

12 May 2016

Back to reality

Georgette Boele
Co-ordinator FX & Precious Metals
Strategy
Tel: +31 20 629 7789
georgette.boele@nl.abnamro.com

- **Brazilian real likely to weaken somewhat...**
- **...as focus turns back to reality**
- **The Polish zloty has been the weakest CEE currency...**
- **...because of political and downgrade risks...**
- **...while we expect the Hungarian forint to shine**

Brazilian political saga

Since the start of this year, the Brazilian real has been the top performer among emerging market currencies. The strong recovery in commodity prices and a downward adjustment in US fed rate hike expectations have given strong support to the real. However, political developments have also been among the major drivers behind the rally in the real. Changes in the real during this week show how sensitive the currency is towards political developments. At the start of the week, the new Lower House leader annulled the impeachment vote of 17 April. This resulted in a 4% drop of the real. In contrast, the Leader of the Senate said that the impeachment vote in the Senate would go ahead. Subsequently, his decision and pressure on the new Lower House leader resulted in a reversal of the cancelation of the impeachment vote of 17 April.

This morning, the Senate voted to suspend President Dilma Rousseff from office to face an impeachment trial. Vice-president Temer will take over for 180 days. Financial markets have widely anticipated this. The real could move somewhat higher on the outcome but most is already reflected in the real. Therefore, the reality that a change in power will not solve the current economic challenges will likely weigh on investor sentiment towards the real. Unpopular and tough measures are needed to put the economy on the right track. Overall, we expect the real to come under some pressure in the coming weeks. Our year-end forecast for USD/BRL is 3.5.

Divergence in currencies of central and eastern Europe...

So far this year, the Polish zloty has weakened more than 4% versus the euro while the Czech koruna has moved sideways and the Hungarian forint has strengthened modestly. There are several reasons for this. S&P's downgrade of Poland to BBB+ on 15 January 2016 with a negative outlook caused a substantial weakening of the zloty. In addition, the announced measures by the PiS party and fears that the new central bank governor may not be as independent as portrayed further dented investor sentiment towards the zloty.

On 13 May Moody's will review Poland's credit rating. The risks of a negative outlook or even a downgrade have increased considerably. Financial markets have anticipated the risk of a downgrade. However, we think that this is not fully reflected in the price yet. So in the near-term, the zloty could remain under pressure. A looming downgrade and the uncertainty surrounding politics will likely result in a more modest recovery that we had pencilled in. As a result, we have downgraded our zloty forecasts versus the euro. We have also adjusted our forecasts in EUR/CZK as we now expect that the Czech central bank will remove the floor in EUR/CZK in Q3 2017.

...and the Hungarian forint to shine

We expect the Hungarian forint to continue to outperform the zloty and the koruna this year. Financial markets have taken Hungarian politics for granted so this will unlikely weigh on investor sentiment towards the forint. What is more, fundamentals are very strong and a rating upgrade is increasingly likely. Hungary has a substantial current account surplus which will likely shield it from a sharp deterioration in investor sentiment on financial market. Despite the fact that the Hungarian central bank will probably further ease monetary policy in the near-term, this will be very modest and less than what financial markets appear to anticipate. Further down the road, higher inflationary pressures and a strong economy will likely result in more aggressive rate hikes later on. This should result in a strong rally in the forint versus the euro. In short, current relatively low levels in the forint are an opportunity to position for strength in later this year and next year.

ABN AMRO emerging market currency forecasts

Changes in red/bold

	12-May	Q2 2016	Q3 2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017
USD/CNY (onshore)	6.51	6.55	6.60	6.70	6.75	6.80	6.80	6.80
USD/CNH (offshore)	6.54	6.55	6.60	6.70	6.75	6.80	6.80	6.80
USD/INR	66.6	66.5	67.0	67.0	67.0	66.0	65.5	65.0
USD/KRW	1,163	1,165	1,165	1,165	1,150	1,140	1,130	1,120
USD/SGD	1.37	1.36	1.38	1.40	1.38	1.36	1.35	1.35
USD/THB	35.26	35.00	35.00	35.00	34.80	34.60	34.40	34.00
USD/TWD	32.40	32.50	32.80	33.00	32.80	32.50	32.20	32.00
USD/IDR	13,304	13,200	13,400	13,500	13,400	13,300	13,200	13,000
USD/RUB	65	66	64	60	59	58	57	55
USD/TRY	2.96	2.85	2.80	2.75	2.75	2.75	2.75	2.75
USD/ZAR	15.12	15.00	14.75	14.50	14.25	14.00	13.75	13.50
EUR/PLN	4.43	4.40	4.40	4.35	4.30	4.25	4.20	4.20
EUR/CZK	27.02	27.00	27.00	27.00	27.00	27.00	26.50	26.00
EUR/HUF	316	310	310	305	300	300	295	290
USD/BRL	3.45	3.60	3.55	3.50	3.45	3.40	3.35	3.30
USD/MXN	18.02	17.25	17.00	16.75	16.50	15.75	15.50	15.25
USD/CLP	680	670	660	650	640	630	620	600

Source: ABN AMRO Group Economics

Find out more about Group Economics at: <https://insights.abnamro.nl/en/>

DISCLAIMER

ABN AMRO Bank
Gustav Mahlerlaan 10 (visiting address)
P.O. Box 283
1000 EA Amsterdam
The Netherlands

This document has been prepared by ABN AMRO. It is solely intended to provide financial and general information on economics. The information in this document is strictly proprietary and is being supplied to you solely for your information. It may not (in whole or in part) be reproduced, distributed or passed to a third party or used for any other purposes than stated above. This document is informative in nature and does not constitute an offer of securities to the public, nor a solicitation to make such an offer.

No reliance may be placed for any purposes whatsoever on the information, opinions, forecasts and assumptions contained in the document or on its completeness, accuracy or fairness. No representation or warranty, express or implied, is given by or on behalf of ABN AMRO, or any of its directors, officers, agents, affiliates, group companies, or employees as to the accuracy or completeness of the information contained in this document and no liability is accepted for any loss, arising, directly or indirectly, from any use of such information. The views and opinions expressed herein may be subject to change at any given time and ABN AMRO is under no obligation to update the information contained in this document after the date thereof.

Before investing in any product of ABN AMRO Bank N.V., you should obtain information on various financial and other risks and any possible restrictions that you and your investments activities may encounter under applicable laws and regulations. If, after reading this document, you consider investing in a product, you are advised to discuss such an investment with your relationship manager or personal advisor and check whether the relevant product—considering the risks involved—is appropriate within your investment activities. The value of your investments may fluctuate. Past performance is no guarantee for future returns. ABN AMRO reserves the right to make amendments to this material.

© Copyright 2016 ABN AMRO Bank N.V. and affiliated companies ("ABN AMRO").

