

Emerging Markets Monthly

USD weakness to support EM FX

- **Relative COVID-19 cases have contributed to relative performance of EM FX.**
- **Slowing growth in new cases shifts focus to global drivers such as direction of USD.**
- **Our base-case is a weakening USD over the coming months as the global and US recovery strengthens, resulting in a cautiously optimistic view on EM FX.**

Over the past month, the COVID-19 virus has continued to affect many emerging and frontier markets. The worst hit region appears to be LATAM, headed by Brazil but India, South Africa, and Russia have also struggled to contain the virus. The bad news is the virus is taking its toll on the economies; last week, the IMF significantly downgraded the growth outlook for 2020; especially for India (-6.5pp), Mexico (-3.9pp) and Brazil (-3.8pp). The good news is the growth rate of new cases is coming down in most countries with the exception of India and South Africa (see chart 1 and more through virus tracker on page 3). However, the test capacity in EM is weaker than in developed countries and this adds to less visibility on the situation (page 3).

Differences in the prevalence of COVID-19 have contributed to relative performance of EM FX over the past month (chart 2). LATAM currencies such as BRL, MXN, CLP and ARG have lost most ground to the USD as policy easing and/or worsening of economic fundamentals have been priced in. Meanwhile, in the other end of the spectre we find currencies of countries with best control over the virus, such as KRW, THB, CZK and to some extent PLN and RUB.

As the spread of the virus is starting to slow down and economic recoveries get underway in most countries, we think global factors will resume as key drivers in EM FX and the USD is set to be pivotal. In our base-case of a weakening USD over the coming months as Fed keeps the printing press open and the global and US recovery strengthens further, we are cautiously optimistic on EM FX. A key risk is the rapid spreading of the virus in many southern and western US states, which could derail the nascent US economic recovery and send the USD higher. In such downside risk scenario, EM FX will be under pressure.

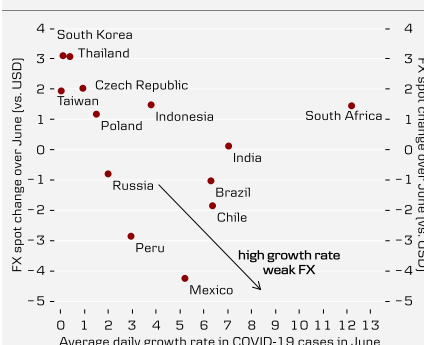
Chart 1. The spread of the virus is slowing in many EMs...

Infections, daily % increase, weekly averages							
	06-Apr	04-May	01-Jun	08-Jun	15-Jun	22-Jun	30-Jun
Latin America							
Brazil	10.6%	7.1%	4.4%	3.4%	3.3%	3.0%	2.1%
Chile	7.6%	5.7%	4.3%	3.9%	5.2%	1.8%	1.5%
Mexico	12.2%	6.1%	3.8%	3.3%	3.0%	2.8%	1.8%
Asia/Middle east							
India	13.9%	6.7%	4.4%	3.8%	3.6%	3.7%	3.5%
Indonesia	9.1%	3.3%	2.4%	3.0%	2.7%	2.3%	2.1%
Philippines	5.3%	2.5%	3.1%	2.5%	2.1%	2.4%	2.3%
Easter/Southern Europe							
Russia	16.3%	7.0%	2.1%	1.8%	1.5%	1.2%	1.1%
Poland	8.4%	2.3%	1.4%	1.6%	1.2%	0.9%	0.7%
Hungary	9.9%	1.2%	0.4%	0.3%	0.1%	0.2%	0.1%
Turkey	11.8%	1.4%	0.5%	0.6%	0.8%	0.7%	0.7%
Africa							
South Africa	3.6%	5.8%	5.8%	5.2%	5.0%	5.2%	4.6%

Note: Past performance is not a reliable guide to future returns

Source: Macrobond Financial, Danske Bank

Chart 2. ...but differences have had significant impact on EM FX in June.



Note: Past performance is not a reliable guide to future returns

Source: Macrobond Financial, Danske Bank

Quick view

- EUR/PLN set to see downward pressure as virus concerns in the global economy ease.
- EUR/HUF re-challenged by dovish central bank. Drift is to go higher.
- EUR/CZK has stabilised but near term we see risks tilted to more CZK strength.
- USD/RUB is likely to have overshot its fair value and we remain optimistic on RUB; target 73.26 versus EUR in 12M.
- USD/TRY is bid as TRY is on the verge of yet another FX crisis and FX interventions are very likely happening. We need broad USD declines to avoid further depreciation of TRY near-term, but this may just happen.
- USD/ZAR continues to drift lower, as investors are being pushed to hunt for yield. Recently, appetite for ZAR has stalled but we remain optimistic for ZAR strength to resume in coming months.
- USD/CNY should move lower with the broad USD weakness. A key upward risk is China-US tensions flaring up over HK.
- USD/INR is lagging versus EM peers, maybe due to continued COVID-19 issues. We target 72.00 on 12M.

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 (virus), commodity prices, US foreign policy (trade) and Fed

Global growth (Green)

The global economy is undergoing a gradual recovery led by China, but strengthening in other regions as well. We expect global PMI to continue to rise over the coming months as confidence increases.

Global monetary Policy (Green)

Fed have cut interest rates substantially and are supporting the global economy. This is starting to suppress broad USD strength. Furthermore, Peoples Bank of China is also easing quite substantially.

US foreign policy (Grey)

We now see a 50/50 risk Trump will scrap the US-China trade deal. The risk will increase as the US election approaches in November. Tariffs and uncertainty can move FX.

Corona virus (Grey)

The spreading of the virus appears to be slowing in most Ems. There are still risks for second wave and we expect the rebound to be rather timid in the most hard-hit countries like Brazil and India.

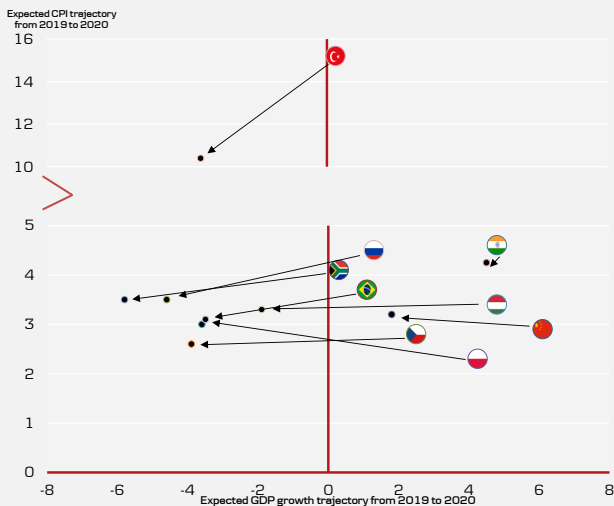
Note: Green reflects optimistic outlook, red is negative and grey is a neutral view
Source: Danske Bank

Near-term negative emerging market environment but turn in store in H2, as virus woes fade

		2019				2020			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
External	China	weak	stimulus effects	trade uncertainty	improving macro	Coronavirus	Fading virus impact	Recovery post-virus	
	Fed		no hike	two cuts	one cut	Fed takes rates to zero, provides USD funding			
	Trade war/commodities	ceasefire	escalation		trade talks	phase 1 deal	cyclical uptick		
Regions	CEE	broad-based slowdown in CEE				stabilizing but inflation adds	Corona shock	Fading virus impact	Recovery post-virus
	Latin America	significant growth downgrades			social turmoil	Brazil weak, Mexico in recession		stabilization	
	Asia	slowing		China drives recovery	Coronavirus	Fading virus impact	Recovery post-virus		

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

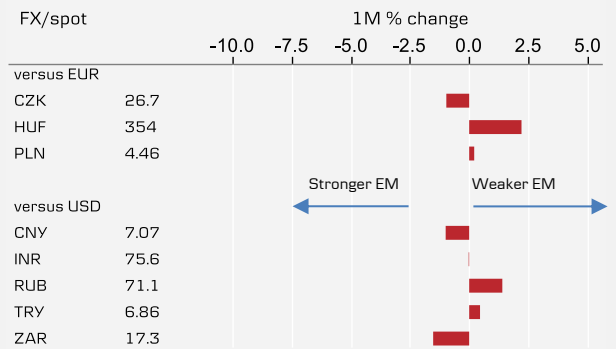
2020 brings weaker growth, lower inflation



Note: Arrows indicate the change in Bloomberg consensus forecasts for growth and inflation from 2019 to 2020

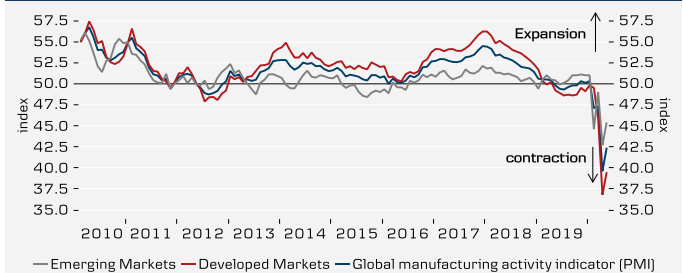
Source: Bloomberg, Macrobond Financial, Danske Bank

EM FX strength stalled over June - we expect it to resume



Note: An increase reflects a stronger currency versus EUR or USD
Source: Bloomberg, Macrobond Financial, Danske Bank

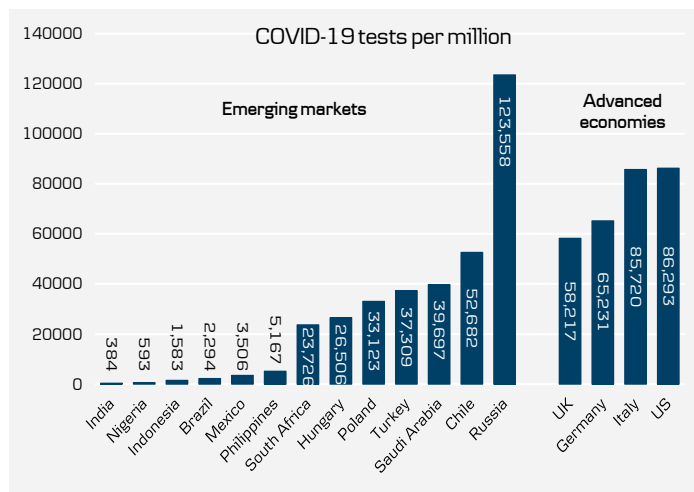
Global activity is starting to rebound but slowly



Source: Bloomberg, Macrobond Financial, Danske Bank

Infections, daily % increase, weekly averages												
	06-Apr	13-Apr	20-Apr	27-Apr	04-May	11-May	18-May	25-May	01-Jun	08-Jun	15-Jun	22-Jun
Latin America												
Brazil	10.6%	8.5%	6.9%	7.4%	7.1%	5.9%	5.9%	5.3%	4.4%	3.4%	3.3%	3.0%
Chile	7.6%	5.0%	4.1%	5.3%	5.7%	6.2%	6.7%	5.5%	4.3%	3.9%	5.2%	1.8%
Mexico	12.2%	8.6%	9.2%	6.9%	6.1%	5.0%	4.9%	4.1%	3.8%	3.3%	3.0%	2.8%
Asia/Middle east												
India	13.9%	9.5%	7.8%	6.1%	6.7%	5.4%	5.5%	4.7%	4.4%	3.8%	3.6%	3.7%
Indonesia	9.1%	7.2%	4.7%	3.4%	3.3%	3.2%	3.6%	2.5%	2.4%	3.0%	2.7%	2.3%
Philippines	5.3%	4.7%	2.6%	2.9%	2.5%	2.1%	1.6%	3.3%	3.1%	2.5%	2.1%	2.4%
Saudi Arabia	9.2%	10.8%	10.2%	6.6%	5.5%	4.9%	4.4%	2.5%	2.5%	3.2%	3.2%	2.1%
Easter/Southern Europe												
Russia	16.3%	15.3%	10.7%	7.5%	7.0%	4.6%	3.1%	2.4%	2.1%	1.8%	1.5%	1.2%
Poland	8.4%	4.7%	3.7%	2.5%	2.3%	2.2%	2.0%	1.7%	1.4%	1.6%	1.2%	0.9%
Hungary	9.9%	4.5%	3.9%	2.6%	1.2%	1.0%	0.9%	0.5%	0.4%	0.3%	0.1%	0.2%
Turkey	11.8%	6.7%	3.9%	2.1%	1.4%	1.1%	0.7%	0.7%	0.5%	0.6%	0.8%	0.7%
Africa												
South Africa	3.6%	5.9%	5.3%	5.5%	5.8%	6.2%	5.8%	5.5%	5.8%	5.2%	5.0%	5.2%
Nigeria	6.1%	8.0%	11.8%	10.6%	8.2%	4.4%	4.3%	3.9%	3.1%	3.6%	3.4%	2.8%

Deaths, daily % increase, weekly averages												
	06-Apr	13-Apr	20-Apr	27-Apr	04-May	11-May	18-May	25-May	01-Jun	08-Jun	15-Jun	22-Jun
Latin America												
Brazil	14.7%	11.1%	8.0%	7.7%	6.7%	5.7%	5.0%	3.9%	3.2%	2.5%	2.3%	1.9%
Chile	15.4%	8.2%	5.3%	4.5%	3.0%	4.8%	6.9%	5.8%	6.4%	11.2%	4.8%	3.2%
Mexico	19.6%	13.3%	10.6%	6.8%	7.2%	6.0%	5.2%	4.5%	4.8%	3.2%	3.0%	3.5%
Asia / Middle East												
India	20.4%	9.3%	7.2%	6.7%	7.2%	4.5%	4.3%	4.2%	4.3%	4.1%	5.5%	2.8%
Indonesia	8.1%	7.4%	4.4%	2.1%	2.1%	1.8%	3.1%	2.2%	2.0%	2.2%	2.2%	1.6%
Philippines	8.2%	7.1%	3.2%	2.9%	2.2%	2.2%	0.8%	1.4%	0.6%	1.1%	1.0%	1.0%
Saudi Arabia	8.8%	8.5%	5.7%	3.8%	4.5%	3.4%	3.3%	3.4%	5.0%	4.7%	4.0%	3.0%
Eastern / Southern Europe												
Russia	14.0%	16.8%	11.8%	8.7%	5.9%	4.8%	4.2%	4.3%	3.3%	2.6%	2.3%	1.6%
Poland	15.0%	7.6%	6.1%	3.5%	2.4%	2.2%	1.2%	1.0%	1.2%	1.0%	1.2%	0.9%
Hungary	16.6%	9.7%	5.4%	3.2%	2.8%	1.3%	1.1%	1.1%	0.5%	0.4%	0.3%	0.2%
Turkey	11.9%	8.0%	5.3%	3.0%	1.6%	1.3%	0.7%	0.7%	0.5%	0.4%	0.4%	0.4%
Africa												
South Africa	16.5%	11.9%	7.6%	5.3%	6.1%	5.0%	6.6%	6.8%	5.8%	5.9%	4.0%	3.7%
Nigeria	14.9%	10.0%	9.2%	13.7%	6.1%	4.7%	3.3%	3.1%	3.3%	2.5%	3.2%	1.4%



Source (all graphs): Macrobond Financial

Danske Bank EM FX forecast vs majors: USD and EUR

USD					
	Spot	+1m	+3m	+6m	+12m
USD/PLN	3.981	3.90	3.87	3.96	3.96
USD/HUF	317	300	304	320	324
USD/CZK	23.820	23.04	22.83	23.42	23.42
USD/RUB	71.126	69.00	68.00	67.00	66.00
USD/TRY	6.855	6.90	7.10	7.20	7.40
USD/ZAR	17.278	17.00	16.50	16.00	15.75
USD/CNY	7.07	7.00	7.00	7.15	7.15
USD/INR	75.60	75.00	75.00	74.00	72.00
EUR					
	Spot	+1m	+3m	+6m	+12m
EUR/PLN	4.457	4.48	4.45	4.40	4.40
EUR/HUF	354	345	350	355	360
EUR/CZK	26.670	26.50	26.25	26.00	26.00
EUR/RUB	79.634	79.35	78.20	74.37	73.26
EUR/TRY	7.677	7.94	8.17	7.99	8.21
EUR/ZAR	19.345	19.55	18.98	17.76	17.48
EUR/CNY	7.912	8.05	8.05	7.94	7.94
EUR/INR	84.971	86.25	86.25	82.14	79.92

Source: Danske Bank

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

DKK					
	Spot	+1m	+3m	+6m	+12m
PLN/DKK	1.672	1.664	1.676	1.695	1.695
HUF/DKK	2.10	2.16	2.13	2.10	2.07
CZK/DKK	0.279	0.281	0.284	0.287	0.287
RUB/DKK	0.094	0.094	0.095	0.100	0.102
TRY/DKK	0.971	0.940	0.914	0.933	0.908
ZAR/DKK	0.385	0.381	0.393	0.420	0.427
CNY/DKK	0.942	0.926	0.927	0.940	0.940
INR/DKK	0.088	0.086	0.086	0.091	0.093
SEK					
	Spot	+1m	+3m	+6m	+12m
PLN/SEK	2.35	2.34	2.36	2.43	2.43
HUF/SEK	2.96	3.04	3.00	3.01	2.97
CZK/SEK	0.39	0.40	0.40	0.41	0.41
RUB/SEK	0.13	0.13	0.13	0.14	0.15
TRY/SEK	1.37	1.32	1.29	1.34	1.30
ZAR/SEK	0.54	0.54	0.55	0.60	0.61
CNY/SEK	1.325	1.304	1.304	1.348	1.348
INR/SEK	0.123	0.122	0.122	0.130	0.134
NOK					
	Spot	+1m	+3m	+6m	+12m
PLN/NOK	2.41	2.39	2.36	2.34	2.32
HUF/NOK	3.04	3.10	3.00	2.90	2.83
CZK/NOK	0.40	0.40	0.40	0.40	0.39
RUB/NOK	0.14	0.13	0.13	0.14	0.14
TRY/NOK	1.40	1.35	1.29	1.29	1.24
ZAR/NOK	0.56	0.55	0.55	0.58	0.58
CNY/NOK	1.360	1.329	1.304	1.298	1.285
INR/NOK	0.127	0.124	0.122	0.125	0.128

Source: Danske Bank

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