19 December 2018

Emerging Markets Briefer

Buying opportunities set to arise after Q1 19

In 2018, emerging markets continued to adapt to rising external challenges. After a slowdown and several crises in 2018, they have shown their increasing ability to adjust to a rapidly changing external environment. First, a rising USD and US yields led to a reversal of capital flows to emerging markets. Emerging market central banks responded to the shrinking global liquidity by tightening explicitly by raising key rates or implicitly through liquidity tools. Even less orthodox monetary policymakers such as Argentina and Turkey had to deliver significant tightening in order to stabilise their financial systems. Even economies with well-anchored inflation such as Brazil and Mexico have kept real rates at historically high levels. Worsening prospects in global trade have weighed on economic growth in Asia and we expect the pressure to remain in 2019. Across several emerging markets, we believe fiscal issues will continue to be in focus. We expect a more conservative stance on fiscal policy to commence in Brazil and Turkey.

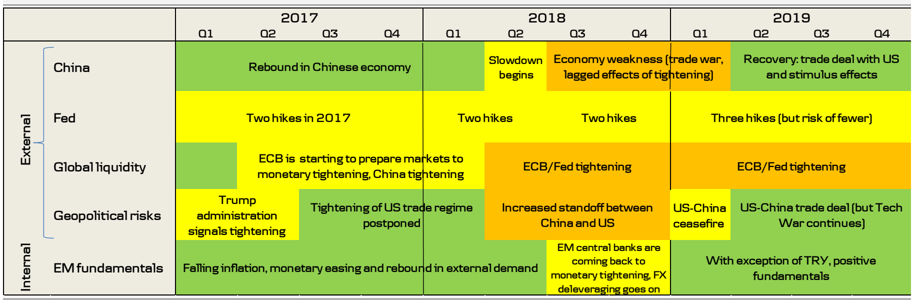
Economic growth in emerging markets is set to slow down in 2018-20. In our view, emerging markets will adjust further to rising trade and monetary challenges. We expect continued free-floating regimes to improve their external balances further across emerging markets. Acceleration in inflation is likely to continue in early 2019 but we expect it to start falling again in the second half of 2019. We expect economic growth to slow down across the majority of emerging markets due to rising rates to fight inflation and FX volatility. However, we expect less aggressive monetary tightening across emerging markets in 2019 than in 2018.

The Chinese economy remains an important driver for emerging market growth. We forecast overall economic growth in China will slow down from 6.6% in 2018 to 6.2% in 2019. As we expect China's leading indicators to reach the bottom in early 2019, we look more positively at Q2 19, seeing buying opportunities for emerging markets arising after Q1 19.

While protectionism, a China slowdown, geopolitics, an uncertain oil price outlook and more aggressive Fed tightening remain key risks for our emerging market forecasts, the Fed's retreat from the current hawkish stance in 2019 and a weakening USD would support emerging markets. At the same time, we believe the ECB's journey towards normalisation of its monetary policy will position CEE central banks on the more hawkish side, pushing CEE currencies higher.

We believe sanction risks will continue to be topical for China, Hungary, India, Iran, Russia, Saudi Arabia and Turkey.

Bank emerging market risks heat map for 2017-19



Source: Danske Bank

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Poland: beyond peak but not out of steam

Macro and political outlook

- The Polish economy continues to enjoy rapid economic growth coupled with remarkably low inflation. In Q3, real GDP growth kept up the pace and expanded by 5.1% y/y, significantly outpacing the expected 4.6% growth rate. However, we think the Polish economy is past its peak and we expect a moderation in economic growth. Indeed, PMI manufacturing continues to decline, falling further to 49.5 in November, which is the lowest level since the start of the recording of the series in December 2015. That said, retail sales are still going strong supported by high real earnings and low unemployment and construction is also expanding at a healthy pace. As a result, we raised our forecast for real GDP growth from 4.7% to 5.1% for 2018 and from 3.5% to 3.8% for 2019 in *Emerging Market Briefer – Switching slowly from red light to yellow*, 3 October.

Monetary policy outlook

- Inflation pressures continue to remain extremely muted; the flash November headline inflation declined to 1.2%, from 1.8% in October, while core inflation remained just below 1.0% in October. In light of the muted inflation pressures, the Monetary Policy Committee of the National Bank of Poland reiterated its relatively dovish tone at the press conference in December, stressing the impact of falling energy prices. The market has accordingly lowered its expectations, pricing in only one rate hike by end-2020, which we see as slightly on the dovish side.

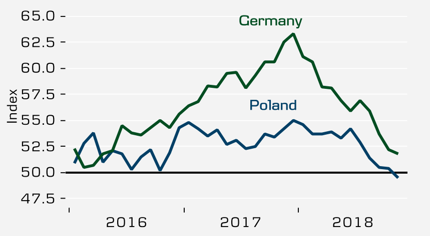
FX outlook

- The PLN has traded in a fairly tight range of 4.28-4.33 to the EUR over the past few months amid weak emerging market sentiment outweighing the relatively strong performance of the Polish economy. Although a China-US trade deal may lift emerging market sentiment in the spring, we expect EUR/PLN to remain in the range on a 3M basis. As a result, our forecasts are 4.28 in 1M, 4.26 in 3M (previously 4.24), declining further to 4.22 in 6M (previously 4.20) and 4.18 in 12M.

Risk factors

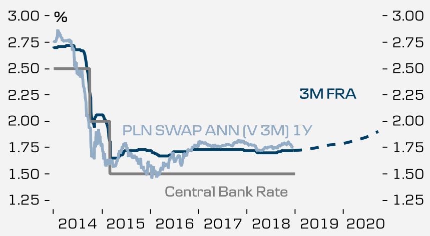
- Risks are skewed slightly on the downside for our EUR/PLN forecast. The most prominent downside risks are improvement in emerging market sentiment and stronger economic releases, while upside risks to the cross include further tensions between the EU and Poland, as well as further escalation in the trade dispute between the US and China.

PMI manufacturing now under the important 50 benchmark



Source: Markit, Macrobond Financial, Danske Bank

Market has more or less priced out any hikes until end-2020



Source: Macrobond Financial

PLN

Credit rating:

S&P: BBB+ (positive)

Currency regime:

Free float (freely convertible)

Inflation target:

2.5%±1pp

Macro forecasts

	2017	2018	2019	2020
GDP (% y/y)	4.8	5.1	3.7	3.1
GDP deflator (% y/y)	1.9	1.3	1.9	1.7
CPI (% y/y)	2.0	1.8	2.3	2.5
Private consumption (% y/y)	4.7	3.7	2.2	3.0
Fixed investments (% y/y)	3.1	5.3	3.3	3.1
Unemployment (%)	6.6	7.1	6.5	6.2
Current account (% of GDP)	0.0	-0.5	-0.9	-1.5

Source: Macrobond Financial, Danske Bank

Interest rate forecast

National Bank of Poland (NBP)		
Policy rate	1.50	
Next meeting	09/01/2019	
Next change	+25bp	Q2, 2019
End-2019	1.75	

Source: Bloomberg, Danske Bank

FX forecasts

EUR/PLN		
	Danske	Forward
17-Dec	4.28	
+3M	4.26	4.31
+6M	4.22	4.33
+12M	4.18	4.38
USD/PLN		
	Danske	Forward
17-Dec	3.78	
+3M	3.77	3.76
+6M	3.58	3.75
+12M	3.34	3.73

Source: Danske Bank

Hungary: slowing down from the peak

Macro outlook

- Economic growth stayed at its 14-year high of 4.9% y/y in both Q2 and Q3 19. Manufacturing PMI stayed firmly above 50.0, falling to 53.5 in November from over 60.0 in early 2018. Hungary's PMI has followed the slowdown in the EU's largest economies closely. Industrial production growth remains solid on fading risks from the escalation in the EU-US trade war. The current stance on monetary policy remains beneficial for further economic expansion in 2019 and 2020, albeit on a lower path.
- The country continues to enjoy strong private consumption, supported by a near all-time low unemployment rate and double-digit gross wage growth. However, consumer confidence has continued to decline since the summer, which signals a slowdown in private consumption in 2019.
- The stand-off continues between the EU and Hungary's Prime Minister Viktor Orbán on his domestic policy and court reform. Any further escalation could result in the introduction of more sanctions by the EU against Hungary and weigh on the HUF.

Monetary policy outlook

- The Hungarian central bank (MNB) has kept rates unchanged throughout 2018 and we expect it to be on hold in early 2019. However, headline inflation has stayed above the 3.0% target since June 2018, decelerating a bit in November to 3.1% y/y. We expect loose monetary policy to continue in Q1 19, while moderate tightening could start ahead of the ECB's preparations to hike in late-2019. Thus, the MNB could hike in Q2 19. We do not exclude implicit tightening through liquidity tools.

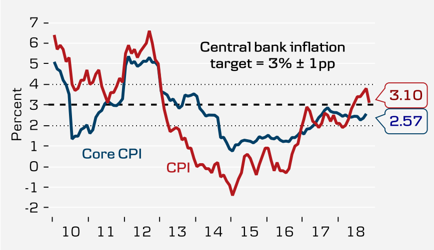
FX outlook

- While EUR's weakness on Italian woes could shake the HUF, we still see it as stronger in the short, medium and long term, while adjusting the pair's forecast according to the current EUR exchange rate. We see EUR/HUF at 322.6 in 1M, at 321.0 in 3M, keeping our long-term forecast unchanged at 317.0 in 6M and in 12M at 310.0.

Risk factors

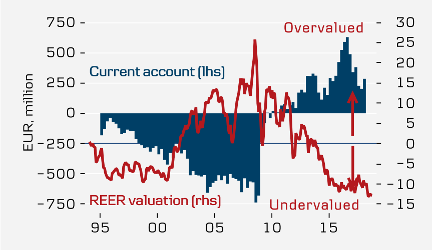
- A clear upside risk to our EUR/HUF forecast is further deterioration of economic and political sentiment within the EU economies, continued dovishness from the ECB in 2019 and increasing political risk on the stand-off between Budapest and Brussels.

Inflation has stayed above the MNB's target, which could cause additional monetary tightening



Source: MNB, Macrobond Financial, Danske Bank

Sustainable current account surplus set to support HUF long term



Source: Macrobond Financial, Danske Bank

HUF

Credit rating:

S&P: 'BBB-' (stable)

Currency regime:

Free float (freely convertible)

Inflation target:

3%±1pp

Macro forecasts

	2017	2018E	2019E	2020E
Real GDP (% y/y)	4.1	4.3	3.4	2.6
CPI (% average)	2.3	2.8	3.4	3.2
Unemployment (%)	3.8	3.8	3.5	3.6
Current account (% of	3.2	3.0	2.1	1.9

Source: Bloomberg, Danske Bank

Interest rate forecast

Hungarian Central Bank (MNB)		
Policy rate	0.90	
Next meeting	29/01/2019	
Next change	+25bp	Q2, 2019
End-2019	1.15	

Source: Bloomberg, Danske Bank

FX forecasts

EUR/HUF		
	Danske	Forward
17-Dec	323.1	
+3M	321.0	323.3
+6M	317.0	323.6
+12M	310.0	325.0

USD/HUF		
	Danske	Forward
17-Dec	284.99	
+3M	284.07	282.05
+6M	268.64	280.05
+12M	248.00	276.76

Source: Danske Bank

Czech Republic: faced with external headwinds

Macro and political outlook

- In Q3 GDP growth (0.6% q/q) was driven both by domestic and foreign demand, but private consumption remains the key growth engine. Compared to 2017, the growth momentum in the Czech Republic has moderated in light of biting capacity constraints (especially in the labour market) and export performance is also faced with increasing global headwinds. Despite the slowdown in economic activity, the growth outlook remains favourable in our view on the back of strong wage growth fuelling domestic demand. We expect annual GDP growth to stay around potential, at 3.0% in 2018 and 2.9% in 2019 (3.3% and 3.1% previously). We expect a high degree of policy continuity under the new ruling coalition of the ANO movement and Social Democrats, and the probability of a push for EU-exit remains very low.

Monetary policy outlook

- Inflation remains elevated and at the November meeting the Czech National Bank (CNB) raised the policy rate by another 25bp to 1.75%, also in light of persistent CZK weakness. For CNB the overall monetary conditions are crucial and hence the timing of the Czech hiking cycle remains dependent on FX movements. We expect the CNB to stay on hold until February 2019, but should CZK continue to trade weaker than envisioned in 2019, we expect the CNB to continue speeding up monetary tightening through the interest rate channel. In total, we currently expect two interest rate rises for next year, which would mean the policy rate would remain below its long-run neutral level (estimated at c.3.0% by the CNB).

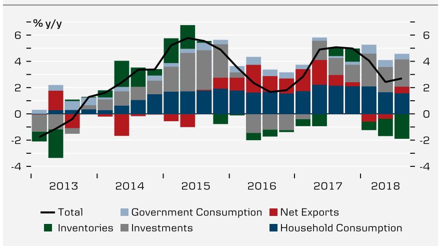
FX outlook

- Adverse global risk sentiment currently maintains the upper hand over strong Czech domestic fundamentals. Eventually, we expect CZK to return to its gradual strengthening path – not least due to the positive interest rate differential vis-à-vis the euro area. However, the timing remains difficult to judge and with the current adverse risk sentiment likely to linger as a CZK headwind and the CNB on hold for now, we expect the cross to continue range-trading around current levels in the near-term. We forecast EUR/CZK at 25.90 in 1M, 25.80 in 3M, 25.10 in 6M and 24.80 in 12M.

Risk factors

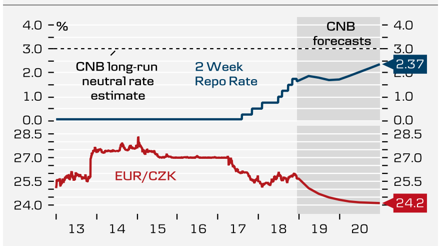
- The risk to our EUR/CZK forecast profile is skewed to the upside due to spill-overs from the current adverse global risk sentiment. Given the sizable amount of long CZK positions accumulated in the market prior to the floor exit, EUR/CZK is especially vulnerable to changes in global investor sentiment.

Growth has slowed but remains underpinned by domestic demand



Source: Macrobond Financial, Danske Bank

CNB expects tightening in 2019 mainly through CZK appreciation



Source: CNB, Macrobond Financial, Danske Bank

CZK

Credit rating:

S&P: 'AA-' (stable)

Currency regime:

Managed float

Inflation target:

2% +/-1pp

Macro forecasts

	2017	2018	2019	2020
GDP (% y/y)	4.5	3.0	2.9	2.9
GDP deflator (% y/y)	1.5	2.2	1.9	1.9
CPI (% y/y)	2.5	2.1	2.0	2.0
Private consumption (% y/y)	4.4	3.4	2.7	2.8
Fixed investments (% y/y)	3.7	9.5	4.0	2.8
Unemployment (%)	4.2	3.2	3.1	3.0
Current account (% of GDP)	1.3	0.7	0.5	0.5

Source: Macrobond Financial, Danske Bank

Interest rate forecast

Czech National Bank (CNB)		
Policy rate	1.75	
Next meeting	20/12/2018	
Next change	+25bp	H2, 2019
End-2019	2.25	

Source: Danske Bank

FX forecasts

EUR/CZK		
	Danske	Forward
17-Dec	25.77	
+3M	25.80	25.83
+6M	25.10	25.97
+12M	24.80	26.22
USD/CZK		
	Danske	Forward
17-Dec	22.74	
+3M	22.83	22.53
+6M	21.27	22.47
+12M	19.84	22.33

Source: Danske Bank

Russia: fading growth ahead

Macro outlook

- The Russian economy grew 1.5% y/y in Q3 18 versus 1.9% y/y a quarter earlier. The Q3 18 estimate was raised by 0.2pp versus the previous release. Industrial production growth has remained in positive territory through 2018, and manufacturing PMI has recovered staying over 50.0. We stick to our GDP growth estimates of 1.6% for 2018, 1.3% for 2019 and 1.4% for 2020, emphasising once more that a continuing tight monetary policy and geopolitical woes remain the major downside risk for our macro forecasts.
- The looming pension reform, VAT and fuel price increases in early 2019 would hit Russian consumers, especially in Russian provinces, where monthly salaries are much lower than in cities with more than one million inhabitants.
- Possible US sanctions on the banking sector would add to volatility in Russian markets in 2019. Yet, as some banks have billions of USD of external obligations, that could limit the level of toughness of the looming sanctions. If the so-called 'bill from hell' in the US becomes law, sanctioning foreign buyers of Russian sovereign debt, Russian banks have surplus liquidity to buy Russian local debt – OFZ – and replace non-residents.

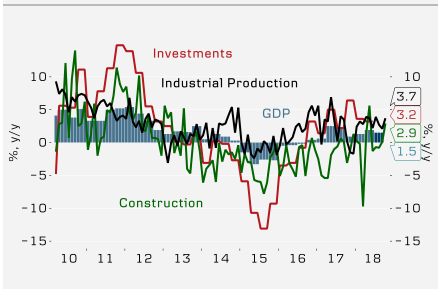
FX and monetary policy outlook

- On 14 December, Russia's central bank (CBR) hiked the key rate by 25bp to 7.75% as we expected, while Bloomberg consensus saw unchanged rate at 7.50%. The rate hike shows that the central bank continues to anticipate inflation risks playing it on the safest side as possible. It also tells us about current concerns of shaky external environment and risk of possible sanctions.
- The RUB markets have seen relief on speculation that the US Congress will be too busy focusing on domestic issues and nominations instead of pushing the anti-Russia sanctions 'bill from hell' over the rest of 2018. We see the current RUB positivism being temporary, as we believe Donald Trump's administration is likely to introduce soon the second stage of anti-Russia sanctions linked to the Sergei Skripal case and we expect the US Congress to return to processing 'the bill from hell' in Q1 19.

Risk factors

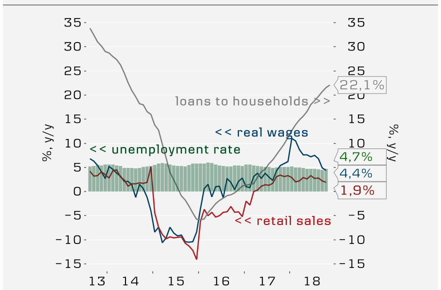
- Further geopolitical escalation, such as a worsening standoff with Ukraine, is a serious short- to medium-term risk for the RUB, Russian stocks and government debt. Upside risks come from an increasing oil price and a more dovish than expected central bank.

Economic growth components stay in green, but growth is set to slow down



Source: Macrobond Financial, Danske Bank

Private consumption set to decelerate in H1 19



Source: Macrobond Financial, Danske Bank

RUB

Credit rating:
S&P: 'BBB-' (stable)

Currency regime:
Free float

Inflation target:
4.0%

Macro forecasts

	2017	2018E	2019E	2020E
Real GDP (% y/y)	1.5	1.6	1.3	1.4
Private consumption, real (% y/y)	3.3	3.0	2.5	2.9
Fixed investments, real (% y/y)	7.5	3.2	2.4	3.1
Brent oil price (USD, average, futures)	54.8	72.4	62.5	60.9
Brent oil price (% y/y)	21.4	32.2	-13.7	-2.6
Exports in USD (average % y/y)	25.1	32.0	18.0	20.0
Imports in USD (average % y/y)	23.8	11.0	2.0	3.2
MosPrime 3 months rate (% average)	9.3	7.7	8.4	8.0
CPI (% Dec/Dec)	2.5	3.8	3.4	3.3
Unemployment (%)	5.2	5.1	5.0	5.0
Budget balance (% of GDP)	-1.7	0.8	0.5	0.5
Current account (% of GDP)	2.5	3.2	2.9	2.7

Source: CBR, Rosstat, Bloomberg, Macrobond Financial, Danske Bank estimates

Interest rate forecast

Bank of Russia (CBR)	
Policy rate	7.75
Next meeting	08/02/2019
Next change	+25bp H1, 2019
End-2019	8.00

Source: Bloomberg, Danske Bank

FX forecasts

EUR/RUB		
	Danske	Forward
17-Dec	75.61	
+3M	81.36	77.51
+6M	87.08	79.06
+12M	93.88	82.50
USD/RUB		
	Danske	Forward
17-Dec	66.70	
+3M	72.00	67.62
+6M	73.80	68.42
+12M	75.10	70.26

Source: Danske Bank

Turkey: risk of recession arises

Macro outlook

- As we expected in in *Emerging Market Briefer – Switching slowly from red light to yellow*, 3 October, Turkish GDP growth saw a sharp slowdown in Q3 18, decelerating to 1.6% y/y from a revised 5.3% y/y a quarter earlier. Industrial production shrank for the first time in two years, while manufacturing PMI has stayed deeply below 50.0 since April 2018. The Turkish central bank's monetary tightening is putting an additional brake on economic expansion in 2019.
- Private consumption expanded 1.1% y/y, which is the lowest growth in two years. Durable goods consumption plummeted 23.9% y/y and semi-durable goods consumption fell 4.5% on rocketing inflation and loans rates. Non-durable goods and services were up. We expect private consumption to slow further down in H1 19.
- We expect 2018 GDP to grow 3.5% y/y, cutting our 2019 GDP growth projection to 1.1% y/y (previously 1.8% y/y) and keeping our 2020 GDP growth projection at 2.1%. We see that risks of technical recession in 2019 remain elevated.

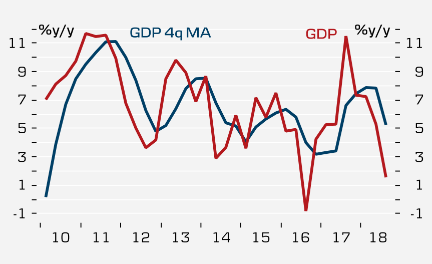
FX and monetary policy outlook

- Turkey's central bank (TCMB) stayed solid on 13 December, keeping the one-week repo rate at 24.00% as we expected, which moved the USD/TRY lower. As inflation started decelerating, falling to 21.6% y/y in November from its 15-year high of 25.2% in October 2018, the TCMB's tone was slightly more dovish. We expect the TCMB to start to make cautious cuts in spring 2019, keeping real rates in positive territory though.
- We see falling volatility in the TRY in the medium term, as the TCMB is returning to a conventional monetary policy framework. We remain cautious in the medium to long term on pressure from a high oil price, volatile portfolio flows and a wide current account deficit.

Risk factors

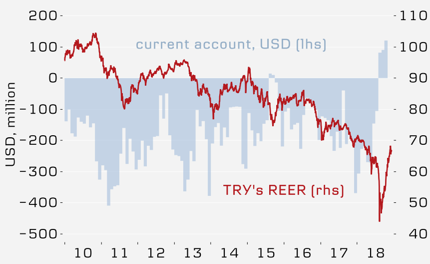
- Downside risks to our TRY forecasts are still geopolitical, if the confrontation with the US escalates, e.g. on the S-400 anti-aircraft weapon system deliveries by Russia, and Turkey's operations in Syria. The TCMB's monetary easing, driven by political pressure and worsening macro factors, also presents downside risks to our TRY forecasts. Fed monetary tightening is the general emerging market risk for the TRY.

Turkey's GDP growth is facing a sharp slowdown on monetary tightening



Source: Macrobond Financial, Danske Bank

TRY's sharp devaluation has pushed CA balance to historical surplus



Source: Macrobond Financial, Danske Bank

TRY

Credit rating:
S&P: 'B+' (stable)

Currency regime:
Free float

Inflation target:
5.0% year-end 2018-20

Macro forecasts

	2017	2018E	2019E	2020E
Real GDP (% y/y)	7.4	3.5	1.1	2.1
Private consumption, real	6.1	3.1	1.2	2.0
Fixed investments, real (%	7.0	4.0	1.0	2.3
CPI (% average)	11.1	15.5	14.7	9.8
Unemployment (%)	10.9	10.2	10.6	11.0
Current account (% of	-5.2	-5.0	-3.1	-3.0

Source: Bloomberg, Danske Bank

Interest rate forecasts

C.B. of the Republic of Turkey (TCMB)	
Policy rate	24.00
Next meeting	16/01/2019
Next change	-100bp H1, 2019
End-2019	17.75

Source: Bloomberg, Danske Bank

FX forecasts

EUR/TRY		
	Danske	Forward
17-Dec	6.11	
+3M	6.67	6.45
+6M	7.20	6.82
+12M	8.13	7.50
USD/TRY		
	Danske	Forward
17-Dec	5.39	
+3M	5.90	5.62
+6M	6.10	5.90
+12M	6.50	6.39

Source: Macrobond Financial, Danske Bank

South Africa: rescinding recession fears

Macro outlook

- After a lacklustre Q2, the South African economy is showing signs of recovery. In Q3, real GDP growth rebounded to 1.1% y/y from 0.4% in the previous quarter. In Q4, tentative indicators such as manufacturing production, mining, electricity and retail sales are gaining strength. The lower oil price is also good for the South African economy, reducing inflation and import needs. However, despite the rebound, business sentiment remains weak and consumers have started to reconsider their initial optimism. In addition, important exports markets such as China and the euro area are set to grow slowly in coming months. While we lift our real GDP growth estimate for 2018 slightly to 0.7% (from 0.5%), we lower our 2019 estimate to 1.5% (from 1.7%). We expect economic growth in 2020 to recover to just above 2.0%.

Monetary policy outlook

- Headline inflation increased to 5.1% in November, which was significantly higher than the mid-range of the central bank's inflation band. Core inflation increased toward the mid-range. The increasing inflation pressures reflect the combined impact of a higher oil price and a weaker ZAR earlier in 2018. Given the rise in inflation, the South African Reserve Bank (SARB) increased its repurchase rate by 25bp to 6.75% at its policy meeting in late November. However, the decision was not unanimous, as three board members voted for an unchanged rate. Given the stabilisation of the ZAR and the significant decrease in the oil price, we believe SARB will keep its rates unchanged at its meetings in Q1 (January and March), as we expect a fall in headline inflation. We expect the next policy change to be a reduction by mid-next year.

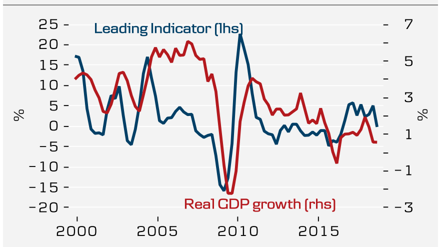
FX outlook

- The ZAR has recovered lately on improving prospects for a global trade deal, a fall in the oil price and a rebound in the South African economy. The ZAR is still viewed as undervalued by SARB at this level and we agree with that view. With China experiencing weakness in coming months and the Fed being priced in over the coming months, the ZAR could get under renewed pressure. As a result, our USD/ZAR forecast is 15.00 in 3M, 14.50 in 6M and 14.25 in 12M as trade concerns ease and the USD weakens.

Risks

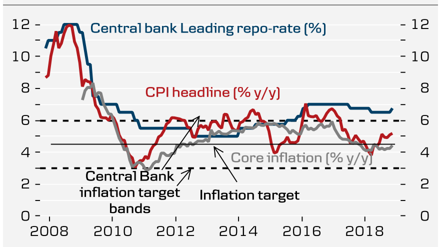
- The risk to our USD/ZAR forecast is skewed to the upside given elections in May 2019 and the looming downgrade from Moody's to junk.

The leading indicator point to modest growth



Source: Macrobond Financial

A decline in inflation is set to allow SARB to lower the policy rate



Source: Macrobond Financial

ZAR

Credit rating:

S&P: BB (stable)

Currency regime:

Free float (freely convertible)

Inflation target:

3-6%

Macro forecasts

	2017	2018	2019	2020	2021
GDP (% y/y)	1.3	0.7	1.8	2.1	2.6
GDP deflator (% y/y)	5.5	5.8	6.6	6.6	6.7
CPI (% y/y)	5.2	4.8	5.0	5.0	5.0
Private consumption (% y/y)	2.2	1.4	1.2	1.8	2.2
Fixed investments (% y/y)	0.4	0.2	1.3	1.8	2.2
Unemployment (%)	26.7	28.0	28.5	28.9	29.1
Current account (% of GDP)	-2.4	-3.4	-3.6	-4.0	-3.5

Source: Bloomberg, Danske Bank

Interest rate forecast

South African Reserve Bank (SARB)		
Policy rate	6.75	
Next meeting	17/01/2019	
Next change	-25bp	H1, 2019
End-2019	6.25	

Source: Bloomberg, Danske Bank

FX forecasts

EUR/ZAR		
	Danske	Forward
17-Dec	16.32	
+3M	16.95	16.58
+6M	17.11	16.91
+12M	17.81	17.59
USD/ZAR		
	Danske	Forward
17-Dec	14.39	
+3M	15.00	14.47
+6M	14.50	14.63
+12M	14.25	14.98

Source: Macrobond Financial, Danske Bank

Brazil: eyeing the new president's first steps

Macro outlook

- Brazil's economic growth accelerated to 1.3% y/y in Q3 18, up from a revised 0.9% y/y expansion in Q2 18, as the previous strike-driven sentiment has vanished and the country's economy has started benefiting from the US-China trade tensions. In expenditure terms, the economy has been boosted by a sharp rise in investments and exports. We cut our 2018 GDP growth forecast from 1.4% y/y to 1.3% y/y, as the negative impact of the lorry drivers' strike on Q2 18 GDP was larger than we previously estimated. We expect GDP to expand 2.0% in 2019 and 2.6% in 2020, while we see downside risks to our forecast from a tightening monetary stance.
- The win by the market-friendly presidential candidate Jair Bolsonaro caused a rally in the BRL and other Brazilian assets. Yet, markets have calmed down and started looking to 2019, when Bolsonaro is set to take his first steps as Brazil's president. The key question for Brazil's macro economy remains a pension reform proposal, which is crucial for fixing the country's bleeding fiscal side.
- The increase in Brazil's public net debt as a percentage of GDP hit a 15-year high in October (53.3%). The current increase should be curbed in 2019, if fiscal-side reforms are implemented, giving space for appreciation of the BRL.

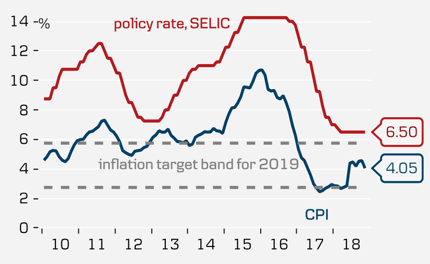
Monetary policy outlook

- Brazil's central bank (BCB) is due to get a new governor in 2019, as the new President brings his own nominee. However, markets expect continuity in the BCB's policies, which have started looking like a dovish outlier among the tightening global and emerging market universe. As inflation remains below the central bank target and economic growth stays moderate, we expect the BCB to deliver a 25bp hike in H2 19.

FX outlook

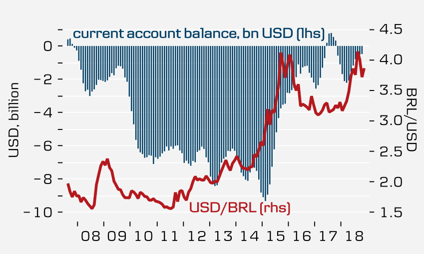
- The BRL has stabilised since the Bolsonaro rally, waiting for concrete steps from the new president in 2019. The long-term prospects for the BRL will depend largely on the presidential election outcome and reforms influenced by Bolsonaro.
- We update our USD/BRL forecast levels to reflect the recent developments in emerging market sentiment and Bolsonaro's victory. Our projections assume the pension reform proposal will go through. Rapid approval of reforms by the government and improving emerging market sentiment in 2019 would be BRL positive.

Central bank is set to stay on hold in H1 19, while the risk of a hike rises as global monetary tightening cycle is on



Source: Macrobond Financial, Danske Bank

Shrinking current account deficit supports the BRL long-term



Source: Macrobond Financial, Danske Bank

BRL

Credit rating:

S&P: BB- (stable)

Currency regime:

Free float (non-convertible)

Inflation target:

4.5% ±1.5pp in 2018

4.25% ±1.5pp in 2019

4.0% ±1.5pp in 2020

3.75% ±1.5pp in 2021

Macro forecasts

	2017	2018E	2019E	2020E
Real GDP (% y/y)	1.0	1.3	2.0	2.6
Private consumption, real	1.0	1.9	2.3	3.0
Fixed investments, real (%	0.0	2.5	3.2	4.5
CPI (% Dec/Dec)	2.95	4.0	4.7	4.2
Unemployment (%)	12.9	12.0	11.2	10.6
Current account (% of	-0.3	-0.6	-0.4	-0.2

Source: Bloomberg, Danske Bank

Interest rate forecasts

Central Bank of Brazil (BCB)	
Policy rate	6.50
Next meeting	06/02/2019
Next change	+25bp H2, 2019
End-2019	6.75

Source: Bloomberg, Danske Bank

FX forecasts

EUR/BRL		
	Danske	Forward
17-Dec	4.43	
+3M	4.12	4.50
+6M	4.19	4.57
+12M	4.13	4.71

USD/BRL		
	Danske	Forward
17-Dec	3.91	
+3M	3.65	3.93
+6M	3.55	3.95
+12M	3.30	4.01

Source: Macrobond Financial, Danske Bank

China: worse before it gets better

Macro outlook

- **The Chinese economy slowed in 2018** as the trade war weighed on exports as well as private investments and consumption of durable goods. The battle to fight China's debt mountain and rise in shadow finance also weighed on activity. The construction sector has generally held up well, as inventories of apartments for sale are low and home sales are supported by monetary easing.
- **We expect the Chinese economy to slow further in the short term but to recover from Q2 19.** We look for a trade deal between the US to be reached at some point in Q2 after a 90-day ceasefire was agreed upon on 1 December between the US and China. We see clear signs that Trump wants to make a deal with China soon after his hand has been weakened by US stock market declines. He also wants to secure gains for voters in US swing states as part of the deal as he eyes the 2020 Presidential election campaign, which starts in 2019. China is also interested in a deal, as the trade war weighs on the economy. If we get a trade deal in Q2, it should remove a sharp headwind for the Chinese economy.
- **We expect fiscal and monetary stimulus to kick in more forcefully in 2019** and we might even see further policy easing. A decent household tax cut and lower tax burden for businesses may be in the pipeline. The sharp decline in bond yields witnessed in 2018 normally feeds through to the construction sector with a six-nine month lag. We thus look for a pick-up in construction activity as 2019 progresses.
- **In the Doing Business 2019 Survey by the World Bank, China jumped 30 places** up the list to number 46 of 190 countries. China was number three on the list of biggest improvers. Contrary to popular belief, China is taking many steps to reform and nurture private entrepreneurship. China is also putting a high focus on technology investments and education. Both factors are key to continue an increase in productivity and prosperity.

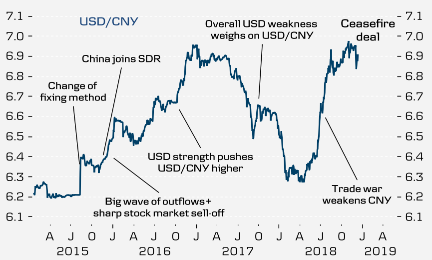
Monetary policy outlook

- The People's Bank of China (PBoC) has **eased policy three times this year** by lowering the Reserve Requirement Ratio. We expect limited further stimulus on the monetary front but look for fiscal stimulus to consumers and businesses through tax cuts.

FX outlook

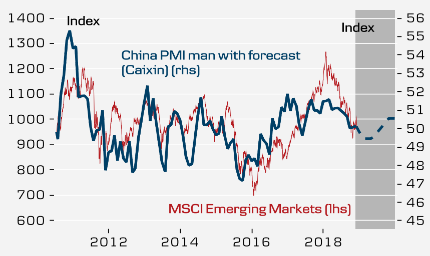
- A halt to the CNY depreciation is set to be part of a coming trade deal. We also see a higher chance of the Fed pausing on its rate hike in H2. We thus no longer expect further weakening of CNY. **We now expect USD/CNY to stay flat in the short term and decline slightly on a 12M horizon** (see *FX Forecast Update – An early Christmas present? To SEK, from the Riksbank*, 17 December).

Deal to keep USD/CNY below 7.0



Source: Macrobond Financial, Bloomberg

China recovery in 2019 to support emerging markets



Source: Macrobond Financial, PBoC, Markit

CNY

Credit rating:

S&P: A+ (stable)

Currency regime:

Managed exchange rate versus basket of currencies

Inflation target:

3.0% for 2018

Interest rate forecast

People's Bank of China (PBOC)		
Policy rate	4.35	
Next meeting	No regular meetings	
Next change	-25bp	Q1, 2019
End-2019	4.10	

Source: Danske Bank

Macro forecasts

	GDP		Inflation	
	Danske	Consensus	Danske	Consensus
2017	6.9	6.9	1.6	1.6
2018	6.6	6.6	2.2	2.2
2019	6.2	6.2	2.0	2.4
2020	6.2	6.0	2.2	2.2

Source: Macrobond Financial Danske Bank

FX forecasts

EUR/CNY		
	Danske	Forward
17-Dec	7.82	
+3M	7.80	7.93
+6M	8.08	8.00
+12M	8.50	8.14
USD/CNY		
	Danske	Forward
17-Dec	6.90	
+3M	6.90	6.91
+6M	6.85	6.92
+12M	6.80	6.94

Source: Bloomberg, Danske Bank

India: robust growth

Macro outlook

- **India's GDP growth eased in Q3 to 7.1% y/y** from 8.2% y/y in Q2 due to softer private consumption and weaker net exports. This is still very robust, though, and we look for India's growth to stay in the 7-8% range in coming years.
- **India has moved forward on reform** under the leadership of Narendra Modi of the BJP party. In its article IV Consultation report in August, the IMF stated that 'Stability-oriented macroeconomic policies and progress on structural reforms continue to bear fruit'. The IMF commended India 'for the important and wide-ranging reforms'.
- **India has experienced financial turmoil this year,** as the major shadow banking institution Infrastructure Leasing and Financial Services was close to a collapse in September. It led to contagion to other shadow finance institutions and exposed the fragility of the financial system in India. Things have calmed again, though.
- **State elections in India showed that continued leadership by Modi after the federal election next year is far from certain**. BJP was neck-on-neck with the opposition Congress Party in the central Indian states of Madhya Pradesh and Chhattisgarh. The two states are normally BJP strongholds. Modi is seen as more reform friendly and Indian equity markets sold off in response to the election results.
- **The steep oil price decline in recent months has provided support to the Indian economy** and given a lift to the Indian rupee. India is a big net importer of oil and the drop in prices benefits India's current account balance.

Monetary policy outlook

- **The Reserve Bank of India (RBI) has been in a stand-off with the government** about the RBI's capital framework. The government believes the central bank is more than adequately capitalised and that it should pass on some of the surplus. The RBI governor Urjit Pated resigned on 10 December in a likely reaction to the rift. The new governor is Shaktikanta Das who is a former top official of economic affairs. RBI has raised rates twice this year but easing inflation has put the RBI on pause. It is still in what it calls 'calibrated tightening' mode, but said on 9 December it needs more data to evaluate the outlook. Inflation declined to 3.3% in October, below the 4% target. **We expect RBI to be on hold until Q3 next year**, when we look for a further hike.

FX outlook

- After significant weakening this year, INR rebounded in early October when oil prices came off the highs. However, we expect oil prices to recover somewhat and expect an **increase in USD/CNY of 73 on 3M. In 12 months, we look for 71** on easing global uncertainty following a US-China trade deal and solid growth in the Indian economy.

INR

Credit rating:

S&P: BBB- (stable)

Currency regime:

Free float

Inflation target:

4% with +/-2% range

Macro forecasts

	GDP		Inflation	
	Danske Bank	Consensus	Danske Bank	Consensus
2017	6.3	6.3	3.3	3.3
2018	7.6	7.5	4.2	4.5
2019	7.5	7.3	4.2	4.2
2020	7.3	7.5	4.5	4.7

Source: Macrobond Financial, Danske Bank

Interest rate forecast

Reserve Bank of India (RBI)		
Policy rate	6.50	
Next meeting	06/02/2019	
Next change	+25bp	Q3, 2019
End-2019	6.75	

Source: Bloomberg, Danske Bank

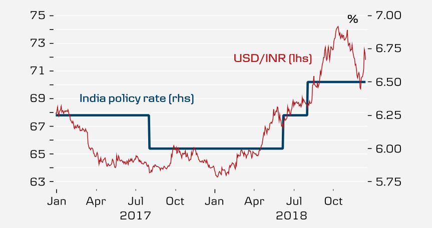
FX forecasts

EUR/INR		
	Danske	Forward
17-Dec	81.16	
+3M	82.49	81.63
+6M	84.96	83.21
+12M	88.75	86.32

USD/INR		
	Danske	Forward
17-Dec	71.59	
+3M	73.00	71.21
+6M	72.00	72.01
+12M	71.00	73.51

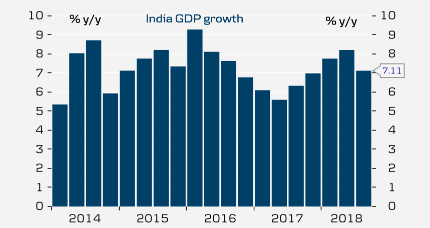
Source: Bloomberg, Danske Bank

INR in a limbo this year



Source: Macrobond Financial, Danske Bank

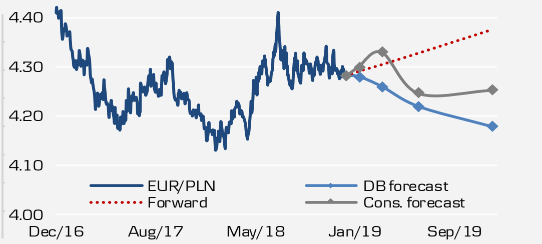
GDP growth hovering around 7-8%



Source: Macrobond Financial, Danske Bank

Danske Bank's hedging recommendations: EMEA

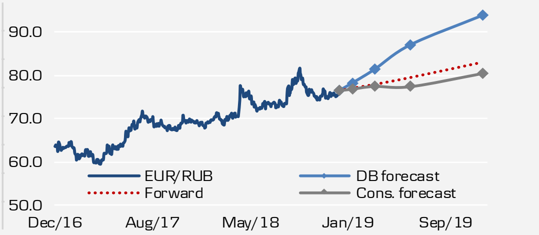
Currency	Instrument: Income	Instrument: Expenses	Forecast
PLN	We recommend hedging PLN income via knock-in forwards.	We recommend hedging PLN expenses via FX forwards.	



	1M	3M	6M	12M
DB forecast	4.28	4.26	4.22	4.18
Forward	4.29	4.30	4.33	4.38
Cons. forecast	4.30	4.33	4.25	4.25

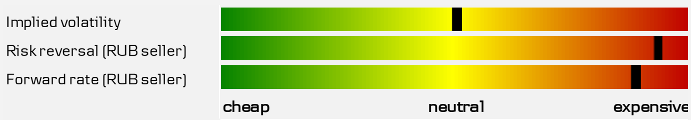
Price indicators

Currency	Instrument: Income	Instrument: Expenses	Forecast
RUB	We recommend hedging RUB income via FX forwards.	We recommend hedging RUB expenses via risk reversals.	

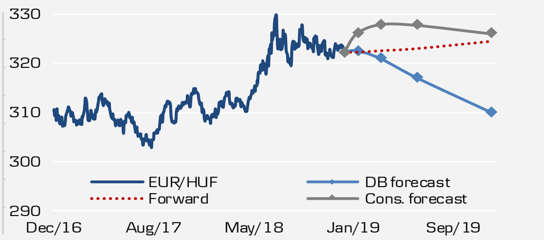


	1M	3M	6M	12M
DB forecast	78.08	81.36	87.08	93.88
Forward	77.00	77.89	79.47	82.93
Cons. forecast	76.78	77.43	77.37	80.31

Price indicators

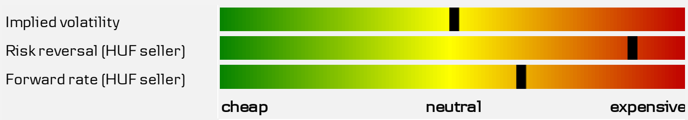


Currency	Instrument: Income	Instrument: Expenses	Forecast
HUF	We recommend hedging HUF income via knock-in forwards.	We recommend hedging HUF expenses via FX forwards.	

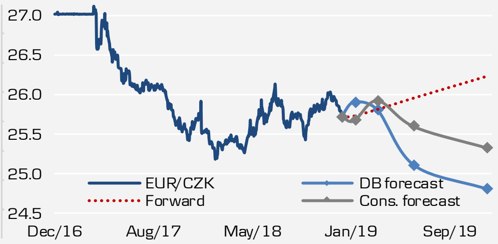


	1M	3M	6M	12M
DB forecast	322.60	321.00	317.00	310.00
Forward	322.23	322.54	323.00	324.52
Cons. forecast	326.06	327.94	327.78	326.07

Price indicators



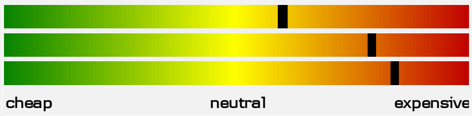
Currency	Instrument: Income	Instrument: Expenses	Forecast
CZK	We recommend hedging CZK income via knock-in forwards.	We recommend hedging CZK expenses via FX forwards.	



	1M	3M	6M	12M
DB forecast	25.90	25.80	25.10	24.80
Forward	25.74	25.82	25.96	26.23
Cons. forecast	25.67	25.93	25.60	25.33

Price indicators

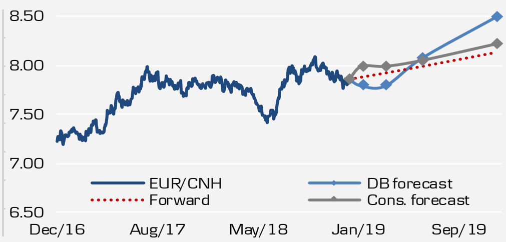
Implied volatility
Risk reversal (CZK seller)
Forward rate (CZK seller)



Source: Danske Bank

Danske Bank's hedging recommendations: other emerging markets

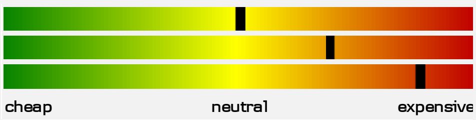
Currency	Instrument: Income	Instrument: Expenses	Forecast
CNH (CNY)	We recommend hedging CNY-denominated income using FX forwards, as we are more bearish on the CNY than the market.	Hedge CNY-denominated expenses via risk reversals to profit from any further CNY weakening	



	1M	3M	6M	12M
DB forecast	7.80	7.80	8.08	8.50
Forward	7.88	7.92	7.99	8.13
Cons. forecast	7.99	7.99	8.05	8.22

Price indicators

Implied volatility
Risk reversal (CNH seller)
Forward rate (CNH seller)

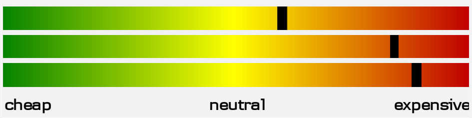


Currency	Instrument: Income	Instrument: Expenses	Forecast
ZAR	We recommend hedging ZAR income via FX forwards.	We recommend hedging ZAR expenses via knock-in forwards.	

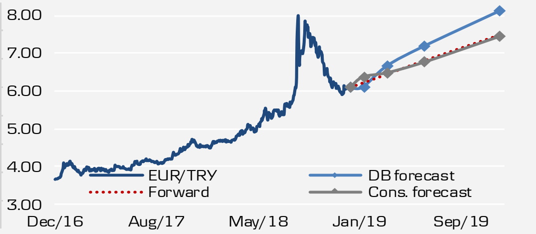
	1M	3M	6M	12M
DB forecast	16.10	16.95	17.11	17.81
Forward	16.36	16.56	16.88	17.57
Cons. forecast	16.30	16.37	16.26	16.45

Price indicators

Implied volatility
Risk reversal (ZAR seller)
Forward rate (ZAR seller)



Currency	Instrument: Income	Instrument: Expenses	Forecast
TRY	We recommend hedging TRY income in 2019 via FX Forwards	We recommend hedging TRY expenses via risk reversals.	



	1M	3M	6M	12M
DB forecast	6.10	6.67	7.20	8.13
Forward	6.20	6.43	6.81	7.49
Cons. forecast	6.36	6.47	6.76	7.45

Price indicators

Source: Danske Bank

FX forecasts

Core – major

Core Majors

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
EUR	17-Dec			1.13		746.7		1025.1		977.9	
	+3M			1.13	1.15	745.5	746.2	1010.0	1028.2	940.0	992.3
	+6M			1.18	1.16	745.5	745.8	1000.0	1029.8	920.0	996.4
	+12M			1.25	1.17	745.5	744.9	1000.0	1029.8	910.0	1005.1
USD	17-Dec	1.13				658.7		904.2		862.6	
	+3M	1.13	1.15			659.7	651.0	893.8	897.0	831.9	865.7
	+6M	1.18	1.16			631.8	645.4	847.5	891.2	779.7	862.3
	+12M	1.25	1.17			596.4	634.3	800.0	877.0	728.0	855.9
JPY	17-Dec	128.1		113.0		5.83		8.00		7.63	
	+3M	127.7	127.9	113.0	111.6	5.84	5.83	7.91	8.04	7.36	7.76
	+6M	134.5	127.9	114.0	110.8	5.54	5.83	7.43	8.05	6.84	7.79
	+12M	143.8	128.0	115.0	109.0	5.19	5.82	6.96	8.05	6.33	7.85

Source: Macrobond Financial, Danske Bank

Wider CEE

Danske Bank CEE forecast

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
PLN	17-Dec	4.28		3.78		174.5		239.5		228.5	
	+3M	4.26	4.31	3.77	3.76	175.0	173.3	237.1	238.8	220.7	230.4
	+6M	4.22	4.33	3.58	3.75	176.7	172.2	237.0	237.9	218.0	230.1
	+12M	4.18	4.38	3.34	3.73	178.3	170.2	239.2	235.3	217.7	229.7
HUF	17-Dec	323.1		285.0		2.31		3.17		3.03	
	+3M	321.0	323.3	284.1	282.0	2.32	2.31	3.15	3.18	2.93	3.07
	+6M	317.0	323.6	268.6	280.0	2.35	2.30	3.15	3.18	2.90	3.08
	+12M	310.0	325.0	248.0	276.8	2.40	2.29	3.23	3.17	2.94	3.09
CZK	17-Dec	25.77		22.74		28.97		39.77		37.94	
	+3M	25.80	25.83	22.83	22.53	28.90	28.90	39.15	39.82	36.43	38.42
	+6M	25.10	25.97	21.27	22.47	29.70	28.72	39.84	39.65	36.65	38.37
	+12M	24.80	26.22	19.84	22.33	30.06	28.41	40.32	39.28	36.69	38.34

Source: Macrobond Financial, Danske Bank

CIS

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
RUB	17-Dec	75.61		66.70		9.88		13.56		12.93	
	+3M	81.36	77.51	72.00	67.62	9.16	9.63	12.41	13.27	11.55	12.80
	+6M	87.08	79.06	73.80	68.42	8.56	9.43	11.48	13.03	10.56	12.60
	+12M	93.88	82.50	75.10	70.26	7.94	9.03	10.65	12.48	9.69	12.18

Source: Macrobond Financial, Danske Bank

MEA

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
TRY	17-Dec	6.11		5.39		122.2		167.8		160.1	
	+3M	6.67	6.45	5.90	5.62	111.8	115.8	151.5	159.5	141.0	153.9
	+6M	7.20	6.82	6.10	5.90	103.6	109.4	138.9	151.0	127.8	146.1
	+12M	8.13	7.50	6.50	6.39	91.8	99.3	123.1	137.3	112.0	134.0
ZAR	17-Dec	16.32		14.39		45.8		62.8		59.9	
	+3M	16.95	16.58	15.00	14.47	44.0	45.0	59.6	62.0	55.5	59.8
	+6M	17.11	16.91	14.50	14.63	43.6	44.1	58.4	60.9	53.8	58.9
	+12M	17.81	17.59	14.25	14.98	41.9	42.4	56.1	58.6	51.1	57.1

Source: Macrobond Financial, Danske Bank

Latin America

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
BRL	17-Dec	4.43		3.91		168.5		231.3		220.7	
	+3M	4.12	4.50	3.65	3.93	180.7	165.8	244.9	228.5	227.9	220.5
	+6M	4.19	4.57	3.55	3.95	178.0	163.2	238.7	225.4	219.6	218.1
	+12M	4.13	4.71	3.30	4.01	180.7	158.1	242.4	218.5	220.6	213.3

Source: Macrobond Financial, Danske Bank

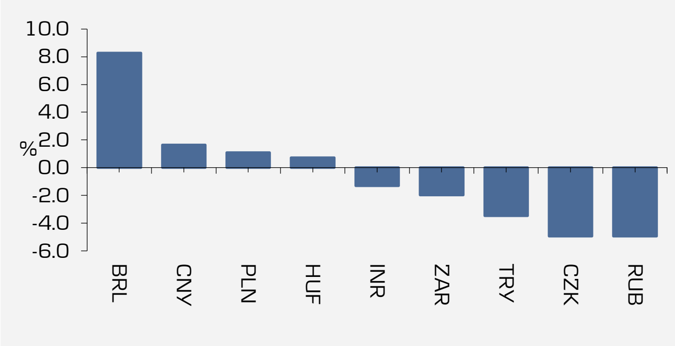
Emerging markets Asia

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
CNY	17-Dec	7.82		6.90		95.5		131.1		125.1	
	+3M	7.80	7.93	6.90	6.91	95.6	94.2	129.5	129.7	120.6	125.2
	+6M	8.08	8.00	6.85	6.92	92.2	93.2	123.7	128.7	113.8	124.5
	+12M	8.50	8.14	6.80	6.94	87.7	91.5	117.6	126.4	107.1	123.4
INR	17-Dec	81.16		71.59		9.20		12.63		12.05	
	+3M	82.49	81.63	73.00	71.21	9.04	9.14	12.24	12.60	11.40	12.16
	+6M	84.96	83.21	72.00	72.01	8.77	8.96	11.77	12.38	10.83	11.97
	+12M	88.75	86.32	71.00	73.51	8.40	8.63	11.27	11.93	10.25	11.64

Source: Macrobond Financial, Danske Bank

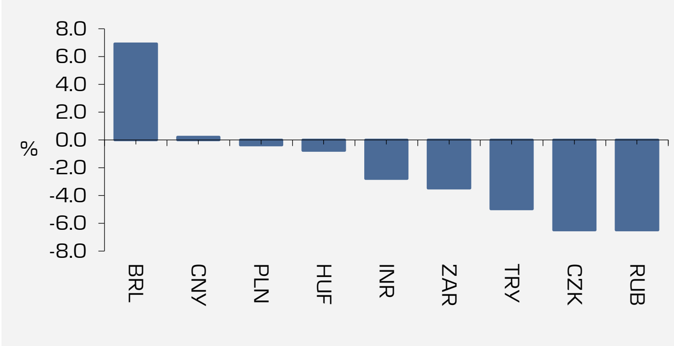
Forecasts vs forwards

3M – base currency EUR



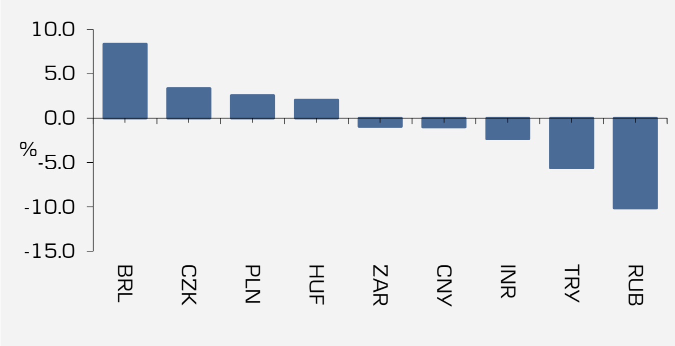
Source: Macrobond Financial, Danske Bank

3M – base currency USD



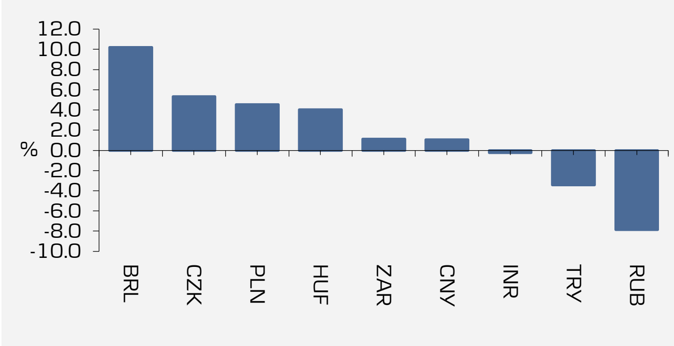
Source: Macrobond Financial, Danske Bank

6M – base currency EUR



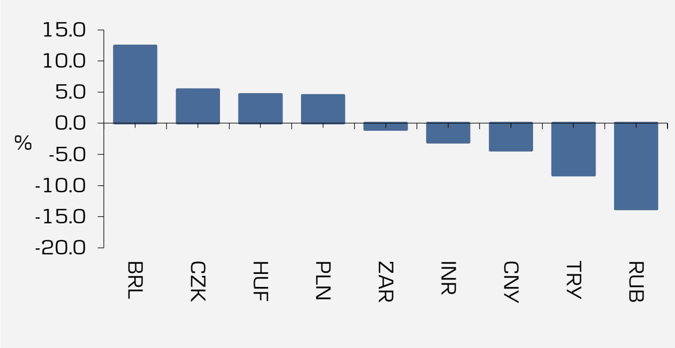
Source: Macrobond Financial, Danske Bank

6M – base currency USD



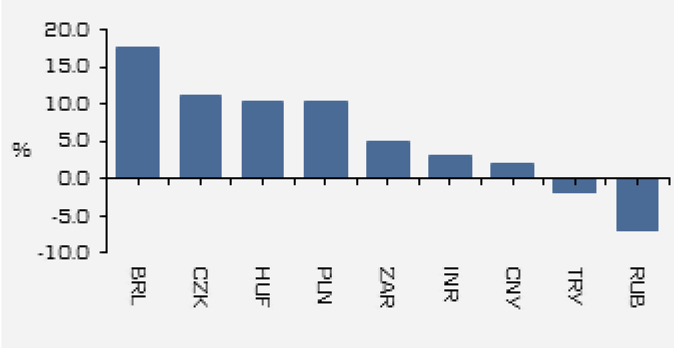
Source: Macrobond Financial, Danske Bank

12M – base currency EUR



Source: Macrobond Financial, Danske Bank

12M – base currency USD



Source: Macrobond Financial, Danske Bank

Monetary policy calendar

Calendar

	Policy Rate (%)	Latest Change		Next Change		Next Meeting	Year-end 2019 (%)
	19 December 2018						
Wider CEE							
PLN	1.50	- 50 bp	Mar, 2015	+25bp	Q2, 2019	09/01/2019	1.75
HUF	0.90	- 15 bp	May, 2016	+25bp	Q2, 2019	29/01/2019	1.15
CZK	1.75	+25 bp	Nov, 2018	+25bp	H2, 2019	20/12/2018	2.25
TRY	24.00	+625bp	Sep, 2018	-100bp	H1, 2019	16/01/2019	17.75
CIS							
RUB	7.75	+25bp	Dec, 2018	+25bp	H1, 2019	08/02/2019	8.00
MEA							
ZAR	6.75	+25bp	Nov, 2018	-25bp	H1, 2019	17/01/2019	6.25
LATAM							
BRL	6.50	-25 bp	Mar, 2018	+25bp	H2, 2019	06/02/2019	6.75
EM Asia							
CNY	4.35	- 25 bp	Oct, 2015	-25bp	Q1, 2019	No regular meetings	4.10
INR	6.50	+ 25 bp	Aug, 2018	+ 25 bp	Q3, 2019	06/02/2019	6.75

Source: Bloomberg, Danske Bank

Disclosures

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Expected updates

Ad hoc.

Date of first publication

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