20 June 2019

Emerging Markets Briefer

Lingering trade war spoils growth in emerging markets

The good start to 2019 for emerging markets and the global economy was spoiled by US President Donald Trump who toughened the US grip on international trade. In Q2 19 we saw not only China striking back at the US tariffs, but also countries such as India and Turkey joining the confrontation with President Trump. In particular, the escalation of the tech war and rising geopolitical tensions in the Middle East are throwing a shadow of uncertainty over emerging markets looking forward to Q3 19.

Yet, major central banks around the world have prepared several injections to alleviate the pain of trade war and economic slowdown. This is good news for both developed and developing economies as, for now, the December 2018 'blood bath' seems to have been postponed (not avoided though), and such countries as South Africa and Turkey will continue to deleverage their balance sheets. Thus, the risk of another TRY crisis is decreasing on a macrofundamental basis. We have already seen that central banks in many emerging economies such as India, Kazakhstan, Russia, and Ukraine have already started cutting rates. We expect that more central banks such as Brazil and Turkey will join the monetary easing trend in Q3 19. On the other hand, those monetary authorities which were moving towards hikes three months ago, like Hungary or Poland, are now set to remain dovish despite a rise in inflation.

We expect that emerging markets currencies will be supported by carry hunters in Q3 19. Despite more upcoming rate cuts by emerging markets central banks, the majority of developing economies will continue to see positive real rates. Good examples of that remain Brazil, Russia, Turkey and several frontier markets.

We believe that the China-US trade deal will be agreed when Trump faces significant financial stress on the US stock market. That could happen closer to Q4 19**.** There is still a risk that Trump could start a trade war against the EU or sanction European companies on the Nord Stream 2 project. If that happens in H2 19, the biggest losers would be Central and Eastern European economies.

Economic growth in emerging markets is set to continue slower in 2019 than in 2018, but monetary easing is bringing hopes for improvements in 2020-21. Given stabilisation in currencies across many emerging markets, accelerated inflation is set to calm down further in H2 19. We now see several already green lights in the emerging markets' risks heat map becoming greener, while yellow lights could still turn red.

The emerging markets heat map signals favourable monetary conditions for developing countries, while escalating trade war remains the major risk

		2018 Q1	2018 Q2	2018 Q3	2018 Q4	2019 Q1	2019 Q2	2019 Q3	2019 Q4
External	China	Rebound in Chinese economy	Slowdown begins	Economy weakness (trade war, lagged effects of tightening)			Trade war escalates		A trade deal is reached
External	Fed	Two hikes		Two hikes		no hike	no hike	three cuts	
External	Global liquidity	ECB is starting to prepare markets to monetary	ECB/Fed tightening			ECB & Fed become less hawkish	ECB & Fed become more dovish		
External	Geopolitical risks	Tightening of US trade regime postponed	Increased standoff between China and US			US-China ceasefire	trade war goes on		US-China trade deal (but Tech War continues)
Internal	EM fundamentals	Falling inflation, monetary easing and rebound in external demand		EM central banks are coming back to monetary tightening, FX deleveraging goes on		With exception of TRY, positive fundamentals			

Source: Danske Bank

Contents

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Poland: defying negative global outlook

Macro and political outlook

- **While the global economy has been feeling the heat** from the trade war between China and the US, the **momentum in the Polish economy has remained intact** driven by solid domestic demand. Manufacturing PMI has stabilised around 49.0. On the consumption side, retail sales are strong, expanding 11% in May (5% in April), supported by low unemployment and rapid wage growth. The relatively good performance of the Polish economy supports our Q2 19 real GDP growth forecast of 0.8% q/q. For 2019 as a whole, we have raised our real GDP growth rate forecast to 4.3% (from 3.6%). This growth rate is still above the potential growth rate of the Polish economy, meaning the labour market could tighten further.

Monetary policy outlook

- **Headline inflation climbed further in May to 2.3% from 2.2% in April.** The rise in the headline number is driven by a combination of higher energy prices and higher core inflation, which stabilised at 1.7% in May (having increased from just 0.6% at the beginning of the year). The low interest rates appear to be accommodative, as broad money supply expanded more than 10% in April. We think that core inflation will increase further to 2.0% towards the end of the year. However, given the dovish signals from global central banks, the market is pricing in a small chance of a 10bp rate cut in 2020, which seems dovish to us.

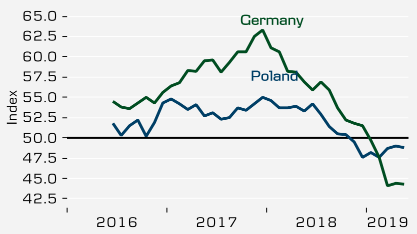
FX outlook

- **The renewed trade dispute between China and the US in early May initially sent EUR/PLN higher,** but with the possible rate cuts by the Fed and ECB, the pair has fallen back to below the range and our short-term forecast. The new-found strength may be premature if there is a severe escalation in trade tensions at the G20 meeting and the Fed does not deliver the rate cuts. We see a 50% chance of further deterioration in US-China trade relations, which would send the pair slightly higher. As a result, we see a slight case for EUR/PLN to edge higher on a short-term basis to 4.28 (previously 4.32) in 1M, but then as the Fed delivers on the cutting side, we see the pair going down to 4.25 (previously 4.28) in 3M, 4.23 (previously 4.25) in 6M and 4.23 (previously 4.23) in 12M.

Risk factors

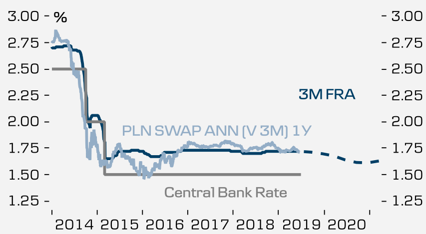
- **Risks are skewed to the downside for EUR/PLN in the near term** due to a potentially positive outcome from trade talks between the US and China at the G20 meeting and continued strong economic releases in Poland, leading to a more hawkish repricing by the central bank

PMI manufacturing now under the important 50 benchmark



Source: Markit, Macrobond Financial, Danske Bank

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



Source: Macrobond Financial

PLN

Credit rating:

S&P: A- (Stable)

Currency regime:

Free float (freely convertible)

Inflation target:

2.5%±1pp

Macro forecasts

	2018	2019	2020	2021	2022
GDP (% y/y)	5.2	4.3	3.8	3.0	3.6
GDP deflator (% y/y)	1.1	2.0	1.9	1.7	1.8
CPI (% y/y)	2.0	1.7	1.8	2.5	2.4
Private consumption (% y/y)	4.4	3.3	3.4	3.1	3.4
Fixed investments (% y/y)	9.2	6.4	3.8	3.1	3.4
Unemployment (%)	5.8	7.1	6.5	6.2	6.2
Current account (% of GDP)	-0.7	-0.5	-0.9	-1.1	-1.1

Source: Macrobond Financial, Danske Bank

Interest rate forecast

National Bank of Poland (NBP)		
Policy rate	1.50	
Next meeting	03/07/2019	
Next change	+25bp	Q1, 2020
End-2019	1.50	

Source: Bloomberg, Danske Bank

FX forecasts

EUR/PLN		
	Danske	Forward
18-Jun	4.26	
+3M	4.25	4.28
+6M	4.23	4.30
+12M	4.23	4.35
USD/PLN		
	Danske	Forward
18-Jun	3.81	
+3M	3.70	3.79
+6M	3.62	3.79
+12M	3.62	3.78

Source: Bloomberg, Danske Bank

Hungary: stellar growth will slow down

Macro outlook

- **Economic growth climbed to its 19-year high of 5.3% y/y in Q1 19** versus 5.1% a quarter earlier. Manufacturing PMI stays firmly above 50.0, despite plunging figures across large European economies. Industrial production growth remained solid through Q2 19 as the USA has not been targeting the EU with any new tariffs, yet. The current stance on monetary policy remains beneficial for further economic expansion in 2019 and 2020, albeit on a lower path.

- **The country continues to enjoy strong private consumption**, supported by a near all-time low unemployment rate and double-digit gross wage growth. However, consumer confidence has stayed shaky since the summer 2018, which signals a slowdown in private consumption in 2019.

- **Recently, Hungary has stayed away from escalating political conflicts with the EU** as the EU leadership is set to be changed in the near future. Yet, Hungary's Prime Minister Viktor Orbán still stands behind 'the independence of member states' economic policies, protesting against fiscal union in Europe.

Monetary policy outlook

- **In May 2019, the Hungarian central bank (MNB) kept its key rate unchanged** despite climbing inflation. We expect loose monetary policy to continue in Q3 19, while tightening could be delivered implicitly through liquidity tools, if inflation accelerates too much. We do not expect a hike by the MNB in 2019 anymore, as a soft ECB and global monetary easing will restrain the MNB.

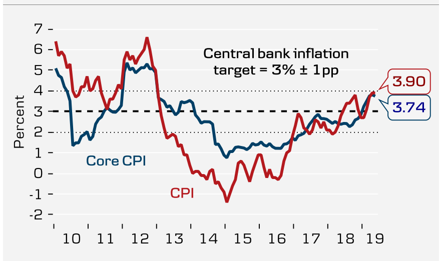
FX outlook

- **EUR's weakness on a soft ECB is set to weigh on the HUF.** Thus, we become bearish on the Hungarian currency in the short-term. Yet, tighter liquidity and a possible change in the ECB's stance in 2020 would support the HUF in the long term. We see EUR/HUF at 328 in 3M, at 320 in 6M and in 12M at 315.0.

Risk factors

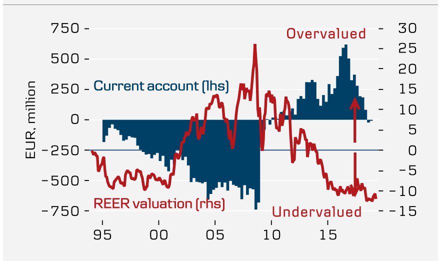
- A clear upside risk to our EUR/HUF forecast would be trade war starting between the EU and the USA, a significant slowdown of the German economy and a more dovish ECB.

Theoretically, a hike is imminent, but global monetary dovishness will not allow that



Source: MNB, Macrobond Financial, Danske Bank

Current account deficit could start weighing more on the HUF, if continued in 2019



Source: Macrobond Financial, Danske Bank

HUF

Credit rating:

S&P: 'BBB' (stable)

Currency regime:

Free float (freely convertible)

Inflation target:

3%±1pp

Macro forecasts

	2018	2019E	2020E	2021E
Real GDP (% y/y)	4.9	3.4	2.6	2.5
CPI (% average)	2.9	3.3	3.2	3.0
Unemployment (%)	3.6	3.5	3.6	3.5
Current account (% of GDP)	0.5	0.1	0.0	0.2

Source: Bloomberg, Danske Bank

Interest rate forecast

Hungarian Central Bank (MNB)	
Policy rate	0.90
Next meeting	25/06/2019
Next change	+25bp 2020
End-2019	0.90

Source: Bloomberg, Danske Bank

FX forecasts

EUR/HUF		
	Danske	Forward
18-Jun	323.3	
+3M	328.0	323.6
+6M	320.0	324.0
+12M	315.0	325.1
USD/HUF		
	Danske	Forward
18-Jun	289.04	
+3M	285.22	286.95
+6M	273.50	285.33
+12M	269.23	282.62

Source: Bloomberg, Danske Bank

Czech Republic: not immune to trade wars

Macro and political outlook

- **Despite a protracted slowdown in the euro area, the Czech economy is still faring pretty well.** Domestic demand is supported by high real wage growth (4.6% in Q1 19) and labour shortages continue to drive investments in automation. Still, export growth has slowed down on the back of weaker external demand and it is the main driver for our slight downward revision in GDP growth to 2.6% this year and 2.7% in 2020 (from 2.9% previously). The open Czech economy is vulnerable to global trade tensions and rising protectionism and a full-blown trade war could cloud the economic outlook significantly. Fiscal policy remains expansionary, but in light of strong tax revenues risks to public finances are low.

Monetary policy outlook

- **The CNB raised policy rates by 25bp to 2.0% in the May meeting**, as risks from the external environment seemingly cleared somewhat in Q1 19 and inflation surged to the upper end of the tolerance band. Since then global trade wars have staged a comeback and risks to the economic outlook have increased, while the koruna has appreciated against the euro. Hence we expect the CNB to be more cautious about further monetary tightening through the interest rate channel. As long as the exchange rate does not suddenly start to weaken again, we expect the CNB to be satisfied with the current interest rate level and foresee no further rate increases before Q2 20.

FX outlook

- **We expect several factors to keep EUR/CZK broadly stable** over the coming half year. A more dovish Fed that opens the door for cuts should improve investors' appetite for EM assets and monetary policy divergence between the CNB and the ECB will help underpin the CZK. On the other hand a further deterioration in the external environment and the relative overboughtness of the currency (as a legacy of the 'floor' policy from 2013-2017) pull in the other direction. As the economy picks up some speed in 2020 and the CNB mulls another rate hike, we see scope for further gradual CZK appreciation on a 12M horizon. Overall, we expect a slightly flatter EUR/CZK profile at 25.6 in 1-3M, 25.5 in 6M and 25.3 in 12M.

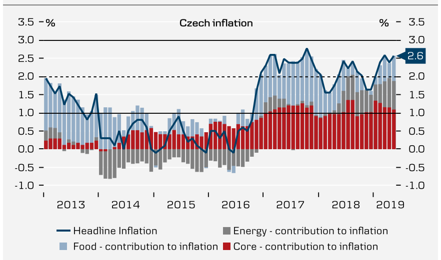
Risk factors

- **Risks to the economic outlook remain tilted to the downside**, notably from a further escalation in the US-China trade war and the lingering threat of US tariffs (Czech manufacturers are integral to Europe's car industry). In such a scenario, we could easily see EUR/CZK breaking back above the 26.0 level.

Open Czech economy is vulnerable to global trade tensions

Source: CPB, Eurostat, Macrobond Financial, Danske Bank

Inflation pressures remain elevated



Source: Eurostat, Macrobond Financial, Danske Bank

CZK

Credit rating:

S&P: 'AA-' (stable)

Currency regime:

Managed float

Inflation target:

2%±1pp

Macro forecasts

	2018	2019	2020	2021
GDP (% y/y)	2.9	2.6	2.7	2.8
CPI (% y/y)	2.1	2.5	2.1	2.0
Private consumption (% y/y)	3.1	3.0	2.7	2.9
Fixed investments (% y/y)	11.2	3.2	5.5	5.9
Unemployment (%)	2.3	2.9	3.2	3.5
Current account (% of GDP)	0.3	0.4	0.4	0.6

Source: Bloomberg, Danske Bank

Interest rate forecast

Czech National Bank (CNB)		
Policy rate	2.00	
Next meeting	26/06/2019	
Next change	+25bp	Q2, 2020
End-2019	2.00	

Source: Danske Bank

FX forecasts

EUR/CZK		
	Danske	Forward
18-Jun	25.61	
+3M	25.60	25.71
+6M	25.50	25.82
+12M	25.30	26.08
USD/CZK		
	Danske	Forward
18-Jun	22.89	
+3M	22.26	22.79
+6M	21.79	22.74
+12M	21.62	22.67

Source: Danske Bank

Russia: sanctions oblivion and weak consumer

Macro outlook

- **Q1 19 GDP preliminary growth data surprised on the downside,** reaching just 0.5% y/y versus the 1.2% expected by Bloomberg consensus and slowing down from the brisk Q4 19 growth of 2.7%. Private consumers did poorly due to a VAT increase and continuing tight monetary policy. We still expect 2019 GDP to expand moderately by 1.3% y/y, while we see some acceleration to 1.8% in 2020 due to notable monetary easing and the initiation of several investment projects by the state.
- **Private consumption hit the bottom in H1 19** due to accelerated inflation, deceleration of real wage growth, and increased VAT, which activated consumers before the hike. We expect a slight acceleration in H2 19 due to falling rates and RUB's stabilisation, if global sentiment does not sour too much.
- **Russia has been surprisingly left in 'sanctions oblivion' by the US.** That allowed the enjoyment of a steady flow from portfolio investors to Russian assets and the RUB. As the EU continues to prolong its sanctions by half a year, economic agents have already priced the current 'new normal'.

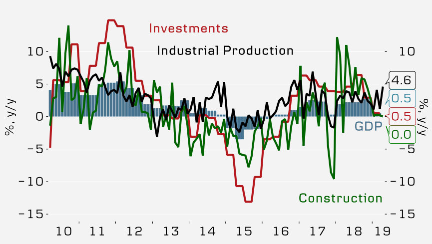
FX and monetary policy outlook

- **In June, the Bank of Russia (CBR) delivered a 25bp rate cut**, lowering the key rate to 7.50% in line with our expectation and Bloomberg and Reuters consensus. The decision fortifies our call for two more 25bp cuts in 2019, making possible a total 100bp decrease in the key rate on a 12M horizon to 6.50%, if the current conditions hold.
- **The RUB continues to enjoy stability,** as US Congress has not been active in pushing through anti-Russia sanctions.

Risk factors

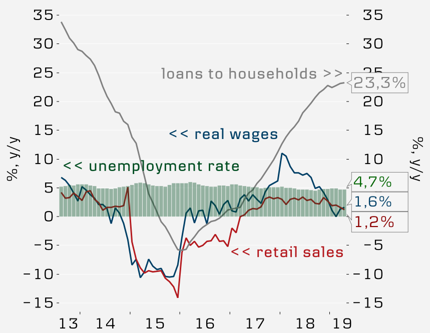
- Further **geopolitical escalation**, such as a worsening standoff with Ukraine, is a serious short- to medium-term risk for the RUB, Russian stocks and government debt. Upside risks come from an increasing oil price and a more dovish than expected central bank.

Economic growth components stay green, but growth is set to continue at a moderate level



Source: Macrobond Financial, Danske Bank

Private consumption is bottoming out in Q3 19



Source: Macrobond Financial, Danske Bank

RUB

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

Currency regime:
Free float

Inflation target:
4.0%

Macro forecasts

	2018	2019E	2020E	2021E
Real GDP (% y/y)	2.3	1.3	1.8	2.4
Private consumption, real (% y/y)	2.3	2.0	3.0	3.6
Fixed investments, real (% y/y)	0.6	2.4	3.8	8.2
Brent oil price (USD, average, futures)	72.4	61.2	60.8	60.5
Brent oil price (% y/y)	72.4	-15.5	-0.7	-0.3
Exports in USD (12M average % y/y)	25.3	18.0	20.0	15.0
Imports in USD (12M average % y/y)	4.4	2.0	3.2	5.0
MosPrime 3 months rate (% average)	7.75	7.90	7.30	7.10
CPI (% y/y)	2.9	4.8	3.8	3.5
Unemployment (%)	4.8	4.9	5.0	4.9
Budget balance (% of GDP)	2.6	1.9	1.0	1.5
Current account (% of GDP)	7.0	5.2	4.0	3.7

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

Interest rate forecast

Bank of Russia (CBR)		
Policy rate	7.50	
Next meeting	26/07/2019	
Next change	-25bp	Q3, 2019
End-2019	7.00	

Source: Bloomberg, Danske Bank

FX forecasts

EUR/RUB		
	Danske	Forward
18-Jun	71.57	
+3M	77.05	73.14
+6M	79.56	74.51
+12M	80.73	77.25

USD/RUB		
	Danske	Forward
18-Jun	63.98	
+3M	67.00	64.84
+6M	68.00	65.62
+12M	69.00	67.15

Source: Danske Bank

Turkey: Fed to bring relief amid recession

Macro outlook

- **The Turkish economy entered a recession in Q4 18,** while Q1 19 GDP climbed into green territory on a quarterly basis posting 1.3%. However, on an annual basis, Q1 19 GDP fell 2.6% y/y versus 3.0% y/y in the previous quarter. Industrial production shrank for the eighth month in a row in April 2019. The recovery in consumer confidence stopped in May 2019. The PMI indicator took a hit, declining further into contractionary territory at 45.3 in May. We expect 2019 GDP to contract 2.0% y/y (previously we expected 1.1% y/y growth) and 2020 GDP to expand 1.7% y/y, versus our previous expectation of 2.1%.
- **In June 2019, Moody's downgraded Turkey's long-term issuer ratings** to junk category B1 from Ba3 and maintained the negative outlook. The downgrade reflects Moody's view that the risk of a balance of payments crisis continues to rise, and with it the risk of a government default.
- **Weak TRY continues to fuel massive tourism expansion,** which is set to keep services up in 2019. Foreign arrivals have been constantly expanding since 2017.

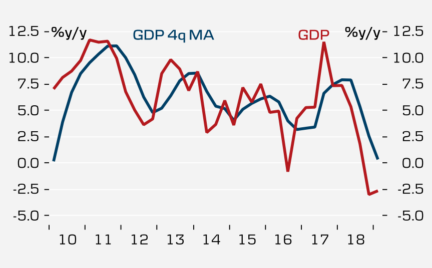
FX and monetary policy outlook

- **Turkey's central bank (TCMB) kept the one-week repo rate at 24%** in June 2019. After falling fairly strongly, CPI inflation has stabilised slightly under 20%, due partly to the pick-up in energy prices. Global monetary easing has opened the door for a 100bp cut in July 2019, we believe.
- **The TRY is stabilising on a global turn in monetary easing,** while the lower oil price could wipe away the extra burden on Turkey's external position. However, domestic risk has not disappeared. Large FX debt redemptions by the Turkish private sector and expected rate cuts are set to weigh on the TRY in 2019 and 2020.

Risk factors

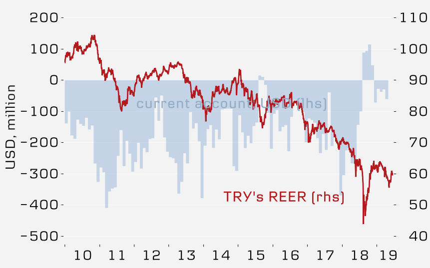
- **Downside risks to our TRY forecasts are both geopolitical and macro related.** If the confrontation with the US escalates, e.g. on the S-400 anti-aircraft weapon system deliveries by Russia. The TCMB's excessive monetary easing, driven by political pressure and worsening macro factors, also presents downside risks to our TRY forecasts. Fed monetary dovishness is a positive factor for TRY's path.

Turkey's GDP slide will reach the bottom in 2019



Source: Macrobond Financial, Danske Bank

Current account's historical surplus was temporary



Source: Macrobond Financial, Danske Bank

TRY

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

Currency regime:
Free float

Inflation target:
5.0% year-end 2020-2021

Macro forecasts

	2018	2019E	2020E	2021E
Real GDP (% y/y)	3.2	-2.0	1.7	3.0
Private consumption, real (%	1.7	-3.5	1.6	3.3
Fixed investments, real (% y/y)	0.0	-7.4	2.0	3.8
CPI (% average)	16.2	15.0	12.0	10.0
Unemployment (%)	11.0	13.0	12.9	11.1
Current account (% of GDP)	-4.0	-3.1	-3.0	-2.8

Source: Bloomberg, Danske Bank

Interest rate forecasts

C.B. of the Republic of Turkey (TCMB)		
Policy rate	24.00	
Next meeting	25/07/2019	
Next change	-100bp	Q3, 2019
End-2019	21.00	

Source: Bloomberg, Danske Bank

FX forecasts

EUR/TRY		
	Danske	Forward
18-Jun	6.54	
+3M	6.79	6.85
+6M	7.14	7.19
+12M	7.37	7.88

USD/TRY		
	Danske	Forward
18-Jun	5.85	
+3M	5.90	6.07
+6M	6.10	6.34
+12M	6.30	6.85

Source: Bloomberg, Danske Bank

South Africa: SARB to follow global central banks

Macro outlook

- **The South African economy contracted sharply in Q1 19** with real GDP falling 3.2% in q/q annualised terms. The contraction was relatively broad-based across sectors, but especially agriculture, mining and manufacturing performed poorly. Despite unstable electricity supply amid the ESKOM problems, manufacturing production grew 4.6% y/y in April, the strongest growth rate since 2016, signalling a positive start to Q2 19. However, with external demand likely to remain subdued given the challenging global macroeconomic situation and South African consumers remaining downbeat on the economic prospects, we expect GDP growth to remain muted. As a result, we have lowered our GDP forecast for South Africa to 0.7% in 2019 (from 1.4%). We have kept the forecast for 2020 unchanged at 1.9% given the possible positive impact of a trade deal between US and China and further easing by global central banks as well as the SARB.

Monetary policy outlook

- **As we called for in the previous EM briefer, inflation pressures have remain muted.** Headline inflation dropped slightly in April. The drop in core inflation was noteworthy, falling to 4.1% from 4.4% amid weak domestic economic momentum. At the last meeting in end-May, SARB highlighted downside risks to the South African economy and lowered its medium-term inflation forecast. While the interest rate was kept unchanged, two out of five members voted for a cut. We continue to believe that a cut in July is in the making given the weakness domestically and a softer monetary policy stance by global central banks. Such a cut will in our view be followed by another cut in November, with the risk of a cut at the September meeting.

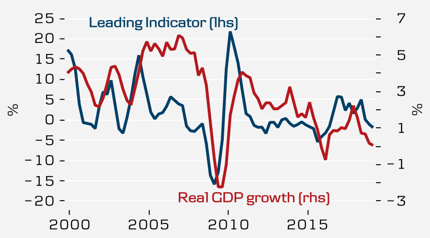
FX outlook

- **The Rand exchange rate has developed broadly as we expected** in the March EM briefer with the USD/ZAR remaining fairly constant with the Fed dovishness helping to cushion the negative impact on the Rand of the renewed trade tensions between the US and China and weak signs of the momentum in China. We see the USD/ZAR moving slightly higher over the next six months and target 14.8 in 3M and 15.0 in 6M while seeing a fall over the 12M to 14.5 as we expect the new government to carry out reforms strengthening the growth potential and trade agreement between the US and China.

Risks

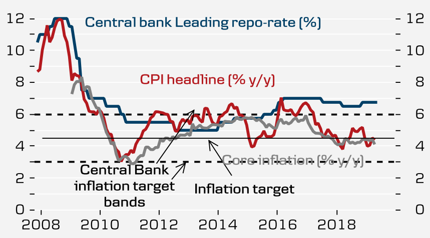
- **Risks are fairly balanced for our USD/ZAR forecast.** Among upside risks are a further deterioration in the US/China trade war and too little policy support from global central banks. Among the downside risks are on the other hand a breakthrough in the US/China negotiations at the G20 meeting end-June and stronger South Africa reform momentum.

The leading indicator points to modest growth



Source: Macrobond Financial

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



Source: Macrobond Financial

ZAR

Credit rating:

S&P: BB (stable)

Currency regime:

Free float (freely convertible)

Inflation target:

3-6%

Macro forecasts

	2018	2019	2020	2021
GDP (% y/y)	0.8	0.7	1.9	2.1
GDP deflator (% y/y)	3.9	5.0	4.8	4.8
CPI (% y/y)	5.2	4.5	4.5	4.5
Private consumption (% y/y)	1.8	1.4	1.7	1.9
Fixed investments (% y/y)	-1.4	-1.1	1.4	1.9
Unemployment (%)	27.1	27.9	28.2	28.3
Current account (% of GDP)	-2.4	-3.4	-3.6	-4.0

Source: Bloomberg, Danske Bank

Interest rate forecast

South African Reserve Bank (SARB)		
Policy rate	6.75	
Next meeting	18/07/2019	
Next change	-25bp	Q3, 2019
End-2019	6.25	

Source: Bloomberg, Danske Bank

FX forecasts

EUR/ZAR		
	Danske	Forward
18-Jun	16.23	
+3M	17.02	16.54
+6M	17.55	16.83
+12M	16.97	17.45

USD/ZAR		
	Danske	Forward
18-Jun	14.51	
+3M	14.80	14.66
+6M	15.00	14.83
+12M	14.50	15.17

Source: Bloomberg, Danske Bank

Brazil: slowing down amid hopes of reforms

Macro outlook

- **Brazil's economic growth slowed down further** to 0.5% y/y in Q1 19 from 1.1% y/y in Q4 18, depressed by the global economic slowdown. In USD terms, Brazil's exports started to grow in Q2 19 versus Q1 19. Yet, compared to Q2 18, the growth has not been stellar.
- **Industrial production growth is struggling to expand.** However, after the weak Q1 19 growth, we have cut our 2019 GDP expansion forecast to 1.2% y/y from the 2.2% y/y we expected in March 2019. Given the increased uncertainty in global growth due to the escalating China-US trade war, we have cut our 2020 GDP growth forecast to 2.1% y/y from 2.6% previously.
- **President Jair Bolsonaro secured a long-awaited victory** in Brazil's Congress when senators approved a proposal to fight social security fraud. That could bring additional relief to the country's fiscal problems, saving some USD26bn over the next ten years. Brazil also seems to be just a few weeks away from announcing a new social security system that will allow further balancing of the fiscal position.

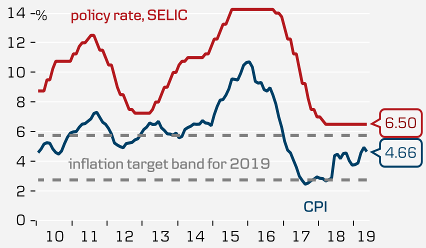
Monetary policy outlook

- **Brazil's central bank (BCB) has remained cautious through H1 19** under the governor Roberto Campos Neto. As Campos Neto has already pointed out, on economic slowdown global central banks continue 'to unleash doves', and inflation remains below the central bank target. We see that chances are growing the BCB will deliver a 25bp cut in Q3 19.

FX outlook

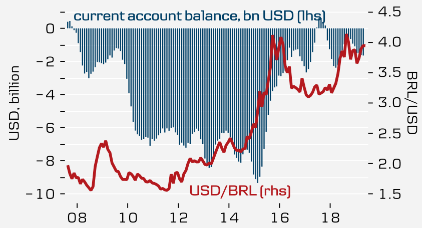
- **In March-May 2019 the BRL deflated on vanished 'Bolsonaro euphoria'** as lack of visible steps in pension reform weighed on the sentiment. Yet, positive news on reform progress and rising monetary dovishness globally fuelled some support to the BRL. Long-term prospects for the BRL will depend largely on the progress of reforms influenced by Bolsonaro.
- **Our USD/BRL projections assume the pension reform proposal will go through** and Brazil's economy will grow faster on rate cuts. Rapid approval of reforms by the government and further improving emerging market sentiment in 2019 on global monetary easing and the long-expected China-USA trade deal would be BRL positive.

A chance for one 25bp cut in 2019 is increasing as global monetary easing gets momentum



Source: BCB, Macrobond Financial, Danske Bank

Shrinking current account deficit supports the BRL long-term



Source: Macrobond Financial, Danske Bank

BRL

Credit rating:

S&P: BB- (stable)

Currency regime:

Free float (non-convertible)

Inflation target:

4.25%±1.5pp in 2019

4.0%±1.5pp in 2020

3.75%±1.5pp in 2021

Macro forecasts

	2018	2019E	2020E	2021E
Real GDP (% y/y)	1.1	1.2	2.1	2.3
Private consumption, real (%	1.9	1.1	2.7	2.9
Fixed investments, real (% y/y)	2.5	2.9	3.2	4.0
CPI (% average)	3.7	3.9	3.9	3.7
Unemployment (%)	12.3	11.9	11.0	10.8
Current account (% of GDP)	-0.8	-0.9	-0.8	-0.8

Source: Bloomberg, Danske Bank

Interest rate forecasts

Central Bank of Brazil (BCB)		
Policy rate	6.50	
Next meeting	31/07/2019	
Next change	-25bp	H2 19
End-2019	6.25	

Source: Bloomberg, Danske Bank

FX forecasts

EUR/BRL		
	Danske	Forward
18-Jun	4.32	
+3M	4.29	4.38
+6M	4.26	4.44
+12M	4.10	4.56

USD/BRL		
	Danske	Forward
18-Jun	3.86	
+3M	3.73	3.88
+6M	3.64	3.91
+12M	3.50	3.97

Source: Danske Bank

China: trade war clouds growth outlook

Macro outlook

- **The Chinese economy slowed down in 2018** as the trade war weighed on exports as well as private investments and household consumption. The battle to fight China's debt mountain and rise in shadow finance also weighed on activity. The squeeze on shadow finance in particular has hurt many private companies. In Q1 19 the economy showed signs of recovery but new headwinds have surfaced following a re-escalation of the trade war with the US in early May.
- **The outlook is now significantly blurred by the uncertainty over how severe the trade war will turn out**. While our baseline scenario is still a trade deal during H2 19, there is also a risk that we see a further escalation and that a deal is delayed into 2020. We expect growth to stay under pressure in the short term but to recovery towards the end of the year on the other side of a trade deal. However, if the risk scenario plays out and a deal is delayed further, the economy is likely to continue to suffer for longer.
- **Fiscal and monetary policy has been eased over the past year**, and the effect of this will help in keeping a floor under economic activity. We look for infrastructure spending and construction activity to stay quite robust.
- **In the World Bank Doing Business 2019 Survey, China jumped 30 places** up the list to number 46 of 190 countries. China was #3 on the list of biggest improvers. Contrary to popular belief, China is taking steps to reform and nurture private entrepreneurship. China also puts a high focus on technology investments and education. Both factors are key to continue an increase in productivity and prosperity. The opening up for investments has also gained pace on the back of the pressure from US President Trump.

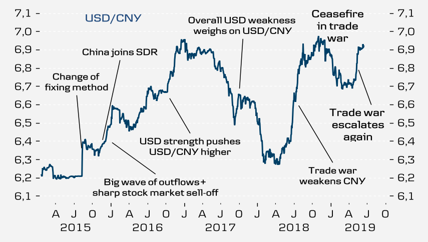
Monetary policy outlook

- The People's Bank of China (PBoC) has **eased policy over the past year and we look for more easing in H2 19 to underpin growth.** PBoC has used targeted lending measures towards the private sector and we look for more of this in the coming quarters on top of a further cut in the Reserve Requirement Ratio.

FX outlook

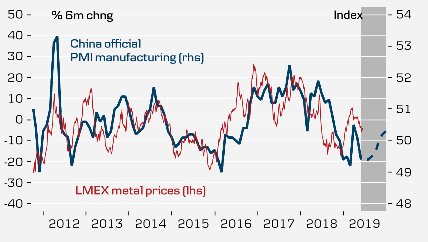
- **We expect the USD/CNY to rise further to 7.10 in 3M** as the road to a trade deal will likely get worse before it gets better. However, rate cuts by the Federal Reserve will temper the CNY weakness. On a 12M horizon we expect USD/CNY to move lower again on the back of a trade deal and moderate Chinese recovery as uncertainty fades gradually.

The tide has turned for USD/CNY



Source: Macrobond Financial, Bloomberg

Manufacturing recovery postponed due to trade war escalation



Source: Macrobond Financial, PBoC, Markit

CNY

Credit rating:

S&P: A+ (stable)

Currency regime:

Managed exchange rate versus basket of currencies

Inflation target:

3.0% for 2019

Interest rate forecast

People's Bank of China (PBOC)		
Policy rate	4.35	
Next meeting	No regular meetings	
Next change	-	Unchanged 2019
End-2019	4.35	

Source: Danske Bank

Macro forecasts

	GDP		Inflation	
	Danske	Consensus	Danske	Consensus
2018	6.6	6.6	2.1	1.6
2019	6.2	6.3	2.5	2.3
2020	6.1	6.0	2.2	2.3
2021	6.1	5.8	2.2	2.3

Source: Macrobond Financial Danske Bank

FX forecasts

EUR/CNY		
	Danske	Forward
18-Jun	7.73	
+3M	8.17	7.82
+6M	8.07	7.89
+12M	7.96	8.04

USD/CNY		
	Danske	Forward
18-Jun	6.91	
+3M	7.10	6.93
+6M	6.90	6.95
+12M	6.80	6.99

Source: Bloomberg, Danske Bank

India: strong mandate for reforms

Macro outlook

- **India's GDP growth slipped to 5.8% in Q1 19, the lowest rate in five years.** The slowdown was broad-based but the biggest drag came from investments. Export and import data also point to weaker growth. The global slowdown and weakness in the agricultural sector is weighing on the economy.
- **Uncertainty has increased due to the escalation of the US-China trade war.** While India may gain in the longer term as supply chains gradually move from China to other low-cost countries, the short-term outlook is weighed down by uncertainty over the effects on the global business cycle.
- **Prime Minister Narendra Modi got a strong mandate to rule for another five years** last month. **India has moved forward on reform** under the leadership of Modi and in its article IV Consultation report in August last year, the IMF stated that 'Stability-oriented macroeconomic policies and progress on structural reforms continue to bear fruit'. **India's financial markets responded positively to the election results and Indian stocks have outperformed most other emerging markets.** Bond yields have fallen sharply, partly also due to monetary policy easing.
- **The current account balance has deteriorated over the past two years** to -2.5% of GDP from around -1.0% in 2015-16. The government expects the fiscal balance to remain unchanged at -3.4% of GDP, but this is based on fairly optimistic assumptions for tax revenue and accounting measures that postpone some expenses.

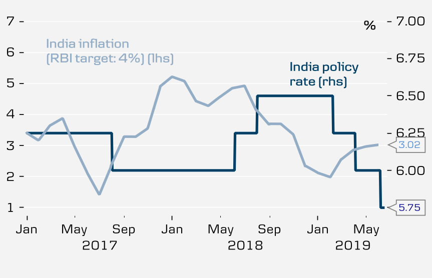
Monetary policy outlook

- **The Reserve Bank of India (RBI) cut its repo rate by 25bp in June to 5.75%** on the back of growth disappointments and inflation running below target (see chart). The RBI has taken a dovish turn with the change of central bank governor last year and we look for another two cuts in H2 19 to support growth.

FX outlook

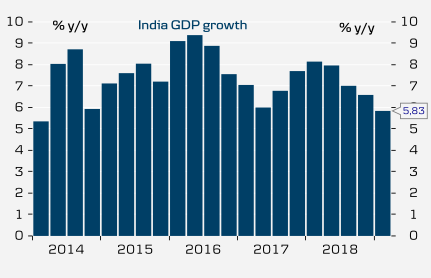
- **The USD/INR has been fairly stable** over the past quarter, trading in a range of 68.4-70.5. The USD/INR is kept in check by opposing forces: softer growth and rate cuts in India are a drag on the INR, while rate cuts by the Federal Reserve and lower oil prices are supporting factors. The Modi victory also helped confidence in reforms.

Falling inflation to pave the way for more monetary easing



Source: Macrobond Financial, Danske Bank

GDP growth hovering around 7%



Source: Macrobond Financial, Danske Bank

INR

Credit rating:

S&P: BBB- (stable)

Currency regime:

Free float

Inflation target:

4%±2pp

Macro forecasts

	GDP		Inflation	
	Danske	Consensus	Danske	Consensus
2018	7.3	7.3	4.1	4.1
2019	6.5	6.7	3.6	3.6
2020	7.0	7.1	4.0	3.7
2021	7.0	7.0	4.0	3.8

Source: Macrobond Financial, Danske Bank

Interest rate forecast

Reserve Bank of India (RBI)	
Policy rate	5.75
Next meeting	07/08/2019
Next change	-25 bp H2 2019
End-2019	5.25

Source: Bloomberg, Danske Bank

FX forecasts

EUR/INR		
	Danske	Forward
18-Jun	77.83	
+3M	79.35	79.02
+6M	79.56	80.45
+12M	78.39	83.26

USD/INR		
	Danske	Forward
18-Jun	69.57	
+3M	69.00	70.06
+6M	68.00	70.85
+12M	67.00	72.37

Source: Bloomberg, Danske Bank

Danske Bank's hedging recommendations: EMEA

Currency: PLN

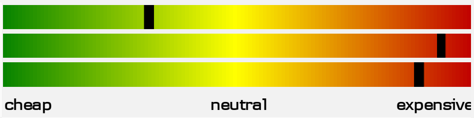
Instrument

Income: We recommend hedging PLN income via knock-in forwards.

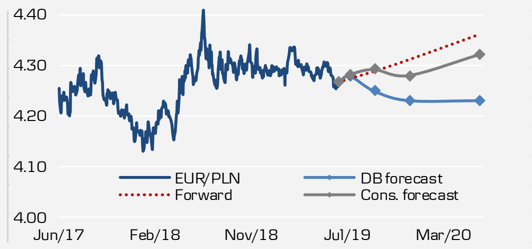
Expenses: We recommend hedging PLN expenses via FX forwards. Alternatively consider risk reversals.

Price indicators

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



Forecast



	1M	3M	6M	12M
DB forecast	4.28	4.25	4.23	4.23
Forward	4.27	4.29	4.31	4.36
Cons. forecast	4.28	4.29	4.28	4.32

Currency: RUB

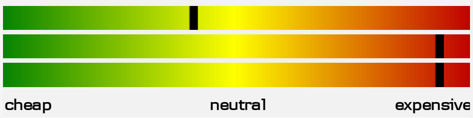
Instrument

Income: We recommend hedging RUB income via FX forwards despite the interest rate differential between RUB and EUR.

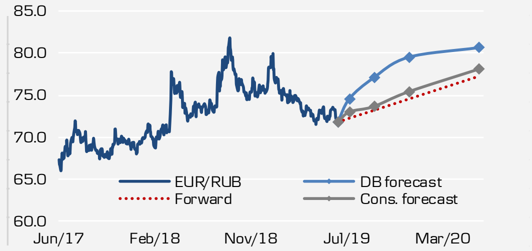
Expenses: We recommend hedging RUB expenses via knock-in forwards. Alternatively consider risk reversals.

Price indicators

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



Forecast



	1M	3M	6M	12M
DB forecast	74.56	77.05	79.56	80.73
Forward	72.23	73.16	74.54	77.33
Cons. forecast	72.99	73.62	75.42	78.18

Currency: HUF

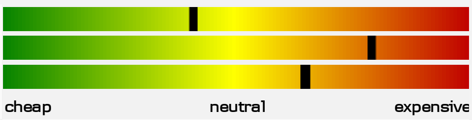
Instrument

Income: We recommend hedging HUF income via knock-in forwards.

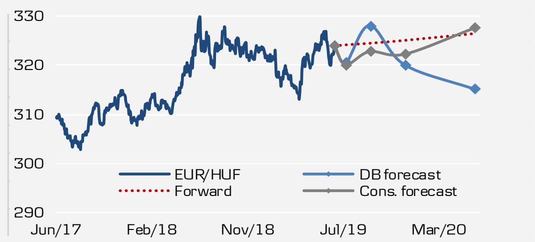
Expenses: We recommend hedging HUF expenses via FX forwards.

Price indicators

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



Forecast



	1M	3M	6M	12M
DB forecast	320.40	328.00	320.00	315.00
Forward	324.22	324.53	325.11	326.46
Cons. forecast	320.02	322.70	322.15	327.59

Currency: CZK

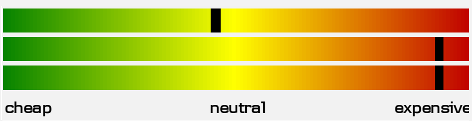
Instrument

Income: We recommend hedging CZK income via knock-in forwards.

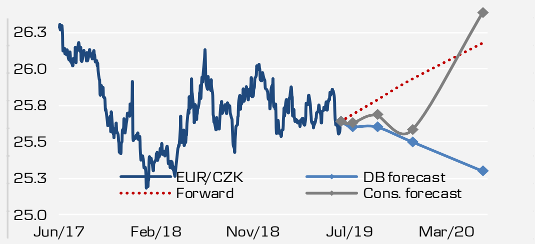
Expenses: We recommend hedging CZK expenses via FX forwards. Alternatively consider risk reversals.

Price indicators

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



Forecast



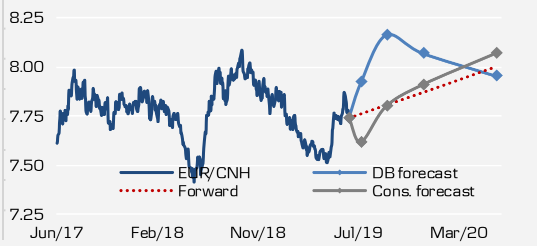
	1M	3M	6M	12M
DB forecast	25.60	25.60	25.50	25.30
Forward	25.68	25.78	25.93	26.18
Cons. forecast	25.63	25.69	25.58	26.38

Source: Danske Bank

Danske Bank's hedging recommendations: other emerging markets

Currency	Instrument: Income	Instrument: Expenses	Forecast
CNH (CNY)	We recommend hedging CNY denominated income via FX forwards despite the interest rate differential between CNH and EUR.	We recommend hedging CNY denominated expenses via FX forwards, which utilises the positive carry. Alternatively consider using risk reversals for near-term expenses, which maintains a larger profit potential.	

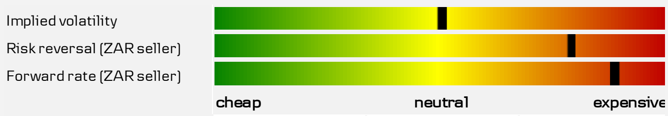
Price indicators

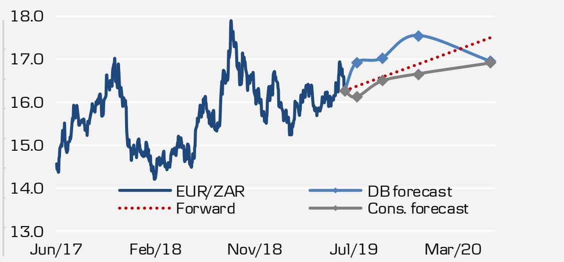


	1M	3M	6M	12M
DB forecast	7.92	8.17	8.07	7.96
Forward	7.76	7.81	7.87	8.01
Cons. forecast	7.62	7.80	7.91	8.07

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

Price indicators

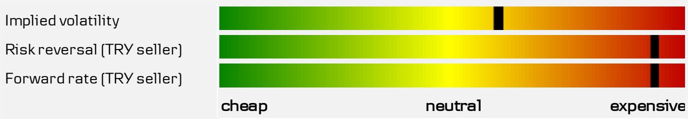


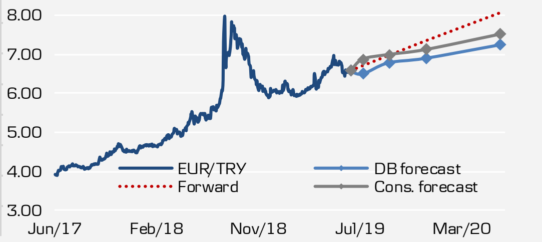


	1M	3M	6M	12M
DB forecast	16.93	17.02	17.55	16.97
Forward	16.39	16.59	16.90	17.52
Cons. forecast	16.14	16.49	16.66	16.91

Currency	Instrument: Income	Instrument: Expenses	Forecast
TRY	We recommend hedging TRY income via knock-in forwards.	We recommend hedging TRY expenses via FX forwards. Alternatively consider risk reversals.	

Price indicators





	1M	3M	6M	12M
DB forecast	6.50	6.79	6.90	7.25
Forward	6.70	6.96	7.35	8.09
Cons. forecast	6.87	6.99	7.11	7.51

Source: Danske Bank

FX forecasts

Core – major

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
EUR	18-Jun			1.12		746.7		1065.5		977.9	
	+3M			1.15	1.13	746.3	746.2	1080.0	1067.1	960.0	983.0
	+6M			1.17	1.14	745.9	745.6	1090.0	1069.9	940.0	987.8
	+12M			1.17	1.15	745.5	744.5	1100.0	1069.9	930.0	998.7
USD	18-Jun	1.12				667.5		952.4		874.1	
	+3M	1.15	1.13			649.0	661.6	939.1	946.1	834.8	871.5
	+6M	1.17	1.14			637.5	656.7	931.6	942.3	803.4	869.9
	+12M	1.17	1.15			637.2	647.1	940.2	930.0	794.9	868.1
JPY	18-Jun	121.4		108.5		6.15		8.78		8.06	
	+3M	123.1	121.4	107.0	107.7	6.07	6.15	8.78	8.79	7.80	8.10
	+6M	128.7	121.5	110.0	107.0	5.80	6.14	8.47	8.81	7.30	8.13
	+12M	128.7	121.5	110.0	105.7	5.79	6.13	8.55	8.80	7.23	8.22

Source: Macrobond Financial, Danske Bank

Wider CEE

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
PLN	18-Jun	4.26		3.81		175.3		250.2		229.6	
	+3M	4.25	4.28	3.70	3.79	175.6	174.3	254.1	249.3	225.9	229.7
	+6M	4.23	4.30	3.62	3.79	176.3	173.3	257.7	248.7	222.2	229.6
	+12M	4.23	4.35	3.62	3.78	176.2	171.2	260.0	246.1	219.9	229.7
HUF	18-Jun	323.3		289.0		2.31		3.30		3.02	
	+3M	328.0	323.6	285.2	286.9	2.28	2.31	3.29	3.30	2.93	3.04
	+6M	320.0	324.0	273.5	285.3	2.33	2.30	3.41	3.30	2.94	3.05
	+12M	315.0	325.1	269.2	282.6	2.37	2.29	3.49	3.29	2.95	3.07
CZK	18-Jun	25.61		22.89		29.16		41.60		38.18	
	+3M	25.60	25.71	22.26	22.79	29.15	29.02	42.19	41.51	37.50	38.23
	+6M	25.50	25.82	21.79	22.74	29.25	28.87	42.75	41.43	36.86	38.25
	+12M	25.30	26.08	21.62	22.67	29.47	28.55	43.48	41.02	36.76	38.29

Source: Macrobond Financial, Danske Bank

CIS

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
RUB	18-Jun	71.57		63.98		10.43		14.89		13.66	
	+3M	77.05	73.14	67.00	64.84	9.69	10.20	14.02	14.59	12.46	13.44
	+6M	79.56	74.51	68.00	65.62	9.38	10.01	13.70	14.36	11.81	13.26
	+12M	80.73	77.25	69.00	67.15	9.23	9.64	13.63	13.85	11.52	12.93

Source: Macrobond Financial, Danske Bank

MEA

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
TRY	18-Jun	6.54		5.85		114.2		162.9		149.5	
	+3M	6.79	6.85	5.90	6.07	110.0	109.0	159.2	155.8	141.5	143.5
	+6M	7.14	7.19	6.10	6.34	104.5	103.7	152.7	148.7	131.7	137.3
	+12M	7.37	7.88	6.30	6.85	101.1	94.5	149.2	135.8	126.2	126.8
ZAR	18-Jun	16.23		14.51		46.0		65.7		60.3	
	+3M	17.02	16.54	14.80	14.66	43.8	45.1	63.5	64.5	56.4	59.4
	+6M	17.55	16.83	15.00	14.83	42.5	44.3	62.1	63.6	53.6	58.7
	+12M	16.97	17.45	14.50	15.17	43.9	42.7	64.8	61.3	54.8	57.2

Source: Macrobond Financial, Danske Bank

Latin America

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
BRL	18-Jun	4.32		3.86		173.0		246.9		226.6	
	+3M	4.29	4.38	3.73	3.88	174.0	170.3	251.8	243.6	223.8	224.4
	+6M	4.26	4.44	3.64	3.91	175.1	167.9	255.9	240.9	220.7	222.4
	+12M	4.10	4.56	3.50	3.97	182.1	163.1	268.6	234.4	227.1	218.8

Source: Macrobond Financial, Danske Bank

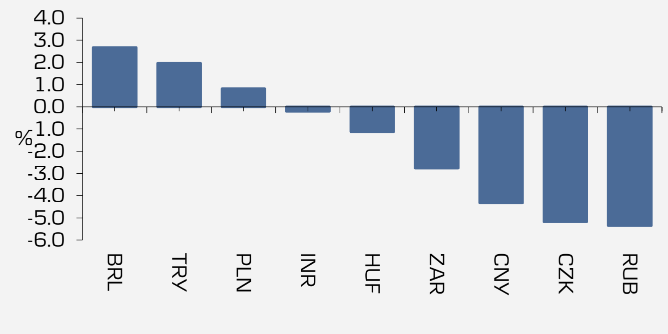
Emerging markets Asia

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
CNY	18-Jun	7.73		6.91		96.6		137.9		126.6	
	+3M	8.17	7.82	7.10	6.93	91.4	95.4	132.3	136.5	117.6	125.7
	+6M	8.07	7.89	6.90	6.95	92.4	94.5	135.0	135.6	116.4	125.2
	+12M	7.96	8.04	6.80	6.99	93.7	92.6	138.3	133.1	116.9	124.2
INR	18-Jun	77.83		69.57		9.59		13.69		12.56	
	+3M	79.35	79.02	69.00	70.06	9.41	9.44	13.61	13.50	12.10	12.44
	+6M	79.56	80.45	68.00	70.85	9.38	9.27	13.70	13.30	11.81	12.28
	+12M	78.39	83.26	67.00	72.37	9.51	8.94	14.03	12.85	11.86	12.00

Source: Macrobond Financial, Danske Bank

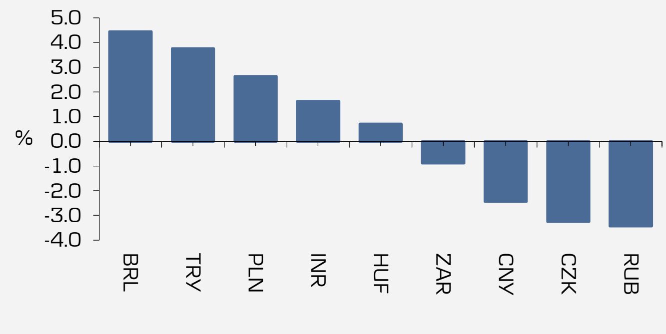
Forecasts vs forwards

3M – base currency EUR



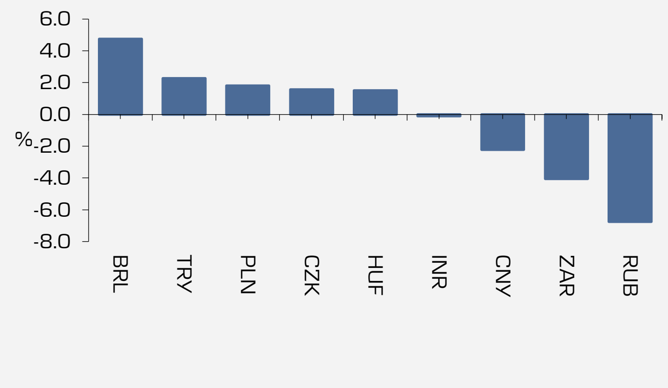
Source: Macrobond Financial, Danske Bank

3M – base currency USD



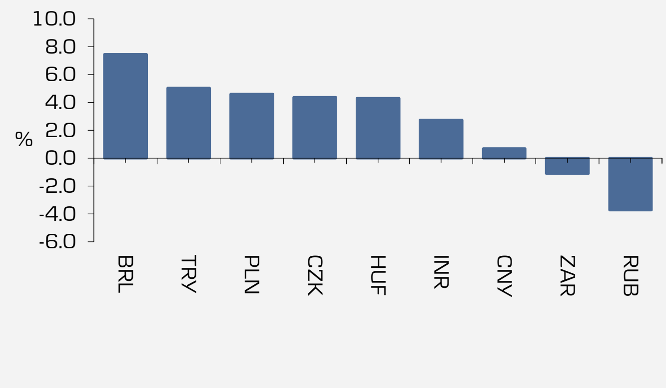
Source: Macrobond Financial, Danske Bank

6M – base currency EUR



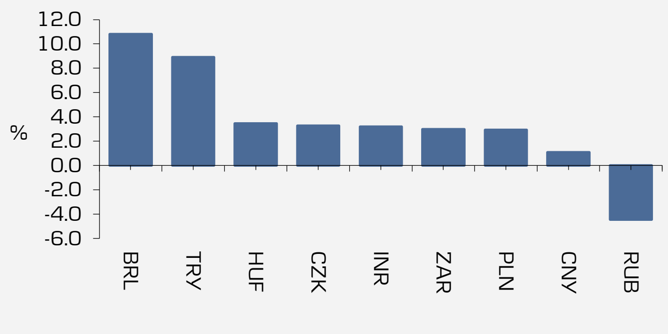
Source: Macrobond Financial, Danske Bank

6M – base currency USD



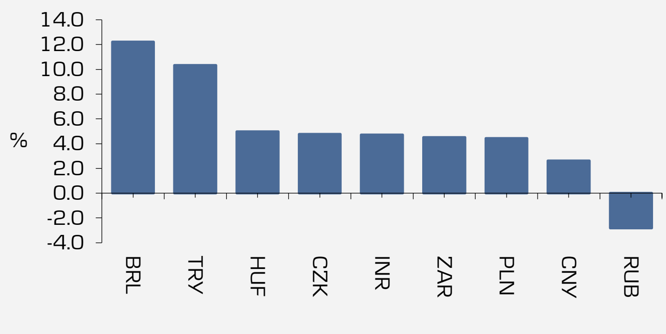
Source: Macrobond Financial, Danske Bank

12M – base currency EUR



Source: Macrobond Financial, Danske Bank

12M – base currency USD



Source: Macrobond Financial, Danske Bank

Monetary policy calendar

Calendar

	Policy Rate (%)	Latest Change		Next Change		Next Meeting	Year-end 2019 (%)
	19 June 2019						
Wider CEE							
PLN	1.50	- 50 bp	Mar, 2015	+25bp	Q1, 2020	03/07/2019	1.50
HUF	0.90	- 15 bp	May, 2016	+25bp	2020	25/06/2019	0.90
CZK	2.00	+25 bp	May, 2019	+25bp	Q2, 2020	26/06/2019	2.00
TRY	24.00	+625 bp	Sep, 2018	-100bp	Q3, 2019	25/07/2019	21.00
CIS							
RUB	7.50	-25 bp	Jun, 2019	-25bp	Q3, 2019	26/07/2019	7.00
MEA							
ZAR	6.75	+ 25 bp	Nov, 2018	-25bp	Q3, 2019	18/07/2019	6.25
LATAM							
BRL	6.50	-25 bp	Mar, 2018	-25bp	Q3, 2019	31/07/2019	6.25
EM Asia							
CNY	4.35	- 15 bp	Oct, 2015	-	Unchanged 2019	No regular meetings	4.35
INR	5.75	- 25 bp	Jun, 2019	-25 bp	H2, 2019	07/08/2019	5.25

Source: Bloomberg, Danske Bank

Disclosures

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Expected updates

Quarterly.

Date of first publication

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Report completed: 19 June 2019, 16:30 CEST

Report first disseminated: 20 June 2019, 06:00 CEST