FINANCIAL MARKET UPDATE June 2006

International Capital Markets Department
Global Markets Analysis Division

Data as of June 9, 2006, or as noted

*Since the release of the April 2006 Global Financial Stability Report (*GFSR*), global financial markets have experienced increased volatility and a sharp correction in the price of riskier assets. The fall in investor risk appetite is a normal and healthy market adjustment to the rising perceived risks at this stage in the global financial and economic cycle, and to the withdrawal of liquidity as global monetary policies normalize.*

Rising inflationary pressures have prompted expectations of a synchronized tightening of global monetary policies. The increased cost of funding leveraged trades and the perceived downside risks for growth triggered a wave of global equities selling from multiyear highs. Market attention was also refocused on the risks of global economic imbalances by the G-7 and IMFC communiqués, with volatilities rising in currency markets. These cyclical challenges and the accompanying monetary policy response have had a powerful impact on investor positioning in risky asset markets, such as carry trade currencies and equities, especially in emerging markets.

However, corrections in mature markets do not appear to signal the beginning of a protracted downturn in the global economy and financial markets. Although equity prices have declined abruptly, valuation measures do not suggest a serious worry that equities are overvalued. The still broadening outlook for the global economy suggests earnings are unlikely to erode sharply. Corporate credit spreads have widened only very moderately, suggesting that healthy balance sheets still provide firm underpinnings to corporate markets.

The sell-off in emerging markets reflects a rise in risk premiums, but not a reassessment of emerging market fundamentals. Emerging market assets with significant valuation gains and local markets with concentrated positions of foreign investors have corrected strongly. However, external debt markets show little concern about the possibility of a sovereign credit distress event. This resilience reflects improved fiscal and current account balances and the favorable supply and demand balance facing emerging market borrowers.

With the correction still ongoing, a full assessment of the implications for emerging markets is not yet possible. Thus far, however, the correction is not expected to have a significant economic impact. Following a significant appreciation of emerging market currencies, especially in the Latin American region, depreciation over the past month relieves concerns over real exchange rate appreciations. The impact of equity market price declines need to be seen against their prior rise, and in most countries, expectations for inflation remain unaffected. Nevertheless, some emerging market countries that are more vulnerable to the external environment have been harder hit.

The Financial Market Update is an online bulletin that covers developments in both mature and emerging markets. It complements the IMF's *Global Financial Stability Report* (GFSR), a print publication that is published twice a year. This update covers developments through June 9, 2006.

Implications for Policies

Policymakers in both mature and emerging markets face renewed challenges in ensuring balanced global growth and financial stability. Central banks need to communicate their assessment of inflation risks and their resolve to contain inflation effectively to financial markets.

In this new environment, emerging market countries with macroeconomic imbalances and that rely heavily on external financing face a narrower margin for policy slippage. Emerging markets should continue to develop domestic capital markets and build a diversified local institutional investor base. Debt management policies need to be consistent with the capacity of local markets to absorb foreign inflows. Given the levels of reserve accumulation and prefinancing, further external borrowing can wait for market conditions to improve. Similarly, in local markets, the authorities can temporarily trim supply and, if needed, conduct secondary operations in support of market liquidity.

What Triggered the Market Correction?

An increase in risk aversion in global financial markets sparked a sharp correction of prices on riskier assets and a rise in volatility. The fall in risk appetite is a typical response to an increase in perceived risks at this stage in the global financial and economic cycle.

In recent weeks, investors and officials have grown more concerned that rising commodity prices, growing capacity utilization, and tightening labor markets could result in an acceleration of inflation in mature markets. In particular, recent developments suggest to some that rising energy and commodity prices, together with other price pressures, may be passing through to higher inflation (Figure 1). Labor markets in the United States have tightened, as payroll growth has driven unemployment rates down to five-year lows. Wage growth is now in line with the pace seen before the economic downturn in 2001 (Figure 2). To date, this has primarily remained a U.S. phenomenon, as labor markets in Japan and the eurozone have only more recently shown signs of recovery.

Figure 1. Commodity Price Developments
(December 31, 2005 = 100)

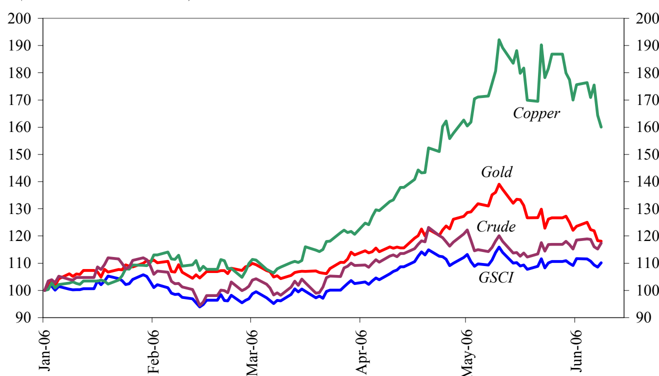
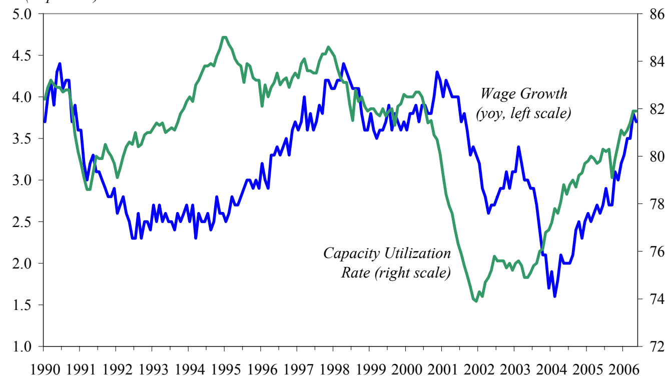
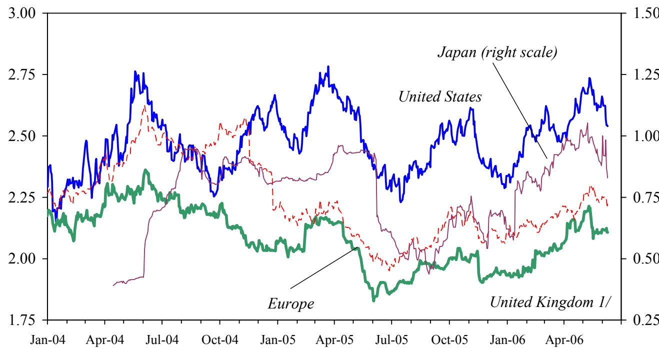


Figure 2. United States: Hourly Earnings Growth and Capacity Utilization Rate
(In percent)



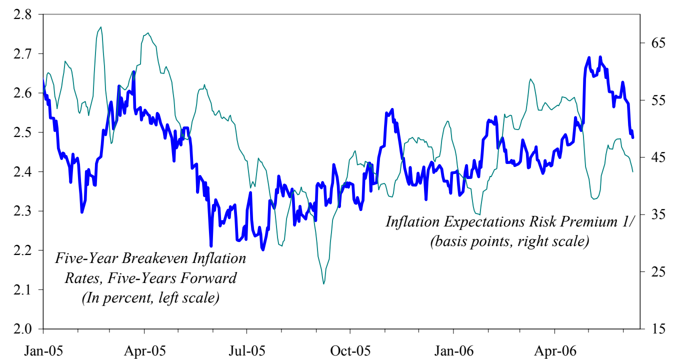
Overall, these developments have translated into a moderate rise in inflation expectations in the United States, while market-derived expectations of inflation have also risen somewhat in Europe (Figure 3). Between end-February and mid-May, long-run inflation expectations, as signaled by the rise in the inflation rate expected in five years' time (the 5-year, 5-year forward TIPS breakeven rate), increased to 2.67 percent (Figure 4). It is important to note, however, that term premiums for risks of more volatile inflation had not increased (spreads further along the breakeven inflation curve have changed little).

Figure 3. Breakeven Long-Term Inflation Rates
(In percent; nominal yields less inflation-indexed yields on ten-year benchmarks)



Sources: Bloomberg L.P.; and IMF staff estimates.
1/ Adjusted using a Bank of Engand estimate for the methodological differences between the RPI and CPI inflation.

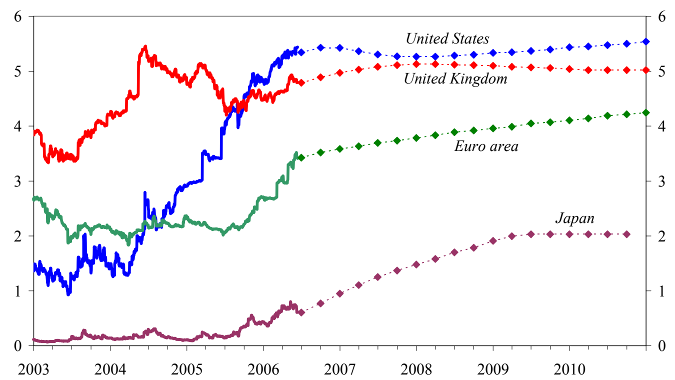
Figure 4. United States: Market Derived Inflation Expectations



Sources: Bloomberg L.P.; and IMF staff estimates.
1/ Defined as the ten-day moving average of the spread between five-year breakeven inflation rates, five-years forward and 10-year breakeven inflation rates, 10-years forward.

Concerns about inflationary pressures and a rise in inflationary expectations have prompted a more hawkish rhetoric by global central banks and a synchronized tightening of global monetary policies. With a further tightening in policies, perceived downside risks for growth triggered a wave of selling of global equities from multiyear highs.

Figure 5. Term Structure of Interest Rate Expectations
(In percent, 3-Month LIBOR Futures Strip)



Source: Bloomberg L.P.

Central banks in mature markets have confronted the threat of higher inflation resulting in a synchronized policy tightening. The timing, pace, and extent of this tightening has varied (Figure 5). The Federal Reserve has continued with its gradual tightening that started in 2004 and has recently sounded a more restrictive tone, raising expectations for further tightening, even as the real Fed Funds rate has now approached 2.7–3.0 percent, depending on the measure of core inflation used. The ECB hiked rates for a third time in June, bringing policy rates to 2.75 percent. The Bank of Japan (BoJ) has maintained its zero interest rate policy, but signaled its desire to raise rates in the coming months; in preparation, the BoJ has withdrawn much of its substantial liquidity support to the Japanese banking system. These increases in rates have been echoed in other central banks, including in some emerging markets, mainly in Asia.

The prospect of further tightening caused many investors to question their global growth projections on the basis that the recoveries in Europe and Japan, and ongoing growth in emerging markets, would find it difficult to endure a steeper-than-expected slowdown in the United States. Equity markets have been among the most sensitive to these changing perceptions. Japanese equities declined the most, as the Topix plunged nearly 15 percent during May and early June (Figure 6). European stocks followed, with the Eurofirst-300 off more than 9 percent since peaking in early May. By comparison, the S&P 500 outperformed, falling by less than 6 percent over the equivalent period. Until recently, investors viewed rising yields as driven by strong noninflationary growth, a favorable outcome for equities. More recently, however, declines in the S&P 500 have often coincided with declines in U.S. Treasury prices with the correlation between the two prices turning positive after several years of being negative (Figure 7).

Figure 6. Equity Market Performance
(Rebased, December 31, 2004 = 100)

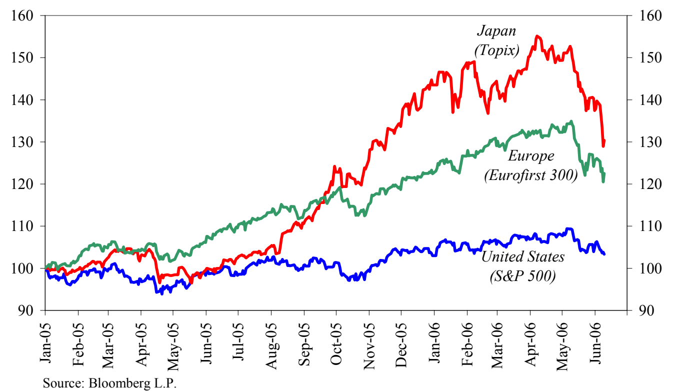
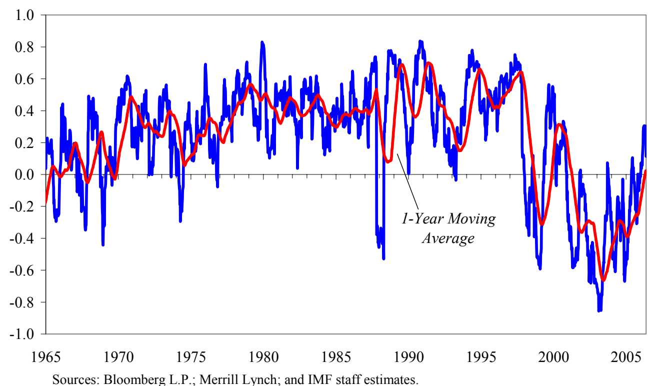


Figure 7. Price Correlations Between Treasuries and S&P 500
(26-Week rolling correlations)

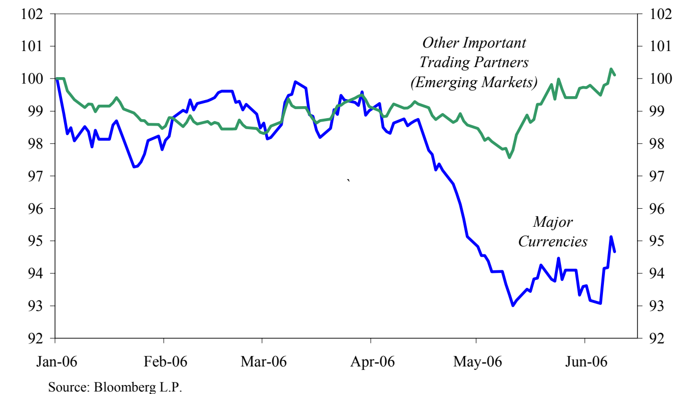


An additional factor contributing to a rise in volatility, particularly currencies, has been the renewed focus on global economic imbalances, following from the G-7 and IMFC communiqués.

Throughout 2005, the dollar found support from the Federal Reserve's tightening campaign. During this time, U.S. interest rates rose to one of the highest levels among the major industrialized economies. As the prospect of the Fed pausing has come into view and market participants have focused again on structural imbalances. In the wake of the G-7/IMFC communiqués issued in mid-April, the U.S. dollar has corrected more strongly, as the policy statements were seen as a signal that the G-7 was more likely to accommodate a depreciation of the dollar, and that currencies of countries with current account surpluses would rise as one element working to resolve global imbalances.

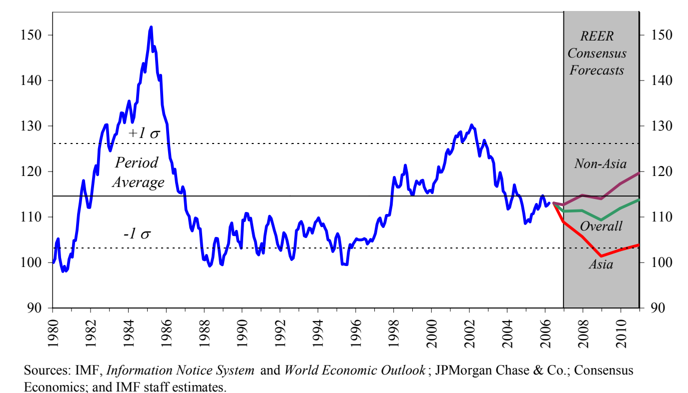
On a trade-weighted basis, the bulk of the dollar's adjustment has occurred against the major currencies, falling nearly 7 percent against this basket (Figure 8). In contrast, emerging market currencies have held fairly stable despite the bout of volatility and risk retrenchment. However, this is the result of a considerable divergence in currency performance among individual countries. Overall, the U.S. dollar has retraced the appreciation gains made during 2005.

Figure 8. Federal Reserve Trade-Weighted U.S. Dollar Index
(Rebased, December 31, 2005 = 100)



In the longer term, consensus opinion suggests that dollar adjustment will be limited and orderly, but with a marked differentiation of performance by region. The dollar's real effective exchange rate is expected to remain relatively stable across all major trading partners, but Asian currencies are expected to outperform over the medium-to-long term and non-Asian currencies are expected to weaken (Figure 9).

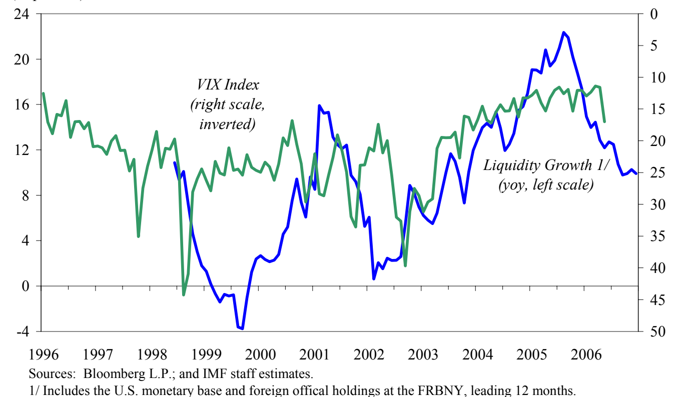
Figure 9. United States: Real Effective Exchange Rate
(January 1980 = 100)



These cyclical challenges and monetary policy response have had a powerful impact on leveraged positions in risky products, most notably in carry trade currencies.

The withdrawal of liquidity has altered the incentives investors face, and changed the perceptions of the balance of risks and rewards (Figure 10). Easy liquidity encouraged a wide array of risky investment strategies as lower funding costs reduced the opportunity cost of capital for leveraged investors. As rates have risen in the United States and Europe, and with a similar move expected in Japan, the appeal of carry strategies declined during the year as investors became increasingly concerned that economic fundamentals may be deteriorating in some of the more popular high-yield markets.[1] In

Figure 10. Liquidity Measure and Market Volatility
(In percent)

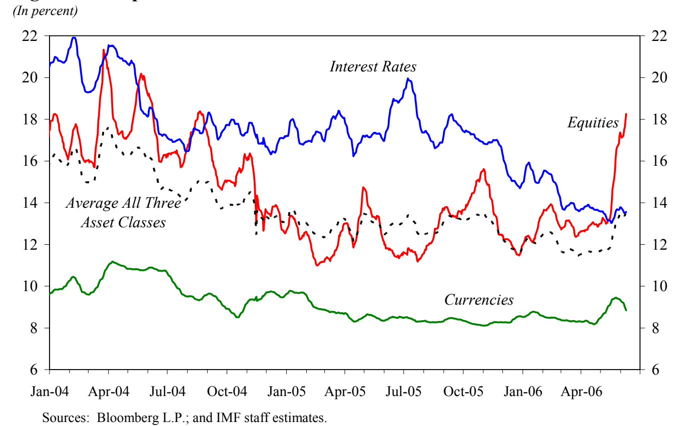


[1] Carry trades are strategies where an investor borrows funds in a currency with low interest rates and deposits them in a higher yielding currency, earning the interest differential. These strategies are particularly attractive when currency volatilities are low, as returns are dependent on the interest differential as well as any underlying currency trend; an unexpected increase in market volatility can result in an adverse currency movement that negates any rate advantage.

Iceland and New Zealand, where deposit yields were among the highest in the mature markets, investors began to question the sustainability of large and persistent current account deficits.

In line with the increase in risk perception, implied volatility as derived from options prices has risen across a wide variety of asset classes since the beginning of May, including in equity, fixed income, and currency markets (Figure 11). In an environment of higher volatility, more risky assets experienced a sharp correction as investors sought to reduce exposure to market price risks.[2] To some extent, therefore, the tightening of monetary policies marks a regime change in trading strategies, away from an emphasis on carry, toward fundamentals-driven "directional" positions.

Figure 11. Implied Volatilities
(In percent)

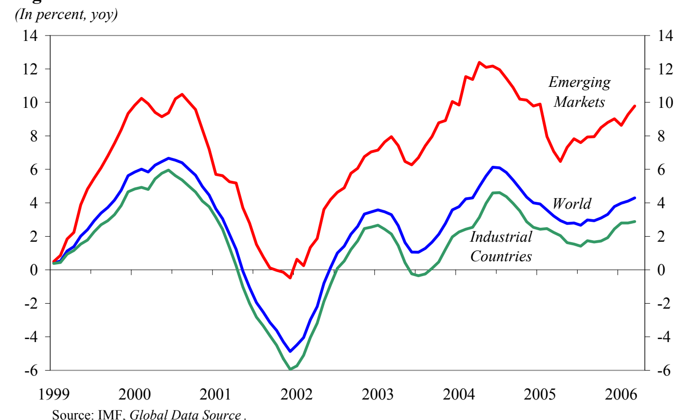


Sources: Bloomberg L.P.; and IMF staff estimates.

Are Mature Markets Signaling the Beginning of a Protracted Downturn in the Global Economy and Financial Markets?

Despite the sudden retraction of risk appetite in the last few weeks, the outlook for global growth remains robust (Figure 12). While growth in the United States is expected to moderate over the next several quarters, this is from an already-high level of activity. The recovery in Japan continues, and the recovery in the euro area is gaining traction. Equity valuations in mature markets are close to or below 15-year average levels (Figure 13), and spreads on corporate bonds have remained fairly stable during this period of market volatility, suggesting that investors do not believe corporates are facing a major deterioration in their business fundamentals (Figure 14).

Figure 12. Global Industrial Production Growth
(In percent, yoy)



Source: IMF, *Global Data Source*.

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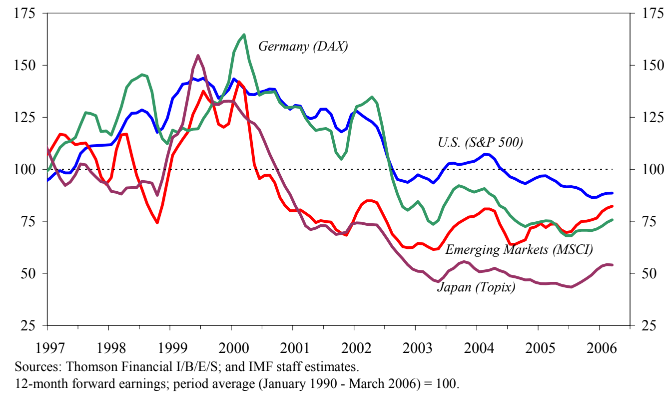
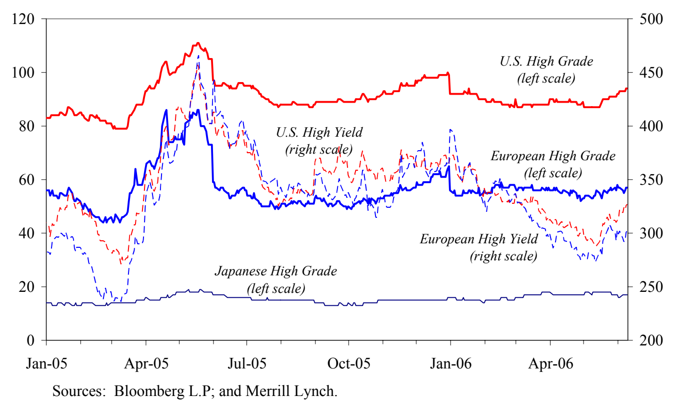
[2] These instruments are particularly sensitive to changes in sentiment, as price declines are magnified in a sell-off, and decreased market liquidity can lead to a more severe price response than would otherwise be the case. Moreover, the risk management techniques of financial institutions are often derived from estimates of market volatility and the comovement of financial prices. As volatility, either realized or implied, increases, these value-at-risk (VAR) models dictate a reallocation into safer assets. While these risk management techniques may be rational from the perspective of an individual institution, some risk remains that they can be destabilizing for the market as a whole, as VAR-driven portfolio reallocations can force an investor to sell into a falling market.

Figure 13. Global Equity Markets: Price-to-Earnings Ratio Indices
(3-month moving average)



Sources: Thomson Financial I/B/E/S; and IMF staff estimates.
12-month forward earnings; period average (January 1990 - March 2006) = 100.

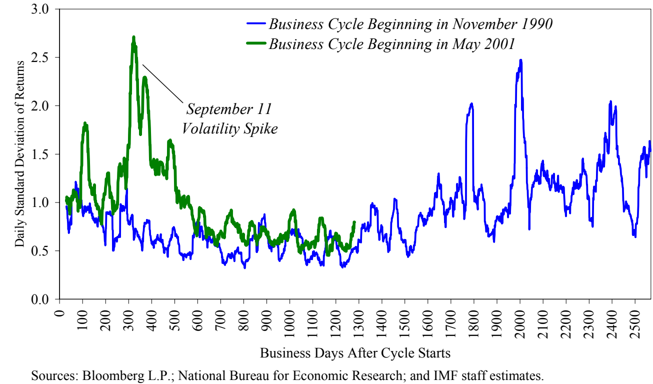
Figure 14. Corporate Spreads
(In basis points)



Sources: Bloomberg L.P; and Merrill Lynch.

Furthermore, the rise in volatility should be welcomed as it helps to reduce investor complacency and better position markets to deal with cyclical pressures that naturally surface as the global economic expansion matures. The correction comes toward the end of a prolonged period of accommodative monetary policy and highly liquid conditions in financial markets that promoted a global "search for yield." In sum, the rise in volatility is broadly consistent with this point in the cycle (Figure 15), but does not signal an impending downturn or significant risks to the economic or financial outlook.

Figure 15. Equity Market Volatility and the Business Cycle
(S&P 500 30-day rolling historical volatility, in percent)



Sources: Bloomberg L.P.; National Bureau for Economic Research; and IMF staff estimates.

Market Correction Extended to Emerging Market Assets

The rise in risk aversion that gripped global markets led to a sharp correction in emerging market asset prices, particularly in the more liquid local markets where foreign investor positioning was concentrated and in those markets that had appreciated the most.

The sell-off was concentrated in local emerging markets, particularly equities and currencies (Figures 16–19). Foreign exchange markets fell as more speculative investors, particularly hedge funds, rapidly unwound leveraged carry trades in the higher-yielding emerging market currencies. The speed and depth of the sell-off was exacerbated through the exercise of stop-losses in foreign exchange markets and other hedging strategies. Meanwhile, losses made in one market induced investors to reduce positions in other emerging market assets.[3]

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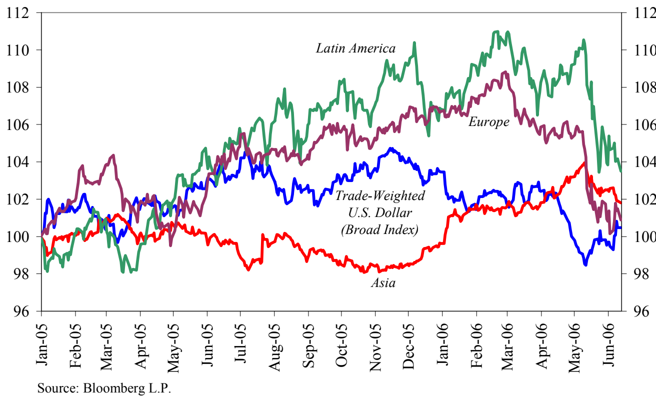
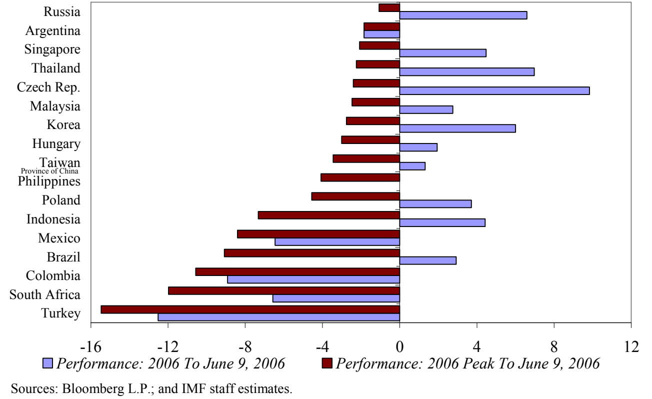
[3] For example, anecdotal evidence suggests that weakness in the Mexican peso was initially due to the unwinding of short-term positions by hedge funds funded in European currencies (most notably the Swiss franc) that took profits on Mexican interest rate positions to cover losses on positions in Turkey.

Figure 16. Emerging Market Currency Performance
(December 31, 2004 = 100)



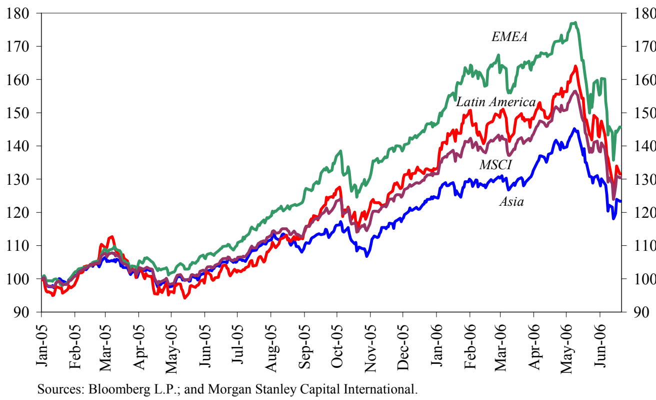
Source: Bloomberg L.P.

Figure 17. Emerging Market Currency Performance
(In percent)



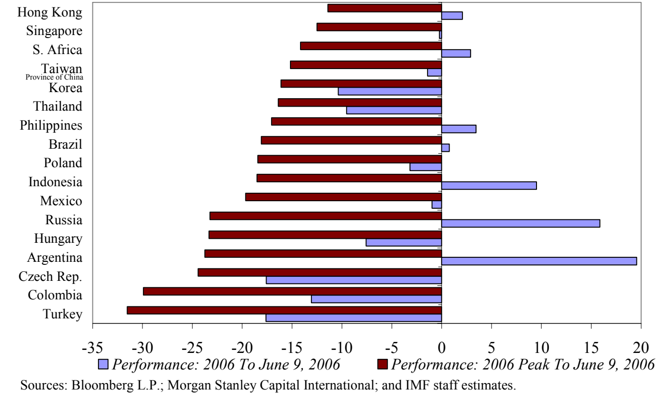
Sources: Bloomberg L.P.; and IMF staff estimates.

Figure 18. Emerging Markets: MSCI Equity Performance
(December 31, 2004 = 100, local currency performance)



Sources: Bloomberg L.P.; and Morgan Stanley Capital International.

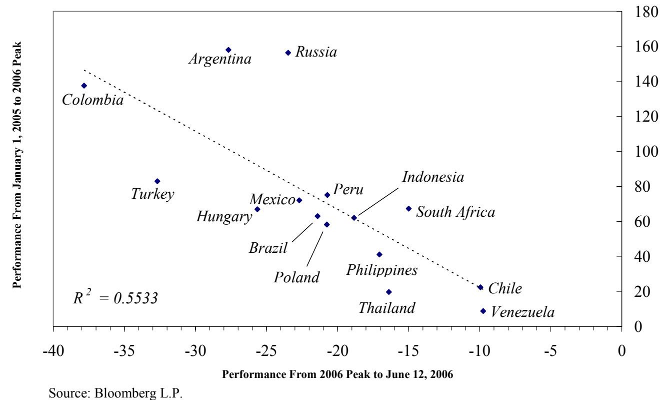
Figure 19. Emerging Markets: MSCI Equity Performance
(In percent, local currency returns)



Sources: Bloomberg L.P.; Morgan Stanley Capital International; and IMF staff estimates.

Equity markets that had seen the highest run-up in prices since 2005, generally the biggest and most liquid, experienced some of the deepest declines, including Brazil, Mexico, Russia, and Turkey (Figure 20). Less risky equity markets fared better. Middle East equity markets also experienced a sharp correction (see Box 1). Similarly, higher yielding currencies (Brazil, Turkey, and Indonesia) that were favored by investors for carry trades in the run-up to the correction sold off the most. These currencies saw significant nominal and real appreciation

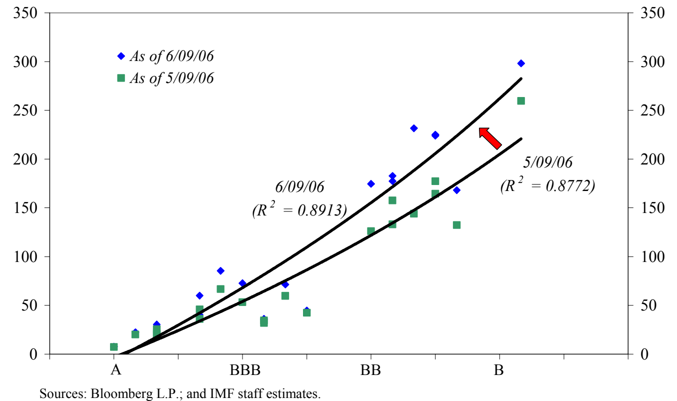
Figure 20. Emerging Markets: Relative Equity Performance
(In percent)



Source: Bloomberg L.P.

during 2005. The market for credit default swaps (CDSs) registered the increase in global risk aversion. Spreads generally widened (the CDS curve shifted up) with those of riskier credits widening the most (the curve steepened), as would be expected (Figure 21).[4]

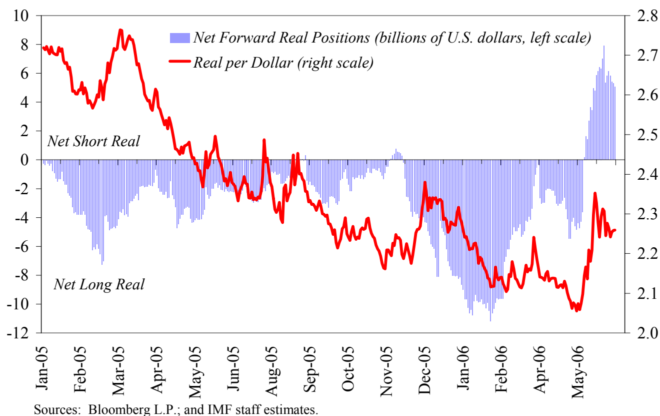
Figure 21. Credit Default Swap Spreads vs. Sovereign Credit Ratings
(In basis points)



Sources: Bloomberg L.P.; and IMF staff estimates.

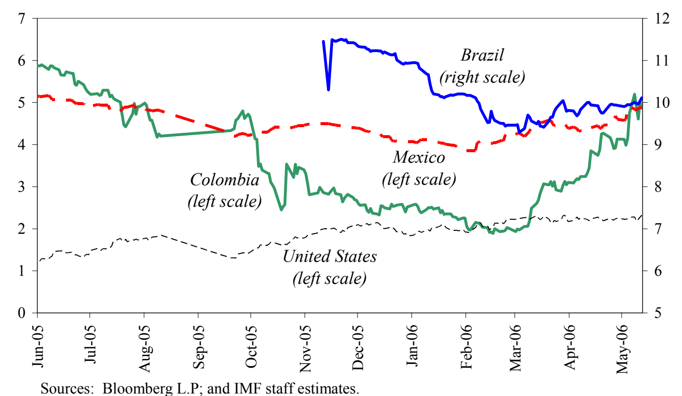
Sizeable inflows into local currency fixed-income markets also led to a build-up of "crowded trades" and subsequent sharp corrections and outflows (Figure 22). Foreign investors generally concentrated their positions in the few, better developed domestic interest rate and government securities markets. In these countries, including Brazil, Colombia, Mexico, and Turkey, foreigners maintained large positions in relation to the size of the local market. Flows into inflation-indexed local instruments in Latin American markets were particularly strong at the beginning of the year, bringing real yields down to record levels and illustrating the compression of risk premiums relative to U.S. real yields before the correction (Figure 23). These, in turn, were some of the local currency instruments that sold off the most in the initial stages of the recent correction.

Figure 22. Brazil: Foreign Exchange Market Positioning



Sources: Bloomberg L.P.; and IMF staff estimates.

Figure 23. Real Yields in Latin Local Currency Bonds
(In percent)



Sources: Bloomberg L.P; and IMF staff estimates.

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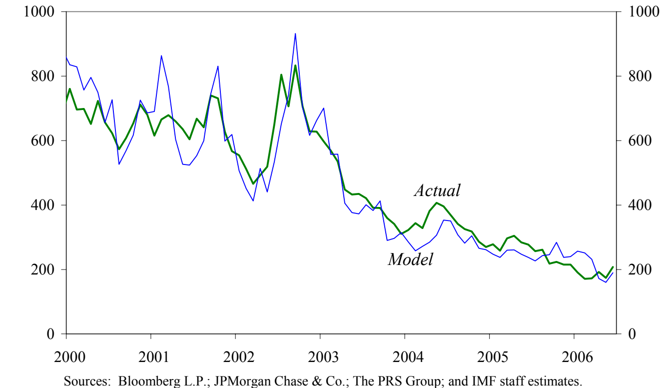
[4] Credit default swap contracts give the buyer of the contract the right to receive the full value of an underlying reference emerging market bond even if a default or credit event occurs. CDS can thus be seen as insurance against the possibility of a credit event. In practice, the value of such insurance rises and falls with the risk perception in the market so these instruments can be used as a hedge against a general retraction from risk. An interesting feature of the May 2006 correction is the growing use of the CDSs to hedge local currency positions. The growing liquidity and size of the CDS market has allowed investors to implement trades that would otherwise be costly, if not impossible, in the cash market. For example, CDSs allow traders to go short a credit (buying protection) without having to repo securities, and these shorts can be implemented across a number of credits, whereas in the cash market there are only a few liquid emerging market external bonds (the Brazil 2040, for example) where repo operations can be implemented easily.

Does the Correction Represent a Reassessment of Emerging Market Fundamentals?

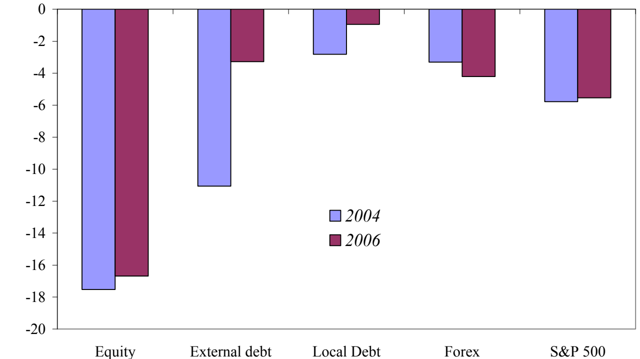
The pattern of the correction does not suggest a reassessment of emerging market fundamentals. Emerging market external bond spreads widened only moderately showing little concern about the possibility of a sovereign credit distress event. This illustrates investors' perception of continued solid fundamentals as well as robust demand for emerging market external debt from institutional and official investors. The model of emerging market spreads presented in the April 2006 GFSR predicts some spread widening in response to recent financial market volatility, but still tight spreads compared with historical levels on the basis of relatively strong emerging market fundamentals (Figure 24). A comparison of asset class performance with the May 2004 sell-off also suggests that the current correction does not reflect a reassessment of emerging market fundamentals. While the percentage price declines in equities and currencies in May 2006 broadly matched those of two years before, valuations have held at higher levels. Furthermore, the size of the correction of external debt markets in 2006 is much less despite more narrow spreads (Figure 25).

Figure 24. Aggregated EMBIG Spreads vs. Model Prediction
(In basis points)



Sources: Bloomberg L.P.; JPMorgan Chase & Co.; The PRS Group; and IMF staff estimates.

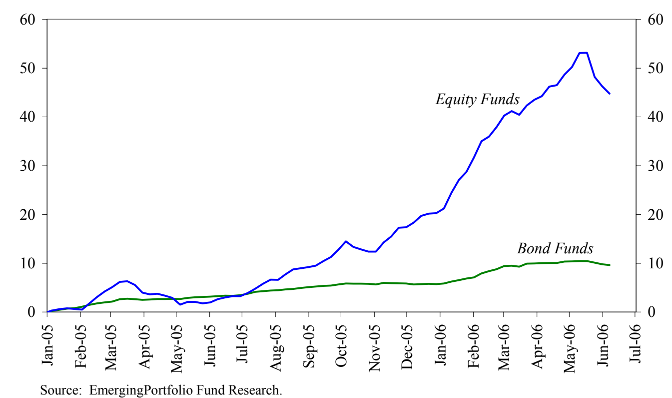
Figure 25. Comparison of Emerging Market Corrections
(In percent)



Sources: Bloomberg L.P.; JPMorgan Chase & Co.; Morgan Stanley Capital International; and IMF staff estimates.

Debt management policies and structural demand from foreign investors have also contributed to resilient external debt markets. On the supply side, the outstanding debt stock continues to be reduced through debt buybacks. Meanwhile, primary market bond issuance has been low in 2006 compared with previous years, reflecting prefinancing done in 2005, coupled with a policy shift by sovereign borrowers to rely more on domestic financing. On the demand side, market technicals remain supportive. Although dedicated emerging market bond funds have experienced outflows in May, these were still small in relation to the cumulative size of inflows into the asset class (Figure 26).

Figure 26. Cumulative Net Flows to Emerging Market Funds
(In billions of U.S. dollars, from January 2005)



Source: EmergingPortfolio Fund Research.

For a few countries, however, the sell-off has brought to light some lingering concerns about a possible deterioration in the fundamentals. This is particularly true of Turkey, where a large current account deficit and rising inflation led to concerns that the deterioration in the external

environment, particularly the depreciation of the exchange rate and pass through to inflation, made the task of achieving domestic targets more difficult. Furthermore, countries with current account deficits and overvalued equity markets could still face further outflows and financial turbulence. In these countries, the nominal exchange rate moved much more strongly than the average of other emerging markets: the new Turkish lira in particular weakened 22 percent against the U.S. dollar over the last three weeks of May, while the South African rand weakened almost 14 percent. This was in comparison with the average move of 3.5 percent for all emerging market currencies (as measured by changes in liquidity and trade-weighted exchange rate indices against the dollar).

Policy Responses and Implications

The policy response to market turbulence has aimed to maintain orderly markets and ensure stability of domestic financial and economic conditions. In Brazil, with yields rising sharply as foreign investors sought to sell positions in illiquid markets, the authorities stepped in quickly to stabilize the market, buying back inflation-linked debt and canceling scheduled debt auctions. In addition, the Treasury resumed offering floating-rate bonds and exchange-rate-linked interest rate swaps to help stabilize market demand. In Turkey, responding to the sharp exchange rate depreciation and the added threat to inflation, the central bank raised interest rates at an extraordinary meeting that underscored its commitment to achieving its inflation aims. Other countries, including India and South Africa, also tightened monetary conditions. In a move to increase the attractiveness of Colombia as a destination for investment inflows, the authorities removed restrictions which had required foreign investments to remain in the country for one year before the repatriation of profits was permitted.

Emerging market sovereigns are generally well placed to withstand the increase in volatility in external markets, having reduced their external financing needs through a combination of prefinancing and debt management. Over 75 percent of sovereign external debt issuance planned for 2006 was completed by the beginning of June (see the appendix). In addition, countries continued to take advantage of their high level of reserves to buy back external debt, further reducing near-term rollover needs and improving the debt profile. Brazil completed the repurchase of $11.7 billion in external debt through the end of May, including all of its Brady bonds. In addition, it concluded in early June a further repurchase auction for $1.1 billion in external bonds ranging in maturity from 2007 to 2030. Panama plans to exercise its option to buy back $360 million of Brady bonds in June. These actions follow repurchases or exchanges of external bonds made earlier in the year by Colombia, Mexico, Russia, and Venezuela.

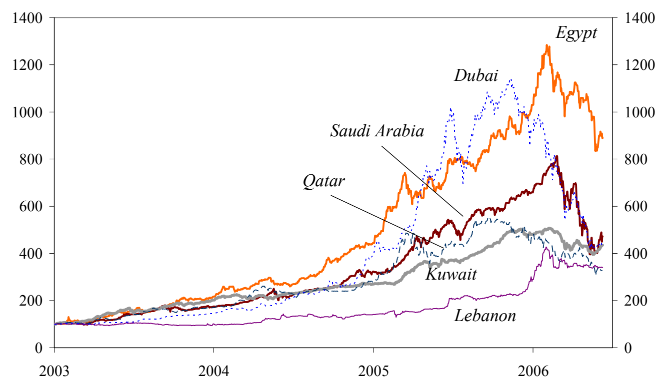
Against the backdrop of heightened risk aversion, investors are likely to differentiate more finely among emerging markets on the basis of fundamentals. Thus, emerging market countries with macroeconomic imbalances, that rely more heavily on external financing, will need to strengthen policies further. In addition, countries should continue developing local capital markets and building up a diversified local investor base, to provide a cushion for domestic markets against sudden changes in market sentiment. The recent correction in local markets also highlights the need to ensure that sovereign debt management policies are consistent with the capacity of local markets to absorb foreign investor inflows.

Box 1. Developments in GCC Equity Markets

After rising rapidly since 2003, the Gulf Cooperation Council (GCC) region equity markets have recently suffered sharp price declines. While the rise in markets during 2003-04 could be largely explained by improved earnings related to the surge in oil prices, the spectacular increase from the beginning of 2005 was mostly a result of unreasonable expectations of corporate profit growth and rapid growth in household credit, combined with structural factors that encouraged risk-seeking behavior among participants.

The market correction, which began in some markets in late 2005, was triggered also in Saudi Arabia and Kuwait when earnings reports for the fourth quarter of 2005, released in early 2006, were lower than the lofty expectations that had been raised by exceptionally high earnings earlier in 2005. Furthermore, there was a growing realization that high profits reported by some listed companies were a result of equity trading rather than operations. In addition, mounting issuance from a large number of initial public offerings (IPOs) across countries and delays in refunding oversubscribed amounts drained liquidity from the market. In Saudi Arabia, some regulatory measures and actions taken to limit speculation were introduced at a time when market confidence was already starting to waver, thus exacerbating the downturn in sentiment. For example, the regulatory action of further limiting daily fluctuations in individual stocks from 10 percent to 5 percent was interpreted by investors as a lack of confidence in market valuations. As prices began to fall, margin calls exacerbated selling pressures. Selling contagion also spread from Saudi Arabia to other regional equity markets where Saudi investors are the dominant suppliers of capital, in part because access to capital from outside the region is limited.

GCC Equity Markets in Perspective
(1/1/2003 = 100)



Source: Bloomberg L.P.

The authorities responded to falling stock markets by enacting policy measures aimed at increasing market liquidity (including through broadening the investor base) and improving transparency. In Saudi Arabia, the authorities reversed their earlier action limiting daily price fluctuations of individual stocks. Stock splits were allowed in order to lower the face value of shares and encourage broader retail ownership. The authorities also permitted foreign residents to trade directly with local exchanges. With a view to improving the quality of information available to investors, the Saudi authorities now license research institutions to analyze new companies and have introduced tough new sanctions against the use of insider information. In the UAE, recognizing that IPOs were locking up market liquidity, the authorities now require companies to refund IPO oversubscriptions within two weeks. They also eased margin requirements from 30 percent to 20 percent to lower the risk of forced stock sales that were adding to market pressures. National authorities have also strengthened monitoring of the banking sector—in the UAE, the central bank expanded reporting requirements by local banks to include indirect stock market exposures. Finally, announcements of potential share purchases by state investment funds operating in the major regional markets lifted market sentiment.

APPENDIX

Emerging Market Financing Flows

Cumulative overall gross issuance (of bonds, equities, and loans) by sovereign and corporate issuers through the end of April remained at record levels, hitting $126.8 million, well above the $113.8 million of 2005. The surge was mainly due to much higher equity and loan issuance, while gross bond issuance was lower, reflecting mostly prefinancing. As detailed in the April 2006 GFSR, equity issuance reflected the surge in Asian initial public offerings in the first part of the year. On a net basis, overall issuance declined, reflecting a large decline in net bond issuance, while net loan issuance increased substantially. Among sectors, gross and net bond issuance were concentrated in public sector non sovereign issuers, reflecting a surge in bond issues by government-related corporates.

Cumulative Gross Annual Issuance of Bonds, Loans, and Equity
(In billions of U.S. dollars)

Source: Dealogic.

Table 1. Emerging Market External Financing

	2000	2001	2002	2003	2004	2005	2004				2005				2006					
							1st qtr.	2nd qtr.	3rd qtr.	4th qtr.	1st qtr.	2nd qtr.	3rd qtr.	4th qtr.	1st qtr.	Jan.	Feb.	Mar.	Apr.	Year-to-date[1]
							(In billions of U.S. dollars)													
GROSS ISSUANCE BY ASSET	**216.4**	**162.1**	**135.6**	**199.7**	**286.5**	**406.0**	**71.6**	**63.5**	**70.2**	**81.2**	**94.4**	**88.9**	**107.1**	**115.6**	**96.0**	**29.6**	**22.5**	**43.9**	**30.8**	**126.8**
Bonds	80.5	89.0	61.6	99.8	135.1	182.3	40.9	29.1	34.5	30.5	61.7	37.8	40.4	42.4	48.9	19.4	8.7	20.8	5.4	54.3
Equities	41.8	11.2	16.4	27.7	45.1	78.1	13.9	10.3	5.6	15.3	10.5	17.4	22.9	27.4	22.4	6.1	7.5	8.8	7.4	29.9
Loans	94.2	61.9	57.6	72.2	106.2	145.5	16.8	24.0	30.1	35.3	22.3	33.8	43.7	45.7	24.7	4.1	6.3	14.3	17.9	42.6
GROSS ISSUANCE BY REGION	**216.4**	**162.1**	**135.6**	**199.7**	**286.5**	**406.0**	**71.6**	**63.5**	**70.2**	**81.2**	**94.4**	**88.9**	**107.1**	**115.6**	**96.0**	**29.6**	**22.5**	**43.9**	**30.8**	**126.8**
Asia	85.9	67.5	53.9	88.8	123.3	149.6	34.1	28.5	25.8	35.0	26.6	33.5	40.8	48.8	36.9	10.6	8.3	18.0	7.9	44.8
Latin America	69.1	53.9	33.4	43.3	54.3	87.5	14.4	9.7	16.2	13.9	34.5	13.8	23.0	16.3	14.9	5.3	2.7	6.9	4.6	19.5
Europe, Middle East, Africa	61.4	40.8	48.3	67.7	108.9	168.9	23.1	25.3	28.3	32.3	33.3	41.7	43.3	50.6	44.3	13.7	11.6	19.0	18.2	62.5
AMORTIZATION BY ASSET	**113.9**	**147.0**	**128.4**	**119.5**	**128.1**	**107.8**	**35.0**	**32.8**	**30.6**	**29.7**	**21.6**	**26.1**	**32.6**	**27.5**	**22.2**	**8.9**	**6.2**	**7.1**	**9.1**	**31.3**
Bonds	51.8	59.0	58.9	57.1	69.6	65.2	21.5	17.5	15.9	14.7	13.3	14.5	21.6	15.8	13.4	4.5	4.5	4.3	6.7	20.1
Equities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	62.1	88.0	69.5	62.4	58.5	42.6	13.5	15.3	14.7	15.0	8.3	11.6	11.0	11.7	8.8	4.3	1.7	2.8	2.4	11.3
AMORTIZATION BY REGION	**113.9**	**147.0**	**128.4**	**119.5**	**128.1**	**107.8**	**35.0**	**32.8**	**30.6**	**29.7**	**21.6**	**26.1**	**32.6**	**27.5**	**22.2**	**8.9**	**6.2**	**7.1**	**9.1**	**31.3**
Asia	56.6	66.0	55.6	45.5	49.8	38.6	13.2	12.9	11.8	11.8	8.0	5.9	11.4	13.4	10.7	3.8	2.9	3.9	3.3	14.0
Latin America	32.3	45.6	40.8	40.4	46.7	37.1	12.3	13.4	10.2	10.9	7.7	10.4	11.1	7.9	7.9	3.9	2.2	1.8	2.4	10.3
Europe, Middle East, Africa	24.9	35.3	32.0	33.6	31.6	32.1	9.5	6.6	8.6	7.0	5.9	9.8	10.1	6.3	3.6	1.1	1.1	1.4	3.4	7.0
NET ISSUANCE BY ASSET	**102.5**	**15.2**	**7.3**	**80.2**	**158.3**	**298.2**	**36.6**	**30.7**	**39.6**	**51.5**	**72.8**	**62.9**	**74.5**	**88.1**	**73.8**	**20.7**	**16.3**	**36.8**	**21.6**	**95.4**
Bonds	28.7	30.1	2.7	42.7	65.5	117.1	19.4	11.6	18.6	15.8	48.4	23.3	18.8	26.6	35.6	14.9	4.2	16.5	-1.3	34.3
Equities	41.8	11.2	16.4	27.7	45.1	78.1	13.9	10.3	5.6	15.3	10.5	17.4	22.9	27.4	22.4	6.1	7.5	8.8	7.4	29.9
Loans	32.1	-26.1	-11.8	9.8	47.7	103.0	3.3	8.7	15.4	20.3	14.0	22.2	32.7	34.1	15.8	-0.3	4.6	11.5	15.5	31.3
NET ISSUANCE BY REGION	**102.5**	**15.2**	**7.3**	**80.2**	**158.3**	**298.2**	**36.6**	**30.7**	**39.6**	**51.5**	**72.8**	**62.9**	**74.5**	**88.1**	**73.8**	**20.7**	**16.3**	**36.8**	**21.6**	**95.4**
Asia	29.2	1.5	-1.7	43.3	73.5	111.0	20.8	15.6	13.9	23.1	18.7	27.6	29.4	35.4	26.2	6.7	5.4	14.1	4.6	30.8
Latin America	36.8	8.3	-7.4	2.9	7.6	50.4	2.1	-3.6	6.0	3.1	26.8	3.4	11.8	8.4	6.9	1.4	0.5	5.1	2.2	9.2
Europe, Middle East, Africa	36.5	5.5	16.3	34.0	77.2	136.8	13.6	18.7	19.6	25.3	27.4	31.9	33.2	44.3	40.7	12.7	10.5	17.6	14.8	55.5
SECONDARY MARKETS																				
Bonds:																				
EMBI Global (spread in bps)	735	728	725	403	347	179	414	482	409	347	373	297	235	237	191	210	187	191	179	179
Merrill Lynch High Yield (spread in bps)	890	795	871	418	310	371	438	404	384	310	352	385	354	371	313	342	337	313	304	304
Merrill Lynch High Grade (spread in bps)	200	162	184	93	83	92	94	97	91	83	93	95	89	92	90	90	90	90	89	89
US 10 yr. Treasury Yield (yield in %)	5.12	5.05	3.82	4.25	4.22	4.39	3.84	4.58	4.12	4.22	4.48	3.92	4.33	4.39	4.85	4.52	4.55	4.85	5.05	5.05
Equity:									*(In percent)*											
DOW	-6.2	-7.1	-16.8	25.0	3.1	-0.6	-0.9	0.8	-3.4	-1.9	-2.8	-2.6	-2.2	2.9	3.7	1.4	1.2	1.1	2.3	6.1
NASDAQ	-39.3	-21.1	-31.5	50.5	8.6	1.4	-0.5	2.7	-7.4	1.9	-8.4	-8.1	2.9	4.6	6.1	4.6	-1.1	2.6	-0.7	5.3
MSCI Emerging Market Free	-31.8	-4.9	-8.0	51.2	22.4	30.3	8.9	-10.3	7.4	-0.2	0.6	1.2	3.0	17.0	11.5	10.9	-0.2	0.7	6.8	19.1
Asia	-42.5	4.2	-6.2	46.1	12.2	23.5	7.6	-12.2	4.2	-0.5	2.8	2.1	2.8	8.5	9.0	7.5	-0.4	1.8	6.9	16.5
Latin America	-18.4	-4.3	-24.8	66.7	34.8	44.9	6.2	-9.2	16.6	-1.1	-0.6	1.8	7.1	29.5	14.9	17.0	0.8	-2.6	7.3	23.3
EMEA	-22.3	-20.9	4.7	51.9	35.8	34.9	13.2	-7.4	7.8	1.0	-3.0	-1.0	0.5	27.1	14.1	13.5	-0.7	1.3	6.3	21.3

Sources: Bloomberg L.P.; Capital Data; J.P. Morgan Chase; Morgan Stanley Capital International; and IMF staff estimates.

1/ Issuance data (net of US trust facility issuance) are as of April 30, 2006 close-of-business London Secondary markets data are as of noon, April 30, 2006 cob New York.

Table 2. Sovereign External New Issuance Estimates in 2006
(In millions of U.S. dollars)

	Planned	Actual	Remaining
Argentina	3,400	2,139	1,261
Bahrain	...	...	...
Belize	...	...	...
Brazil	4,500	5,330	(830)
Bulgaria	650	...	650
Chile	...	...	...
China	...	...	...
Colombia	2,000	2,237	(237)
Costa Rica	...	...	...
Croatia	...	...	...
Czech Republic	1,700	...	1,700
Dominican Republic	300	300	...
Ecuador	500	650	(150)
Egypt	1,000	...	1,000
El Salvador	625	400	225
Estonia	...	...	...
Guatemala	...	...	...
Hungary	3,500	2,837	663
Iran	...	...	...
Indonesia	2,000	2,000	...
Israel	900	...	900
Jamaica	...	...	...
Jordan	...	...	...
Latvia	...	...	...
Lebanon	2,000	267	1,733
Lithuania	500	480	20
Malaysia	500	...	500
Mexico	2,900	2,900	0
Morocco	500	...	500
Nigeria	...	...	...
Pakistan	500	800	(300)
Panama	640	1,613	(973)
Peru	...	...	...
Philippines	3,100	2,250	850
Poland	5,500	3,630	1,870
Qatar	...	...	...
Romania	...	...	...
Russia	...	...	...
Serbia	...	...	...
Slovak Republic	1,200	1,200	...
Slovenia	...	...	...
South Africa	1,000	907	93
South Korea	1,000	...	1,000
Sri Lanka	...	...	...
Thailand	1,000	200	800
Trinidad & Tobago	...	...	...
Turkey	5,500	3,129	2,372
Tunisia	650	...	650
Ukraine	1,500	...	1,500
Uruguay	500	1,560	(1,060)
Venezuela	3,000	4,215	(1,215)
Vietnam	250	...	250
Asia	8,350	5,250	3,100
Emerging Europe	20,050	11,275	8,775
Latin America	18,365	21,344	(2,979)
Middle East & Africa	6,050	1,174	4,876
Total	52,815	39,043	13,772

Source: JPMorgan Chase & Co.
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