

# Emerging Markets View

## The Fed will not save emerging markets

So far, 2019 has been a bumpy ride for emerging markets. The trade war along with the Fed's U-turn have been clear drivers of volatility in emerging markets. Looking into the second half of 2019, the question is whether these two factors can lead emerging markets towards sunnier skies. We remain sceptical. The market has currently priced in just below four Fed cuts over the next 12 months, leaving little room to positively surprise the market, which in turn could spur further optimism in emerging markets. Furthermore, we still see dark clouds on the geopolitical front and for China's growth momentum. Overall, we find more conditions supporting a defensive view towards emerging markets.

### CNY: Pushing the limit

The downward pressure on the CNY has been increasing in June owing to a combination of trade war worries and disappointing growth numbers. We do not expect USD/CNY to breach the 7.00 level ahead of the G20 meeting, which will be a make or break moment for trade talks.

### RUB: In a comfort zone

The RUB remains on a strong footing, supported by hopes for an OPEC+ deal extension and by foreign portfolio investment inflows. The approaching dividend season will likely support the RUB in late June and weaken the RUB in August.

### PLN: Bucking the seasonal trend in 2019

So far this year, EUR/PLN has moved against its usual seasonal pattern in four out of five months. We examine potential causes and whether this is likely to persist over the summer.

### The tapestry of CIS currency risks

CIS currencies have been performing quite decently lately, but vulnerabilities remain. External debt service and seasonality patterns make us sceptical about the UAH's prospects. The BYN is largely dependent on the tax reform outcome in Russia, whereas the KZT looks slightly less vulnerable in the absence of sizeable external shocks.

FX hedging considerations, the EM Traffic Light and our financial forecasts are also covered in this publication.

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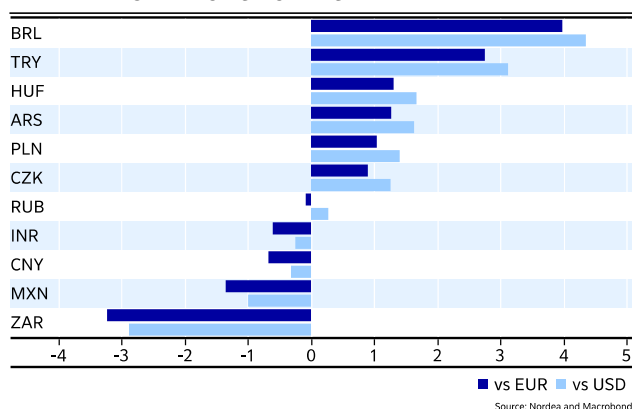
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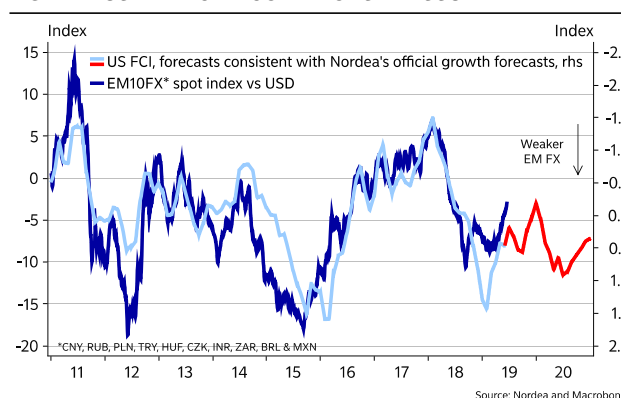
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EM FX PERFORMANCE SINCE LAST EM VIEW



TIGHTER US FINANCIAL CONDITIONS PRESSURE EM FX



# The Fed will not save emerging markets

Emerging markets are currently at a crossroads with high geopolitical uncertainty and markets betting on a dovish Fed. Overall, we favour a defensive stance towards emerging markets.

2019 has been a bumpy EM ride, and more of the same lies ahead

Back in November, we wrote that 2019 was going to be a [bumpy ride](#) for EM – a view that we continue to espouse. So far, EM FX indices are down and growth has been slowing; conversely though, equities and bonds are in green territory.

We see the greatest risks for EM FX and equities

Even though we expect EM bonds to perform relatively well thanks to the dovish repricing of G10 central banks and the hunt for carry, we believe the picture is gloomier for EM FX and equities. Our overall defensive EM stance is based on four key factors: 1) tightening financial conditions in the US; 2) slowing global trade/growth; 3) geopolitical uncertainty; and 4) a slowdown in China.

US financial conditions are set to tighten despite the dovish Fed

Starting with the US financial conditions, it may seem counterintuitive that we believe EM should suffer when the Fed enters an easing cycle (we have pencilled in [four Fed cuts over the next 12 months](#)). However, one of the main arguments for the Fed cuts is the fear of slowing growth, which should lead to higher credit spreads and lower equity earnings – two important elements of US financial conditions.

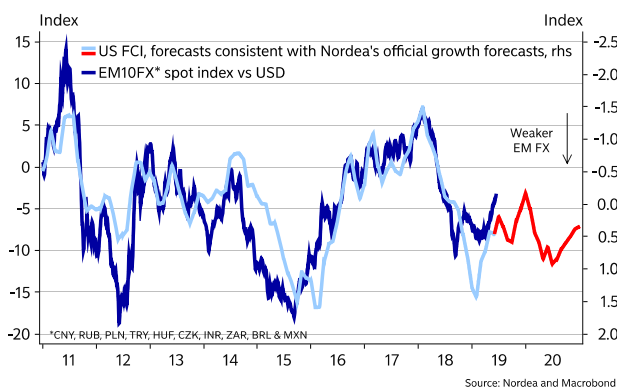
The USD weakness in a Fed easing cycle is short-lived

While we recognise that another important variable, the USD, tends to weaken heading into a Fed easing cycle, that pattern does not persist for long. [The USD typically strengthens 6-12 months](#) into the cutting cycle, as other central banks usually follow the Fed's lead on cuts.

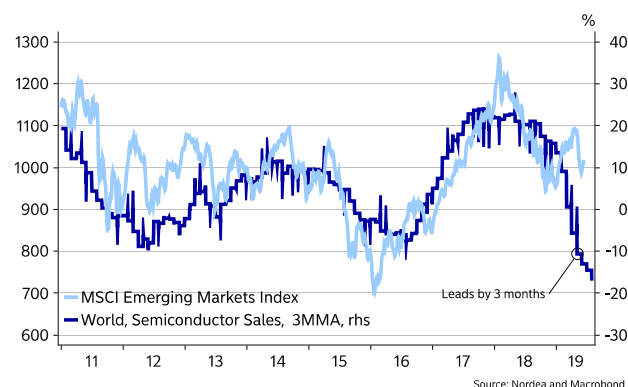
A lot is expected of the Fed; if it does not deliver, things could turn really bad for EM FX

Overall, our model indicates that US financial conditions will tighten both in the short run and over the next 9-12 months, in line with previous Fed easing cycles and periods of slowing growth. This normally spells trouble for EM FX (see chart below). This trouble can be exacerbated if the Fed, in fact, does not exercise its put option by delivering several cuts in a timely manner. In that case, financial conditions could tighten rapidly and act a toxic driver for EM FX, much like the situation in 2018.

**TIGHTER US FINANCIAL CONDITIONS PRESSURE EM FX**



**DOWNSIDE RISKS TO EM EQUITIES**



The second reason behind our defensive EM stance is slowing trade/growth. Besides tightening US financial conditions, second-round effects from last year's FX sell-off and political uncertainty both point to weaker macro momentum.

If not a US-China trade war, then a US trade war with Europe or Japan

The trade war is still alive and kicking, and while we expect a US-China deal by year-end, we do not expect Trump to scale back his Twitter-trade game anytime soon. If a truce is reached with Beijing, we simply expect Trump to redirect his wrath towards Europe, Japan or a third country with which the US has a current account deficit.

Political uncertainty should remain high and continue to weigh on EM

On top of the trade war, political uncertainty is underpinned by [Brexit](#), Russian/Iranian sanctions and [populism in Latin America](#). In recent years, political uncertainty has negatively correlated with EM FX – a pattern that we expect to persist (see chart).

KRW and PLN are the most trade-sensitive currencies

When linking global trade to EM currencies, our models indicate that KRW, PLN and CZK are the most sensitive to trade (see chart). This makes sense given the economies' openness.

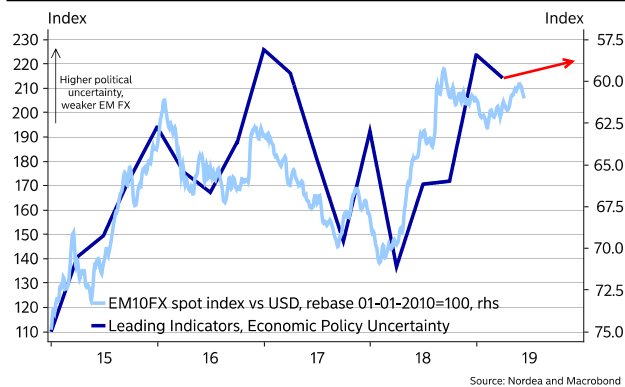
ARS and TRY suffer when trade is either increasing or decreasing

As the chart also shows, the performances of ARS and TRY are negatively correlated with increasing trade. This by no means indicates resilience in times of slowing global growth; instead, it suggests that these two currencies suffer from long-term structural problems, as they also take a beating in times of slowing growth.

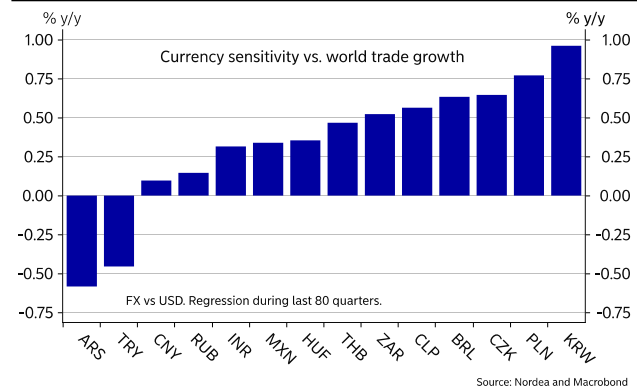
USD-dependent countries are among the most vulnerable during trade slowdowns

Digging into periods with global trade slowdowns, the PLN is one of the currencies that suffers the most, along with USD-debt dependent currencies such as the BRL, INR and MXN. The results are less grim when adjusted for carry; however, in a material slowdown scenario (such as in 2008), the carry will not save many EM currencies.

**POLITICAL UNCERTAINTY IS A NEGATIVE FACTOR FOR EM FX**



**KRW, PLN AND CZK ARE THE MOST EXPOSED TO TRADE**



China is facing a slowdown

Lastly, our defensive EM view is based on China. The trade war has had a clear impact on the real economy. Even though the authorities have tried to counter the negative effects by increasing infrastructure investments and lowering reserve requirements for small and medium-sized banks, we believe China is facing a slowdown.

Driving growth through credit comes at a cost for China

Even though we also believe that Beijing has sufficient fiscal and monetary artillery to avoid a rapid slowdown, there are two important things to bear in mind here. First, China's growth stimulus comes at the cost of pouring further "credit gasoline" on its already large "debt fire". In the long run, this is bad news for China. Second, the credit injection has not yet been fully transmitted into the economy, as this normally takes 6-12 months. At best, the credit impulse is neutral at the moment, which does not speak in favour of going further out on the risk curve for Chinese assets.

Monetary policy is not yet growth-supportive

Breaching the level of 7.00 in USD/CNY could be a negative game changer for the EM sentiment

In the near term, Chinese assets may also come under pressure if USD/CNY breaches the psychologically important level of 7.0. Such an event could lead to a capital flight reminiscent of the 2015-16 situation, adding more downward pressure on growth. So far, the Chinese authorities have tried to combat any FX speculation, but if the trade war escalates, we could envisage a shift of level in USD/CNY, thereby leading to a new round of risk aversion.

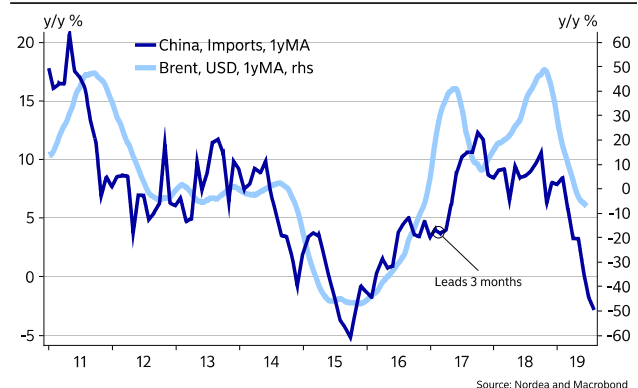
The slowing growth outlook for China is overall bad news for EM given China's position in the global supply chain, as well as China's link to commodity prices. Taken altogether with the tightening financial conditions in the US, slowing global trade/growth and geopolitical uncertainty, we foresee more dark clouds and volatility ahead for EM.

*By Morten Lund*

**CHINA: MONETARY POLICY IS NOT GROWTH-SUPPORTIVE YET**



**LESS CHINESE IMPORTS SUGGEST LOWER OIL PRICES**



# CNY: Pushing the limit

The downward pressure on the CNY has been increasing in June owing to a combination of trade war worries and disappointing growth numbers. We do not expect USD/CNY to breach the 7.00 level ahead of the G20 meeting, which will be a make or break moment for trade talks.

USD/CNY heading to the magic 7.00 level

In June, the CNY has been trading dangerously close to the ceiling that has not been passed since 2008, namely 7.00 to the USD. Fears of capital flight motivate efforts to keep the pair below this threshold, but there are limits to the PBoC's willingness, which became clear when the governor said that there is no "red line" for the exchange rate.

More government stimulus is expected

Strong signs of waning growth momentum suggest that the weak yuan is not an intentional outcome of interventions from China's side as Trump suggests, but rather a reflection of decreased confidence in the Chinese economy and the trade war. Infrastructure investments did not deliver the expected boost, and the government will likely ramp up stimulus again, which should support the yuan later this year.

Tensions are building ahead of the G20 meeting

The next big test for the CNY will be this month's G20 meeting, where Trump and Xi have agreed to have an "extended meeting". China seems to have dodged the bullet of 25% tariffs on a further USD 300bn of US imports from China. The yuan jumped on the news of the two presidents meeting, but this optimism might be premature.

Reaching an agreement would be best for everyone

American businesses argue that a deal would be in the US's best interests. Hundreds of US companies and trade associations are urging Trump not to "hurt the heartland" by proceeding with further tariffs, which he will surely consider with re-election in mind.

Risk of escalation has decreased

The biggest danger of the yuan drifting beyond the 7.00 level seems to have subsided for now, but as previous talks broke down last minute, we remain cautious. In case of escalation, the yuan could weaken markedly and the PBoC will eventually cease efforts to restrain it from drifting beyond the 7.00 level, despite capital outflow risks.

Relief should come towards the end of the year

We still expect growth stimulus to pick up later in the year, and we believe that both sides' interests in reaching a deal will lead to a recovery of the yuan over a six-month horizon. Nonetheless, we expect the trade conflict to weigh on the yuan for some time.

*By Inge Klaver*

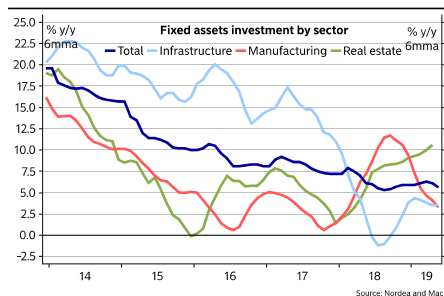
## RISK FACTORS

- Trade war escalation at G20
- Capital outflows
- Failing stimulus

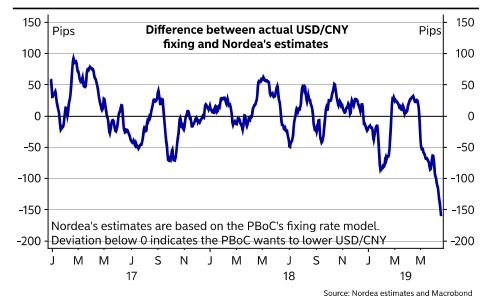
## EM TRAFFIC LIGHT

- Risk level: 10% (green, unchanged from the previous month)

## SLOWING INFRASTRUCTURE INVESTMENT



## INTERVENTIONS BY STRONGER FIXING RATE



## FINANCIAL FORECASTS – CHINA

We keep our USD/CNY forecasts unchanged, as we still expect the uncertainties related to the trade war to push down the pair for now, but not beyond 7.00. A near agreement and extra government stimulus should strengthen the yuan again towards the end of the year.

Forecasts	Spot	3M	End-2019	Mid-2020	End-2020
USD/CNY	6.92	6.95	6.80	6.80	6.75
Policy rate	4.35	4.35	4.35	4.35	4.35

Source: Nordea estimates

## USD/CNY FORECASTS



Source: Nordea estimates and Macrobond

# RUB: In a comfort zone

The RUB remains on a strong footing, supported by hopes for an OPEC+ deal extension and foreign investment inflows. The dividend season will likely support the RUB in June and weaken it in August.

Foreign portfolio inflows keep RUB on a strong footing

Russian financial markets have been calm over the past month with the RUB remaining on a strong footing, even though the oil price was in close proximity to a psychologically important level of USD 60/bbl. Foreign capital inflows primarily into Russian sovereign debt (OFZ) remained an important driver for the RUB. At the end of May, total non-resident holdings of OFZ reached a historical maximum of USD 37bn.

Central Bank giving a clear easing message

The CBR's latest comments were more dovish than expected, giving more room for a further reduction in OFZ yields and stimulating investors to buy these instruments ahead of a more significant yield drop. Two more rate cuts this year now seem likely unless external conditions deteriorate markedly. By mid-2020, the CBR expects the key rate to be 6-7% versus the current 7.5%. Internal factors (gradually slowing inflation, weak internal demand, and sluggish economic growth) speak jointly in favour of further cuts.

OPEC+ deal extension hope, making oil price slump less likely

The extension of OPEC+ oil production cuts till the end of 2019 seems almost a done deal given the rising crude oil stocks, ever-increasing US production and risks of global growth deceleration. The seeming joint readiness of OPEC+ countries to keep the market in balance provides a firm floor for the oil price, protecting the RUB from scenarios like 2014 when oil was in free fall.

Dividend season: First RUB positive then RUB negative

From late June to early August, the RUB will be impacted by dividend season. Dividend payments first make Russian exporters exchange more FX into RUB, which will likely support the RUB in late June. In August, the flow will likely be RUB negative, as shareholders exchange part of the dividends back into hard currency. In July, the effect may be neutral as the opposing flows should counterbalance one another.

*By Tatiana Evdokimova and Grigory Zhirnov*

## RISK FACTORS

- Fed not delivering cuts according to market expectations
- OPEC+ deal falling apart
- Trade war escalation

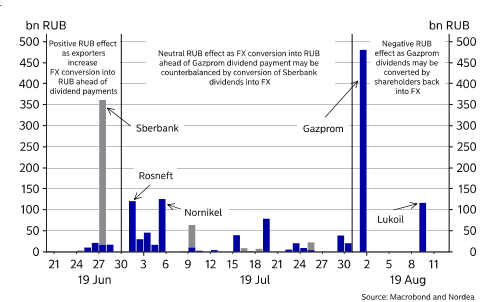
## EM TRAFFIC LIGHT

- Risk level: 27% (yellow; +3 pp from last month)

## OFZ MARKET DOES NOT YET FULLY PRICE IN THE UPCOMING EASING



## DIVIDEND PAYMENT FACTOR



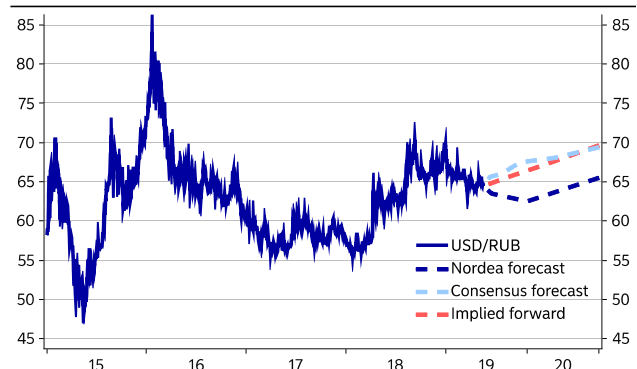
## FINANCIAL FORECASTS: RUSSIA

We keep our bullish forecasts for the RUB unchanged, and see continued portfolio inflows as the key support factor, similar to the 2017 scenario. Given the muted inflation dynamics, two rate cuts from the CBR are now looking possible before the end of the year, hence we change our previous forecast of only one more cut this year.

Forecasts	Spot	3M	End-2019	Mid-2020	End-2020
USD/RUB	64.30	63.50	62.50	64.00	65.50
Policy rate	7.50	7.25	7.00	6.75	6.50

Source: Nordea estimates

## USD/RUB FORECASTS



# PLN: Bucking the seasonal trend in 2019

So far this year, EUR/PLN has moved against its usual seasonal pattern in four out of five months. We examine potential causes and whether this is likely to persist over the summer.

Fading European Parliament election risk and increasing inflationary pressure have underpinned the zloty

In the first three weeks of May, the zloty was following its usual seasonal pattern of weakening versus the euro. However, as the risk related to the European Parliament election faded, the PLN gained. The EUR/PLN downtrend has continued in June and is currently testing support levels despite the recent pressure on EM FX. A likely explanation is that the inflationary uptick has continued, with core inflation being at its highest level since 2013, prompting hawkish remarks from MPC members. As such, it appears that the tight labour market finally has made its way to consumer prices.

Market pricing of NBP has dropped recently

Despite rising inflation, the global drop in interest rates has also affected the pricing of the NBP. Thus, the FRA market is currently pricing in roughly 25% probability of a rate cut over the next 12 months compared with early May when markets were pricing in a full hike within two years.

Income repatriation usually puts downward pressure on the PLN in the early summer

Looking ahead, the PLN usually weakens in June and July. This is partly flow-driven, as the current account tends to be drawn further down by an outflow of primary income. For example, foreign corporations based in Poland tend to repatriate income in June.

Polish dividend season brings a few noteworthy days

In late July/early August, the seasonal pattern also seems to work against the zloty, as some of the largest Warsaw-listed firms distribute dividends. The noticeable share of foreign ownership could put downside pressure on the zloty on 30 July, 5 August and 14 August. On these days, a total of PLN 1.6bn will be distributed to foreign investors, which is significant given the average daily trading volume of PLN 13bn.

EUR/PLN should appreciate from here

Despite EUR/PLN performing against its seasonality in 2019, we do not believe this pattern will persist, thereby burdening the PLN over the summer. Combined with our defensive EM view, we instead believe EUR/PLN will test the 4.32 level over the summer.

*By Morten Lund and Nick Fisker*

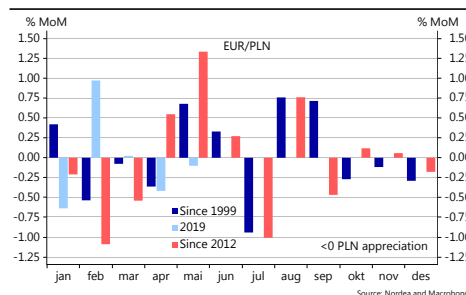
## RISK FACTORS

- Weak EM sentiment
- European industrial cycle
- Dovish NBP
- Seasonality and dividend distributions

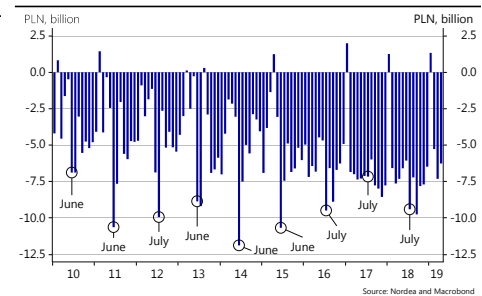
## EM TRAFFIC LIGHT

- Risk level: 13% (green, unchanged from the previous month)

### IN 2019, EUR/PLN HAS NOT FOLLOWED ITS USUAL PATTERN



### POLAND'S CURRENT ACCOUNT USUALLY WEAKENS DURING THE SUMMER



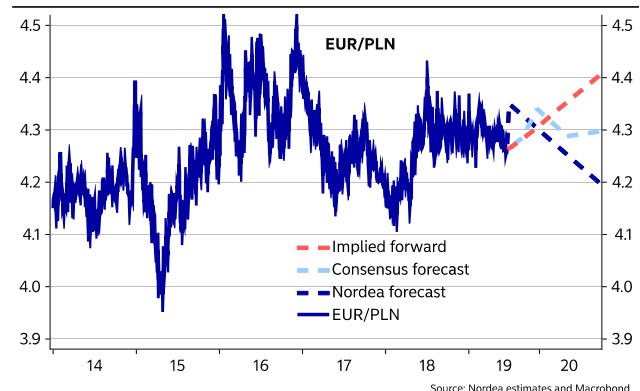
## FINANCIAL FORECASTS – POLAND

Owing to a combination of lukewarm market sentiment, a dovish central bank and rising political uncertainty, we expect EUR/PLN to keep testing levels up to 4.35 in the short term. Further ahead, we expect a mild PLN appreciation as the European industrial cycle rebounds from current lows.

Forecasts	Spot	3M	End-2019	Mid-2020	End-2020
EUR/PLN	4.26	4.35	4.30	4.25	4.20
Policy Rate	1.50	1.50	1.50	1.50	1.75

Source: Nordea Estimates

## EUR/PLN FORECAST



Source: Nordea estimates and Macrobond

# The tapestry of CIS currency risks

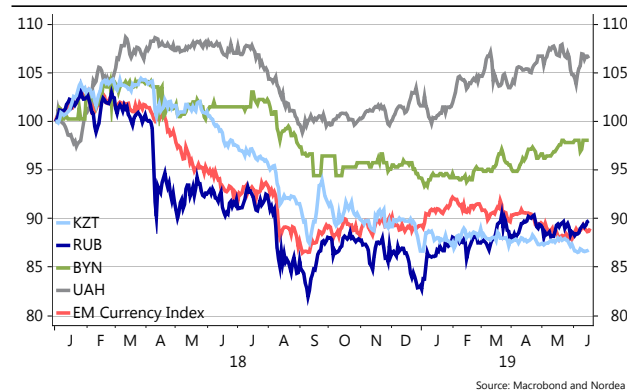
CIS currencies have been performing quite well lately, but vulnerabilities remain. External debt service and seasonality patterns make us sceptical about the UAH's prospects. The BYN is largely dependent on the tax reform outcome in Russia, whereas the KZT looks slightly less vulnerable in the absence of sizeable external shocks.

Weak fundamentals signal vulnerability to external shocks

A quick look at the key fundamentals of the CIS countries reveals that most of them suffer from significant external debt burdens, sizeable current account deficits, and a limited cushion in the form of reserves. Even though external imbalances are now lower than in 2010-14, the buffers are still not large enough to give complete comfort in the face of potential external shocks. Most currencies in the CIS countries have a relatively short history of free-floating FX rates (2015-19).

Consequently, the threshold for intervening in the FX market to defend the local currency is relatively low. In our view, Ukraine seems to be the most vulnerable, with its reserve adequacy, debt service schedule and current account deficit all raising red flags. Belarus is in slightly better shape thanks to a lower debt burden. Against this backdrop, Kazakhstan seems to be more or less balanced thanks to its ample reserves and current account surplus.

**RUB AND KZT HAVE BEEN UNDERPERFORMING UAH AND BYN DESPITE STRONGER FUNDAMENTALS**



**FUNDAMENTALS POINT TO NUMEROUS RISKS**

	Reserves (in months of imports)	External debt (in % of GDP)	Current account balance (in % of GDP)
Kazakhstan	8.1	93%	0.6%
Ukraine	3.2	92%	-3.7%
Belarus	2	65%	-0.4%
Georgia	3.3	110%	-7.7%
Armenia	3.8	85%	-9.1%
Uzbekistan	12.8	35%	-7.1%

Source: IMF

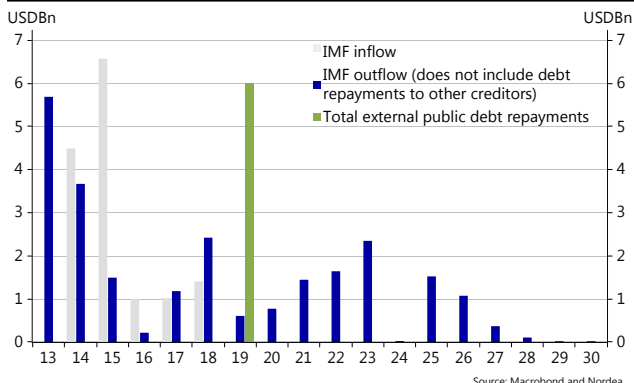
Massive debt burden makes for a fragile UAH outlook

The most urgent problem for Ukraine is its huge external debt (public debt-to-GDP ratio of 53%), which is gradually coming due (USD 15.5bn is maturing this year). Debt service this year will be problematic without the IMF's helping hand. Meanwhile, the IMF has suspended further disbursements through a standby arrangement owing to the lack of progress in the promised reforms. Talks should resume as soon as the new government is formed after parliamentary elections (scheduled for 21 July). Although the newly elected president Mr Zelenskiy appears determined to continue working with the IMF, there is a risk that the timing of the IMF's disbursements will be deferred, thereby causing problems with debt service.

Seasonal UAH weakness is on the cards

Moreover, the UAH could come under pressure in the second half of the year given the seasonal pattern of the current account. The UAH has been weak versus the USD during almost every Q3 for the last 15 years. Thus, seasonal risks for the UAH are currently tilted to the downside. The current account deficit reached 3.6% of GDP in 2018, which is the highest CA deficit value since 2013 (when it was 8.7% of GDP).

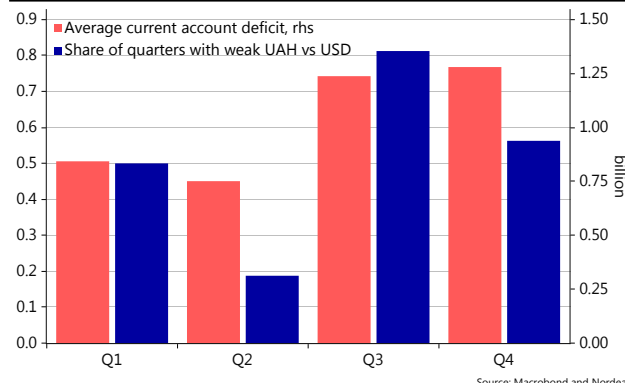
**UKRAINE'S DEBT SERVICE PROFILE LOOKS PROBLEMATIC**



The external debt burden is less crucial for Belarus, but continuous inflow of financing from Russia is crucial

Belarus's current account deficit may be exacerbated by changes to Russia's tax regime

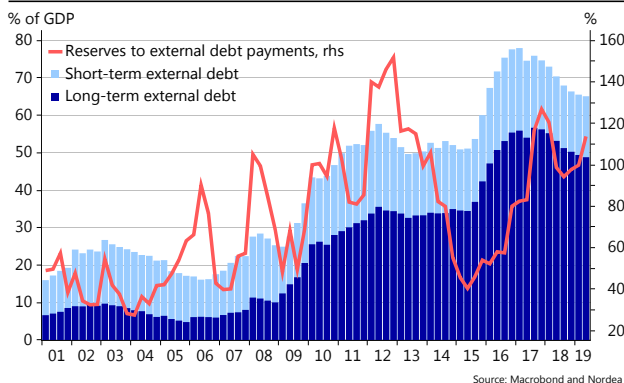
**SEASONAL PATTERN IN UAH POINTS TO H2 RISKS**



In our view, the external debt of Belarus appears less worrying (65% of GDP) than those of Ukraine and Kazakhstan, although international reserves barely cover short-term debt. With the IMF's support being out of reach for political reasons, Belarus is extremely dependent on financing from Russia. In 2017, Russia lent USD 700bn to Belarus, but Belarus asked for USD 600bn more in 2019.

A potentially more pressing risk for Belarus is its current account deficit. Though currently at just 0.4% of GDP (the lowest level since 2006), the balance may deteriorate quickly due to the oil sector tax reform in Russia. Belarus currently imports crude oil from Russia free of export duty; it is then refined in Belarus and re-exported. The reform in Russia will cause oil import prices to rise for Belarus. The IMF expects the current account deficit to deepen to unsustainable levels (up to 5% of GDP on the 2022 horizon and onwards) if the changes are implemented in their current form. The BYN outlook depends heavily on the outcome of negotiations on this issue.

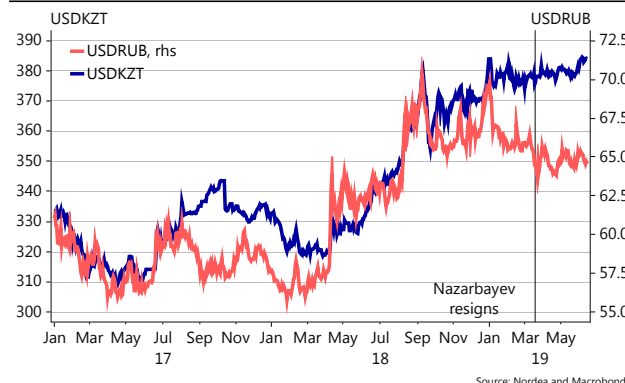
**BELARUS: SHORT-TERM EXTERNAL DEBT BARELY COVERED BY RESERVES**



KZT remains weak YTD, decoupling from RUB and oil

A worryingly fast decline in Kazakhstan's reserves in 2019

**USD/KZT HAS RECENTLY DECOUPLED FROM USD/RUB**



Even though Kazakhstan's economy looks fundamentally less vulnerable than those of Ukraine and Belarus, the KZT has been performing quite poorly since early 2018, mimicking RUB weakness in the face of sanction threats. Currently, the KZT remains close to its historically weakest levels of around 384 versus the USD with no substantial changes since the start of 2019 (-0.8% versus USD), despite oil prices having risen by 18% and the RUB appreciating by 7.5% YTD. It appears as though the KZT's correlation with the RUB has become asymmetric, with the KZT being sensitive to negative spillovers, but relatively irresponsive to positive developments (both in 2017 and 2019).

Devaluation expectations are high and any sentiment deterioration may easily throw the KZT off balance. One recent cause for concern was an unexpected decline in foreign currency reserves (-9% since the beginning of 2019). The National Bank of Kazakhstan has denied speculation about FX market interventions at the time of the power transition in March-April 2019. Even though NBK reserves are currently equal to 7.5 months of imports, which is comfortably above the minimum adequacy level of three months, the pace of decline in the reserves was worryingly fast. One of the biggest internal risks to the KZT is the first power transition in the country since 1991, and its unpredictable medium-term outcome could keep risk-averse investors away.

By Grigory Zhimov & Tatiana Evdokimova

# Hedging considerations

## CNY vs EUR

### Income

Nordea continues to see downside risk for CNY in the short term, ie a high hedge ratio in the short term, using mainly FX forwards, as EUR/CNY forward premiums remain well below Nordea's EUR/CNY short-term forecast. Nordea has turned more negative on EUR in the longer run, ie a low hedge ratio in the long term, using zero-cost option strategies as a hedging instrument.

### Expenses

A low hedge ratio in the short term, using a mix of FX forwards and zero-cost strategies; a high hedge ratio in the long term, using FX forwards, as they trade much higher than Nordea's long-term spot forecast. If hedging is required, use mainly zero-cost option strategies, eg participating forwards.

Forecasts	Spot	3M	End-2019	Mid-2020	End-2020
EURCNY	7.73	8.06	7.96	7.75	7.56
Policy rate	4.35	4.35	4.35	4.35	4.35

## RUB vs EUR

### Income

Our EUR/RUB forecasts are below FX forwards. A low to middle hedge ratio in the short and long term, using mainly zero-cost option strategies. EUR/RUB volatility continues to drift lower. Implied volume (6M) is approaching 10%, down from over 14% at the beginning of the year.

### Expenses

A high hedge ratio in the short and long term, using FX forwards, benefiting from forward premiums that are higher than our forecasts for the EUR/RUB spot rate.

Forecasts	Spot	3M	End-2019	Mid-2020	End-2020
EURRUB	71.61	73.66	73.13	72.96	73.36
Policy rate	7.50	7.25	7.00	6.75	6.50

## PLN vs EUR

### Income

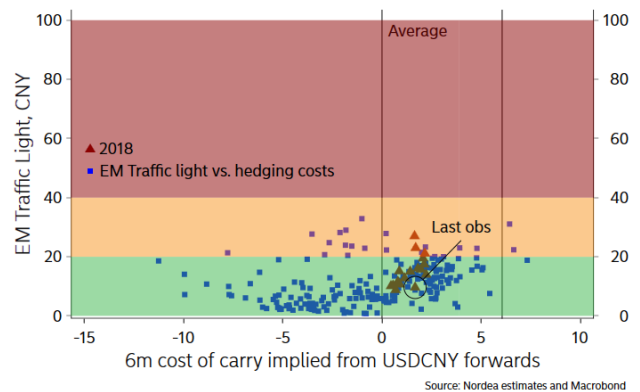
A middle hedge ratio in the short term (3M), using FX forwards; a low hedge ratio in the long term, as we expect PLN to strengthen towards the end of 2019 and in 2020, using zero-cost option strategies, eg participating forwards, as EUR/PLN volumes remain low.

### Expenses

A low hedge ratio in the short term, using a mix of FX forwards and zero-cost option strategies; a high hedge ratio in the long term, using FX forwards, mainly to take advantage of high forward premiums on EUR/PLN.

Forecasts	Spot	3M	End-2019	Mid-2020	End-2020
EURPLN	4.26	4.35	4.30	4.25	4.20
Policy rate	1.50	1.50	1.50	1.50	1.75

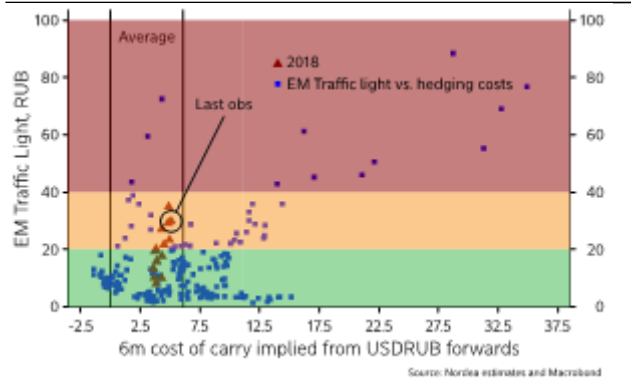
### COST OF CARRY VS RISK LEVEL



Implied ATM Vol (6m)	25D RR (6m)	Forward (6m)
5.61	1.11	7.86

Source: Bloomberg

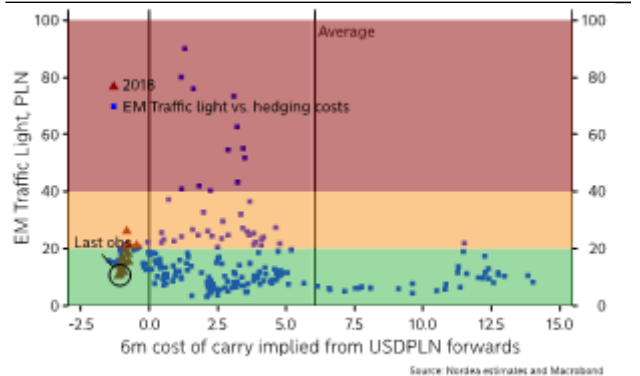
### COST OF CARRY VS RISK LEVEL



Implied ATM Vol (6m)	25D RR (6m)	Forward (6m)
10.23	2.93	74.49

Source: Bloomberg

### COST OF CARRY VS RISK LEVEL



Implied ATM Vol (6m)	25D RR (6m)	Forward (6m)
3.98	1.18	4.35

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
RUB	Russia	27%									
ZAR	South Africa	27%									
CZK	Czech Republic	21%									
PEN	Peru	20%									
UAH	Ukraine	19%									
CLP	Chile	19%									
ILS	Israel	18%									
TWD	Taiwan	18%									
BRL	Brazil	17%									
COP	Colombia	17%									
RSD	Serbia	16%									
KES	Kenya	16%									
MXN	Mexico	16%									
BGN	Bulgaria	15%									
KRW	South Korea	15%									
HUF	Hungary	14%									
SAR	Saudi Arabia	13%									
PLN	Poland	13%									
THB	Thailand	13%									
KZT	Kazakhstan	12%									
SGD	Singapore	12%									
RON	Romania	12%									
TRY	Turkey	12%									
HKD	Hong Kong	11%									
ARS	Argentina	10%									
IDR	Indonesia	10%									
CNY	China	10%									
MYR	Malaysia	9%									
INR	India	9%									
HRK	Croatia	8%									
PHP	Philippines	7%									
NGN	Nigeria	7%									
EGP	Egypt	3%									
EM general		13%									

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: May 2019 \(6 June\)](#)
- New signals: No new signals.
- Biggest changes: ARS (-4 pp) and RUB (+3 pp).

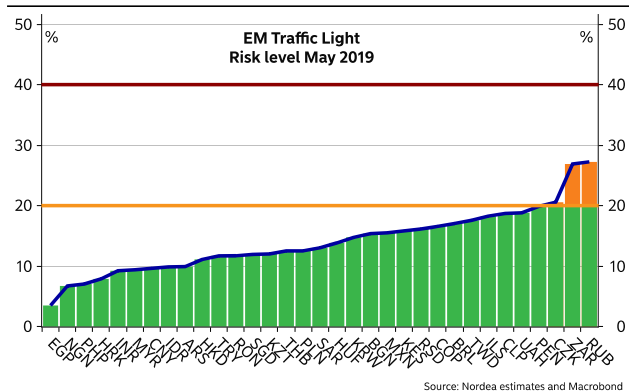
### Methodology note:

- [EM Traffic Light: Methodology note](#)

### Track record:

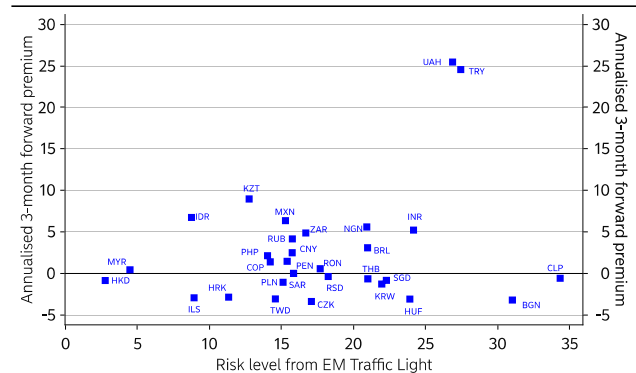
- [EM Traffic Light: Track record – May 2019](#)

### OVERALL RISK LEVEL



Source: Nordea estimates and Macrobond

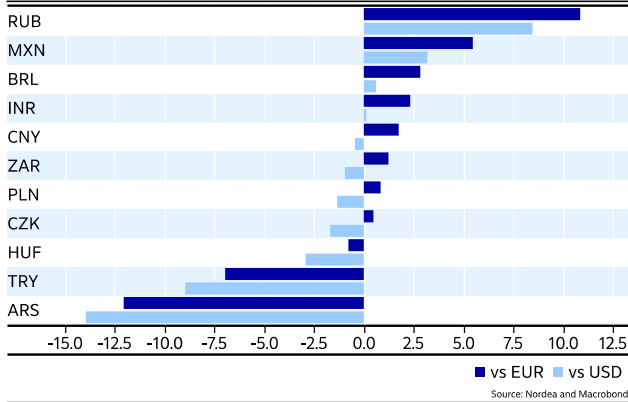
### TRAFFIC LIGHT VS COST OF CARRY



Source: Nordea and Macrobond

# Emerging market performance

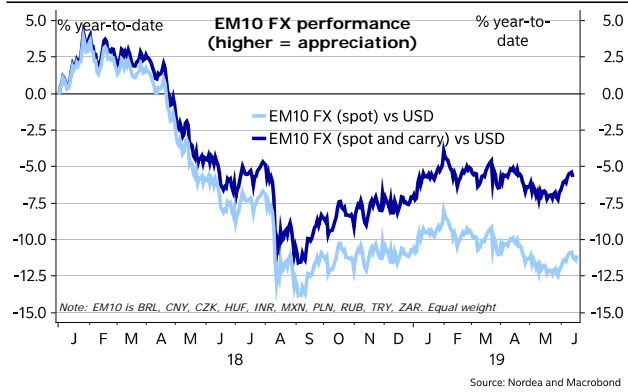
## YTD EM FX PERFORMANCE



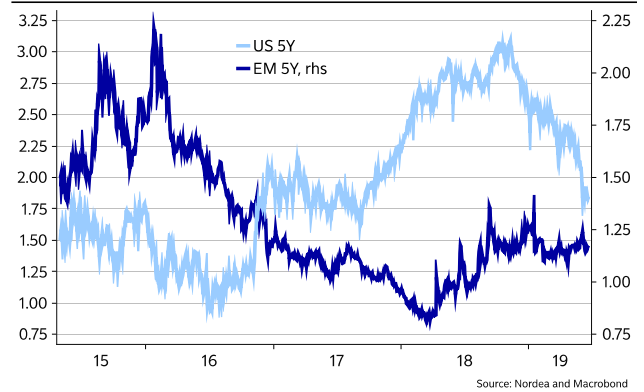
## EQUITIES' PERFORMANCE



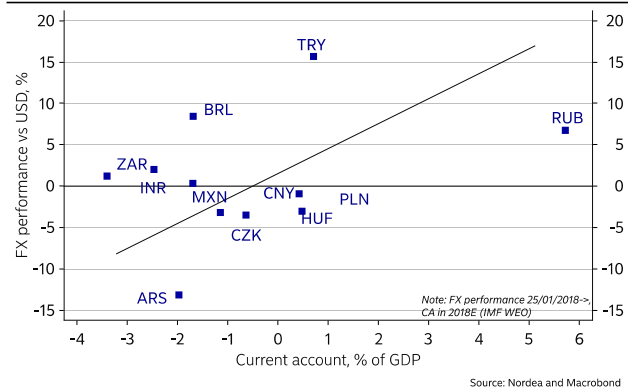
## FX PERFORMANCE, CARRY-ADJUSTED



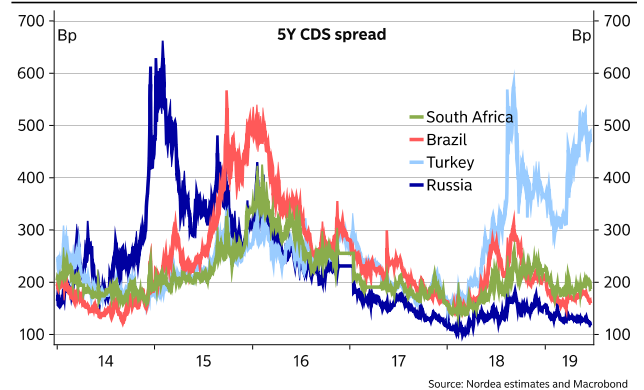
## SWAPS



## FX PERFORMANCE (2018) VS CURRENT ACCOUNT



## CDS SPREADS



# Forecast overview

## FX FORECASTS VS EUR

	Spot	3M	End-2019	Mid-2020	End-2020
EUR/BRL	4.316	4.64	4.74	4.67	4.65
EUR/CNY	7.727	8.06	7.96	7.75	7.56
EUR/CZK	25.61	27.0	26.0	26.0	26.0
EUR/HUF	323.3	325.0	325.0	323.0	320.0
EUR/INR	77.83	80.0	83.1	79.8	78.4
EUR/PLN	4.259	4.35	4.30	4.25	4.20
EUR/MXN	21.35	22.0	22.8	22.2	22.4
EUR/RUB	71.57	73.7	73.1	73.0	73.4
EUR/TRY	6.54	6.85	7.10	7.40	7.60
EUR/ZAR	16.23	16.8	17.6	17.7	17.9
EUR/USD	1.119	1.16	1.17	1.14	1.12
EUR/SEK	10.65	10.7	10.8	10.6	10.5
EUR/NOK	9.779	9.70	9.60	9.40	9.30
EUR/DKK	7.467	7.47	7.47	7.46	7.46

Source: Nordea estimates

## FX FORECASTS VS USD

	Spot	3M	End-2019	Mid-2020	End-2020
USD/BRL	3.858	4.00	4.05	4.10	4.15
USD/CNY	6.907	6.95	6.80	6.80	6.75
USD/CZK	22.89	23.3	22.2	22.8	23.1
USD/HUF	289	280	278	283	286
USD/INR	69.57	69.0	71.0	70.0	70.0
USD/MXN	19.08	19.0	19.5	19.5	20.0
USD/PLN	3.807	3.75	3.68	3.73	3.75
USD/RUB	63.98	63.5	62.5	64.0	65.5
USD/TRY	5.846	5.91	6.07	6.50	6.80
USD/ZAR	14.51	14.5	15.0	15.5	16.0

Source: Nordea estimates

## POLICY RATE FORECASTS, %

Policy rates	Spot	3M	End-2019	Mid-2020	End-2020
Russia	7.50	7.25	7.00	6.75	6.50
Poland	1.50	1.50	1.50	1.50	1.75
Hungary	0.90	0.90	0.90	0.90	1.20
Czech Republic	2.00	2.00	2.00	2.25	2.50
Turkey	24.00	24.00	22.00	20.00	18.00
South Africa	6.75	6.75	6.50	6.50	6.25
Brazil	6.50	6.50	6.50	6.75	6.75
Mexico	8.25	8.25	8.00	8.00	7.75
China	4.35	4.35	4.35	4.35	4.35
India	5.75	5.75	5.75	5.75	5.75

Source: Nordea estimates

<b>Brazil</b>	No changes.
<b>China</b>	No changes.
<b>Czech Republic</b>	No changes.
<b>Hungary</b>	We no longer expect a rate hike from the central bank, due to soft communications recently and the dovish shift from G10 central banks.
<b>India</b>	We lower our policy rate forecast to 5.75% after the 25 bp rate cut that was delivered at the last meeting. The shift to an 'accommodative' stance could point to further easing ahead and poses downside risk to our forecast.
<b>Mexico</b>	No changes.
<b>South Africa</b>	No changes.
<b>Poland</b>	No changes.
<b>Russia</b>	We now expect two further cuts from the Bank of Russia by the end of the year and one more cut in H1 2020 compared to two cuts for the same horizon previously. The USD/RUB forecast remains unchanged. Our RUB/EUR forecast is now stronger, in line with the recent major currencies forecast update.
<b>Turkey</b>	The TRY has been volatile recently owing to political turbulence. We therefore adjust our EUR/TRY forecast slightly but keep our negative stance on the TRY – <a href="#">click here to read our arguments.</a>

# Recent research and profile descriptions

## Recent Emerging Markets Research

- [Kazakhstan elections: Ticking the box \(10 June\)](#)
- [CBR Preview: Back on easing track \(7 June\)](#)
- [India: Third time's the charm \(6 June\)](#)
- [RUB seasonality: Trust facts, not rumours \(4 June\)](#)
- [China View: Trade war tensions the new normal \(3 June\)](#)

## Previous issues of Emerging Markets View

- [Emerging Markets View: Carry on Modi \(22 May\)](#)
- [Emerging Markets View: Where the inflation anchor drops \(25 April\)](#)
- [Emerging Markets View: The Brexit stranglehold \(21 March\)](#)

## Latest EM Traffic Light

- [EM Traffic Light May 2019 \(6 June\)](#)

## Latest Financial Forecast Update

- [Majors Forecasts: Low\(er\) for even longer! \(13 June\)](#)

## Latest Economic Outlook

- [Nordea Economic Outlook: Waiting ground \(15 May\)](#)

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