

# Emerging Markets Briefer

November 02, 2007

Investment research

## The central banks' new dilemma

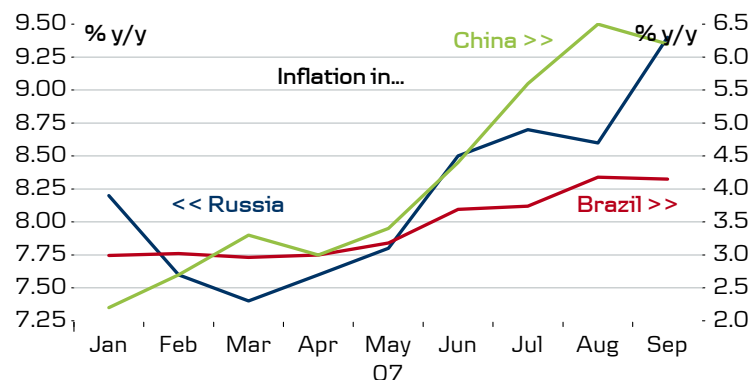
### The positive EM sentiment continued in October...

- October has brought another Fed cut, continued USD weakness, and surging commodity prices. The positive Emerging Markets (EM) sentiment we saw in September has carried on into October as most EM currencies have moved more strongly and local equity markets have set new records.
- Higher commodity prices have indeed supported external balances in those countries that are net-exporters of commodities, and have thus stimulated the respective currencies. In particular the Latin American region has benefited from this.

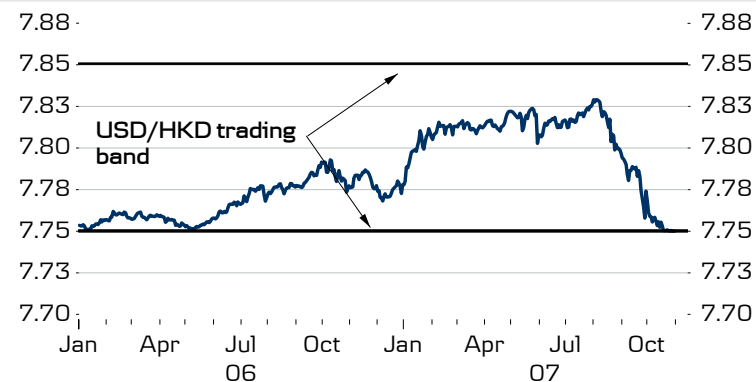
### ...But how will authorities react to higher inflation?

- There are good reasons to believe that Asia will continue to look very strong. While this naturally should support performance in those markets, it also adds to an increased probability of event risks - eg, local authorities may consider imposing capital restrictions.
- We expect CEE currencies to outperform EUR, and major LATAM currencies to outperform USD. But one should not forget that chances of more negative events can hit the markets - mainly from the financial sector, but also from a less positive outlook for US growth.

### Inflationary pressures rising globally



### Speculation about wider HKD trading band



## Movers and shakers – last month and in the month ahead

### The central banks' new dilemma

October has brought another Fed cut, continued USD weakness and surging commodity prices. The positive Emerging Markets (EM) sentiment we saw in September has carried on into October as most EM currencies have moved stronger and local equity markets have set new records. Higher commodity prices have indeed supported external balances in those countries that are net exporters of commodities, and have thus stimulated the respective currencies. In particular the Latin American region has benefited from this.

But there is a flipside to the coin. During October it has become increasingly noticeable that rising commodities feed into inflationary pressures in Emerging Markets. In Central and Eastern Europe for example inflation data has during the last month brought some worrying surprises driven by in particular higher food prices, which in turn presented local monetary authorities with a new dilemma.

The trade-off between high economic growth and low and stable inflation is now more visible than it has been over the last couple of years, where an increasingly globalised world has brought lower inflation, and rich access to liquidity on global financial markets has supported economic growth. In the current environment with tighter global credit conditions and rising inflationary pressures, the relevant question is now how local central banks will deal with this trade-off.

The answer naturally depends on local monetary regimes. In the major **LATAM countries**, currencies are, with the exception of Argentina, freely floating, and local central banks have recently decided to tighten monetary conditions or bring ongoing monetary easing cycles to an end. Among the freely floating currency regimes in the **CEE region**, central banks have in general moved toward a more hawkish stance and we have seen a few rate hikes recently. Among the “peggers” in CEE – including the Baltics and Bulgaria – central banks have no direct measurements to dampen inflation through higher rates, and those countries are therefore among those who now face the highest inflation in the EM universe – something that is clearly unsustainable for much longer..

In the **CIS region** similar problems arise as the largest economies are all “dollar-peggers” to some extent. Central banks in CIS have been very reluctant to allow for any appreciation against USD, which means that the ongoing USD weakness has an even larger effect on inflation in this region. Another factor adding to this is that food expenditures constitute as much as 50% of the total consumption basket in this region. In the short run, we do not expect authorities to allow for stronger currencies, instead they will “try out” different well-known (and not very useful) measures such as price controls and export tariffs. This will not help bring down inflation, instead they should probably allow for more freely floating currencies.

In **Asia** old habits die hard too. Most countries are still trying to “shadow” USD even though decoupling of Asian and US growth and the weaker USD increasingly make it incompatible with price stability. Financial markets are increasingly questioning the sustainability of the monetary and exchange rate regimes in Asia. Recently there has been increasing speculation about a major one-off revaluation of CNY and possible widening of the narrow HKD trading band, see *Flash Comment - China: Is the gradual CNY appreciation policy sustainable?* – 24 October. However in China the boost to inflation from food prices probably peaked in August, which is probably the main reason why the Chinese authorities will allow another boost from a 10% increase in oil prices in November.

Going forward, there are good reasons to believe that Asia will continue to look very strong. Capital is basically flooding Asian markets. While this naturally should support performance in those markets, it also adds to an increased probability of event risks – eg, local authorities may consider imposing capital restrictions or similar measures to reduce monetary pressures. The outlook for USD is still rather bleak, and this will in our view support CEE currencies over the coming months, as they tend to strengthen against the euro, when EUR/USD rises. Furthermore the major LATAM currencies are expected to outperform USD, as commodities should remain strong if USD should weaken further. Clearly one should not forget that chances of more negative events can hit markets – mainly stemming from the financial sector, but also the less positive outlook for US growth in the coming quarters.

# Emerging Market performance over the past month

Chart 1: FX change against EUR and USD

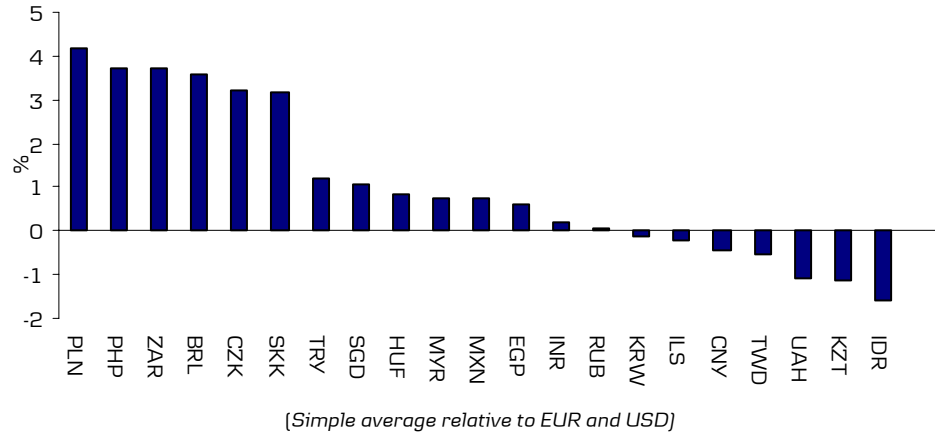


Chart 2: Risk adjusted FX change against EUR and USD

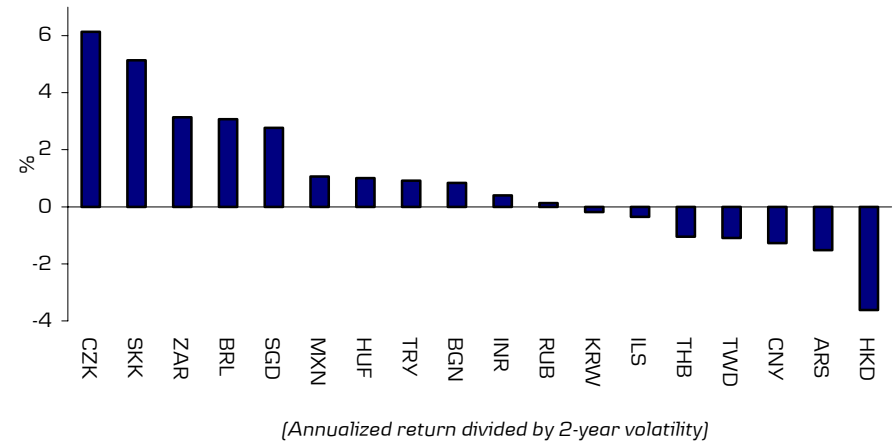


Chart 3: Change in 2 year swap yield

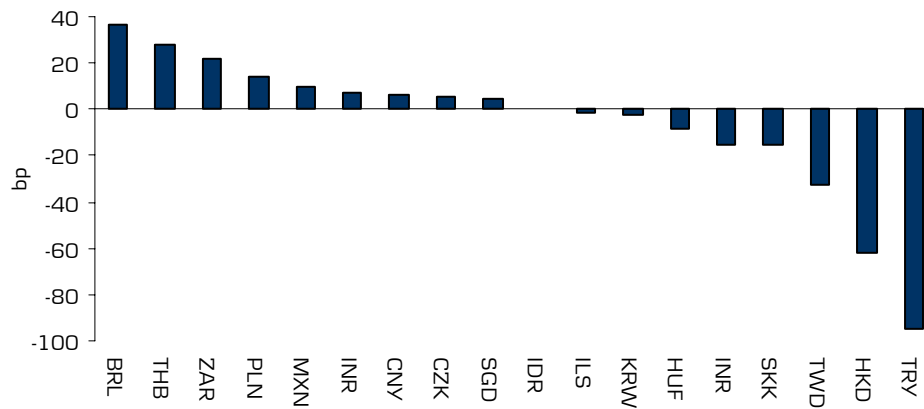
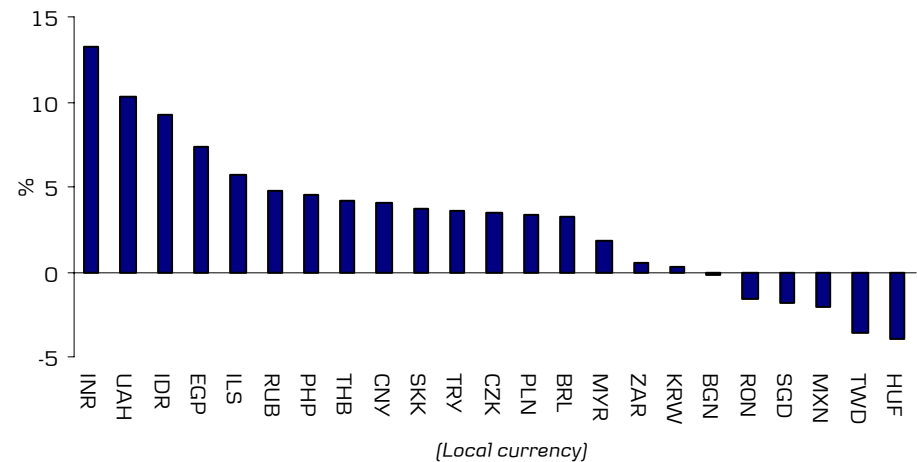
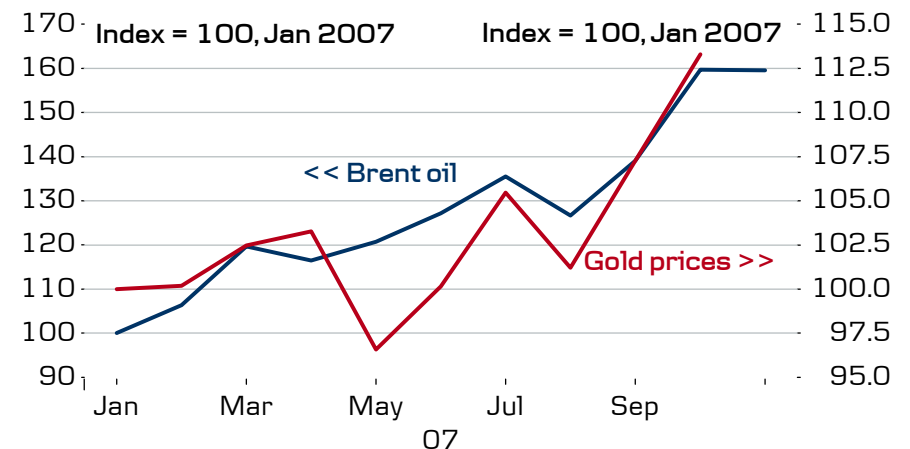
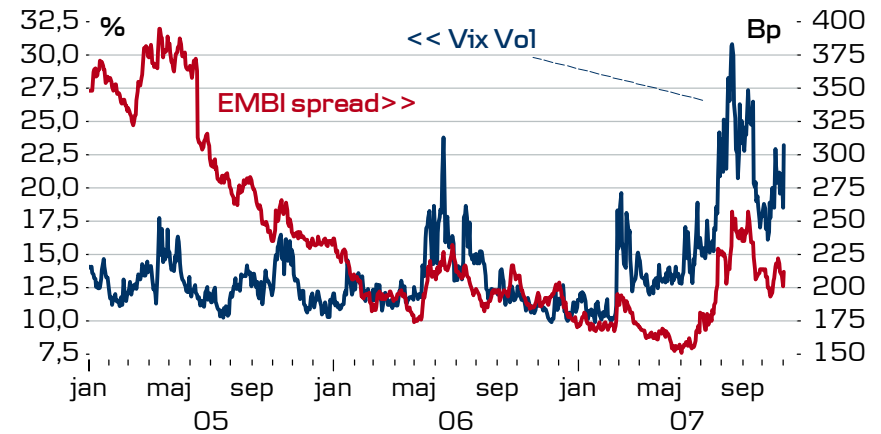


Chart 4: Stock market performance



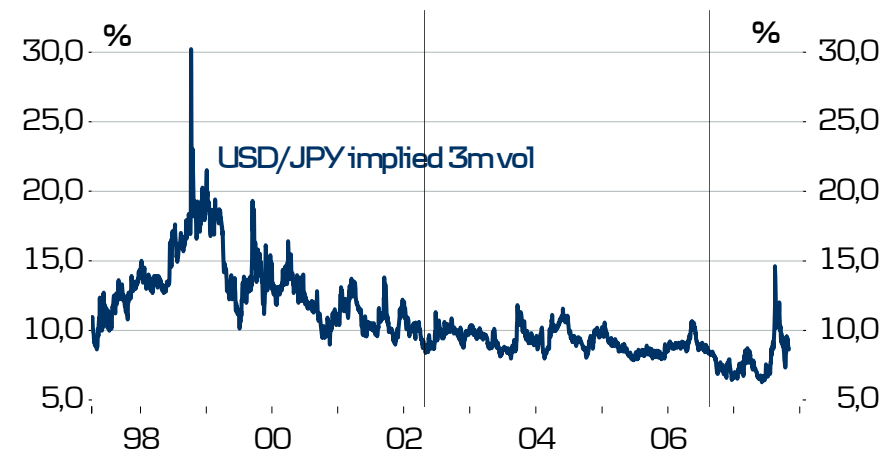
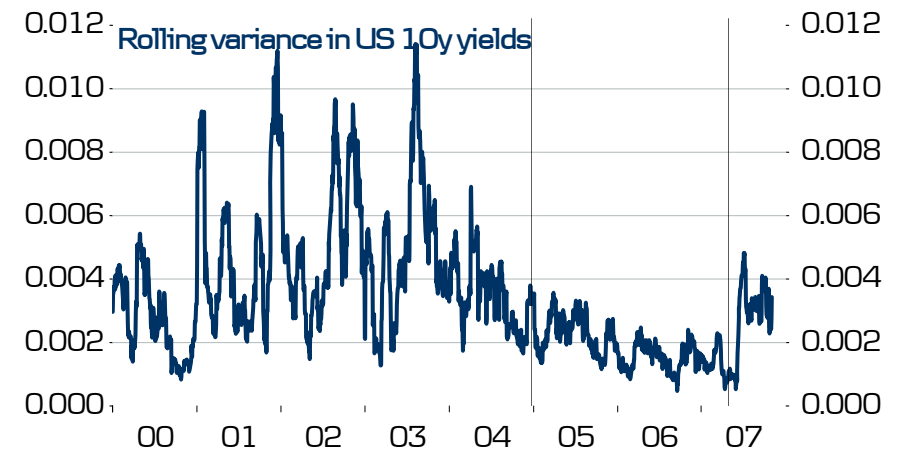
## Financial indicators - I

- The Vix volatility index has moved higher in October after dropping markedly in September.
- The Emerging Markets bond spread (EMBI spread) has remained fairly stable throughout October.
- Commodity prices continue to rise to new highs, driven higher by strong demand and continued USD weakness.



## Financial indicators - II

- Volatility in the US fixed income markets has remained at relatively high levels, and the down trend in variability since 2003 is broken.
- JPY volatility has been extremely low over the past couple of years. As the credit crunch spread we saw a spike, which made carry trades significantly riskier.
- After the FED cut, JPY volatility has fallen as carry trades came in fashion again.





## FX Trade recommendations



### Performance



Performance	Count	Av. return	Av. Horizon (days)	Av Vol.
Closed	11	0.11	43	10.29
Open	3	0.83	112	4.61
All	14	0.26	55	9.39



Recently closed	Start Date	Closing date	Spot open	Spot close	Target	Stop	P/L (incl carry)
Buy USD/ZAR	28-09-2007	11-10-2007	6.880	6.780	7.15	6.78	-1.64


Open	Start Date	Today	Spot open	Spot	Target	Stop	P/L (incl carry)
Buy RUB-basket	09-02-2007	02-11-2007	29.92	29.62	29.00	30.10	1.75
Buy EUR/RON	05-09-2007	02-11-2007	3.322	3.345	3.45	3.25	0.31
Buy PLN/SKK	22-10-2007	02-11-2007	9.09	9.13	9.32	8.94	0.41



	Macro Outlook	FX & Monetary Policy	Other factors
<b>Region: CEE</b>			
<b>Poland</b>  PLN	<ul style="list-style-type: none"> <li>• Growth is strong, but industrial production is beginning to show some moderate signs of slowing due to capacity constraints.</li> <li>• The current account situation remains healthy, but strong domestic demand is beginning to put some pressure on the current account.</li> </ul>	<ul style="list-style-type: none"> <li>• Underlining inflationary pressures are going to increase and we expect inflation to rise above the central bank's target.</li> </ul>	<ul style="list-style-type: none"> <li>• The liberal and reformist Civic Platform won a landslide victory in the recent parliament elections and is likely to form a government with the centrist Peasant Party (PSL). This is good news for the Polish markets.</li> </ul>
<b>Czech Republic</b>  CZK	<ul style="list-style-type: none"> <li>• The economic growth remains strong, still driven by consumer spending.</li> <li>• Inflation is heading upwards. Food prices and higher regulated prices add some additional pressures on inflation. Fiscal reforms effective from next year will add further to accelerating inflation.</li> </ul>	<ul style="list-style-type: none"> <li>• Despite leaving interest rates on hold in October monetary policy remains biased on the upside. After the pause in October, the chance of a 25bp rate hike in November is high.</li> <li>• CZK is at a record high, both against EUR and USD driven by positive sentiment against Emerging Markets and the weak dollar. Further firming is limited though.</li> </ul>	<ul style="list-style-type: none"> <li>• The Czech government will implement fiscal package reforms from January next year. But major reforms - for instance pension reform and health care reform - are still missing.</li> </ul>


Region: CEE	Macro Outlook	FX & Monetary Policy	Other factors
<p><b>Slovakia</b></p>  <p><b>SKK</b></p>	<ul style="list-style-type: none"> <li>The economy continues to grow strongly driven by household consumption in Q2. Exports should improve in the coming quarters.</li> <li>Inflation is low at this moment but inflationary pressures are squeezed rather on the upside partly due to accelerating food prices.</li> </ul>	<ul style="list-style-type: none"> <li>The Slovak central bank will keep interest rates stable until the end of this year. It needs to keep a cautious stance in respect to inflation.</li> <li>SKK is being driven by global factors and by the sentiment against emerging Markets. But some disappointing news in regards to the Slovak euro adoption might trigger a sell-off.</li> </ul>	<ul style="list-style-type: none"> <li>The Slovak government is confident in meeting all Maastricht criteria in order to qualify for euro adoption in 2009. We continue to be less optimistic as we see real convergence of Slovakia as questionable in the longer run. That could be the main reason for Slovakia to be rejected in 2009.</li> </ul>
<p><b>Hungary</b></p>  <p><b>HUF</b></p>	<ul style="list-style-type: none"> <li>Hungarian growth has slowed down significantly on the back of last year's tightening of fiscal policy.</li> <li>This is positive as it contributes to improving both fiscal balances and the current account situation, but also increases the risk of political unrest resurfacing.</li> </ul>	<ul style="list-style-type: none"> <li>The Hungarian central bank (MNB) has initiated a monetary easing cycle.</li> <li>We expect more rate cuts in the coming months on the back of the continued slowdown in domestic demand. That said, MNB will remain cautious given the rise in global financial market uncertainties</li> </ul>	<ul style="list-style-type: none"> <li>Tighter global credit conditions could potentially hit the fairly indebted Hungarian economy hard. This is the main risk to the Hungarian markets.</li> <li>There are signs of internal disagreement in the Hungarian government over fiscal policy. Any loosening of fiscal policy would be very negative for the Hungarian markets.</li> </ul>


Region: CEE	Macro Outlook	FX & Monetary Policy	Other factors
<p><b>Romania</b></p>  <p><b>RON</b></p>	<ul style="list-style-type: none"> <li>• Inflation is on the upside and out of the central bank's inflation target 4%+/-1%-points, driven by rising food prices but also strong wage growth and robust consumer spending.</li> <li>• Romania is running a high risk of economic overheating with surging inflation and the current account deficit reaching unsustainable levels.</li> </ul>	<ul style="list-style-type: none"> <li>• Monetary policy is biased on the upside in order to keep inflation under control. Higher interest rates can be expected.</li> <li>• Romanian external imbalances make the Romanian leu very vulnerable to worsening of global liquidity conditions and worsening of the sentiment against Emerging Markets.</li> </ul>	<ul style="list-style-type: none"> <li>• The Romanian government needs to keep tight fiscal policy. Any further loosening would deteriorate economic imbalances further.</li> </ul>
<p><b>Bulgaria</b></p>  <p><b>BGN</b></p>	<ul style="list-style-type: none"> <li>• The economy continues to grow strongly but it is driven more by consumer spending than investment. The government sees next year's GDP growth at 6.4%.</li> <li>• Food prices pushed inflation to double-digit numbers in the last two months and year-end inflation close to 10% is a reality. A high current account deficit is the key risk.</li> </ul>	<ul style="list-style-type: none"> <li>• Widening of external balances makes Bulgaria vulnerable to worsening global credit and liquidity conditions.</li> <li>• Bulgaria's currency, the lev, is pegged to the euro. The central bank is within a currency board set-up. Tight fiscal policy and a close monitoring of credit growth is needed to maintain a credible FX peg.</li> </ul>	<ul style="list-style-type: none"> <li>• Bulgaria has ambitions to join the ERM-2 system and adopt the euro afterwards as soon as possible.</li> <li>• But with such high inflation and an unsustainable current account deficit, Bulgaria has to put a big effort into tackling these imbalances before any discussions can start.</li> </ul>



	Macro Outlook	FX & Monetary Policy	Other factors
<b>Region: Baltic</b>			
<b>Estonia</b>  <b>EEK</b>	<ul style="list-style-type: none"> <li>The Estonian economy has grown strongly in recent years and has been exhibiting clear signs of overheating, but signs of a fairly substantial slowdown are now apparent. The jury is, however, still out on whether the economy will undergo a hard or a soft landing.</li> <li>Inflation and wage growth have accelerated further and the development is clearly not sustainable.</li> </ul>	<ul style="list-style-type: none"> <li>The Estonian krooni (EEK) is pegged to the euro through ERM II.</li> <li>Until now, Estonia's currency board has functioned well and has not been questioned, but rising concerns over increased imbalances and contagion from the crisis in Latvia have increased uncertainty.</li> </ul>	<ul style="list-style-type: none"> <li>Credit-fuelled demand and high growth in private credit will continue to fuel inflation. We believe that euro adoption will be postponed until well after 2010.</li> <li>The property market in Estonia has cooled significantly.</li> </ul>
<b>Latvia</b>  <b>LVL</b>	<ul style="list-style-type: none"> <li>Latvian growth is far too strong, but a significant slowdown in growth is very likely. Signs of a slowdown in the economy are beginning to emerge.</li> <li>The Latvian real estate market has cooled down significantly, but a further drop in real estate prices is very likely.</li> <li>Inflation and wage growth is accelerating massively. This is obviously completely unsustainable.</li> </ul>	<ul style="list-style-type: none"> <li>The Latvian lat (LVL) is pegged to the euro through ERM II, but renewed pressure on the currencies should certainly not be ruled out.</li> <li>The Latvian central bank has been defending the peg by actively intervening in the FX market. The situation remains very critical.</li> </ul>	<ul style="list-style-type: none"> <li>There are clear concerns about financial and economic stability in Latvia. Fiscal policy is overly loose.</li> <li>The political situation has deteriorated significantly and the pressures on the Prime Minister to step down are mounting.</li> </ul>


Region: Baltic	Macro Outlook	FX & Monetary Policy	Other factors
<p><b>Lithuania</b></p>  <p>LTL</p>	<ul style="list-style-type: none"> <li>• GDP remains very strong and worryingly there are clear signs the overheating of the economy continues. In particular, we are concerned that credit growth remains strong.</li> <li>• The economy in Lithuania looks a bit more balanced than Estonia and Latvia, but the imbalances in the economy are, nonetheless, large.</li> </ul>	<ul style="list-style-type: none"> <li>• Lithuanian litai (LTL) is pegged to the euro through ERM II.</li> <li>• Large imbalances and negative contagion from the crisis in Latvia could increase volatility in the Lithuanian markets further.</li> </ul>	

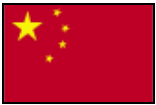

	Macro Outlook	FX & Monetary Policy	Other factors
<b>Region: CIS</b>			
<b>Russia</b>  <b>RUB</b>	<ul style="list-style-type: none"> <li>We expect growth to have peaked. Domestic demand will moderate in coming quarters as higher inflation and tighter monetary conditions will dampen consumption and investment.</li> <li>Inflationary pressures are mounting as food price growth rates accelerate. Inflation will move above 11% y/y before year end.</li> </ul>	<ul style="list-style-type: none"> <li>The RUB will remain stable against the dual basket for the remainder of the year. Some appreciation can be expected next year, but not too much.</li> <li>There are still strains in the money markets, as MosPrime rates remain elevated and the central bank still has to supply money markets with short-term liquidity.</li> </ul>	<ul style="list-style-type: none"> <li>Russian President Vladimir Putin told the congress early in October that he aims to head United Russia's candidate list in the December parliamentary elections.</li> <li>He added that it was "entirely" realistic he might be elected as prime minister after the Parliamentary elections in December.</li> </ul>
<b>Ukraine</b>  <b>UAH</b>	<ul style="list-style-type: none"> <li>Annual growth is around 8% and driven by consumption and investments. Accelerating private consumption will weigh negatively on the current account.</li> <li>Inflation moved above 14% y/y in September and is at unsustainable levels.</li> </ul>	<ul style="list-style-type: none"> <li>The Ukrainian central bank (NBU) is unlikely to introduce any major policy changes despite excessive inflation.</li> <li>The NBU will keep a firm grip on UAH, which is pegged against USD.</li> </ul>	<ul style="list-style-type: none"> <li>The results from the Ukrainian parliamentary election were as close as many had feared.</li> <li>The Yulia Tymoshenko Bloc and Our Ukraine-People's Self-Defence bloc plan to set up a coalition in the new Parliament.</li> </ul>



	Macro Outlook	FX & Monetary Policy	Other factors
Region: EMEA			
<p><b>Turkey</b></p>  <p><b>TRY</b></p>	<ul style="list-style-type: none"> <li>• There are increasing signs of a slowdown in domestic demand and GDP growth in the Turkish economy and on the back of tighter credit conditions and a strong lira.</li> <li>• The current account deficit has increased significantly and is now at quite dangerous levels.</li> </ul>	<ul style="list-style-type: none"> <li>• While the Turkish markets have weathered the recent political turmoil well, increasing worries on global credit conditions could obviously hit the heavily indebted Turkish economy and markets hard.</li> <li>• Inflation continues to decline and that has opened the door for an easing of monetary policy in Turkey. That said, looking ahead there is some inflationary risk in the form of higher food and energy prices and the risk of a renewed sell-off in the lira.</li> </ul>	<ul style="list-style-type: none"> <li>• The risk of a full-scale Turkish military operation into northern Iraq has clearly increased. However, until now the Turkish markets have taken the rise in geo-political risk very calmly.</li> </ul>



Region: EMEA	Macro Outlook	FX & Monetary Policy	Other factors
<p data-bbox="170 277 376 304"><b>South Africa</b></p>  <p data-bbox="192 469 271 496"><b>ZAR</b></p>	<ul data-bbox="568 284 1003 759" style="list-style-type: none"> <li data-bbox="568 284 1003 520">• Economic activity remains decent despite significant monetary tightening. Rising food and energy prices are the main culprits behind rising inflation. Second-round inflationary pressures are clearly present.</li> <li data-bbox="568 560 1003 759">• The current account deficit narrowed to 6.5% of GDP in Q2 (down from 6.9% in Q1), but remains high and no dramatic improvement is expected this year. It remains a key risk.</li> </ul>	<ul data-bbox="1097 284 1568 898" style="list-style-type: none"> <li data-bbox="1097 284 1568 619">• CPIX Inflation in September presented an unpleasant surprise of 6.7% y/y. Also private sector credit in September has slowed down less than expected. Hence, pressure on Reserve Bank to deliver another hike in December remains very high. We keep the doors open for a further 50bp rate hike.</li> <li data-bbox="1097 659 1568 898">• The rand has strengthened significantly over the last month driven by dollar weakness and high risk appetite for emerging markets currencies. A further rate hike could be supportive for the rand in the short run.</li> </ul>	<ul data-bbox="1659 284 2069 655" style="list-style-type: none"> <li data-bbox="1659 284 2069 655">• The vote for the new leader of the ruling ANC party is drawing closer. In December the party needs to find a new leader who will almost certainly become the new South African president. The ANC is however deeply split who the new leader is going to be. Politics will get more into the spotlight going forward.</li> </ul>


	Macro Outlook	FX & Monetary Policy	Other factors
<b>Region: LATAM</b>			
<b>Brazil</b>  <b>BRL</b>	<ul style="list-style-type: none"> <li>Industrial production (IP) has risen significantly and domestic demand is strong. Retail sales are growing faster than IP and this shows that demand is expanding faster than supply.</li> <li>A strong currency reduces inflation through imports, but an easing monetary stance, higher growth, and rising food prices increase the inflationary risks.</li> </ul>	<ul style="list-style-type: none"> <li>We expect the BCB to take a longer pause from the easing cycle. It kept its leading rate unchanged at the October meeting and we expect it to stay on hold well into 2008.</li> <li>BRL is now at its strongest levels vis-à-vis USD since 2000, supported by renewed risk appetite for high yielding currencies.</li> </ul>	<ul style="list-style-type: none"> <li>The ongoing boom has hampered the outlook for the trade balance surplus. Chances are that the trade surplus, despite high commodity prices, could be gone before entering 2009.</li> </ul>
<b>Argentina</b>  <b>ARS</b>	<ul style="list-style-type: none"> <li>The consumption boom, a record-high harvest and the sustained service sector performance lift growth projections for this year. Growth is currently around 8.7% y/y; we expect it to moderate into 2008.</li> <li>High inflationary pressures persist and are a serious threat to stability.</li> </ul>	<ul style="list-style-type: none"> <li>The Argentinean central bank is targeting inflation by controlling the money supply (M2) growth.</li> <li>The peso (ars) is pegged to the USD and this is unlikely to change in the foreseeable future.</li> </ul>	<ul style="list-style-type: none"> <li>As expected, Cristina Fernández de Kirchner won the first round in the presidential elections and both chambers of congress will be controlled by the ruling Victory Front.</li> </ul>

Region: LATAM	Macro Outlook	FX & Monetary Policy	Other factors
<p><b>Mexico</b></p>  <p><b>MXN</b></p>	<ul style="list-style-type: none"> <li>Industrial activity accelerated its recovery as it rebounded from a dismal first half of the year, driven particularly by improvements in the manufacturing sector. We expect a gradual improvement in GDP growth.</li> <li>Inflation moved below the upper limit of the comfort zone (4% y/y) in October, but the inflation outlook has worsened due to higher food prices and a new fuel tax.</li> </ul>	<ul style="list-style-type: none"> <li>The central bank (Banxico) maintains its tightening bias, and decided to hike its leading rate to 7.50%. We would certainly not rule out another hike at the beginning of 2008.</li> <li>The Mexican peso (MXN) has gained some momentum, especially after the central bank hiked the key rate.</li> </ul>	<ul style="list-style-type: none"> <li>2008 Revenue Bill should be approved by the Senate before 30 October, while the budget package must be approved by the Senate before November 15.</li> <li>We expect the public budget to improve after the newly approved tax-reform, which should improve non-oil related revenues..</li> </ul>

	Macro Outlook	FX & Monetary Policy	Other factors
<b>Region: EM Asia</b>			
<b>China</b>  CNY	<ul style="list-style-type: none"> <li>GDP growth declined slightly to 11.5% in Q3. However, the economy gained new momentum in September and could very well re-accelerate in Q4 07. Growth is expected to slow moderately to just below 11% next year.</li> <li>Inflation has soared above 6% recently, mostly due to higher food prices. Inflation probably peaked in August and is expected to decline below 4% during 2008 on the back of lower food prices.</li> </ul>	<ul style="list-style-type: none"> <li>The Chinese authorities are likely to maintain a tightening stance on credit / monetary policy. Another rate hike is likely in Q4. The likelihood of some administrative tightening measures has increased after the winding-up of the Communist Party Congress in October.</li> <li>We expect the appreciation of CNY against USD to accelerate to about 7% on a yearly basis. A major one off revaluation cannot be ruled out although we do not believe it is imminent. China will continue to liberalise its capital account.</li> </ul>	<ul style="list-style-type: none"> <li>President Hu Jintao did not consolidate his power as much as expected at the Party Congress. However we still believe future policy focus will be stronger on environmental and social development goals.</li> <li>Protectionist pressure is on the rise in Washington. A blow out with the US in late 2008 cannot be ruled out.</li> </ul>
<b>South Korea</b>  KRW	<ul style="list-style-type: none"> <li>Growth has accelerated in Q3 07 on the back of strong private consumption and fixed investments. Growth will continue to improve as domestic demand picks up.</li> <li>Inflation is still well within Bank of Korea's official inflation target of 2.5% +/-1%.</li> </ul>	<ul style="list-style-type: none"> <li>After the latest 25bp rate hike to 5.0% in August, rates will probably remain on hold until late H1 08.</li> <li>We expect further KRW strengthening on a 12-month horizon on the back of both strong growth in Asia and a stronger JPY and CNY</li> </ul>	<ul style="list-style-type: none"> <li>President Roh's political position is weak. The right-wing GNP is expected to win both the presidential election in December 2007 and the general election in April 2008, ending current political gridlock.</li> <li>Six-party talks on ending North Korea's nuclear ambitions continue. This should ease political tensions in the region.</li> </ul>

Region: EM Asia	Macro Outlook	FX & Monetary Policy	Other factors
<p><b>Thailand</b></p>  <p><b>THB</b></p>	<ul style="list-style-type: none"> <li>Political uncertainty remains a drag on the domestic economy</li> <li>Domestic demand remains weak but recovery is expected in 2008. However, exports are still booming, supporting growth. The C/A has shifted back into surplus, riding on slowing imports and booming exports.</li> <li>Core CPI is well within the 0%-3% inflation target band.</li> </ul>	<ul style="list-style-type: none"> <li>Fed rate cuts and recent THB appreciation have created room for easing bias in monetary policy. Another 25bp rate reduction to 3.0% to stimulate domestic demand is possible.</li> <li>A gradual decline in political risk premium and an end to the easing cycle should support further appreciation of THB.</li> </ul>	<ul style="list-style-type: none"> <li>Political developments in Thailand are still in the spotlight, with political changes interfering with financial markets.</li> <li>The general election is preliminarily scheduled for December 23. Election victory to supporters of former PM Thaksin could complicate transition from military rule and extend political uncertainty,</li> </ul>
<p><b>Hong Kong</b></p>  <p><b>HKD</b></p>	<ul style="list-style-type: none"> <li>Momentum in the economy has been maintained around 6% GDP growth and will be supported by lower interest rates and booming stock and real estate market.</li> <li>Inflation is picking up because of a tighter labour market and appreciation of RMB.</li> </ul>	<ul style="list-style-type: none"> <li>The USD peg is expected to stay. However risk of revaluation/trading band widening is increasing. We expect USD/HKD to stay below 7.80 in coming months on the back of strong capital inflows into the Hong Kong market.</li> <li>Money market rates will gradually decline as the Fed eases and USD inter-bank interest rates decline.</li> </ul>	<ul style="list-style-type: none"> <li>No change in Hong Kong's political status is expected soon.</li> <li>China's gradual capital account liberalisation is expected to boost capital inflow into Hong Kong.</li> </ul>

Region: EM Asia	Macro Outlook	FX & Monetary Policy	Other factors
<p><b>Philippines</b></p>  <p><b>PHP</b></p>	<ul style="list-style-type: none"> <li>• Strong growth is supported by continued strong exports and renewed strength in domestic demand. A big current account surplus around 4% of GDP is supported by remittances from Philipinos living abroad and strong FDI.</li> <li>• The budget deficit has been reduced significantly partly through privatisation. The target is to eliminate the budget deficit by 2008. Ability to reach this goal is important for financial markets.</li> <li>• Inflation has fallen below 3% and significantly below central bank 2007 target of inflation at 4%-5%.</li> </ul>	<ul style="list-style-type: none"> <li>• The PHP is currently supported by a strong current account surplus and capital inflows. The PHP is expected to strengthen further, especially when domestic demand picks up.</li> <li>• Fed easing and stronger PHP has created room for another 25 bp rate reduction in Q4 08.</li> </ul>	<ul style="list-style-type: none"> <li>• Strong growth is supported by continued strong exports and renewed strength in domestic demand. A big current account surplus around 4% of GDP is supported by remittances from Philipinos living abroad and strong FDI.</li> <li>• The budget deficit has been reduced significantly partly through privatisation. The target is to eliminate the budget deficit by 2008. Ability to reach this goal is important for financial markets.</li> </ul>
<p><b>Indonesia</b></p>  <p><b>IDR</b></p>	<ul style="list-style-type: none"> <li>• Growth has rebounded above 6%. Exports are strong and domestic demand is picking up. The current account surplus is around 3% of GDP and the public sector deficit has been reduced significantly partly through privatisation revenues.</li> <li>• Risk of weaker public finances as Indonesia prepares for 2009 general election</li> <li>• Inflation has been creeping up lately to 6.5% y/y but is still within BI's target range and core inflation is only 5.7% y/y</li> </ul>	<ul style="list-style-type: none"> <li>• The Bank of Indonesia's (BI) inflation target is 5%-7% and it is satisfied with the USD/IDR trading within 8,500-9,500. With recent appreciation of IDR and current high real rates, BI again has an easing bias.</li> <li>• USD/IDR will remain flat in the short run but is expected to strengthen on a 12-month horizon supported by strong current account flows.</li> </ul>	<ul style="list-style-type: none"> <li>• Growth has rebounded above 6%. Exports are strong and domestic demand is picking up. The current account surplus is around 3% of GDP and the public sector deficit has been reduced significantly partly through privatisation revenues.</li> <li>• Risk of weaker public finances as Indonesia prepares for 2009 general election</li> </ul>

Region: EM Asia	Macro Outlook	FX & Monetary Policy	Other factors
<p><b>India</b></p>  <p><b>INR</b></p>	<ul style="list-style-type: none"> <li>Growth has been slowing down on the back of weaker exports and private consumption while investments remain strong. C/A and trade balances are in slightly negative territory due to strong domestic demand.</li> <li>Positive long-run fundamentals remain intact with FDI and corporate investments remaining strong.</li> <li>Inflation has fallen below the 5% central bank target although this is mostly due to a base effect from lower food prices. Inflation will increase in 2008 as food prices become neutral, but is expected to stay below 5%.</li> </ul>	<ul style="list-style-type: none"> <li>The Reserve Bank of India (RBI) is on hold. However RBI will continue to hike commercial banks' required reserve ratio to sterilise very strong FX reserve inflows.</li> <li>The INR has appreciated strongly against USD and RBI has been selling INR to stem further appreciation. New controls on capital inflows are a possibility. RBI is stable in the short run but is expected to continue its appreciation trend later in 2008.</li> </ul>	<ul style="list-style-type: none"> <li>Prime Minister Singh faces problems in advancing much-needed structural reforms because of a highly-fragmented government. The Communist party has threatened to withdraw support to the government coalition because of a civilian nuclear deal with the US.</li> <li>The next general election is in May 2009. The pace of budget consolidation could slow in 2008 as India increasingly focuses on the upcoming general election.</li> </ul>

## FX Forecast

Core Majors											
		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
EUR	O2-nov			1,45		745,3		925,2		784,9	
	+1m			1,44	1,45	746,0	745,4	920,0	925,1	775,0	785,6
	+3m			1,48	1,45	746,0	745,4	920,0	924,9	770,0	787,2
	+6m			1,50	1,45	746,0	745,6	920,0	924,8	765,0	789,3
	+12m			1,38	1,45	746,0	745,8	930,0	925,3	760,0	793,8
USD	O2-nov	1,45				515,2		639,5		542,5	
	+1m	1,44	1,45			518,1	515,0	638,9	639,2	538,2	542,8
	+3m	1,48	1,45			504,1	514,7	621,6	638,7	520,3	543,6
	+6m	1,50	1,45			497,3	514,7	613,3	638,5	510,0	544,9
	+12m	1,38	1,45			540,6	515,1	673,9	639,0	550,7	548,2
JPY	O2-nov	165,9		114,7		4,49		5,58		4,73	
	+1m	164	165	114	114	4,55	4,51	5,61	5,59	4,73	4,75
	+3m	168	164	114	114	4,44	4,53	5,48	5,63	4,58	4,79
	+6m	173	163	115	112	4,31	4,58	5,32	5,68	4,42	4,84
	+12m	163	160	118	111	4,58	4,66	5,71	5,78	4,66	4,96
Wider CEE											
PLN	O2-nov	3,65		2,53		204,0		253,2		214,8	
	+1m	3,60	3,66	2,50	2,53	207,2	203,9	255,6	253,1	215,3	214,9
	+3m	3,60	3,66	2,43	2,53	207,2	203,7	255,6	252,8	213,9	215,1
	+6m	3,60	3,67	2,40	2,53	207,2	203,3	255,6	252,3	212,5	215,3
	+12m	3,70	3,69	2,68	2,55	201,6	202,2	251,4	250,9	205,4	215,3
HUF	O2-nov	252,4		174,4		2,95		3,67		3,11	
	+1m	250,0	253,1	173,6	174,8	2,98	2,95	3,68	3,66	3,10	3,10
	+3m	260,0	254,2	175,7	175,6	2,87	2,93	3,54	3,64	2,96	3,10
	+6m	265,0	255,8	176,7	176,6	2,82	2,91	3,47	3,62	2,89	3,09
	+12m	270,0	258,7	195,7	178,7	2,76	2,88	3,44	3,58	2,81	3,07
CZK	O2-nov	26,97		18,64		27,64		34,31		29,11	
	+1m	27,20	26,95	18,89	18,62	27,43	27,66	33,82	34,33	28,49	29,15
	+3m	27,30	26,90	18,45	18,57	27,33	27,72	33,70	34,39	28,21	29,27
	+6m	27,40	26,85	18,27	18,54	27,23	27,77	33,58	34,45	27,92	29,40
	+12m	27,10	27,23	19,64	18,80	27,53	27,39	34,32	33,98	28,04	29,16
SKK	O2-nov	33,34		23,05		22,35		27,75		23,54	
	+1m	33,50	33,34	23,26	23,04	22,27	22,36	27,46	27,74	23,13	23,56
	+3m	34,00	33,32	22,97	23,01	21,94	22,37	27,06	27,76	22,65	23,63
	+6m	34,10	33,29	22,73	22,98	21,88	22,40	26,98	27,78	22,43	23,71

## FX Forecast

<b>Wider CEE (Cont.)</b>											
		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
RON	02-nov	3,34		2,31		223,0		276,9		234,9	
	+1m	3,42	3,35	2,38	2,31	218,1	222,5	269,0	276,1	226,6	234,5
	+3m	3,45	3,35	2,33	2,31	216,2	222,4	266,7	275,9	223,2	234,8
	+6m	3,50	3,35	2,33	2,31	213,1	222,4	262,9	275,8	218,6	235,4
	+12m	3,60	3,35	2,61	2,31	207,2	222,5	258,3	276,1	211,1	236,8
BGN	02-nov	1,96		1,35		380,3		472,1		400,5	
	+1m	1,96	-	1,36	-	381,6	-	470,6	-	396,4	-
	+3m	1,96	-	1,32	-	381,6	-	470,6	-	393,9	-
	+6m	1,96	-	1,30	-	381,6	-	470,6	-	391,3	-
	+12m	1,96	-	1,42	-	381,6	-	475,7	-	388,7	-
TRY	02-nov	1,71		1,18		435,8		541,0		459,0	
	+1m	1,70	1,73	1,18	1,19	438,8	431,4	541,2	535,4	455,9	454,7
	+3m	1,80	1,76	1,22	1,22	414,4	423,3	511,1	525,2	427,8	447,0
	+6m	1,90	1,81	1,27	1,25	392,6	412,6	484,2	511,8	402,6	436,8
	+12m	1,90	1,90	1,38	1,31	392,6	393,0	489,5	487,5	400,0	418,3
<b>CIS</b>											
RUB	02-nov	35,68		24,67		20,89		25,93		22,00	
	+1m	35,71	35,76	24,80	24,70	20,89	20,85	25,76	25,87	21,70	21,97
	+3m	36,32	35,84	24,54	24,75	20,54	20,80	25,33	25,81	21,20	21,96
	+6m	35,90	35,95	23,93	24,82	20,78	20,74	25,63	25,72	21,31	21,95
	+12m	34,39	36,18	24,92	24,98	21,69	20,62	27,04	25,58	22,10	21,94
UAH	02-nov	7,31		5,06		101,9		126,5		107,3	
	+1m	7,20	7,29	5,00	5,04	103,6	102,2	127,8	126,9	107,6	107,8
	+3m	7,37	7,28	4,98	5,03	101,2	102,4	124,8	127,0	104,5	108,1
	+6m	7,47	7,29	4,98	5,03	99,9	102,2	123,2	126,8	102,4	108,2
	+12m	6,84	7,30	4,96	5,04	109,0	102,1	135,9	126,7	111,0	108,7

## FX Forecast

Baltics											
		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
EEK	02-nov	15,65		10,81		47,6		59,1		50,2	
	+1m	15,65	15,65	10,87	10,81	47,67	47,63	58,79	59,11	49,52	50,20
	+3m	15,65	15,66	10,57	10,82	47,67	47,59	58,79	59,06	49,20	50,19
	+6m	15,65	15,68	10,43	10,82	47,67	47,55	58,79	59,02	48,88	50,16
	+12m	15,65	15,71	11,34	10,85	47,67	47,44	59,42	58,87	48,56	50,01
LTL	02-nov	3,45		2,39		215,86		267,95		227,31	
	+1m	3,45	3,46	2,40	2,39	216,23	215,62	266,67	267,60	224,64	227,26
	+3m	3,45	3,46	2,33	2,39	216,23	215,17	266,67	267,04	223,19	226,78
	+6m	3,45	3,48	2,30	2,40	216,23	214,49	266,67	266,19	221,74	226,06
	+12m	3,45	3,50	2,50	2,42	216,23	212,69	269,57	263,96	220,29	224,17
LVL	02-nov	0,702		0,49		1061,69		1317,89		1118,05	
	+1m	0,70	0,70	0,49	0,49	1065,71	1057,85	1314,29	1312,85	1107,14	1114,93
	+3m	0,70	0,71	0,47	0,49	1065,71	1044,02	1314,29	1295,69	1100,00	1100,35
	+6m	0,70	0,71	0,47	0,49	1065,71	1044,02	1314,29	1295,69	1092,86	1100,35
	+12m	0,70	0,71	0,51	0,49	1065,71	1044,02	1328,57	1295,69	1085,71	1100,35

## FX Forecast

<b>MEA</b>											
		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
ILS	02-nov	5,74		3,97		129,7		161,0		136,6	
	+1m	5,83	5,75	4,05	3,97	127,9	129,7	157,8	161,0	132,9	136,7
	+3m	5,99	5,74	4,05	3,97	124,5	129,8	153,5	161,0	128,5	137,1
	+6m	6,15	5,74	4,10	3,97	121,3	129,8	149,6	161,0	124,4	137,4
	+12m	5,66	5,76	4,10	3,97	131,8	129,6	164,4	160,8	134,3	137,9
ZAR	02-nov	9,54		6,59		78,1		97,0		82,3	
	+1m	9,50	9,69	6,60	6,62	78,5	76,9	96,8	95,5	81,5	81,9
	+3m	9,92	9,69	6,70	6,69	75,2	76,9	92,8	95,4	77,7	81,2
	+6m	10,20	9,85	6,80	6,80	73,1	75,7	90,2	93,9	75,0	80,2
	+12m	9,66	10,16	7,00	7,02	77,2	73,4	96,3	91,1	78,7	78,1
EGP	02-nov	7,93		5,48		94,0		116,7		99,0	
	+1m	8,19	7,94	5,69	5,49	91,0	93,8	112,3	116,5	94,6	98,9
	+3m	8,41	7,97	5,68	5,51	88,7	93,5	109,4	116,0	91,6	98,7
	+6m	8,49	8,03	5,66	5,54	87,9	92,9	108,4	115,2	90,1	98,3
	+12m	7,76	8,14	5,62	5,62	96,2	91,6	119,9	113,6	98,0	97,5
<b>LATAM</b>											
BRL	02-nov	2,53		1,75		294,7		365,9		310,4	
	+1m	2,45	2,54	1,70	1,75	304,7	293,5	375,8	364,3	316,6	309,4
	+3m	2,44	2,56	1,65	1,77	305,5	291,1	376,7	361,2	315,3	307,4
	+6m	2,55	2,59	1,70	1,79	292,5	287,7	360,8	356,9	300,0	304,6
	+12m	2,42	2,67	1,75	1,84	308,9	279,6	385,1	346,9	314,7	297,6
ARS	02-nov	4,53		3,13		164,4		204,1		173,1	
	+1m	4,54	4,55	3,15	3,14	164,5	163,9	202,8	203,4	170,9	172,7
	+3m	4,74	4,60	3,20	3,18	157,5	161,9	194,3	200,9	162,6	171,0
	+6m	4,88	4,68	3,25	3,23	153,0	159,4	188,7	197,8	156,9	168,8
	+12m	4,55	4,84	3,30	3,34	163,8	154,1	204,2	191,1	166,9	164,0
MXN	02-nov	15,48		10,70		48,16		59,8		50,7	
	+1m	15,26	15,52	10,60	10,72	48,9	48,0	60,3	59,6	50,8	50,6
	+3m	15,54	15,60	10,50	10,77	48,0	47,8	59,2	59,3	49,5	50,5
	+6m	15,83	15,60	10,55	10,77	47,1	47,8	58,1	59,3	48,3	50,6

## FX Forecast

EM Asia											
		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
CNY	02-nov	10,79		7,46		69,10		85,8		72,8	
	+1m	10,70	10,73	7,43	7,41	69,7	69,5	86,0	86,2	72,4	73,2
	+3m	10,91	10,59	7,37	7,32	68,4	70,4	84,3	87,3	70,6	74,3
	+6m	10,80	10,41	7,20	7,19	69,1	71,7	85,2	88,9	70,8	75,8
	+12m	9,52	10,06	6,90	6,95	78,3	74,1	97,7	92,0	79,8	78,9
KRW	02-nov	1312		907		0,57		0,71		0,60	
	+1m	1303	1311	905	906	0,57	0,57	0,71	0,71	0,59	0,6
	+3m	1332	1309	900	904	0,56	0,57	0,69	0,71	0,58	0,6
	+6m	1335	1308	890	903	0,56	0,57	0,69	0,71	0,57	0,6
	+12m	1228	1306	890	902	0,61	0,57	0,76	0,71	0,62	0,6
THB	02-nov	45,9		31,7		16,2		20,2		17,1	
	+1m	46,1	46,1	32,0	31,8	16,2	16,2	20,0	20,1	16,8	17,0
	+3m	45,9	46,2	31,0	31,9	16,3	16,1	20,1	20,0	16,8	17,0
	+6m	45,0	46,4	30,0	32,0	16,6	16,1	20,4	19,9	17,0	17,0
	+12m	41,4	46,5	30,0	32,1	18,0	16,0	22,5	19,9	18,4	17,1
SGD	02-nov	2,1		1,45		355		445		458	
	+1m	2,08	2,10	1,45	1,45	359	356	442	442	372	375,0
	+3m	2,12	2,09	1,43	1,44	352	357	435	443	364	377,0
	+6m	2,10	2,08	1,40	1,44	355	359	438	445	364	379,7
	+12m	1,93	2,06	1,40	1,42	386	362	481	449	393	385,1
HKD	02-nov	9,85		7,76		75,7		94,7		85,6	
	+1m	11,17	11,22	7,76	7,76	67	66,4	82,3	82,4	69,4	70,0
	+3m	11,48	11,22	7,76	7,74	65,0	66,5	80,1	82,5	67,0	70,2
	+6m	11,66	11,20	7,77	7,73	64,0	66,6	78,9	82,5	65,6	70,5
	+12m	10,76	11,17	7,80	7,72	69,3	66,8	86,4	82,8	70,6	71,0

## FX Forecast

EM Asia (Cont.)											
		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
MYR	02-nov	4,84		3,34		154		191		162	
	+1m	4,8	4,90	3,34	3,39	155	152	191	189	161	160
	+3m	4,9	4,90	3,30	3,39	153	152	188	189	158	161
	+6m	4,9	4,90	3,25	3,39	153	152	189	189	157	161
	+12m	4,5	4,90	3,25	3,39	166	152	207	189	169	162
PHP	02-nov	62,6		43,3		11,9		14,8		12,5	
	+1m	61,9	62,7	43,0	43,4	12,0	11,9	14,9	14,7	12,5	12,5
	+3m	62,9	62,4	42,5	43,1	11,9	11,9	14,6	14,8	12,2	12,6
	+6m	63,0	62,5	42,0	43,1	11,8	11,9	14,6	14,8	12,1	12,6
	+12m	58,0	62,6	42,0	43,2	12,9	11,9	16,0	14,8	13,1	12,7
IDR	02-nov	13211		9132		0,056		0,070		0,059	
	+1m	12960	13249	9000	9154	0,058	0,056	0,071	0,070	0,060	0,059
	+3m	13172	13289	8900	9177	0,057	0,056	0,070	0,070	0,058	0,059
	+6m	13200	13365	8800	9227	0,057	0,056	0,070	0,069	0,058	0,059
	+12m	12144	13519	8800	9337	0,061	0,055	0,077	0,068	0,063	0,059
INR	02-nov	49,9		39,4		14,9		18,7		16,9	
	+1m	56,2	57,1	39,0	39,4	13,3	13,1	16,4	16,2	13,8	13,8
	+3m	57,3	57,2	38,7	39,5	13,0	13,0	16,1	16,2	13,4	13,8
	+6m	57,0	57,4	38,0	39,6	13,1	13,0	16,1	16,1	13,4	13,7
	+12m	52,4	57,7	38,0	39,9	14,2	12,9	17,7	16,0	14,5	13,8
TWD	02-nov	41,1		32,4		18,1		22,7		20,5	
	+1m	46,1	46,8	32,0	32,3	16	15,9	20,0	19,8	16,8	16,8
	+3m	45,9	46,5	31,0	32,1	16,3	16,0	20,1	19,9	16,8	16,9
	+6m	46,5	46,2	31,0	31,9	16,0	16,1	19,8	20,0	16,5	17,1

## Monetary Policy Calendar

	Policy Rate (%)	Latest Change	Next Change	Next Meeting
	2. november 2007			
<b>Wider CEE</b>				
PLN	4,75	+ 25 bp (Aug, 2007)	+ 25bp (Nov, 2007)	28. november 2007
HUF	7,50	- 25 bp (Sep, 2007)	-25bp (Nov, 2007)	26. november 2007
CZK	3,25	+ 25 bp (Aug, 2007)	+ 25bp (Q4, 2007)	29. november 2007
SKK	4,25	- 25 bp (Apr, 2007)	Unchanged 2007	27. november 2007
RON	7,50	+ 50 bp (Oct, 2007)	+50 bp (Q1, 2008)	4. januar 2008
TRY	16,75	- 50 bp (Oct, 2007)	-25bp (Q4, 2007)	14. november 2007
<b>MEA</b>				
ILS	4,00	+ 25 bp (Aug, 2007)	Unchanged 2007	26. november 2007
ZAR	10,50	+ 50 bp (Oct, 2007)	+50 bp (Q4, 2007)	6. december 2007
<b>LATAM</b>				
BRL	11,25	- 25 bp (Sep, 2007)	- 25 bp (Q1, 2008)	5. december 2007
MXN	7,25	+ 25 bp (Oct, 2007)	+25 bp (Q1, 2008)	23. november 2007
<b>EM Asia</b>				
CNY	7,29	+27 bp (Sep, 2007)	+25 bp (Nov, 2007)	Not announced
KRW	5,00	+25 bp (Aug, 2007)	+25 bp (Q2, 2008)	8. november 2007
THB	3,25	+25 bp (Oct, 2007)	-25 bp (Q4, 2007)	4. december 2007
HKD	6,00	-25 bp (Okt, 2007)	Unchanged 2007	Not announced
MYR	3,50	+ 25 bp (Apr, 2006)	Unchanged 2007	26. november 2007
PHP	5,75	-25 bp (Oct, 2007)	-25bp (Q1, 2008)	15. november 2007
IDR	8,25	-25 bp (July, 2007)	-25bp (Q1, 2008)	6. november 2007
INR	7,75	+25 bp (Apr, 2007)	Unchanged 2008	Not announced
TWD	3,25	+ 12.5 bp (Mar, 2007)	+25 bp (Dec, 2007)	Not announced

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