Emerging Markets View

September 2018: House of Cards

EM currencies have stabilised somewhat since the latest edition of the Emerging Markets View, not least due to significant support from the central banks of Turkey, Argentina and Russia. Most emerging markets remain vulnerable and several vicious cycles are still at play that could spark a fresh round of sell-offs. 1) FX weakness will pass through to higher inflation and, in turn, to lower growth, adding to the risk of more FX weakness. 2) FX weakness will make USD debt tougher to finance and service, increasing the risk of further FX weakness. 3) Crisis countries pose a contagion risk through trade and financial linkages as well as owing to the adverse impact on general emerging market sentiment.

This Emerging Markets View takes a look at the vulnerability related in particular to FX-denominated debt.

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CNY: Devaluation unlikely but not impossible

Interventions are likely to mitigate persistent selling pressure on the CNY unless the trade war escalates.

RUB: Adjusting to a new normal

Sanctions risks will remain high in October and November, but the RUB weakening has already reached the central bank's tolerance and a 25 bp rate hike has made a clear distinction between central bank independence in Russia and Turkey.

PLN: Political risks are rising

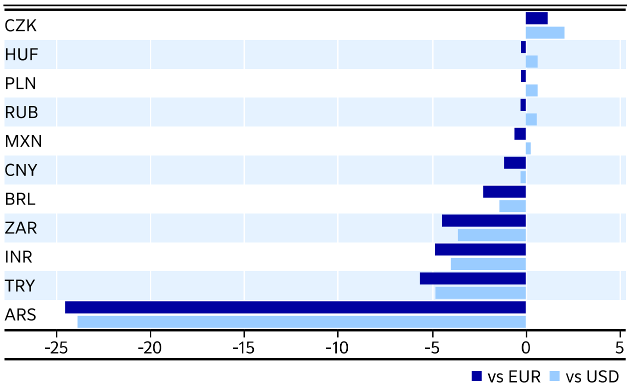
Key drivers could change from general sentiment to political risks. The Article 7 process and local elections are most pressing, but Poland will also receive far less EU funding in the future.

In focus – ARS: First to fold

There is no easy solution in sight. The ARS is likely to suffer further while authorities continue to take measures to restore confidence.

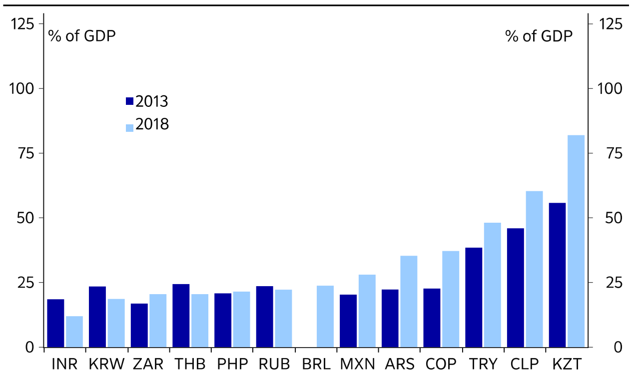
FX hedging considerations, the EM Traffic Light and Financial forecasts are also covered in this edition of Emerging Markets View.

EM FX PERFORMANCE SINCE LAST EM VIEW



Source: Nordea and Macrobond

FX-DENOMINATED EXTERNAL DEBT



Source: Nordea and Macrobond

House of Cards

Following months of severe emerging market (EM) FX sell-offs, some EM countries are starting to look quite vulnerable in terms of their FX-denominated debt. At the same time, concerns about the contagion risks emanating from crisis countries are rising.

Contagion risks are rising

The financial markets are getting more and more concerned about the contagion risks emanating from the meltdowns in Turkey (TRY) and Argentina (ARS). Contagion would likely mainly be via trade links, which could prompt competitive devaluations, and via cross-border financial links. Contagion would also come from the massive general EM FX sell-off in recent months, which is particularly concerning for countries with a large share of FX-denominated debt. This is the topic of this month's Emerging Markets View.

Rising external debt burden

The costs of USD financing for EM countries are rising. According to Bloomberg Barclays' EM USD Aggregate, yields have risen from 4.5% at the beginning of the year to 6%. Firstly, we attribute this to the Fed's monetary tightening having pulled capital back to the US and out of emerging markets, and lowered general demand for EM assets. EM corporate and sovereign bond placements this summer have, for example, been the lowest since 2013. The second main cause we see is general EM risk premiums having increased significantly, not least due to the crisis countries.

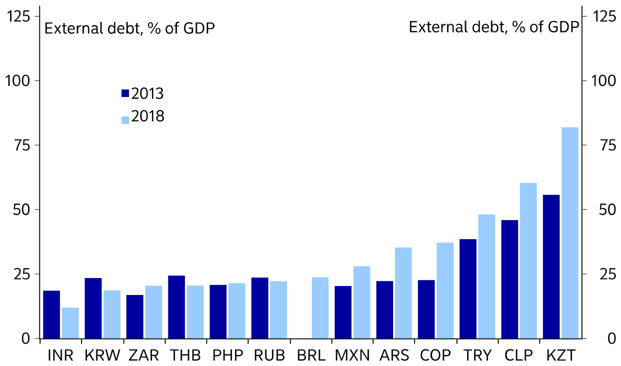
Who's next?

Contagion risks from FX-denominated debt have increased somewhat since the taper tantrum in 2013, judging by FX-denominated debt levels and the higher reliance on shorter-term external debt. Several currencies, apart from the TRY and ARS, look quite vulnerable to us , according to three measures of vulnerability related to FX-denominated debt: 1) The KZT (Kazakhstan), CLP (Chile) and COP (Columbia)have very high levels of FX-denominated debt relative to GDP (see chart). 2) South Africa (ZAR) has a relatively high share of short-term external debt relative to exports, though much less than Argentina and Turkey (see chart). 3) FX reserves of the ZAR and CLP are too low (see chart). Other currencies still enjoy pretty sizeable buffers. EM countries with tougher external debt profiles are thus high on the list of the next potential victims.

Similar evidence from EM traffic light

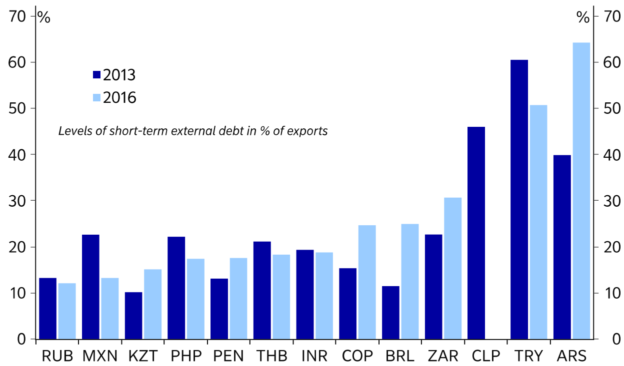
Our EM Traffic Light supports these findings. In August, the biggest changes in risk level occurred for the ZAR (+5 points) and for the CLP (+5 points). Both currencies have a yellow warning light, while the KZT and COP are still green. The fundamental risks for EM as a whole are still moderate but are increasing and will likely continue to do so given the persistent internal and external shocks.

FX-DENOMINATED DEBT IS HIGH IN KAZAKHSTAN AND CHILE



Source: Nordea, Worldbank and Macrobond

TRY AND ARS AT RISK FROM S-T EXTERNAL DEBT/EXPORTS

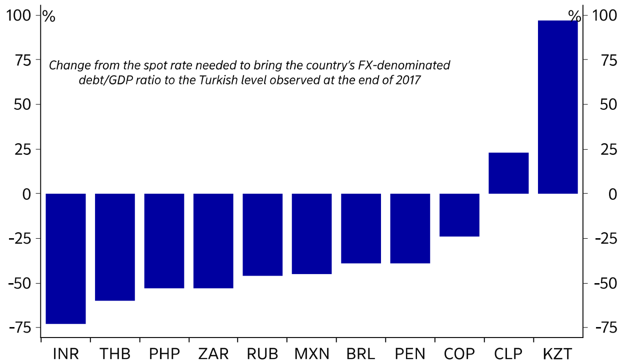


Source: Nordea, Worldbank and Macrobond

Turkish threshold is still far

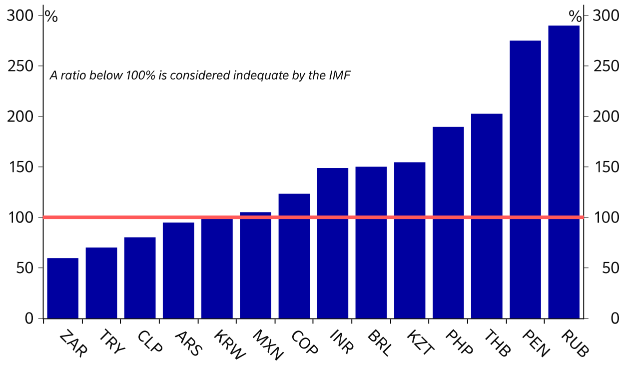
The Turkish and Argentine experiences show us that even moderate levels of FX-denominated debt can become troublesome if the domestic currency weakens enough. A weaker currency and rising FX-denominated debt can easily go into a vicious cycle. Turkey started the year with FX-denominated debt-to-GDP of 52%, which was already seen as a substantial risk. The levels in Kazakhstan and Chile were even above the Turkish level. For most EM countries, a lot of FX weakening will be needed to reach the same level of FX-denominated debt-to-GDP as Turkey (see chart). The least is needed for Columbia and Peru (PEN).

MOST CURRENCIES STILL HAVE TO DEPRECIATE A LOT TO REACH TURKISH DEBT BURDEN LEVELS



Source: Nordea, World Bank and Macrobond

RESERVE ADEQUACY RATIO (IMF METHODOLOGY)



Source: Nordea, IMF and Macrobond

Sanctions channel

The CIS region has also started showing some signs of contagion, but through a different channel. Rising sanctions risks in Russia put the RUB under pressure in September, and this spilled over to some of the CIS currencies. Notably, the KZT and BYR (Belarus) have faced higher devaluation pressure, reflecting the fact that the Kazakh and Belarus economies are closely linked to Russia. The CIS currencies may face more challenges with stronger geopolitical pressure on Russia.

Decisive response

Since our August Emerging Markets View, the monetary policy stance has been tightened in several countries. The Central Bank of Argentina proceeded to a policy rate hike to 60%, the Central Bank of Turkey delivered a surprise and much needed policy rate hike of 625 bp and the Russian Central Bank decided to show its commitment to inflation with a 25 bp policy rate hike. While these hikes are unlikely to completely erase investor concerns, the actions show increasing readiness to react in an orthodox manner to the rising risks and are likely to mitigate some of the market worries.

Risks are numerous

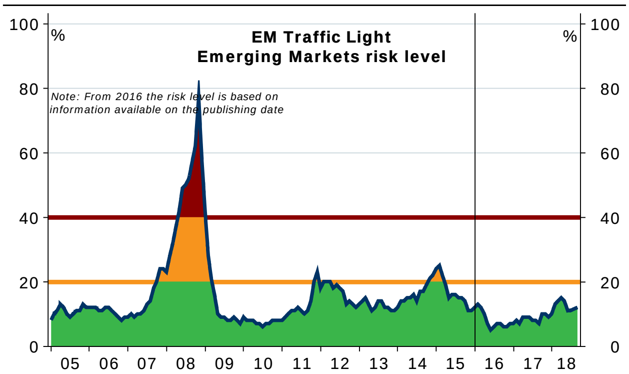
The risks remain high, but most probably, EM currencies will keep on muddling through for the time being. However, there are a number of risks that could darken the outlook even more: a further escalation of trade tensions, rising political risks linked to elections, much slower growth, and weaker commodity prices.

Forecasts broadly unchanged

We leave our EM FX forecasts broadly unchanged compared to the latest Emerging Markets View. Our list of potential new victims of contagion is significant and the outlook for EM FX remains rather bleak, in our view. Continued Fed tightening and capital outflows are likely to put further pressure on the EM currencies, but we expect a gradual recovery in 2019. Following Turkish and Russian surprise hikes we now forecast a more hawkish monetary stance from the EM central banks.

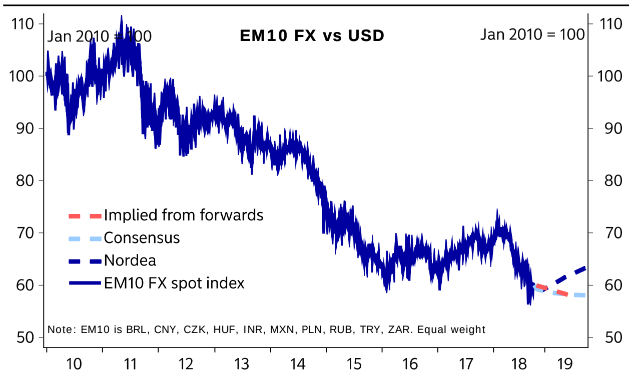
By Tatiana Evdokimova

RISING RISKS FROM LOW LEVELS



Source: Nordea and Macrobond

FORECASTING SLIGHT RECOVERY



Source: Nordea estimates and Macrobond

CNY: Devaluation unlikely, not impossible

More selling pressure on the CNY will likely be countered by PBoC intervention. Devaluation could happen if the trade war escalates significantly, but that is not likely at the moment. A sustained devaluation could spell contagion risk to other emerging-market currencies.

Market weakening pressure offset by PBoC interventions

Despite the continued general EM sell-off during the past month, the CNY has been stable around 6.85 against the USD. Weakening pressure from trade war concerns did not ease, but the CNY took comfort in the PBoC's intensified interventions.

Noticeably, the counter-cyclical factor was reintroduced to USD/CNY fixings in August. On paper, this factor supposedly corrects any directional bias from the market. In reality, a lack of transparency with regards to how it is calculated provides the PBoC with flexibility to set any USD/CNY fixing rate as it sees fit, and it has been used to guide the USD/CNY spot rate lower.

Little contagion risk to the CNY

As an EM currency, the fortune of the CNY is to some extent tied to the general EM sentiment, although the CNY is not that vulnerable to contagion risks. Although China is flirting with a current account deficit at the moment, its external balances remain solid. Its gross foreign debt accounts for 15% of GDP and about half of FX reserves.

The CNY is more likely to spread risk to other EM FX

We see the CNY more as a source of contagion. Trade war escalation would add more stress on the CNY, emanating to other EM currencies.

Devaluation is a risk scenario…

In our previous EM View, we highlighted reasons why the Chinese authorities have no interest in a much weaker CNY. For now, we consider devaluation a risk scenario.

…that could happen if the trade war escalates further

Devaluation could take place if the US levies tariffs again after this week's 200bn escalation, and even more so if Trump continues talking down the USD, which he has tried repeatedly. Any attempt from the US to influence the USD would give Beijing justification to do the same or simply stop defending the CNY and letting the market drive it lower.

By Amy Yuan Zhuang

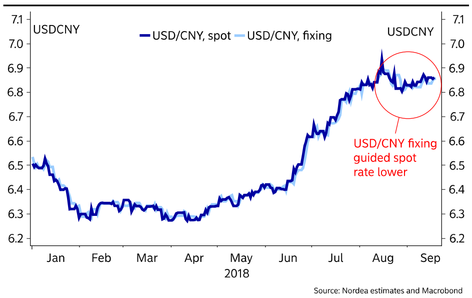
RISK FACTORS

- Trade war escalations
- Devaluation / capital outflows
- Delaying deleveraging

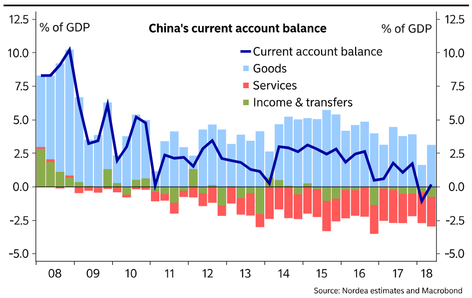
EM TRAFFIC LIGHT

- Risk level: 15% (green, +1 pp from previous month)
- Trade war risks not included in the model

THE PBOC INTERVENES THROUGH FIXING



WORSENING CURRENT BALANCE



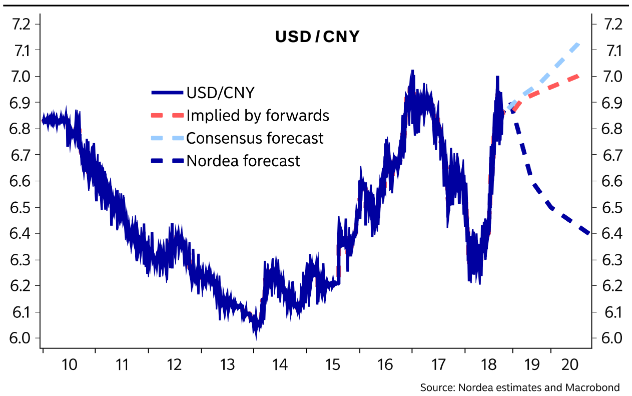
FINANCIAL FORECASTS – CHINA

Selling pressure on the CNY will likely persist for a while, as the trade war remains unsettled and sentiment towards EM is negative. Market pressure is expected to be countered by PBoC interventions to keep the CNY within 6.8-6.9 of the USD. If we are right about the USD rally losing steam before the end of the year, the CNY could be strengthened as quickly as it was weakened.

Forecasts	Spot	3M	Mid-2019	End-2019	End-2020
USD/CNY	6.86	6.90	6.60	6.50	6.40
Policy rate	4.35	4.35	4.35	4.35	4.35

Source: Nordea estimates

USD/CNY FORECAST



RUB: Adjusting to a new normal

RUB risks remain tilted to the downside, as sanctions threats are still relevant. October and November look risky, but we find the longer-term outlook positive given robust fundamentals for the Russian economy.

Waiting for sanctions to concretise

The RUB continues to be driven purely by geopolitics, reacting mostly to sanctions news. September brought virtually no clarity. The DASKAA bill, introducing “sanctions from hell” (a definition coined by the author of the bill), is still under consideration in the US Congress. A combination of sanctions on sovereign debt and oligarchs is viewed by the senators as the most efficient way to proceed. As such, these changes to the current sanctions regime are highly likely; more extreme scenarios, with restrictions for state-owned banks, will probably not materialise. The implementation timeline is uncertain, but October and November are likely to bring more concrete news and more market volatility. The RUB may well face more pressure during the autumn, but the extent of this will almost solely depend on the wording of the sanctions.

CBR keeps the situation under control

The RUB's weakness has reached the tolerance level of the CBR. In August-September, the currency was losing up to 10%, thereby causing inflation forecasts to deviate substantially from the 4% target (to 5.0-5.5%). Not waiting for the Turkish scenario to materialise, the CBR lifted the key rate by 25 bp and issued a much more hawkish press release. FX purchases made in accordance with the budget rule have been suspended until year-end to avoid additional market volatility, thereby removing demand for around USD 20bn from the market until then. Emergency measures (eg FX repo, direct sovereign debt purchases, regulatory exemptions for banks) may be rapidly activated if needed. More rate increases, including emergency ones, are likely until the end of the year if RUB pressure persists.

Resilient to threats

So far, Russia's financial stability is not threatened. Ample FX reserves (USD 460bn) easily cover short-term external debt (USD 60bn) or FX-denominated deposits of households (around USD 89bn). Still, devaluation expectations are now at their highest (50% of those surveyed) since the start of the survey's history in 2013, and deposits showed a minor drop in August (-0.6%). Businesses are trying to prepare for harsh sanctions considering changes in the FX payments structure.

By Tatiana Evdokimova

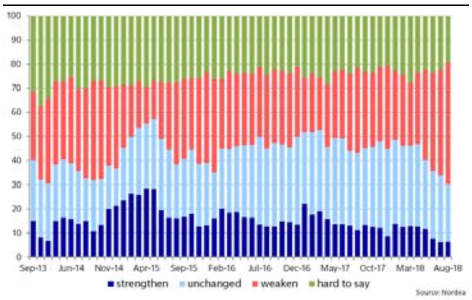
RISK FACTORS

- Tougher sanctions from the US
- European support for sanctions
- Higher devaluation expectations and bank runs

EM TRAFFIC LIGHT

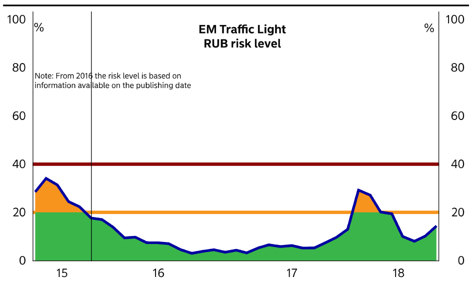
- Risk level: 16% (green, +2 pp from the previous month)
- Sanctions are the main risk

RECORD-WEAK RUB EXPECTATIONS



Source: Nordea

ROBUST FUNDAMENTALS



Source: Nordea and Macrobond

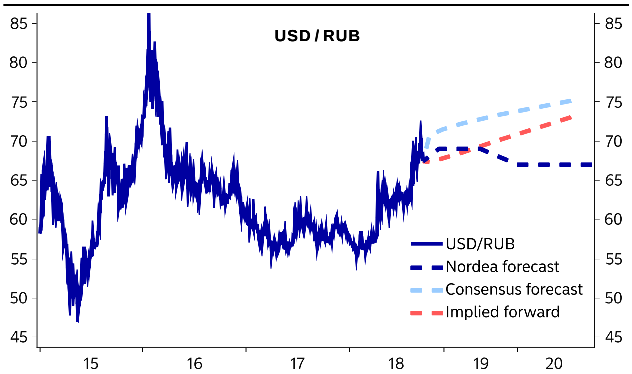
FINANCIAL FORECASTS — RUSSIA

Lots of foreign investors exited the Russian market in August-September, causing the RUB to tumble. Once the new sanctions regime is announced, lower uncertainty will likely increase the appetite for the Russian risks. Exceptionally strong Russian fundamentals will tempt foreigners to return, helping the RUB to recover in 2019E. However, harsh sanctions and RUB pressure remain non-negligible tail risks. Rates are likely to climb further as inflation pressure is rising.

Forecasts	Spot	3M	Mid-2019	End-2019	End-2020
USD/RUB	67.4	69.0	69.0	67.0	67.0
Policy rate	7.50	7.75	7.50	7.25	6.75

Source: Nordea estimates

USD/RUB FORECAST



Source: Nordea estimates and Macrobond

PLN: Political risks are rising

While general market sentiment is the main driver of the Polish zloty (PLN), politics is next in line. Thus, Poland's clash with the EU keeps weighing on the Polish zloty.

The EU and Juncker fully support the Article 7 process against Poland

Besides lingering EM woes, rising political risks are the main drivers of EUR/PLN. One key issue is Poland's clash with the EU on the rule of law dispute. According to the EU, Poland has breached the EU's democracy values with the substitution of Supreme Court judges. In September, tensions mounted as the EC President, Jean-Claude Juncker, gave his full support to the Article 7 process against Poland. With Juncker's support, any doubt about whether the EU would try to not add fuel to the eurosceptic fire ahead of the European Parliament election in May 2019 has now been removed.

Lower EU funding is the real threat

Although it is unlikely that the Article 7 process will actually lead to a loss of voting rights (as Hungary would veto), Juncker's support is a signal that EU funding after 2020 could be more linked to adhering to the rule of law. As Poland is a big net beneficiary of cohesion funding, this constitutes the real threat. As a result, lower EU funding would hamper public investments and the current account, which in turn would weigh on Poland's credit rating and ultimately the zloty.

Net external debt level is trending down, but remains a significant risk factor

Another risk factor for the PLN and Poland's credit rating is the high share of external debt. Poland has around 30% of net external debt (~70% gross) while almost 35% of the general government debt is denominated in foreign currencies. In addition, the share of CHF-denominated loans in the corporate sector and among households is still relatively high.

Although the level of debt has decreased slightly in recent years, Poland is still exposed to external shocks – a risk that consequently attracts a lot of political attention. Thus, prudent fiscal policy and a reduction in debt top the economic agenda. In terms of the CHF-denominated loans, President Duda has vowed to legislate in favour of the troubled CHF borrowers. The bill, which will likely be at the cost of the local banks, is speculated to be adopted this autumn.

The ruling PiS party is increasing its lead in local election polls

A final looming political risk is the local election on 21 October. Polls indicate that the ruling PiS-party could win 10 out of 16 provinces (up from 5). Such a win would cement PiS' power, create headaches in Brussels and put downward pressure on the PLN.

By Morten Lund

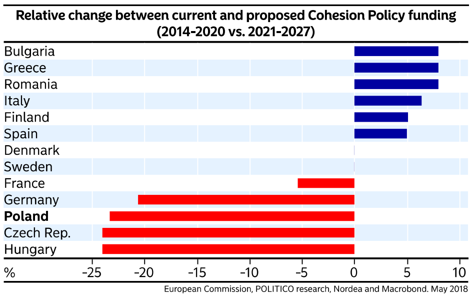
RISK FACTORS

- Weak EM sentiment
- Politics
- Low core inflation/dovish NBP

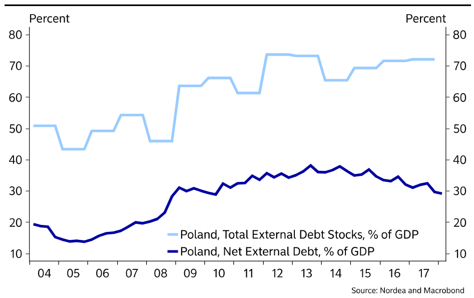
EM TRAFFIC LIGHT

- Risk level: 15% (green, -1 pp from previous month)

LOWER EU FUNDING LOOKS INEVITABLE



EXTERNAL DEBT EXPOSURE STILL HIGH



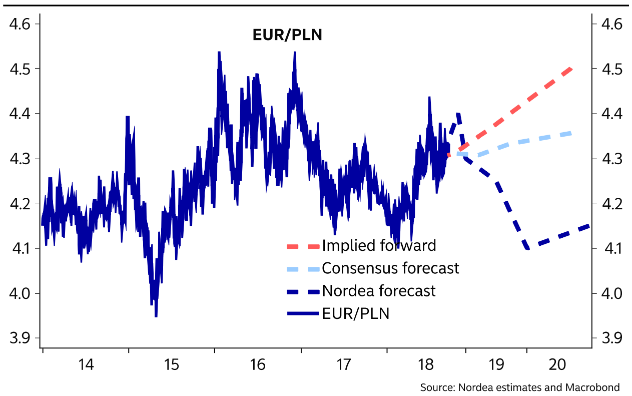
FINANCIAL FORECASTS – POLAND

Due to a combination of lukewarm market sentiment, a dovish central bank and rising political uncertainty, we still expect the EUR/PLN to keep testing levels up to 4.40 in the short term. However, we do not expect a move above 4.40, as Eurozone economic indicators have stabilised lately. Longer out, we expect a mild PLN appreciation as market tensions cool off and the NBP gets closer to a rate hike.

Forecasts	Spot	3M	Mid-2019	End-2019	End-2020
EUR/PLN	4.29	4.40	4.25	4.10	4.15
Policy rate	1.50	1.50	1.50	1.75	2.00

Source: Nordea estimates

EUR/PLN



ARS: First to fold

The ARS is the worst performing emerging market currency this year, having declined by more than 50% against the USD year-to-date. USD-denominated debt is a problem and a recession in Argentina in 2018 seems likely. Devaluation risks have become default risks.

Fiscal imbalances have become a major problem

The ARS has sold off massively and is the worst performing currency of the year. The reasons include severe fiscal imbalances and heavy reliance on external financing. The current account deficit is around 5% of GDP and the primary fiscal deficit is more than 3% of GDP. To cover this twin deficit, external borrowing has grown rapidly and fiscal imbalances have led to a vicious circle of high inflation and a weakening ARS.

Argentina's debt is one of the highest in the emerging markets

While Argentina's general government debt in relation to GDP is much lower than before the 2008 financial crisis, the debt level is one of the highest in the emerging markets. Another problem lies in the private sector, which has over USD 50bn in USD-denominated debt compared to USD 5bn in ARS-denominated debt, prompting another vicious cycle between rapid FX devaluation and higher FX-denominated debt.

When the ARS weakened significantly and short-term liquidity risks were rising, Argentina was forced to seek help from the IMF in mid-May and the IMF has agreed a USD 50bn credit line to Argentina.

Recession in Argentina in 2018 seems likely

The Central Bank of Argentina (BCRA) has made several attempts at stabilising the ARS to contain the pass-through to even higher inflation. Policy rate hikes and USD-selling have so far not had any major stabilising effect, and the FX reserves have shrunk by 20% since June, which limits the BCRA's ability to defend the ARS. After Argentina sought help from the IMF, the economy minister presented a tight budget to calm the markets. We expect that the tight budget, high inflation, 60% policy rate and weak ARS will all lead to a hard landing, and a recession in 2018 seems likely, to us.

ARS will continue to suffer

Argentina has been the first to fold as a reaction to higher US rates and a stronger USD. There is no easy way out. We argue that the ARS will continue to suffer and the authorities will continue to take measures to restore confidence.

By Kristian Nummelin

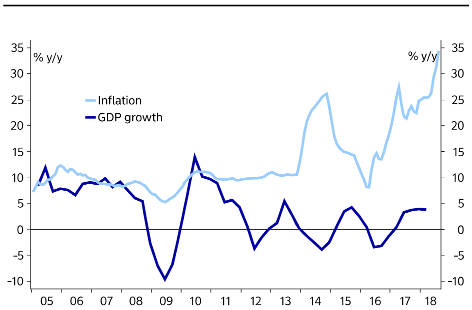
RISK FACTORS

- Economy will face a hard landing
- Large twin deficits
- External debt

EM TRAFFIC LIGHT

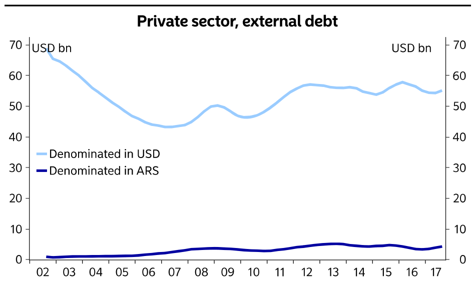
- Risk level: 9% (green, unchanged from previous month)

INFLATION IS OVERSHOOTING



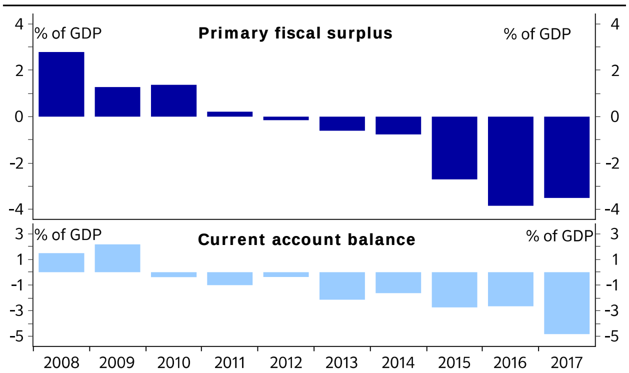
Source: Nordea Markets and Macrobond

USD-DENOMINATED DEBT IS A PROBLEM



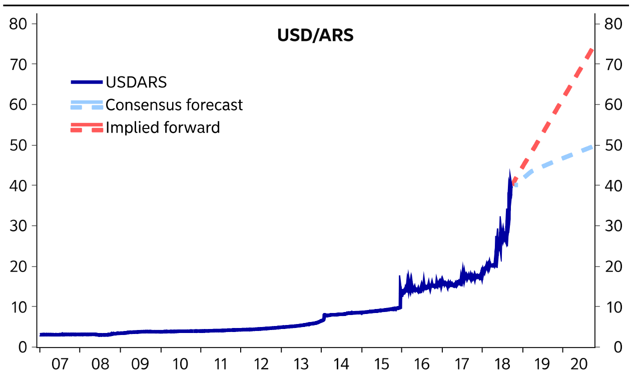
Source: Nordea and Macrobond

ARGENTINA SUFFERS FROM A WIDE TWIN DEFICIT



Source: Nordea and Macrobond

USD/ARS



Source: Nordea and Macrobond

Hedging considerations

CNY (vs EUR)

Income

Middle hedge ratio in the short term, using mainly FX forwards. Middle to high hedge ratio in the long term – high share of zero-cost option strategies, eg participating forwards.

Expenses

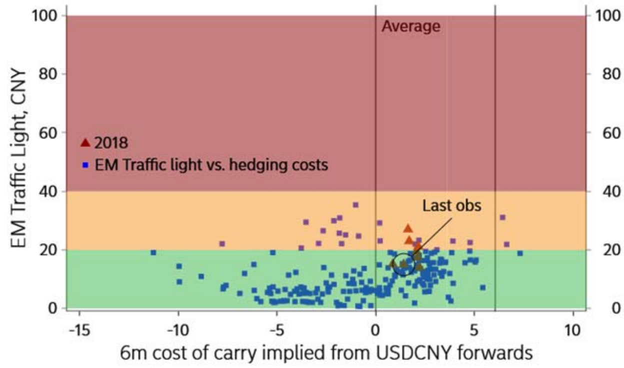
Middle hedge ratio in the short term, using a mix of FX forwards and zero-cost strategies. High hedge ratio in the long term, using FX forwards and benefiting from high forward premiums.

NORDEA ESTIMATES

Forecasts	Spot	3M	Mid-2019	End-2019	End-2020
EUR/CNY	8.00	8.00	7.85	8.00	8.19
Policy rate	4.35	4.35	4.35	4.35	4.35

Source: Nordea estimates

COST OF CARRY VS RISK LEVEL



Source: Nordea estimates and Macrobond

Implied ATM vol (6M)	25D RR (6M)	Forward (6m)
6.59	0.39	8.19

Source: Bloomberg

RUB (vs EUR)

Income

High hedge ratio in the short term, using mainly FX forwards. Middle to high hedge ratio in the long term, using a mix of FX forwards and zero-cost option strategies, eg forward extra.

Expenses

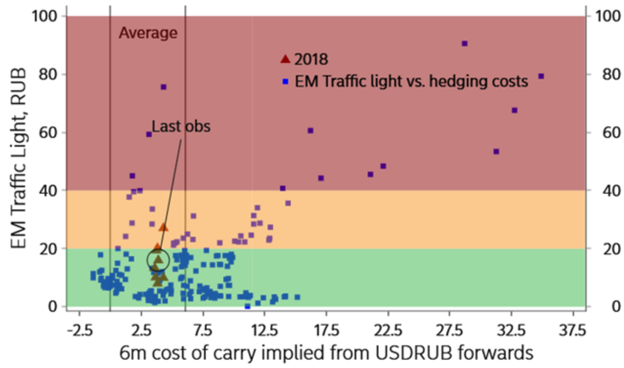
High hedge ratio in the short term, using a mix of forwards and zero-cost option strategies, eg risk reversals, benefiting from cheap RUB calls and expensive RUB puts.

NORDEA ESTIMATES

Forecasts	Spot	3M	Mid-2019	End-2019	End-2020
EUR/RUB	78.9	80.0	82.1	82.4	85.8
Policy rate	7.50	7.75	7.50	7.25	6.75

Source: Nordea estimates

COST OF CARRY VS RISK LEVEL



Source: Nordea estimates and Macrobond

Implied ATM vol (6M)	25D RR (6M)	Forward (6m)
14.92	4.67	81.1

Source: Bloomberg

PLN (vs EUR)

Income

High hedge ratio in the short term, using FX forwards. Low to middle hedge ratio in the long term – high share of zero-cost option strategies, eg participating forwards.

Expenses

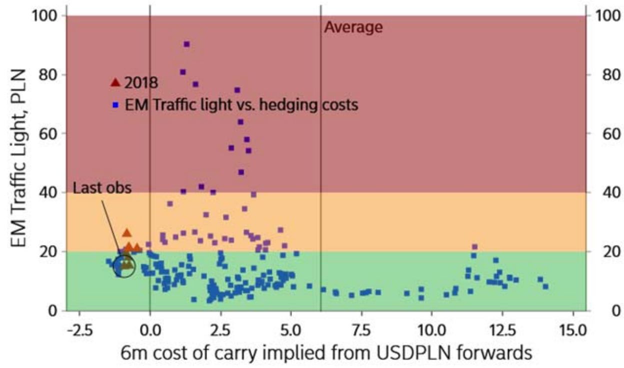
Middle hedge ratio in the short term, using FX forwards. High hedge ratio in the long term, using forwards mainly. Consider using zero-cost risk reversal option strategies – benefiting from RR biased towards EUR calls.

NORDEA ESTIMATES

Forecasts	Spot	3M	Mid-2019	End-2019	End-2020
EUR/PLN	4.31	4.40	4.25	4.10	4.15
Policy rate	1.50	1.50	1.50	1.75	2.00

Source: Nordea estimates

COST OF CARRY VS RISK LEVEL



Source: Nordea estimates and Macrobond

Implied ATM vol (6M)	25D RR (6M)	Forward (6m)
5.78	1.49	4.34

Source: Bloomberg

EM Traffic Light

EM TRAFFIC LIGHT

ISO	Country	Risk level	Credits	ST external debt	Inflation	GDP	Capital flows	Rating	FX overvaluation	Commodities	Contagion
TWD	Taiwan	26%									
CLP	Chile	25%									
ZAR	South Africa	23%									
ILS	Israel	22%									
HUF	Hungary	22%									
SAR	Saudi Arabia	22%									
TRY	Turkey	21%									
KRW	South Korea	20%									
CZK	Czech Republic	19%									
KES	Kenya	18%									
BRL	Brazil	18%									
SGD	Singapore	18%									
MXN	Mexico	18%									
HRK	Croatia	17%									
BGN	Bulgaria	17%									
RUB	Russia	16%									
RSD	Serbia	15%									
UAH	Ukraine	15%									
PLN	Poland	15%									
COP	Colombia	15%									
CNY	China	15%									
HKD	Hong Kong	15%									
PHP	Philippines	14%									
THB	Thailand	14%									
PEN	Peru	13%									
INR	India	12%									
RON	Romania	12%									
MYR	Malaysia	11%									
ARS	Argentina	9%									
IDR	Indonesia	8%									
KZT	Kazakhstan	5%									
NGN	Nigeria	4%									
EGP	Egypt	3%									
	EM general	12%									

*Note: **The risk level** is the probability of extreme currency pressure in at least one of the next six months, where extreme is a 2 standard deviation weakening (2.5% event). **Credits(+, change)** : The change in the ratio of money supply (M2) to GDP. **Short-term external debt(+, change)** : The ratio of short-term foreign claims on domestic banks over FX reserves. **Inflation (+, change)** : Change in CPI inflation . **GDP (-, change):** Change in real GDP growth. **Capital flows(-, level and +, change):** The level of and change in the ratio of net foreign assets to GDP. **Rating(+, change):** The change in the sovereign rating from S&P. **FX overvaluation(+, level):** The strengthening of FX spot not explained by relative CPI inflation and relative productivity growth. **Commodities (-, change):** The change in the commodities terms of trade, ie the change in export prices less the change in import prices. **Contagion (+, level):** the number of currencies under pressure plus a recent history of pressure on the currency in question.*

Source: Nordea estimates and Macrobond

Latest EM Traffic Light:

- EM Traffic Light: August 2018 (4 Sep)
- **New signals:** ZAR to yellow from green, HRK and BGN to green from yellow.
- **Biggest changes:** The biggest changes involve the HRK (-9 pp), the ZAR (+5 pp) and the CLP (+5 pp).

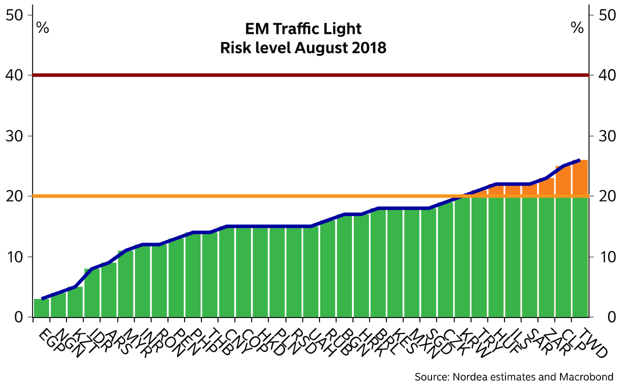
Methodology note:

- EM Traffic Light – methodology note

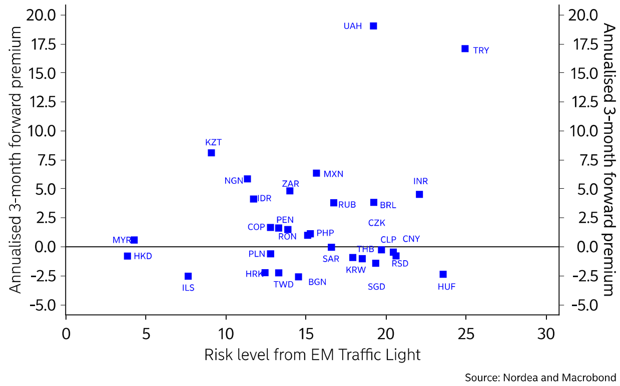
Track record:

- EM Traffic Light – Track record - August 2018

OVERALL RISK LEVEL

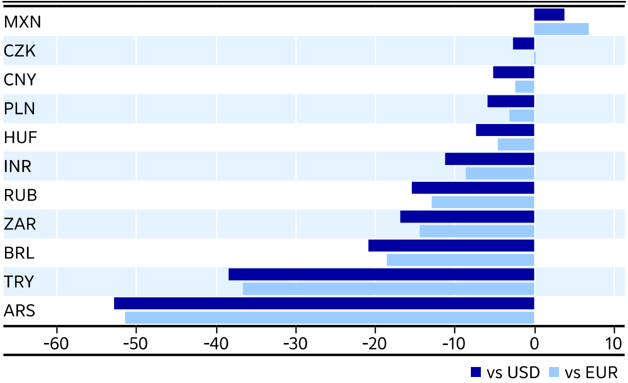


TRAFFIC LIGHT VS COST OF CARRY



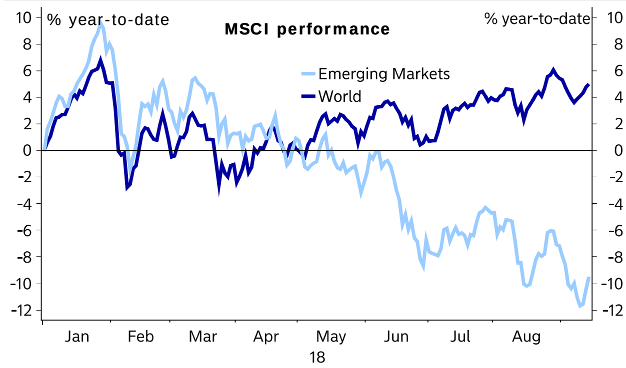
Emerging market performance

YTD EM FX PERFORMANCE



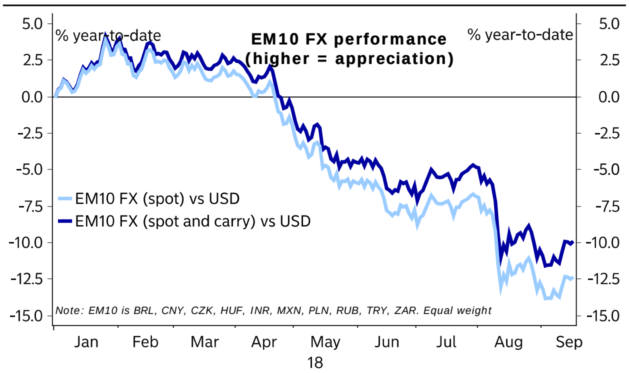
Source: Nordea and Macrobond

YTD EQUITIES PERFORMANCE



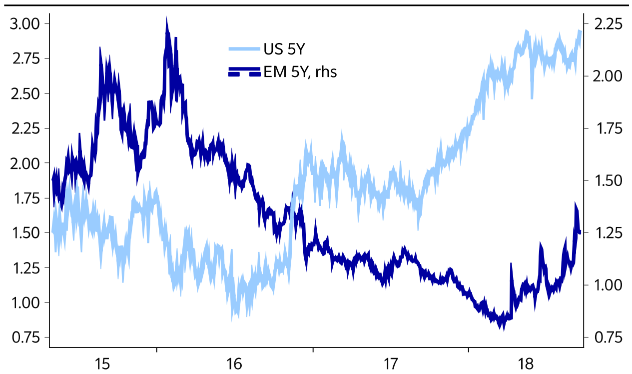
Source: Nordea and Macrobond

YTD FX PERFORMANCE CARRY ADJUSTED



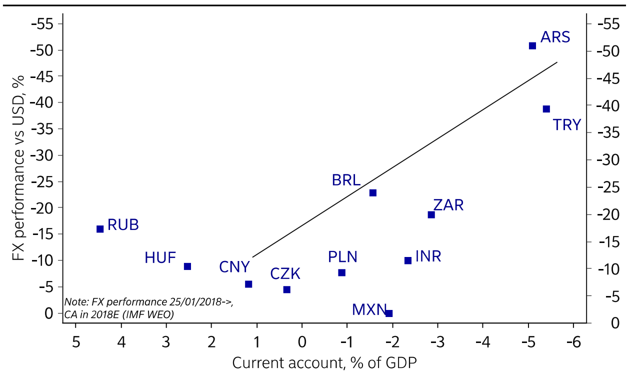
Source: Nordea and Macrobond

SWAPS



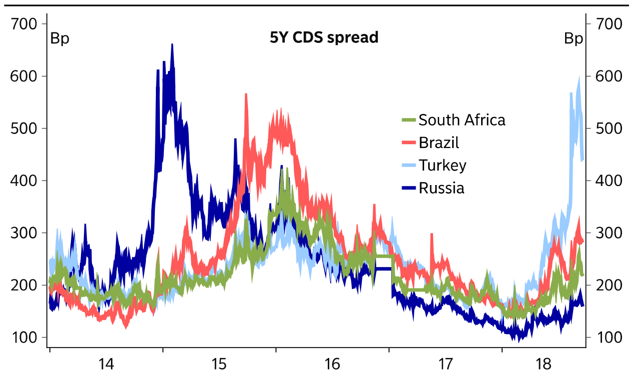
Source: Nordea and Macrobond

YTD FX PERFORMANCE VS CURRENT ACCOUNT



Source: Nordea Markets and Macrobond

CDS SPREADS



Source: Nordea estimates and Macrobond

Forecast overview

FX FORECASTS AGAINST EUR

	Spot	3M	Mid-2019	End-2019	End-2020
EUR/BRL	4.843	4.81	4.52	4.55	4.74
EUR/CNY	8.027	8.00	7.85	8.00	8.19
EUR/CZK	25.42	25.5	24.8	24.5	24.5
EUR/HUF	323.9	325	320	315	320
EUR/INR	85.09	84.7	83.3	83.6	84.5
EUR/PLN	4.294	4.40	4.25	4.10	4.15
EUR/MXN	21.96	23.2	21.4	20.9	21.8
EUR/RUB	78.9	80.0	82.1	82.4	85.8
EUR/TRY	7.434	7.60	7.90	8.20	8.60
EUR/ZAR	17.35	17.1	17.9	19.1	20.5
EUR/USD	1.17	1.16	1.19	1.23	1.28
EUR/SEK	10.42	10.3	10.2	10.0	9.70
EUR/NOK	9.538	9.50	9.15	9.00	9.00
EUR/DKK	7.46	7.46	7.46	7.46	7.46

Source: Nordea estimates

FX FORECASTS AGAINST USD

	Spot	3M	Mid-2019	End-2019	End-2020
USD/BRL	4.139	4.15	3.80	3.70	3.70
USD/CNY	6.861	6.90	6.60	6.50	6.40
USD/CZK	21.73	22.0	20.8	19.9	19.1
USD/HUF	276.9	280	269	256	250
USD/INR	72.72	73.0	70.0	68.0	66.0
USD/MXN	18.77	20.0	18.0	17.0	17.0
USD/PLN	3.67	3.79	3.57	3.33	3.24
USD/RUB	67.43	69.0	69.0	67.0	67.0
USD/TRY	6.354	6.55	6.64	6.67	6.72
USD/ZAR	14.83	14.8	15.0	15.5	16.0

Source: Nordea estimates

POLICY RATE FORECASTS

Policy rates	Spot	3M	Mid-2019	End-2019	End-2020
Russia	7.50	7.75	7.50	7.25	6.75
Poland	1.50	1.50	1.50	1.75	2.00
Hungary	0.90	0.90	0.90	1.20	1.50
Czech Republic	1.25	1.50	1.75	2.00	2.25
Turkey	24.00	24.00	24.00	24.00	24.00
South Africa	6.50	6.50	6.25	6.00	6.00
Brazil	6.50	6.50	7.00	7.50	8.00
Mexico	7.75	7.75	7.50	7.25	6.75
China	4.35	4.35	4.35	4.35	4.35
India	6.50	6.50	6.75	6.75	6.75

Source: Nordea estimates

Brazil

We reiterate our overall forecast profile – we do not believe the weak BRL will be enough for the BCB to hike the Selic rate this year.

China

No changes.

Czech Republic

No changes.

Hungary

The HUF appreciated after the latest MNB meeting, where a termination was announced for the two easing measures, MIRS and the mortgage-note purchases (scheduled for the end of 2018). Governor Nagy, however, still sounded dovish at the press conference. Bearing in mind the still-sour EM sentiment, we maintain our flat HUF profile for the rest of 2018.

India

The INR has weakened considerably in recent months and we lift our three-month forecast for USD/INR somewhat in response. We believe more weakening could be on the cards in the near term.

Mexico

No changes.

South Africa

No changes.

Poland

No changes.

Russia

Our FX forecast remains the same as in the last edition of Emerging Markets View. As sanction threats are still high, RUB risks are tilted towards the downside. The key rate outlook changed to a more hawkish stance, reflecting the CBR's decisive response to rising inflation pressure.

Turkey

We lift our policy rate forecast following the surprise 625 bp rate hike. We have no more rate hikes in our forecast. Despite the rate hike, our EUR/TRY forecast has played out nicely, hence we maintain our profile on the TRY.

Recent research and profile descriptions

Recent Emerging Markets Research
- CBR: Better hawkish than Turkish scenario (14 September)
- TRYing to restore confidence (13 September)
- China monthly: Muddling through (6 September)
- RUB: Sanctions from hell (13 August)
- TRY: A bloodbath (10 August)
- TRY: The price of central bank independence (24 July)
- Putin and Trump: Enemies, allies or competitors? (17 July)
- China's GDP growth: No drama (16 July)
- KZT: Don't expect immediate major support from Clearstream (12 July)
- China-US trade war has escalated (11 July)

Previous Emerging Markets Views
- Emerging Markets View August 2018: Thunderstruck (23 August)

Latest EM Traffic Light
- EM Traffic Light August 2018 (4 September)

Latest Financial Forecast Update
- Majors forecast update: Tensions are yet to hit the US economy (15 August)

Latest Economic Outlook
- Nordea Economic Outlook: The wage engine (5 September)

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