

Market Comment | Risk-on sentiment this week on French "vote relief"

Global Financial Markets Unit
28 Apr 2017

- **Financial markets rallied early this week** boosted mainly by the decrease in concerns about French politics, while the ECB also contributed to the risk-on mood as it said it saw the risk to growth more balanced. The rebound in European inflation and the announcement of the US tax cut plan had a mild effect on financial markets. **Nonetheless markets have been steady at the end of the week** ahead of next week's FOMC meeting and the US payrolls release.
- Emmanuel Macron, the pro-EU candidate, won the first round of the French election ([see results](#)), **easing concerns about a potential Frexit**, as it is widely-expected that Macron will comfortably beat Le Pen. As a result, investors wound down the cautious stance of the last few weeks, thereby dragging down European core bond yields and boosting both European stocks and European peripheral debt, with a significant narrowing of peripheral risk premiums. The EUR also appreciated significantly ([see](#)). European stocks increased (especially French stocks and the banking sector), driving German stocks to all-time highs ([see](#)).
- **ECB keeps monetary policy stance unchanged** ([see](#)). The central bank left key policy rates as they were and confirmed that the monthly asset purchases of €60 billion were intended to run until the end of March 2017, or beyond, if necessary. Although, in the short term, perhaps at the June meeting, it is probable that it could adopt a neutral bias regarding interest rates (removing the downward bias) but maintaining a very cautious approach. The ECB statement seems to have been perceived as slightly more dovish than expected given the market reaction, as European sovereign bond yields (and peripheral risk premiums) declined and the EUR depreciated.
- **EZ inflation accelerated in April**, driven mostly by higher prices of services (Easter effect), reversing the recent easing in inflation. Moreover, core inflation also accelerated, beating expectations, which may exert additional pressure on the ECB to remove its downward bias earlier. Following the release, the EUR appreciated and European sovereign bond yields increased across the board.
- U.S. Treasury Secretary Steven Mnuchin confirmed that the **Trump administration's tax plan** will include a 15% corporate tax rate ([see](#)), although financial markets received the announcement in a muted way as investors remained cautious, waiting for the official details of the tax overhaul and US lawmakers' final approval of the proposed reforms. Moreover, US 1Q17 GDP surprised to the downside ahead of next week's FOMC meeting.
- In these circumstances, EM currencies mainly depreciated on the back of lower oil prices. Nonetheless, the volatility in the Mexican peso increased during the week in line with some erratic declarations regarding the **US commitment to NAFTA**. Finally the announcement by the White House that it will not abandon the NAFTA agreement shored up the MXN. Meanwhile the TRY appreciated, supported by slight central bank tightening.

FOMC preview

- The FOMC's discussion at the May 2nd-3rd meeting will likely focus on the evolution of the labor market, balance sheet normalization strategy, and risks from abroad. With the unemployment rate at 4.5%, the uptick in labor force participation and global economic vulnerabilities contained (China and elections in Europe), there is a strong possibility that the topic of accelerating the pace interest rate increases will be brought up. The hawk's will have leverage to strengthen their argument for rapid removal of policy accommodation position in the not-too-distant future, if they can make a case that the economy is at full employment, and as more than a handful of inflation indicators are trending above the committee's target.
- That being said, we do not anticipate the committee to raise interest rates. The statement should reflect the committee keen awareness of the downside risks to miscommunicating or rushing the exit strategy (Taper Tantrum), suggesting only a slightly more hawkish bias. As such, we do not anticipate the committee will discontinue its reinvestment policy, as the FOMC will continue crafting a strategy to be set in motion at the end of the year. Markets will likely have to wait for the minutes to pull back the curtain on the committee's discussion on the timing, composition, magnitude and ending point of the balance sheet normalization.

BBVA Research suggest the following reading list:

- Theory and evidence for the last two decades of tariff reductions (see)
- An upswing in the world economy is not sustained growth (see)
- It is premature to abandon global reflation theme (see)

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Table 1

Debt markets (10Y, % changes in bp)					
Developed Markets	level	Daily	Weekly	Monthly	YTD
US (2-yr)	1.27	0.8	8.6	0	9
US	2.30	0.5	5.2	8	114
GER (2-yr)	-0.73	0.5	5.8	1	4
Germany	0.32	2.2	6.5	-3	4
France	0.84	0.8	-10.3	-10	3
Spain	1.65	2.3	-4.6	1	14
Italy	2.28	3.9	2.1	15	41
Portugal	3.55	8.7	-19.6	-46	63
Greece	6.34	-3.6	-29.4	-61	-54
Japan (2-yr)	-0.21	-2.2	1.1	4	-2
Japan	0.02	0.2	-4.0	-5	-5
Emerging Markets	level	Daily	Weekly	Monthly	YTD
Brazil	10.35	-2.2	18.5	24	-106
Chile	4.02	0.1	13.0	-13	-31
Colombia	6.22	-0.2	-13.6	-47	-88
Mexico	7.23	-3.5	2.0	16	-41
Peru	5.66	-3.6	9.1	-11	81
Poland	3.44	2.7	2.1	-10	-28
Russia	7.77	-12.2	-7.3	-29	-67
Turkey	10.23	11.0	-14.0	-53	-77
India	6.96	2.0	3.9	21	58
Indonesia	7.05	0.6	-5.7	-4	-79
Country risk (Spreads in bp)	level	Daily	Weekly	Monthly	YTD
Developed Markets					
10-yr sovereign spread vs Germany					
France	52	-1.4	-16.8	-7	-2
Italy	197	1.7	-4.4	17	37
Portugal	323	6.5	-26.1	-43	-39
Spain	133	0.1	-11.1	3	17
2-yr sovereign spread vs Germany					
France	28	-1.1	-22.3	-13	17
Italy	66	0.6	-13.3	-1	5
Portugal	118	8.0	-3.7	-16	-29
Spain	48	-1.2	-13.0	-7	0
Emerging Markets	level	Daily	Weekly	Monthly	YTD
5-yr sovereign CDS *					
Brazil	217	-4	-7	-11	-55
Chile	73	-1	-6	0	9
Colombia	127	-3	-8	-6	-36
Mexico	120	-6	-10	-12	-36
Peru	38	-1	-7	-5	-10
Venezuela	3,377	28	-113	-104	-526
Poland	67	0	-2	-3	-9
Russia	153	2	-10	-19	-23
Turkey	208	-4	-20	-26	-64
China	82	1	-6	-2	-35
India	99	0	-5	-1	-28
Indonesia	127	2	-7	-2	-79
Risk indicators	level	Daily	Weekly	Monthly	YTD
Volatility indicators (%)					
VIX	11	6.9	-24	-3	-1
VSTOXX	17	5.9	-32	7	1
EM ETT volatility index	15	2.1	-2.8	9	27
Dollar/euro volatility	8	-0.1	-39	-6	-24
EM FX volatility index	9	0.6	-3	4	21
Credit spread (BAA) (bps)	228	-0.5	0	4	1
US bonds volatility index	60	-1.9	-22	2	-22
Banking 5y CDS (bps) *					
US	58	0.5	-3	-8	-14
EZ	92	0.6	-21	-12	-16
UK	66	0.4	-13	-9	-24
Large Spanish	86	0.3	-20	-21	-31
Medium Spanish	161	4.0	-3	1	9
Corporate 5y CDS (bps)					
US Non-financial	149	0.5	-3	-6	-14
EZ Non-financial	95	0.6	-21	-12	-16
UK Non-financial	116	0.6	-7	-6	-9
Interbank markets (% changes in bp)	level	Daily	Weekly	Monthly	YTD
EONIA Index	-0.36	0.00	0.0	0.0	0.0
Euribor 3m	-0.33	0.00	0.0	0.0	0.0
Earibor 12m	-0.12	0.00	0.0	0.0	0.0
Libor 3m	1.17	0.00	0.0	0.0	0.2
Libor 12m	1.78	-0.01	0.0	0.0	0.1
EZ TED spread 3m	50.8	3.40	3.1	-10.2	-15.6
Stock markets (%)	level	Daily	Weekly	Monthly	YTD
Main Indices					
S&P500	2,384	-0.2	1.5	1	5
Dow Jones	20,945	-0.2	1.9	1	5
Nikkei	19,197	-0.3	3.1	0	-2
FTSE 100	7,204	0.5	1.3	2	0
EuroStoxx 50	3,560	0.1	3.5	2	7
BEX	10,716	0.3	3.3	3	13
DAX	12,438	0.0	3.2	2	7
CAC	5,267	-0.1	4.1	4	8
MIB	20,609	0.1	4.4	2	5
ASE Athens	712	0.8	6.0	7	8
MSCI Latam *	76,914	0.5	0.7	-1	5
Ibovespa (Brazil)	65,345	1.0	2.5	0	6
Mercol	49,331	-0.2	0.7	1	6
MSCI EM Europe *	4,959	-0.7	3.5	1	-2
Poland	2,377	-0.2	5.0	7	19
Mosc (Russia)	2,917	0.3	3.7	0	-11
Ise 100 (Turkey)	94,655	0.4	2.4	6	24
MSCI EM Asia *	776	0.0	2.4	2	12
Shanghai Com (China)	3,155	0.1	-0.6	-3	0
Jakarta (Indonesia)	5,685	-0.7	1.6	3	8
Banking sector					
US banks	117.6	0.0	3.8	0	-2
JPM	87.6	-0.1	3.6	-1	1
Cit	59.4	0.0	2.9	0	-3
BoA	23.5	-0.5	3.6	1	3
MS	43.6	0.2	4.3	2	0
GS	226.5	0.3	4.4	1	7
EZ banks	111.5	0.1	7.0	6	6
BNP	64.8	0.3	4.5	4	3
Credit Agricole	13.7	0.6	9.0	8	11
Deutsche Bank	16.5	-1.0	6.2	2	1
ING	14.9	0.0	5.2	7	8
Intesa	2.7	0.1	6.4	6	5
SG	59.2	0.9	8.5	6	4
Unicredit	14.9	-0.1	9.5	5	6
UK banks	87.6	-0.6	5.0	0	0
HSC	636.5	-0.7	2.0	-3	5
RIS	255.4	-4.7	10.7	10	13
Barclays	212.3	-5.2	2.1	-7	-10
Lloyds	69.2	0.3	7.5	4	7
Large Spanish banks	89.6	0.4	4.5	3	15
Santander	6.0	0.8	5.6	5	17
BBVA	7.3	-1.4	3.6	2	13
Medium Spanish banks	82.3	1.0	3.7	2	13
Caixabank	4.2	3.3	6.2	5	27
Populr	0.6	0.2	-4.7	-30	-35
Sabadell	1.8	-0.2	5.2	3	28
Banqueparibas	0.1	0.1	1.0	4	7
Banika	1.1	1.5	5.2	5	9
Currencies (% red for currency depreciation)	level	Daily	Weekly	Monthly	Year
Developed					
EURUSD	1.09	0.2	1.6	-1.2	4
GBPUSD	1.29	0.2	0.9	4.0	5
USDJPY	111.43	-0.2	-2.1	0.4	-5
DXY	99.04	0.0	-0.9	1.0	4
Emerging					
USDARS (Argentina)	15.42	0.0	0.3	0.1	4
USDBRL (Brazil)	3.19	-0.2	-1.4	-2.2	1
USDCLP (Chile)	666.61	-0.4	-2.2	-0.5	1
USDCOR (Colombia)	2947	-0.3	-2.4	0.2	1
USDMXN (Mexico)	18.94	0.5	-0.7	-1.3	12
USDPEN (Peru)	3.25	0.0	-0.2	0.1	4
LACI	64.99	0.0	-1.2	-1.5	5
USDPOLN (Poland)	3.88	0.0	2.4	1.2	7
USDRUB (Russia)	57.02	0.0	-0.6	-0.7	6
USDTRY (Turkey)	3.55	0.2	2.4	2.5	1
USDCNY (China)	6.99	0.1	0.1	0.0	1
USDINR (India)	64.25	-0.1	0.6	1.0	6
USDIDR (Indonesia)	13,329	-0.1	-0.1	-0.1	1
ADXY	105.4	-0.1	0.0	-0.2	2
Commodities (%)	level	Daily	Weekly	Monthly	Year
Brent					
Brent	51.5	0.2	-0.8	-2	-9
WTI	49	-0.1	-1.4	-1	-6
Copper	260	0.6	2.4	-3	2
Gold	1267	0.2	-1.3	1	9
S&P Spot commodity *	380	-0.8	-0.7	-1	-4
S&P Brent Spot *	441	-1.1	-1.2	-1	-8
S&P Metals Spot *	319	-0.9	0.6	-4	5
S&P Agricultural *	287	0.2	-0.1	-1	-4

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Chile	72	-1	-6	0	-9
Colombia	127	-3	-8	-6	-36
Mexico	120	-6	-10	-12	-36
Peru	98	-1	-7	-5	-10
Venezuela	3,377	28	113	164	528
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Euribor 3m	-0.33	0.00	0.0	0.0	0.0
Euribor 12m	-0.12	0.00	0.0	0.0	0.0
Libor 3m	1.17	0.00	0.0	0.0	0.2
Libor 12m	1.78	-0.01	0.0	0.0	0.1
EZ TED spread 3m	50.8	3.40	3.1	-10.2	-15.6
Stock markets (%)					
level	Daily	Weekly	Monthly	YTD	
Main indices					
S&P500	2,384	-0.2	1.5	1	5
Dow Jones	20,945	0.2	1.9	1	5
Nikkei	19,197	-0.3	3.1	0	-2
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IBEX	10,716	0.3	3.3	3	13
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MSCI Latam *	76,914	-0.5	0.7	-1	5
Bovespa (Brazil)	65,345	-1.0	2.5	0	6
Moodi	49,331	-0.2	0.7	1	6
MSCI EM Europe *	4,959	-0.7	3.5	1	-2
Poland	2,377	-0.2	5.0	7	19
Mircz (Russia)	7,017	0.3	3.7	0	-11
Ise 100 (Turkey)	94,655	0.4	2.4	6	24
MSCI EM Asia *	776	0.0	2.4	2	12
Shanghai Com (China)	3,155	0.1	0.6	-3	0
Jakarta (Indonesia)	5,685	-0.7	1.6	3	8
Banking sector					
US banks	117.6	0.0	3.8	0	-2
JPM	87.6	-0.1	3.6	-1	1
Citi	99.4	0.0	2.9	0	-3
BoA	23.5	-0.5	3.6	1	3
MS	43.6	0.2	4.3	2	0
GS	226.5	0.3	4.4	1	-7
EZ banks	111.5	0.1	7.0	6	6
BNP	64.8	-0.3	4.5	4	3
Credit Agricole	13.7	0.6	9.8	8	11
Deutsche Bank	16.5	-1.0	6.2	2	1
ING	14.9	0.0	5.2	7	8
Intesa	2.7	0.1	6.4	6	5
SG	50.2	0.9	8.5	6	4
Unicredit	14.9	-0.1	9.5	5	6
UK banks	87.6	-0.6	5.0	0	0
HSBC	636.5	-0.7	2.0	-3	-5
RBS	265.4	4.7	10.7	10	13
Barclays	212.3	-5.2	2.1	-7	-10
Lloyds	69.2	0.3	7.5	4	7
Large Spanish banks	89.6	-0.4	4.5	3	15
Santander	6.0	0.8	5.6	5	17
BBVA	7.3	-1.4	3.6	2	13
Medium Spanish banks	22.3	1.0	3.7	2	13
Cabobank	4.2	3.3	6.2	5	27
Popular	0.6	0.2	-4.7	-30	-35
Sabadell	1.8	-0.2	5.2	3	28
Bankinter	0.3	-0.1	1.0	4	7
Bankia	1.1	1.5	5.2	5	9
Currencies (% red for currency depreciation)					
Developed	level	Daily	Weekly	Monthly	Year
EURUSD	1.09	0.2	1.6	1.2	4
GBPUSD	1.29	0.2	0.9	4.0	5
USDJPY	111.43	-0.2	-2.1	0.4	-5
DKY	99.04	0.0	0.9	1.0	4
Emerging					
USDARS (Argentina)	15.42	0.0	0.3	0.1	4
USD BRL (Brazil)	3.19	-0.2	-1.4	-2.2	1
USD CUP (Cuba)	666.61	-0.4	-2.2	-0.5	1
USDCOP (Colombia)	294.7	0.9	2.4	2.1	1
USDMXN (Mexico)	18.94	0.5	-0.7	-1.3	12
USD PEN (Peru)	3.25	0.0	-0.2	0.1	4
LACI	64.99	0.0	-1.2	-1.5	5
USD PLN (Poland)	3.88	0.0	2.4	1.2	7
USD RUB (Russia)	57.02	0.0	0.6	0.7	6
USD TRY (Turkey)	3.55	0.2	2.4	2.5	1
USDCNY (China)	6.89	0.1	-0.1	0.0	1
USD INR (India)	64.25	-0.1	0.6	1.0	6
USD IDR (Indonesia)	13,329	-0.1	-0.1	0.1	1
ADXY	105.4	-0.1	0.0	-0.2	2
Commodities (%)					
level	Daily	Weekly	Monthly	Year	
Brent	51.5	0.2	-0.8	-2	-9
WTX	49	-0.1	-1.4	-1	-8
Copper	260	0.6	2.4	-3	2
Gold	1267	0.2	-1.3	1	9
S&P Spot commodity *	380	-0.8	-0.7	-1	-4
S&P Brent Spot *	441	-1.1	-1.2	-1	8
S&P Metals Spot *	319	-0.9	0.6	-4	5
S&P Agricultural *	287	0.2	-0.1	-1	-4

Source: Bloomberg, Datastream and Haver

* With one day delay

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