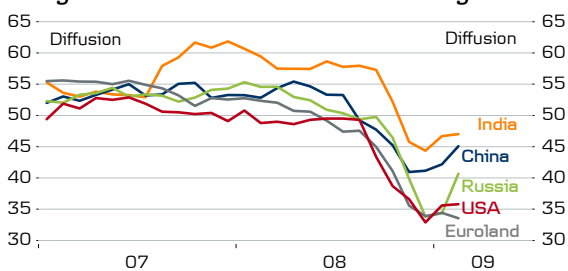


trade impact from lower commodity prices is not symmetrical. Obviously it is negative for commodity producing countries in Latin America, CIS and Middle East. On the other hand lower commodity prices represent major terms of trade gain for CEE and Asia. In Asia and CEE significant lower inflation is now supporting real income growth and giving most central banks the freedom to ease monetary policy aggressively. Our short term outlook for commodity prices is stabilization with gradual recovery later in 2009. For crude oil prices supply constraints could become a concern later in 2010.

Finally, there is the impact from the global credit crunch. The credit crunch has reduced capital flows to emerging markets and countries with a substantial finance requirement (current account deficit) and dependence on short term bank funding are most vulnerable. CEE and some CIS countries are most vulnerable (see below). Ultimately this vulnerability might limit emerging markets central banks freedom to ease monetary policy. While we believe the current credit crunch will gradually ease, deleveraging will be an ongoing process. In the countries hurt most by the global credit crunch financial sector reconstruction and consolidation will remain on the agenda and increasing private saving will continue to weigh on domestic demand longer term. This has two important consequences for emerging markets. The recovery in developed market will most likely not be fast and emerging markets hurt by the credit crunch will underperform.

Signs of stabilisation in manufacturing PMI's



Source: Reuters Ecowin

## China; Last in, first out

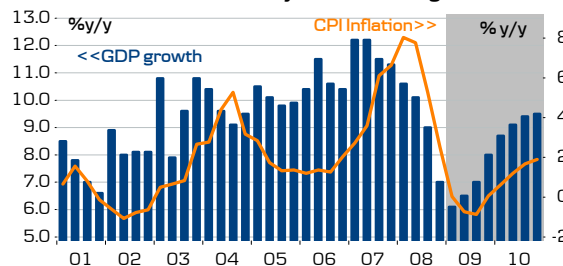
### Policy response has been effective

Currently China is clearly the best recovery case in Asia. In fact China was one of the last economies to be hit severely by the impact from the global financial crisis and at the moment it looks like it might be one of the first major economies to recover. In recent months the PMI indicators for industrial activity have rebounded strongly, lending growth has accelerated sharply and car sales have improved. This suggests that the Chinese economy has bottomed out in Q1 09 or Q2 09. There are several reasons for the Chinese economy's comparatively strong performance.

First, China's policy response has been among the strongest in Asia. Fiscal policy has been eased aggressively and we reckon that higher public investments and tax cuts might add as much as 3pp to GDP growth in 2009. In addition monetary policy has been eased aggressively by cutting interest rates and more importantly lending quotas have been eliminated. In addition with very liquid balance sheets and external capital controls remaining in place, the health of the financial sector is less an issue in China and hence the monetary transmission at the moment seems to be working.

Second, real incomes in China have been boosted by the terms of trade gains from lower commodity prices and the gradual normalisation of food prices following the spike in food prices last year. This is reflected in the sharp decline in inflation. In February headline inflation in fact turned negative for the first time since 2002. This raises the question if we should be concerned about deflation in China. In our opinion not yet. Wage growth remains robust and the recent sharp acceleration in M2 money supply growth (usually a reliable indicator for inflation one year ahead) suggests inflation will start to pick up next year.

Chinese economy is bottoming out



Source: Reuters Ecowin

Finally, while China's exports have not been immune to the global financial crisis, China's export nonetheless has performed much better than some of its main competitors, particularly some of the more developed Asian countries like Japan, South Korea and Taiwan. Apparently China continues to gain market shares and at the moment China's competitiveness does not seem to be a major issue despite the continued appreciation of the effective CNY exchange rate since.

**Danske Bank forecast**

Danske Bank	China		
	2008	2009	2010
GDP	9.1	7.2	9.2
Private consumption	15.7	15.0	16.0
Investment	12.8	10.3	14.3
Export	14.4	-6.5	11.2
Import	20.4	-4.0	13.8
Industrial production	13.1	7.8	12.1
Inflation excl. food and energy	-	-	-
Inflation	5.9	-0.4	1.4

At the moment it looks like China's stimulus measures are working. Domestic demand is improving but because of the weak global environment there remains considerable downside risk for the Chinese economy. For the Chinese leadership policy it will be "wait and see" in the short run. If the economy continues to improve the leading interest rate will probably not be cut further. China will outperform in 2009, where our forecast for GDP growth has only been adjusted slightly downwards and overall the decline in GDP growth is modest compared to other emerging markets. The exchange rate policy will be status quo in the short run meaning broadly unchanged against USD and a slight appreciation in the effective exchange rate. We still believe that CNY's appreciation trend against USD will be resumed when the Chinese leadership feel more confident about the recovery.

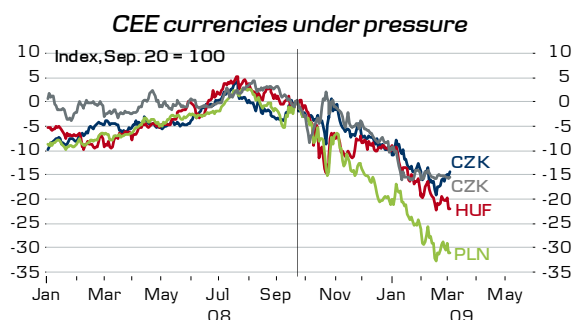
**Central & Eastern European crisis intensifies**

In recent weeks the worries over the situation in the Central and Eastern European (CEE) economies have increased significantly. This has been very visible in

the CEE markets that have significant underperformed most other Emerging Markets.

The concerns about the situation in the region should hardly be a surprise to investors familiar with the region. In late 2006 and early 2007 we warned that the large imbalances that most CEE economies have seen in recent years could be a danger to economic and financial stability in the region. International institutions like the IMF and the World Bank and the major rating agencies have raised similar concerns for some time. However, it was not until recently that we have seen the situation develop into what could be termed a currency crisis. Four factors have in our view been keys to the sharply rising concerns in the markets over the CEE economies in recent weeks.

First, since the collapse of Lehman Brothers in the autumn we have seen global risk aversion rise sharply and with credit condition tightening globally the CEE economies - which for most parts have large external funding needs due to large current account deficits - has suffered a (near) sudden stop to the funding of these external imbalances. The graph below clearly illustrates that the sell-off in the CEE currencies more or less coincide with the collapse of Lehmann Brothers on September 20, 2008



Source: Reuters Ecowin

Second, there is no doubt that the sharp drop in economic activity in the region has made investors nervous (see below).

Third, worries over the state of the banking sector in region - that is mostly Western owned - has risen somewhat. Especially since the rating agency Moody's in February published a report warning of the risks to Western European banks with exposure to CEE. See more on the Western European banking sector's exposure to CEE on.

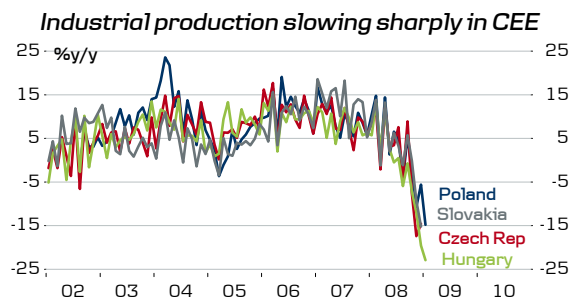
Four, market participants have clearly increased the attention to the fact that many households and corporation across the region in recent years have become significantly exposed to foreign currency loans. There are clear differences across the region, but only the Czech Republic has only modest exposure to foreign currency loans. The largest currency mismatch in funding is in the Baltic States, Hungary, Ukraine, Bulgaria and Romania

Looking forward we still see clear risks that the situation in the region could continue in a negative direction and the “event risk” seems to be extraordinary high across the region. The largest event risks are to be found in the Baltic States, Bulgaria, Romania, Hungary and Ukraine. These are the countries in the region that is struggling with the largest imbalances. Risks are smaller in the Czech Republic, Poland, Slovenia and Slovakia. That said, even the more “healthy” countries can be hit by contagion from problems other places in the region due to the significant financial links through the banking sector in the region

**Significant macro economic shock**

There is no doubt that the “sudden stop” to the funding of the current account deficits that we have seen across the region is likely to have a significantly negative impact on growth in most countries in the region. In fact we have already seen a very sharp drop in industrial production across the strongly export oriented economies in the region. Especially the car industry in countries like the Czech Republic and Slovakia has been hard hit. Furthermore, the so-called “gas dispute” between Russia and Ukraine have disrupted energy supplies to a number of countries in the region. Besides Ukraine there have been serious disruptions of energy

supplies in Slovakia and Bulgaria. These shocks have sent industrial production plummeting in most countries in the region.



Source: Reuters Ecowin

Until now private consumption have however been holding up quite well – with the exception of the Ukraine, Baltic States, Hungary and the Czech Republic. That said, we expect private consumption to slow dramatically across region on the back of weaker local currencies (and hence rising cost of debt servicing on FX loans), tighter credit condition and a sharp deterioration of labour market conditions. Therefore we would expect most countries in region to see GDP contract in 2009 – and for the hardest hit countries we expect a double digit drop in GDP. The hardest hit countries are the Baltic States, Romania, Bulgaria and Ukraine.

Given the large imbalances in most economies in the region we only expect a gradually recovery in growth during 2010. We expect the countries with the smallest imbalances and the highest degree of currency flexibility – that is Poland and the Czech Republic - to recover the fastest. Much will however for these economies dependent on how the euro zone economy recovers.

Danske Bank	USA			Euroland			Japan			China		
	2008	2009	2010	2008	2009	2010	2008	2009	2010	2008	2009	2010
GDP	1.1	-2.7	2.5	0.7	-2.7	0.8	-0.7	-5.0	2.8	9.1	7.2	9.2
Private consumption	0.2	-0.8	1.8	0.5	-0.5	0.4	0.7	-0.2	1.4	15.7	15.0	16.0
Investment	-3.9	-13.0	7.2	0.6	-6.0	0.6	-4.8	-6.4	2.1	12.8	10.3	14.3
Export	6.2	-14.1	0.5	1.7	-10.1	2.4	1.9	-27.2	18.2	14.4	-6.5	11.2
Import	-3.4	-9.5	5.4	1.7	-7.3	2.8	1.1	-12.6	1.1	20.4	-4.0	13.8
Industrial production	-1.8	-7.5	2.0	-2.1	-4.4	2.8	-3.4	-26.5	10.2	13.1	7.8	12.1
Inflation excl. food and energy	2.3	1.3	1.2	1.8	1.5	1.3	0.0	-0.3	-0.3	-	-	-
Inflation	3.8	-0.8	2.5	3.3	0.5	1.3	1.5	-0.9	-0.1	5.9	-0.4	1.4

*This report has been prepared by Danske Research, which is part of Danske Markets, a division of Danske Bank. Danske Bank is under supervision by the Danish Financial Supervisory Authority.*

*Danske Bank has established procedures to prevent conflicts of interest and to ensure the provision of high quality research based on research objectivity and independence. These procedures are documented in the Danske Bank Research Policy. Employees within the Danske Bank Research Departments have been instructed that any request that might impair the objectivity and independence of research shall be referred to Research Management and to the Compliance Officer. Danske Bank Research departments are organised independently from and do not report to other Danske Bank business areas. Research analysts are remunerated in part based on the over-all profitability of Danske Bank, which includes investment banking revenues, but do not receive bonuses or other remuneration linked to specific corporate finance or debt capital transactions.*

*Danske Bank research reports are prepared in accordance with the Danish Society of Investment Professionals' Ethical rules and the Recommendations of the Danish Securities Dealers Associations.*

*Financial models and/or methodology used in this report*

*Risk warning*

*Major risks connected with recommendations or opinions in this report, including as sensitivity analysis of relevant assumptions, are stated throughout the text.*

**Expected updates**

*Global Scenarios is a quarterly forecast, but new statistical data may give rise to changes in our views on individual economies. The next edition of Global Scenarios is due to be released in June 2009.*

**First date of publication**

*Please see the front page of this research report.*

**Disclaimer**

*This publication has been prepared by Danske Markets for information purposes only. It has been prepared independently, solely from publicly available information and does not take into account the views of Danske Bank's internal credit department. It is not an offer or solicitation of any offer to purchase or sell any financial instrument. Whilst reasonable care has been taken to ensure that its contents are not untrue or misleading, no representation is made as to its accuracy or completeness and no liability is accepted for any loss arising from reliance on it. Danske Bank, its affiliates or staff, may perform services for, solicit business from, hold long or short positions in, or otherwise be interested in the investments (including derivatives), of any issuer mentioned herein. The Equity and Corporate Bonds analysts are not permitted to invest in securities under coverage in their research sector. This publication is not intended for retail customers in the UK or any person in the US. Danske Markets is a division of Danske Bank A/S. Danske Bank A/S is authorized by the Danish Financial Supervisory Authority and subject to limited regulation by the Financial Services Authority (UK). Details on the extent of our regulation by the Financial Services Authority are available from us on request. Copyright (C) Danske Bank A/S. All rights reserved. This publication is protected by copyright and may not be reproduced in whole or in part without permission.*