	-57
Italy	1.57	4.0	19.7	39	-3
Portugal	3.30	1.3	10.5	-3	78
Greece	8.39	0.0	-5.1	12	11
Japan (2-yr)	0.24	2.3	1.4	6	-23
Japan	0.04	1.0	4.8	-31	-31
Emerging Markets					
Brazil	11.39	1.4	22.0	-27	-513
Chile	4.18	0.0	0.3	1	-48
Colombia	7.27	0.0	5.5	26	-139
Mexico	6.21	0.3	14.7	18	-5
Peru	5.70	0.0	-1.7	-9	-160
Poland	3.09	-5.5	13.1	22	14
Russia	8.52	-4.5	17.4	29	-104
Turkey	9.85	10.0	23.0	49	-62
India	7.39	0.0	-4.0	-13	-26
Indonesia	7.29	16.9	20.8	35	-146
Country risk (bp, change in bp)					
Developed Markets					
10-yr sovereign spread vs Germany					
France	29	1.0	1.3	-1	-6
Italy	141	4.7	4.0	8	44
Portugal	313	2.0	-5.2	-34	125
Spain	104	1.3	-6.9	0	-10
2-yr sovereign spread vs Germany					
France	3	-0.4	-1.7	-3	-1
Italy	59	1.9	0.4	2	28
Portugal	91	-0.2	-1.2	-16	46
Spain	45	1.9	0.1	-3	10
Emerging Markets					
5-yr sovereign CDS *					
Brazil	271	6	13	1	-221
Chile	88	1	3	3	-39
Colombia	171	1	4	-2	-68
Mexico	149	4	7	-17	-21
Peru	103	2	6	-4	-83
Venezuela	3,727	196	148	250	-2316
Poland	75	1	0	4	3
Russia	223	-1	2	8	-78
Turkey	248	1	7	-10	-25
China	105	0	0	-3	-4
India	137	0	-2	-3	-11
Indonesia	151	1	0	-2	-76
Risk indicators					
Volatility indicators (%)					
VIX	15	-0.9	14	23	-3
VSTOXX	19	2.3	15	-3	-3
EM EFT volatility index	22	0.0	11	5	5
Dollar/euro volatility	7	-0.3	-6	3	-29
EM FX volatility index	9	-0.1	1	-6	-17
Credit spread (BAA/Baa)	254	0.5	-6	-15	-69
US bonds volatility index	63	5.1	10	9	-8
Banking 5y CDS (bps) *					
US	74	-1.7	1	-6	-1
EZ	114	-0.8	3	-14	31
UK	99	-5.2	-3	-5	21
Large Spanish	117	-2.7	-4	-21	-20
Medium Spanish	154	-0.8	1	-4	3
Corporate 5y CDS (bps) *					
US Non-financial	195	-1.7	1	-6	-1
EZ Non-financial	106	-0.8	3	-14	31
UK Non-financial	136	-0.6	0	-6	-56
Interbank markets (% change in bp)					
EONIA Index	-0.35	0.00	0.0	0.0	-0.2
Euribor 3m	-0.31	0.00	0.0	0.0	-0.2
Euibor 12m	-0.07	0.00	0.0	0.0	-0.1
Libor 3m	0.89	0.00	0.0	0.1	0.3
Libor 12m	1.58	0.00	0.0	0.0	0.4
EZ TED spread 3m	56.1	0.90	2.1	9.9	15.3
Stock markets (%)					
Asian indices					
S&P500	2,133	0.0	-0.4	-2	-4
Dow Jones	18,170	0.0	0.1	-1	4
Nikkei	17,446	0.6	1.5	6	-8
FTSE 100	6,986	0.0	-0.5	2	12
EuroStoxx 50	3,076	0.3	0.0	3	6
IBEX	9,164	-0.4	0.7	5	-4
DAX	10,698	0.2	0.1	2	0
CAC	4,546	0.3	0.2	3	-2
MBI	17,307	0.7	0.8	7	-19
ASE Athens	589	0.0	-0.9	5	-7
MSCI Latam *	76,380	0.5	0.4	6	29
Bovespa (Brazil)	64,250	0.0	0.2	6	48
Mobvil	48,115	0.0	-0.6	0	12
MSCIEM Europe *	4,523	-0.1	0.4	2	6
Poland	1,805	0.5	3.0	4	-3
Mircex (Russia)	1,980	0.0	1.1	0	12
Ise 100 (Turkey)	78,333	-0.5	-0.6	1	9
MSCIEM Asia *	716	-0.4	-0.9	-1	8
Shanghai Com (China)	3,104	-0.3	0.4	11	-12
Jakarta (Indonesia)	5,410	0.2	0.1	0	18
Banking sector					
US banks					
JPM	91.4	0.0	1.3	8	-3
Citi	69.2	0.0	1.3	41	5
BofA	49.9	0.0	0.7	7	-4
MS	16.9	0.0	1.4	10	0
GS	33.8	0.0	1.1	6	6
US	177.8	0.0	1.8	9	-11
EZ banks					
BNP	85.7	-0.9	2.8	14	-21
Credit Agricole	53.1	-0.7	2.0	16	2
Deutsche Bank	9.9	-0.7	3.5	13	-9
ING	13.3	-0.5	1.4	24	-41
Intesa	12.0	-0.3	2.1	11	-3
SG	2.2	-1.5	2.6	11	-30
UniCredit	36.0	-1.4	3.6	16	-16
UK banks	2.4	-1.3	3.1	14	-54
RBS	76.2	-0.7	1.9	9	-13
HSC	620.3	1.1	-1.0	9	16
RBS	192.3	-2.1	1.2	9	-36
Birclays	191.0	0.2	4.2	15	-13
Lloyds	57.4	-0.3	4.0	3	-22
Large Spanish banks					
Santander	73.7	-1.1	5.0	19	-2
BBVA	4.5	-1.3	3.5	15	-2
CaixaBank	6.6	-0.9	6.2	23	-3
Medium Spanish banks					
Populär	64.0	-2.0	1.6	12	-22
Sabadell	2.7	0.4	5.2	25	-15
Bankia	1.0	-7.9	-6.8	-7	-63
Banque	1.2	-4.8	-1.6	8	-25
Banque	7.0	-0.9	2.1	12	6
Banque	0.8	-0.5	4.2	16	-24
Currencies (% net for currency depreciation)					
Developed					
EURUSD	1.09	0.2	0.3	-2.7	0
GBPUSD	1.21	-0.2	-0.8	-6.8	-18
USDJPY	105.28	0.0	-1.4	-4.6	12
DDX	98.03	0.1	-0.1	-3.6	0
Emerging					
USDARS (Argentina)	15.17	0.0	-0.3	1.3	-17
USDBRL (Brazil)	3.16	0.2	0.1	1.8	20
USDCUP (Cuba)	649.95	0.0	2.5	1.8	8
USDCOP (Colombia)	2960	0.0	-0.9	1.7	7
USDMXN (Mexico)	18.81	0.2	-1.2	2.9	-9
USDPEN (Peru)	3.36	0.0	-0.1	0.4	2
USDPLN (Poland)	65.50	0.1	0.2	1.8	5
USDPLN (Poland)	3.97	0.3	0.0	-3.7	-1
USDROL (Russia)	62.90	-0.3	-0.8	0.3	13
USDTRY (Turkey)	3.12	-0.2	-1.3	-4.7	-7
USDCNY (China)	6.78	0.0	0.2	-1.6	-4
USDINR (India)	66.79	0.1	0.2	-0.5	-1
USDIDR (Indonesia)	13,051	-0.1	-0.1	-0.7	5
ADXY	105.7	0.1	-0.2	-1.8	-1
Commodities (%)					
Brent	50.3	-0.3	2.8	3	35
WTI	49.5	-0.5	2.7	5	34
Copper	216	-0.1	3.9	-1	2
Gold	1,267	-0.1	0.0	-4	19
S&P Spot commodity *	374	0.9	-0.5	4	20
S&P Brent Spot *	439	1.1	-2.1	5	37
S&P Metals Spot *	282	1.0	3.9	1	12
S&P Agricultura *	306	0.5	1.3	4	8

Source: Bloomberg, Datastream and Haver

* With one day delay

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