

# Market Comment | Fed will start to shrink its balance sheet in October

Global Financial Markets Unit  
21 Sep 2017

- **As we expected, the FOMC maintained the Fed funds rate at 1%-1.25% and announced the start of the balance sheet normalization process in October.** The median forecasts on inflation edged down slightly. The Fed's interest projection (Dot Plot) showed few changes, the median forecast for long-term interest rates inching down. Nonetheless, in the press conference Chair Yellen suggested an additional rate hike this year (December) ([see](#)). After yesterday's **FOMC meeting futures on the Fed fund priced in a 61% probability of a rate hike in December 2016.**
- The **USD strengthened by 0.8% following the meeting.** Regarding the EUR, it broke through the US\$1.19 level right after the meeting, but trimmed losses today, returning to levels above US\$1.19 on the back of positive preliminary EZ consumer confidence figures for September ([see](#)). Apart from this, the euro seems relatively resilient, as the FOMC decision relieves pressure on the ECB to calibrate the APP. Against this backdrop, EM currencies depreciated slightly across the board on the back of increasing expectations of a Fed rate hike this year. However, the increase in oil prices and the limited impact of the FOMC's decision on US yields provided some support.
- **US Treasury yields rose moderately after the FOMC decision as the Fed's rate expectations remained unchanged,** but showing a limited impact, and slightly pushed up European sovereign yields during today's session, especially among peripherals. On the other hand, the US yield curve flattened as the Fed showed a lower long-term forecast for interest rates.
- Share prices showed a mixed performance today. In **EZ stocks prices rose**, led by the financial sector, recovering some ground after recent losses, whereas in the **US share prices remained on a slightly downward trend**, following yesterday's monetary policy statement by the Fed, which was perceived as hawkish ([see](#)).
- The **BoJ left its monetary policy unchanged** ([see](#)). Nonetheless, there was a dovish surprise as one member voted to change monetary policy to make it more accommodative so that the bank could reach its inflation target. The **JPY was lower as divergence between the BoJ and the Fed widened further.**
- The **CNY depreciated slightly after S&P's rating agency revised China's credit rating down to A+ from AA-**. Little market reaction was perceived ([see](#)). At the same time, the OECD raised its forecast for China's economic growth to 6.8% in 2017, citing higher infrastructure investment ([see](#)).

Update 17.45 CET 21 September, 2017  
Table 1

Debt markets (% 10Y, % changes in bp)					
Developed Markets	level	Daily	Weekly	Monthly	YTD
US (2-yr)	1.43	-0.8	6.9	11	22
US	2.26	-1.1	7.2	4	-18
GER (2-yr)	-0.68	1.3	4.0	4	10
Germany	0.46	1.2	4.2	6	10
France	0.74	0.9	3.8	3	-7
Spain	1.62	3.9	1.9	-5	5
Italy	2.11	3.6	4.8	1	24
Portugal	2.43	4.7	-38.4	-35	-175
Greece	5.58	0.4	16.2	1	-131
Japan (2-yr)	-0.13	-0.5	0.0	0	7
Japan	0.04	-1.0	-0.3	-3	-3
Emerging Markets	level	Daily	Weekly	Monthly	YTD
Brazil	9.62	-7.2	-16.4	-53	-179
Chile	4.33	-0.8	0.3	-1	1
Colombia	6.50	1.1	-4.2	-27	-59
Mexico	6.82	-1.5	2.1	1	-82
Peru	4.88	0.1	-17.9	-16	-159
Poland	3.37	5.1	14.6	4	-34
Russia	7.67	3.4	5.1	-22	-77
Turkey	10.65	8.0	28.0	30	-35
India	6.68	10.0	8.7	14	30
Indonesia	6.45	0.0	-9.1	43	-140
Country risk (bp, changes in bp)					
Developed Markets	level	Daily	Weekly	Monthly	YTD
10-yr sovereign spread vs Germany					
France	28	-0.2	-0.3	-2	-18
Italy	165	2.4	0.6	-5	14
Portugal	198	3.5	-42.6	-40	-157
Spain	117	2.7	-2.3	-13	-11
2-yr sovereign spread vs Germany					
France	21	-1.2	-1.3	-2	10
Italy	46	-1.7	-7.6	-10	-15
Portugal	67	-0.5	-4.4	-11	-80
Spain	39	1.6	-3.2	1	-9
Emerging Markets	level	Daily	Weekly	Monthly	YTD
5-yr sovereign CDS *					
Brazil	200	22.2	21	-3	-72
Chile	61	8.5	8	-2	-22
Colombia	130	18.9	17	-1	-33
Mexico	116	16.3	17	7	-41
Peru	86	14.2	16	8	-22
Venezuela	6.552	124.3	445	353	2646
Poland	57	1.7	2	-1	-16
Russia	150	15.0	13	1	-27
Turkey	183	18.4	21	7	-89
China	58	5.6	1	-8	-58
India	82	4.1	3	-4	-45
Indonesia	100	8.6	4	-11	-56
Risk indicators					
Volatility indicators (%)	level	Daily	Weekly	Monthly	YTD
VIX	10	0.2	16	114	-2
VSTOXX	11	-5.1	-9	-32	-5
EM EFT volatility index	15	-0.5	7	9	-24
Dollar/euro volatility	7	-3.4	-5	-10	-30
EM FX volatility index	8	-0.3	-1	5	-31
Credit spread (BAA) (bps)	208	1.1	-4	-3	-19
US bonds volatility index	49	-1.4	-3	-4	-36
Banking CDS (bps) *	level	Daily	Weekly	Monthly	YTD
US	56	4.9	2	-9	-16
EZ	50	3.3	-1	-7	-58
UK	46	0.1	-1	5	-44
Large Spanish	50	3.9	2	-6	-67
Medium Spanish	83	1.4	-1	-8	-68
Corporate CDS (bps) *	level	Daily	Weekly	Monthly	YTD
US Non-financial	150	4.9	2	-3	-16
EZ Non-financial	73	3.3	-1	-7	-58
UK Non-financial	106	4.2	7	-4	-15
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
Euribor 12m	-0.17	0.00	0.0	0.0	-0.1
Libor 3m	1.32	0.00	0.0	0.0	0.3
Libor 12m	1.75	0.00	0.0	0.0	0.1
Stock markets (%)					
level	Daily	Weekly	Monthly	YTD	
Main indices					
S&P500	2,505	-0.1	0.4	2	10
Dow Jones	22,390	-0.1	0.8	2	12
Nikkei	20,347	0.2	2.7	5	4
FTSE 100	7,267	-0.1	-0.4	-2	1
EuroStoxx 50	3,542	0.5	0.4	3	7
BSE	10,302	0.1	-0.6	-1	9
DAX	12,607	0.3	0.5	3	9
CAC	5,273	0.6	0.9	3	8
MIB	22,509	0.7	1.0	4	15
ASE Athens	766	1.1	-3.2	-8	16
MSCI Latam *	85,728	0.1	1.1	6	17
Ibovespa (Brazil)	75,554	-0.6	1.2	8	23
Bovespa	50,289	0.1	0.4	-2	8
MSCI EM Europe *	5,170	0.4	-0.7	3	2
Poland	2,469	-1.2	-1.5	3	23
Moscú (Russia)	2,061	0.2	0.4	6	9
Ise 100 (Turkey)	104,001	-1.3	-3.9	-4	37
MSCI EM Asia *	891	0.0	1.5	4	28
Shanghai Com (China)	3,358	-0.2	-0.4	2	6
Jakarta (Indonesia)	5,907	0.1	-0.0	1	12
Banking sector					
level	Daily	Weekly	Monthly	YTD	
US banks					
JPM	129.0	0.4	3.2	5	8
Cit	95.1	0.6	4.6	4	9
Ch	71.7	0.4	3.6	7	17
BoA	25.1	0.3	3.7	5	10
MS	48.0	0.2	3.4	5	10
GS	231.0	0.5	1.8	3	9
EZ banks					
BNP	115.0	1.8	0.4	2	10
BNP	66.9	1.3	0.6	3	7
Crédit Agricole	15.2	2.0	-0.5	0	24
Deutsche Bank	13.8	2.6	-0.9	1	-15
ING	15.4	1.4	0.6	2	11
Intesa	3.0	1.3	1.5	3	17
SG	48.9	2.4	0.3	4	1
Unicredit	17.9	2.4	0.9	2	27
UK banks					
HSC	88.0	1.5	1.1	0	0
HSC	722.7	0.0	0.3	3	8
Barclays	260.3	1.6	2.8	2	11
Barclays	190.7	2.6	0.4	-1	-19
Lloyds	67.5	2.7	1.6	4	4
Large Spanish banks					
Santander	89.4	1.7	1.0	2	15
Santander	5.7	1.4	0.8	4	13
BBVA	7.5	2.0	1.1	0	16
Medium Spanish banks					
Cajabank	78.1	1.0	-0.8	-4	7
Cajabank	4.2	2.3	-1.8	-3	30
Sabadell	1.7	0.1	-2.0	-7	26
Bankinter	7.9	1.0	-0.5	-2	4
Bankia	4.0	0.9	1.1	-3	-2
Currencies (% red for currency depreciation)					
Developed	level	Daily	Weekly	Monthly	Year
EURUSD					
EURUSD	1.20	0.5	0.3	1.6	14
GBPUSD	1.36	0.6	1.3	5.8	10
USDJPY	112.32	-0.1	-1.9	2.5	-4
DKK	92.20	-0.3	0.1	1.4	10
Emerging					
USDARS (Argentina)	17.28	-0.5	-1.7	-0.4	-7
USD BRL (Brazil)	3.14	-0.1	-0.5	0.8	3
USDCUP (Cuba)	623.90	-0.5	0.1	2.7	7
USDCOP (Colombia)	2915	-0.8	-0.5	2.3	2
USDMXN (Mexico)	17.83	-0.4	-0.9	-1.0	17
USDPEN (Peru)	3.25	0.0	-0.3	-0.4	4
LKR	65.47	0.0	-1.0	0.4	8
USDPLN (Poland)	3.58	0.6	0.4	1.6	14
USD RUB (Russia)	57.94	0.4	-0.8	1.9	4
USDTRY (Turkey)	3.50	0.2	-1.8	0.0	2
USDCNY (China)	6.59	-0.2	-0.5	1.1	5
USDINR (India)	64.80	-0.8	-1.1	-1.1	5
USDIDR (Indonesia)	13,339	-0.4	-0.7	0.0	1
ADNY	108.0	-0.1	-0.3	0.6	5
Commodities (%)					
level	Daily	Weekly	Monthly	Year	
Brent					
Brent	56.2	-0.1	1.3	8	0
WTI	51	0.3	1.4	6	5
Copper	293	-0.7	-0.3	-2	15
Gold	1294	-0.5	-2.7	1	11
S&P Spot commodity *	399	1.3	1.1	6	1
S&P Brent Spot *	476	1.9	1.3	8	-1
S&P Metals Spot *	366	1.1	2.5	1	20
S&P Agricultural *	283	0.9	-0.2	3	-6



Debt markets (10Y, %, changes in bp)					
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Peru	4.88	0.1	-17.9	-36	-159
Poland	3.37	5.1	14.6	4	-34
Russia	7.67	3.4	5.1	-22	-77
Turkey	10.65	8.0	20.0	30	-35
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Indonesia	6.45	0.0	-9.1	-43	-140
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Russia	150	15.0	13	1	-27
Turkey	183	18.4	21	7	-89
China	58	5.6	1	-8	-58
India	82	4.1	3	-4	-45
Indonesia	100	8.6	4	-11	-56
Risk indicators					
level	Daily	Weekly	Monthly	YTD	
<b>Volatility indicators (%)</b>					
VIX	10	0.2	-6	-11	-2
VSTOXX	11	-5.1	-9	-32	-5
EM EFT volatility Index	15	-0.5	7	-9	-24
Dollar/euro volatility	7	-3.4	-5	-10	-30
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Banking by CDS (bps) *					
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Euribor 3m	-0.33	0.00	0.0	0.0	0.0
<b>Euribor 12m</b>	-0.17	0.00	0.0	0.0	-0.1
Libor 3m	1.32	0.00	0.0	0.0	0.3
Libor 12m	1.75	0.00	0.0	0.0	0.1
Stock markets (%)					
level	Daily	Weekly	Monthly	YTD	
<b>Main indices</b>					
S&P500	2,505	-0.1	0.4	2	10
Dow Jones	22,390	-0.1	0.8	2	12
Nikkei	20,347	0.2	2.7	5	4
FTSE 100	7,267	-0.1	-0.4	-2	1
<b>EuroStoxx 50</b>	3,542	-0.5	0.4	-3	7
IBEX	10,302	0.1	-0.6	-1	9
DAX	12,607	0.3	0.5	3	9
CAC	5,273	0.6	0.9	3	8
MIIB	22,569	0.7	1.0	4	15
ASE Athens	766	1.1	-3.2	-8	16
<b>MSCI Latam *</b>	85,728	0.1	1.1	6	17
Ibovespa (Brazil)	75,554	-0.8	1.2	8	23
Merck	50,289	-0.1	0.4	2	8
<b>MSCI EM Europe *</b>	5,170	0.4	-0.7	3	2
Poland	2,469	-1.2	-1.5	3	23
Micex (Russia)	2,061	-0.2	0.4	6	9
Isr 100 (Turkey)	104,001	-1.3	-3.9	-4	37
<b>MSCI EM Asia *</b>	891	0.0	1.5	4	28
Shanghai Com (China)	3,358	-0.2	-0.4	2	6
Jakarta (Indonesia)	5,907	0.1	1.0	1	12
Banking sector					
level	Daily	Weekly	Monthly	YTD	
<b>US banks</b>					
JPM	129.0	0.4	3.2	5	8
CB	95.1	0.6	4.6	4	9
BoA	71.7	0.4	3.6	7	17
MS	25.1	0.3	3.7	5	10
GS	48.0	0.2	3.4	5	10
WFC	231.0	0.5	1.8	3	-5
<b>EZ banks</b>	115.9	1.8	0.4	2	10
BNP	66.9	1.3	0.6	3	7
Credit Agricole	15.2	2.0	-0.5	0	24
Deutsche Bank	13.9	2.6	-0.9	1	-15
ING	15.4	1.4	0.6	2	11
Intesa	3.0	1.3	1.5	3	17
SG	48.9	2.4	0.3	4	1
Unicredit	17.9	2.4	0.9	2	27
<b>UK banks</b>	88.0	1.5	1.1	0	0
HSBC	722.7	0.0	0.3	-3	8
RBS	260.3	1.6	2.8	-2	11
Barclays	190.7	2.6	0.4	-1	-19
Lloyds	67.5	2.7	1.6	4	4
<b>Large Spanish banks</b>	89.4	1.7	1.0	2	15
Santander	5.7	1.4	0.8	4	13
<b>BBVA</b>	7.5	2.0	1.1	0	16
<b>Medium Spanish banks</b>	78.1	1.0	-0.8	-4	7
CaixaBank	4.2	2.3	-1.8	-3	30
Sabadell	1.7	0.1	2.0	-7	26
Bankinter	7.9	1.0	-0.5	-2	4
Bankia	4.0	0.9	1.1	-3	2
Currencies (% , red for currency depreciation)					
Developed	level	Daily	Weekly	Monthly	Year
<b>EURUSD</b>					
EURUSD	1.20	0.5	0.3	1.6	14
GBPUSD	1.36	0.6	1.3	5.8	10
USD JPY	112.32	-0.1	-1.9	2.5	-4
USD AUD	92.20	-0.3	0.3	1.4	10
Emerging					
level	Daily	Weekly	Monthly	Year	
USDARS (Argentina)	17.28	-0.5	-1.7	-0.4	-7
USD BRL (Brazil)	3.14	-0.1	-0.5	0.8	3
USD COP (Colombia)	623.90	-0.5	0.1	2.7	7
USD CUP (Cuba)	2915	-0.8	-0.5	2.3	2
USD MXN (Mexico)	17.83	-0.4	-0.9	-1.0	17
USD PEN (Peru)	3.25	0.0	-0.3	-0.4	4
LACI	66.47	0.0	-1.0	0.4	8
USD PLN (Poland)	3.58	0.6	0.4	1.6	14
USD RUB (Russia)	57.94	0.4	-0.8	1.9	4
USD TRY (Turkey)	3.50	0.2	-1.8	0.0	-2
USD CNY (China)	6.59	-0.2	-0.5	1.1	5
USD INR (India)	64.80	-0.8	-1.1	-1.1	5
USD IDR (Indonesia)	13,339	-0.4	-0.7	0.0	1
ADXY	100.0	-0.1	-0.3	0.6	5
Commodities (%)					
level	Daily	Weekly	Monthly	Year	
<b>Brent</b>					
Brent	56.2	-0.1	1.3	8	0
WTI	51	0.3	1.4	6	5
Copper	293	-0.7	-0.3	-2	15
Gold	1294	-0.5	-2.7	1	11
S&P Spot commodity *	399	1.3	1.1	6	1
S&P Brent Spot *	476	1.9	1.3	8	1
S&P Metals Spot *	366	1.1	2.5	1	20
S&P Agricultural *	283	0.9	-0.2	3	6

Source: Bloomberg, Datastream and Haver

\* With one day delay

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- After yesterday's widespread positive mood after easing concerns over North Korea, **today financial markets were broadly steady**, with little variation among stock and bond prices.
- The **USD continued in its recent upward trend while the EUR continued eroding its recent high level**, as factors recently weighing on USD strength started to blur: geopolitical tensions, political uncertainty and hurricane effects, among others.
- **US Treasury yields inched up after the release of PPI inflation**, which rose on the back of **surging gasoline prices due to the effects of hurricanes** ([see](#)). Financial markets will be closely watching the developments of US inflation (tomorrow), a key variable for the Fed to design the path of US interest rate hikes onwards.
- Stock prices inched up in Europe, led by industrials and the finance sector. Meanwhile, US indices remained hovering around their highest levels despite the disappointment about the release date of the new Apple product, which affected suppliers ([see](#))
- **Oil prices increased after the IEA released its report** ([see](#)) pointing to lower inventories due to higher demand. Moreover, today's release of gasoline inventories, which dropped significantly more than expected, supported the increase in oil prices. EM currencies also benefited from the higher oil prices.