

Emerging Markets Monthly

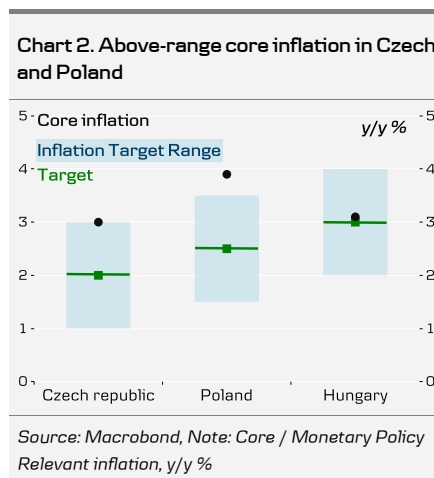
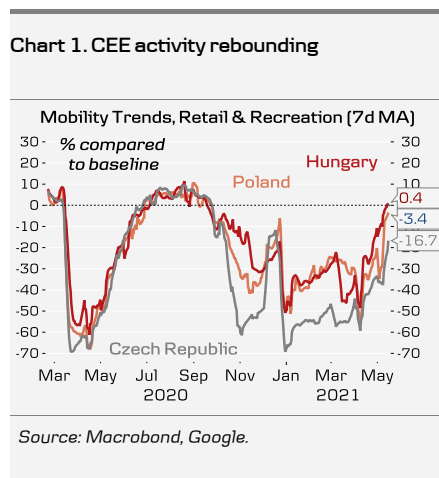
Eastern Europe leading the lift-off for rates

- Strong recovery in the making on back easing restrictions and strong global demand.
- Inflation pressures prompting change in central bank narrative.
- CEE FX to benefit from CB hawkishness.

The CEE countries are gearing up for a fast recovery after coming to terms with the third COVID wave. In both Czech Republic, Poland and Hungary, the daily cases are back to Autumn lows as restrictions have worked together with warmer weather and vaccine roll-out. On the latter, Hungary is standing out, as the early decision to use the Russian Sputnik vaccine has advanced vaccine coverage to same levels as in the US and UK, with Poland and Czech Republic closer to EU average. This has allowed for a relatively early easing of restrictions in Hungary, prompting a strong rebound in activity, but similar picture is emerging in Poland and Czech Republic too (Chart 1).

Furthermore, the countries are witnessing persistently high inflation. There are clear signs of manufacturing sector overheating in Poland, where supply constraints and labour shortages are limiting output. Both core and headline inflation are now above the central bank's target band at 3.9% y/y (Chart 2). Furthermore, the recent rise in commodity prices globally has an accentuated effect on CEE countries' inflation, as they have notably higher weight for goods in consumer price indices, compared to the Euro Area or the US.

While expansionary monetary policy and negative real rates have supported the recovery, the heightened inflation pressures have turned the local central banks more hawkish. The National Bank of Hungary used to be the more dovish of the bunch, but the deputy governor Virag surprised the markets this week by calling for preparation for a rate hike, and the Czech central bank is targeting a rate hike in June already. The Polish central bank remains divided on the issue, but the more hawkish members are calling for a hike already this summer. The divided policy committee make us a bit more hesitant on the upside for PLN compared with the two others but overall we see stronger CEE currencies.



Quick view

- **EUR/PLN** We expect modest strengthening of PLN given the continuing reopening of the economy and possibility of a more hawkish central bank
- **EUR/HUF** have moved lower on expectations for rate hikes. To see a further push lower, one needs to expect CPI to roll over. This is still to be seen.
- **EUR/CZK** should go lower, supported by pulling forward of expectations to rate hikes, structural catch-up and near-term weakness of the dollar.
- **USD/RUB** has removed some of the volatility related to Ukraine, as the situation have de-escalated. If this continues, RUB can strengthen but tail risks remain very high.
- **USD/TRY** will near-term stay in the 8-area.
- **USD/ZAR** has moved lower as investors have been pushed to hunt for yield and amid still-strong commodity prices. We look for the cross to bottom out in 2021.
- **USD/CNY** to rise as the relative growth between US and China is reversing during 2021.
- **USD/INR** has moved lower as India seems to be past the peak in covid-19 outbreak. We look for higher USD/INR in H2 as broader dollar strength sets in.

Find our most recent [FX Forecast Update](#) for G10 and emerging markets [here](#). See also our weekly [FX Essentials](#) publication.

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What-to-watch: Growth, vaccines, China and elevated asset prices amid uncertainty

Global growth
Reopening of economies supported by vaccines and warmer weather boost global growth during Q2. Relative picture of Chinese outperformance will reverse in favor of US during 2021.

The Fed
The Fed has for now convinced markets that a tightening of monetary policy is a story for the fall. However, if employment and inflation surprises on the upside, fear of earlier Fed action can hurt EM currencies.

China
Data and markets continue to signal the Chinese credit cycle is peaking. We expect GDP growth to align with pre-corona trend as fiscal tightening and deleveraging continue.

Corona virus
While DM economies are expected to reopen during Q2, EM picture remains mixed. Most EM countries still rely on the Chinese and Russian vaccines.

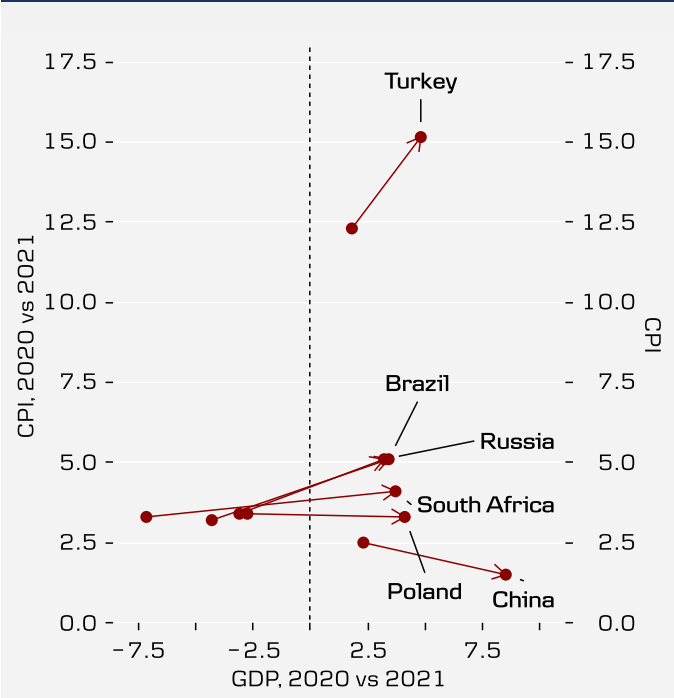
Note: Green reflects optimistic outlook, red is negative and grey is a neutral view
Source: Danske Bank

Moderating Chinese growth limits upside for commodity prices and EM FX

		2020				2021			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
External	China	Coronavirus	Fading virus impact	Recovery post-virus		China curbs credit, pace of growth comes down			
	Fed	Fed takes rates to zero, provides USD funding				Fed relatively sidelined			
	Trade war/commodities	phase 1 deal	cyclical uptick		tensions are to stay but more gradual and less disruptive				
Regions	CEE	high cpi	Corona shock	Fading virus impact	Recovery post-virus	Gradual recovery in CEE, inflation to stay			
	Latin America	Brazil weak, Mexico in recession		stabilization		Econs to remain low-growth environment			
	Asia	Coronavirus	Fading virus impact	Recovery post-virus		Asia remains relatively strong, tailwind from China fades			

Note: Green reflects optimistic outlook, red is negative and grey is a neutral view; colours reflect a broad macroeconomic view and are not necessarily FX specific.
Source: Danske Bank

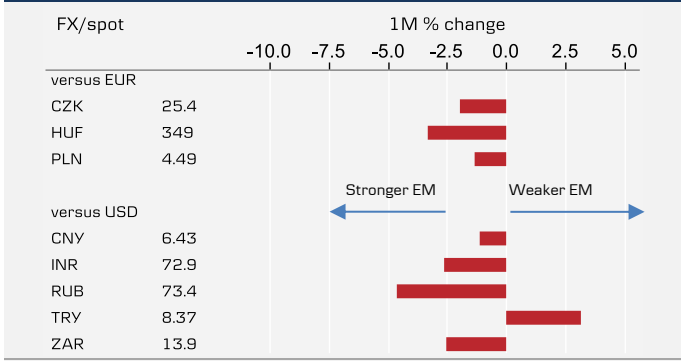
2021 generally brings GDP-recovery versus 2020



Note: Arrows indicate the change in Bloomberg consensus forecasts for growth and inflation from 2020 to 2021

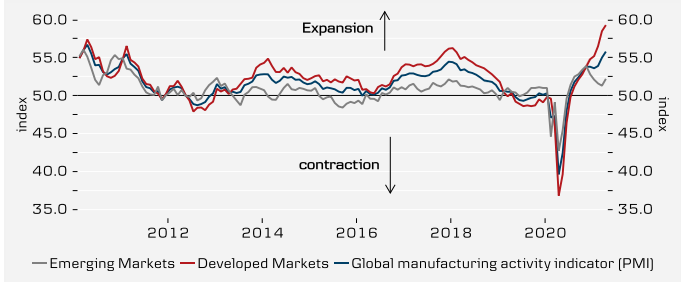
Source: Bloomberg

EM generally stronger this month, amid broad dollar decline



Note: An increase reflects a weaker currency versus EUR or USD.
Source: Bloomberg

Emerging markets staying in slight expansionary mode



Source: Bloomberg

Danske Bank EM FX forecast vs majors: USD and EUR

USD						
	Spot	+1m	+3m	+6m	+12m	
USD/PLN	3.683	3.78	3.78	3.83	3.87	
USD/HUF	286	304	307	318	324	
USD/CZK	20.857	21.25	21.26	21.45	21.74	
USD/RUB	73.589	75.00	75.00	72.00	72.00	
USD/TRY	8.380	8.30	8.50	8.70	9.10	
USD/ZAR	13.987	14.00	14.00	13.80	13.50	
USD/CNY	6.44	6.40	6.40	6.60	6.70	
USD/INR	73.05	73.50	73.50	74.00	74.50	
EUR						
	Spot	+1m	+3m	+6m	+12m	
EUR/PLN	4.500	4.53	4.50	4.48	4.45	
EUR/HUF	350	362	365	372	373	
EUR/CZK	25.5	25.5	25.3	25.1	25.0	
EUR/RUB	89.9	90	89	84	83	
EUR/TRY	10.24	10.0	10.1	10.2	10.5	
EUR/ZAR	17.09	16.8	16.7	16.1	15.5	
EUR/CNY	7.86	7.68	7.62	7.72	7.71	
EUR/INR	89.3	88.2	87.5	86.6	85.7	

Source: Danske Bank

Danske Bank EM FX forecast vs Scandies: DKK, SEK and NOK

DKK						
	Spot	+1m	+3m	+6m	+12m	
PLN/DKK	1.65	1.64	1.65	1.66	1.67	
HUF/DKK	2.12	2.05	2.04	2.00	2.00	
CZK/DKK	0.29	0.29	0.29	0.30	0.30	
RUB/DKK	8.27	8.26	8.34	8.84	8.99	
TRY/DKK	0.73	0.75	0.74	0.73	0.71	
ZAR/DKK	0.44	0.44	0.45	0.46	0.48	
CNY/DKK	0.95	0.97	0.98	0.96	0.97	
INR/DKK	0.083	0.084	0.085	0.086	0.087	
SEK						
	Spot	+1m	+3m	+6m	+12m	
PLN/SEK	2.25	2.23	2.27	2.30	2.34	
HUF/SEK	2.90	2.79	2.79	2.77	2.79	
CZK/SEK	0.40	0.40	0.40	0.41	0.42	
RUB/SEK	0.11	0.11	0.11	0.12	0.13	
TRY/SEK	0.99	1.01	1.01	1.01	0.99	
ZAR/SEK	0.59	0.60	0.61	0.64	0.67	
CNY/SEK	1.290	1.315	1.339	1.334	1.350	
INR/SEK	0.114	0.115	0.117	0.119	0.121	
NOK						
	Spot	+1m	+3m	+6m	+12m	
PLN/NOK	2.26	2.23	2.29	2.32	2.36	
HUF/NOK	2.91	2.79	2.82	2.80	2.82	
CZK/NOK	0.40	0.40	0.41	0.41	0.42	
RUB/NOK	0.11	0.11	0.12	0.12	0.13	
TRY/NOK	0.99	1.01	1.02	1.02	1.00	
ZAR/NOK	0.60	0.60	0.62	0.64	0.68	
CNY/NOK	1.294	1.315	1.352	1.347	1.363	
INR/NOK	0.114	0.115	0.118	0.120	0.123	

Source: Danske Bank

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