

The EEMEA FX Strategist

Between a US rock and a Chinese hard place

EM FX is still close to the sell signal

We remain cautious on EEMEA FX against the USD as the market might still question Fed cuts priced in for this year. Moreover, our EM FX sentiment indicator is still close to the sell signal, as is Michael Hartnett's bull-bear index.

On a more positive note, the global growth recovery is broadening, which is usually positive for EEMEA FX. To capture this trend, investors need to focus on idiosyncratic positive stories (such as Poland), expressing the FX view against the EUR or even CNH.

PLN (bullish): strong inflows coupled with equity and bond inflows should drive the PLN stronger; EU funds have been unblocked faster than expected, which should also support the zloty.

ZAR (neutral): we are cautious for now, given the political risks related to elections and the global backdrop. A weaker USD should ultimately lead to a stronger ZAR this year.

TRY (neutral): we are bullish TRY against the EUR as we do not expect any rate cuts this year. We expect orderly depreciation in line with forwards in Q1 and Q2. Elevated inflation and a still significant current account deficit remain concerns.

ILS (neutral): geopolitical risks are crucial for the ILS, making the outlook binary; the importance of US equities and the broader USD for the ILS has declined, in our view.

CZK (neutral): the easing cycle and a stronger USD are likely to be headwinds for the koruna in the short term; this should reverse from H2.

HUF (neutral): a focus on growth means that the HUF should weaken in line with forwards; a weaker USD from H2 should provide some support.

Exhibit 1: EEMEA FX forecasts for the next four quarters

Bullish PLN, neutral ZAR, ILS and CZK, bearish HUF

Currency	View/bias	Spot	Forecasts			
			1Q 2024	2Q 2024	3Q 2024	4Q 2024
EUR/PLN	bullish	4.31	4.30	4.25	4.23	4.20
USD/ZAR	neutral*	19.14	19.0	19.2	18.5	18.0
USD/TRY	neutral*	31.15	32.0	35.0	37.0	40.0
USD/ILS	neutral*	3.63	3.7	3.7	3.6	3.6
EUR/CZK	neutral*	25.32	25.5	25.5	25.0	24.7
EUR/HUF	neutral*	389	390.0	395.0	395.0	399.0

#See inside for longer-term forecasts. *We form a view/bias based on our forecast for the spot exchange rate versus forward rate at the end of next quarter considering alternative scenarios as well **Neutral = our view approximately agrees with the forwards. **Source:** BofA Global Research

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Refer to important disclosures on page 16 to 18.

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GEM FI & FX Strategy
EEMEA

Mikhail Liluashvili
EEMEA Local Markets Strategist
MLI (UK)
+44 20 7996 1142
mikhail.liluashvili@bofa.com

Mai Doan
CEE Economist
MLI (UK)
+44 20 7995 9597
mai.doan@bofa.com

Zumrut Imamoglu
Turkey & Israel Economist
MLI (UK)
+44 7749 727 494
zumrut.imamoglu@bofa.com

Tatonga Rusike
Sub-Saharan Africa Economist
MLI (UK)
+44 20 7996 8446
tatonga.rusike@bofa.com

David Hauner, CFA >>
Global EM FI/FX Strategist
MLI (UK)
+44 20 7996 1241
david.hauner@bofa.com

Vladimir Osakovskiy >>
EM Sovereign FI/EQ strategist
Merrill Lynch (DIFC)
+971 4 425 8291
vladimir.osakovskiy@bofa.com

Jean-Michel Saliba
MENA Economist/Strategist
MLI (UK)
+44 20 7995 8568
jean-michel.saliba@bofa.com

EEMEA FI Strategy & Economics
MLI (UK)

GEMs FI Strategy & Economics
BofAS

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For a list of open trade recommendations and trade recommendations closed in the last 12 months, see [Global Emerging Markets Weekly: What if the Fed doesn't cut? 23 February 2024](#)

EEMEA is Emerging Europe, Middle East and Africa

FX is foreign exchange

BoP is balance of payments

USD is US dollar

EM is Emerging Market

Poland: sooner EU funds boost sentiment

Mai Doan
MLI (UK)
mai.doan@bofa.com

Mikhail Liluashvili
MLI (UK)
mikhail.liluashvili@bofa.com

View: political transition brings noise, but +ve trend intact

We expect the EUR/PLN to go lower due to the prospect of large inflows under the new market-/EU-friendly government. The National Bank of Poland (NBP) has turned hawkish, as we expected, with rates most likely on hold for an extended period. EU funds have been unblocked sooner than we expected, adding to a positive PLN sentiment.

Key macro developments: The quick progress in unblocking EU funds in recent weeks supports our positive bias on Polish assets post elections. Political tensions will likely remain high domestically, including the government's threat to put NBP Governor Glapinski before a state tribunal, but we don't see a material impact on PLN fundamentals. In total for 2024, Poland could get c.EUR27bn in recovery and cohesion money (c.3.2% of GDP), with another EUR11.5bn of RRP funds likely in 1Q 2025. For 2024, this amount has been budgeted for, but it adds to the strong financing so far and creates more flexibility for FinMin on price/timing of issuance. FinMin expects to cover more than 50% of this year's gross borrowing requirement by end-March, before counting these EU inflows.

We expect the NBP to be in defensive mode in response to the government's motion, which means no rate cuts any time soon with rates likely held steady at 5.75% this year. The legal process could be lengthy and uncertain, so it is too early to say when or if Glapinski will be suspended from his duties, or how the MPC might behave subsequently. However, we still believe that the next move is likely to be a cut. Easing room is limited though, as the economy is on a recovery track, and we see long-term inflation pressures from energy transition and higher unit labour costs vs pre-pandemic years.

Activity improved in January and is, in our view, consistent with a solid recovery in GDP growth to 3% this year. Retail sales grew by 3% yoy after -2.3% in December, while IP growth picked up to +1.6% yoy from -3.5%. CPI meanwhile has been surprising further on the downside, easing to 3.9% in January. The trough in inflation could be around 2% in the coming months. But the outlook is highly uncertain in 2H when the inflation shield is due to expire. We see YE2024 inflation close to 6%, assuming VAT on basic food resumes in July, and energy prices rise by c.10%.

Valuations: the PLN is undervalued on our current account (long-term) model

Positioning: the market remains long PLN

Risks to our views: further increase in political risks

Upcoming risk events: NBP decisions (6 Mar), State Tribunal on NBP Governor (1H)

Corporate hedging: we recommend hedging against PLN strength

Rates: no strong views

Exhibit 2: EUR/PLN forecasts vs forwards

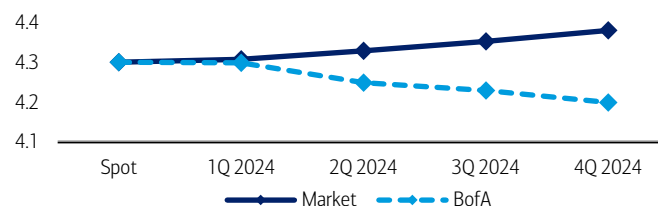
We expect EUR/PLN at 4.20 by the end of 2024

Spot	current 4.30	chg (diff) -0.09	Forward	
	Forecast		current	chg (diff)
Period	current	chg (diff)	current	chg (diff)
1Q 2024	4.30	-0.06	4.31	-0.09
2Q 2024	4.25	-0.08	4.33	-0.10
3Q 2024	4.23	-0.06	4.35	-0.10
4Q 2024	4.20	-0.05	4.38	-0.10

Source: BofA Global Research, Bloomberg

Exhibit 3: EUR/PLN forecasts

Our forecast path is below forwards



Source: BofA Global Research, Bloomberg

Cross currency basis EUR/PLN

Exhibit 4: EUR/PLN cross currency basis

1y xccy basis at 32bp

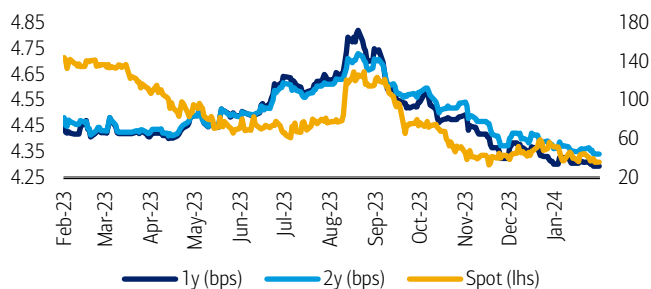
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	32.00	-4.0	-51.0	-41.0	32.0		172.0	82.6	9.5	68.3	-6.2	-1.6
2y	44.50	-5.0	-52.5	-36.0	44.5		148.0	86.1	7.5	53.8	-5.4	-1.7
5y	56.00	-3.0	-48.0	-41.5	56.0		129.5	88.8	6.4	46.4	-4.5	-1.7
10y	58.00	-2.0	-46.0	-46.5	58.0		119.0	88.3	6.3	45.3	-4.6	-1.9

Note: ● : current value; ◇ : 1y average. The z-score measures the distance between the current value and the mean in standard deviation units. Source: BofA Global Research, Bloomberg

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Exhibit 5: Short-term basis swaps vs EUR/PLN spot

Xccy at lower historical range

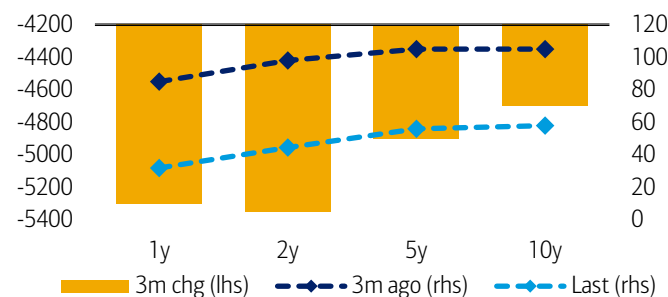


Source: BofA Global Research, Bloomberg

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Exhibit 6: Term structure of basis swaps (bps)

Short end moving lower



Source: BofA Global Research, Bloomberg

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Volatility surface EUR/PLN

Exhibit 7: Current implied volatilities

Slightly upward sloping

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	5.27	5.19	5.39	5.92	6.60
3m	5.56	5.47	5.77	6.52	7.49
6m	5.54	5.54	5.94	6.84	7.96
1y	5.60	5.63	6.07	7.08	8.36

Source: BofA Global Research

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Exhibit 8: 3m z-scores of implied volatilities

Changes over time

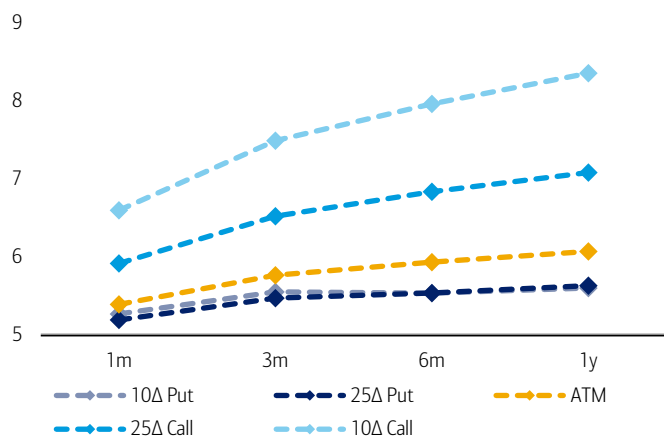
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-1.8	-1.7	-1.6	-1.7	-1.8
3m	-1.4	-1.4	-1.4	-1.5	-1.6
6m	-1.6	-1.4	-1.4	-1.6	-1.7
1y	-1.6	-1.5	-1.5	-1.6	-1.8

Source: BofA Global Research

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Exhibit 9: Term structures of implied volatilities

Slightly upward sloping

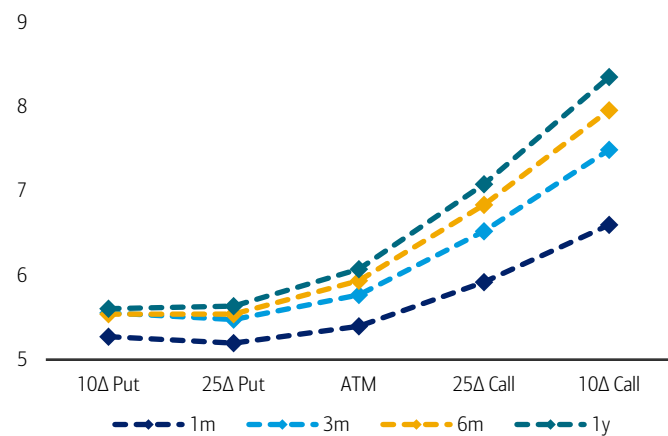


Source: BofA Global Research

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Exhibit 10: Implied volatility smiles

Implied vol smiles are somewhat skewed



Source: BofA Global Research

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South Africa: neutral ZAR view

Tatonga Rusike

MLI (UK)

tatonga.rusike@bofa.com

Mikhail Liluashvili

MLI (UK)

mikhail.liluashvili@bofa.com

View: bullish medium term, cautious in the short run

A stronger broader dollar in the short term is a headwind to our bullish rand view. In addition, political risks around elections and weak fiscal should make investors cautious on the currency. As a result, we are bullish the ZAR only in the medium-term when we expect the broader USD to weaken.

Key macro developments: With no real new tax measures, the National Treasury largely kept its call for a spending grip with nominal cuts in non-interest spending, no new allocations to state-owned enterprises and slower growth in debt service costs, helping to keep fiscal forecasts more constructive than our base case. Non-interest spending is set to grow 4-5% per year vs under 10% for interest spending. Risks to spending assumptions could impact fiscal outcomes. The government expects a main budget deficit of -4.7% of GDP in 2023/24 (BoFA -4.8%) and -4.3% for the 2024/25 budget (BoFA -4.5%). Our all-in deficit including Eskom support above the line is -6.1% in 2023/24, -5.5% in 2024/25 and -5.4% in 2025/26. These forecasts underscore our overall dim view of public finances. To be constructive fiscally, we wait for 2026, when phased-out Eskom support is likely to result in a stronger primary surplus.

Immediate access to central bank profits (unrealised revaluation gains from central bank FX reserves in the Gold & Foreign Exchange Contingency Reserve Account, GFECRA) reduces near-term borrowing requirements. The government is set to tap into R150bn (about 2% of GDP) of GFECRA funds over the next three years. Net borrowings, excluding redemptions are set to decline to R385bn in 2024/25, from R407bn in 2023/24 but then increase to R418bn in 2025 due to lower GFECRA drawdowns. As Eskom support is phased out, net borrowings should fall more significantly in 2026 to below R300bn.

Valuations: the ZAR is broadly fairly valued on our FEER model

Positioning: investors are short ZAR

Risks to our view: weaker data in China, even stronger-than-expected USD

Upcoming risk events: SARB meeting (21 March), elections (29 May)

Corporate hedging: we recommend hedging against rand strength in the medium term

Rates: no strong views

Exhibit 11: USD/ZAR forecasts vs forwards

We expect USD/ZAR at 18.0 by the end of 2024

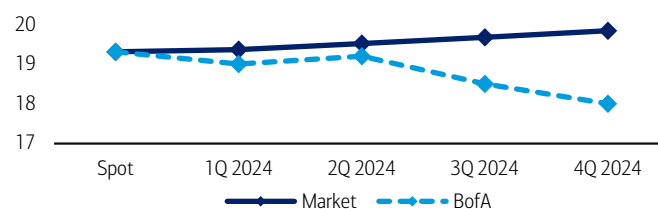
Spot	current 19.31	chg (diff) +0.27	Forward	
	Forecast		current	chg (diff)
Period	current	chg (diff)	current	chg (diff)
1Q 2024	19.00	+0.40	19.4	+0.21
2Q 2024	19.20	+0.70	19.5	+0.21
3Q 2024	18.50	+0.80	19.7	+0.20
4Q 2024	18.00	+0.20	19.8	+0.19

Source: BofA Global Research, Bloomberg

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Exhibit 12: USD/ZAR forecasts

Our forecast path is below forwards



Source: BofA Global Research, Bloomberg

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Cross currency basis USD/ZAR

Exhibit 13: USD/ZAR cross currency basis

1y xccy basis at 13.30bp

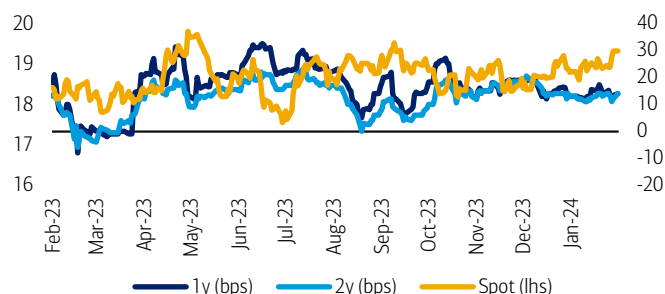
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	13.30	-0.9	0.4	-3.7	-8.0		32.5	16.2	5.3	38.0	-1.5	-0.4
2y	12.00	-1.0	-1.0	-1.0	-6.0		23.0	12.4	3.7	26.7	-2.8	-0.1
5y	8.00	-1.5	-4.0	-6.0	-2.0		19.5	9.6	2.9	20.7	-3.7	-0.3
10y	-4.00	-1.0	-1.0	8.4	-22.0		8.5	-10.0	3.1	22.6	-3.3	0.7

Note: ● : current value; ◇ : 1y average. The z-score measures the distance between the current value and the mean in standard deviation units. Source: BofA Global Research, Bloomberg

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Exhibit 14: Short-term basis swaps vs USD/ZAR spot

Xccy basis flattish

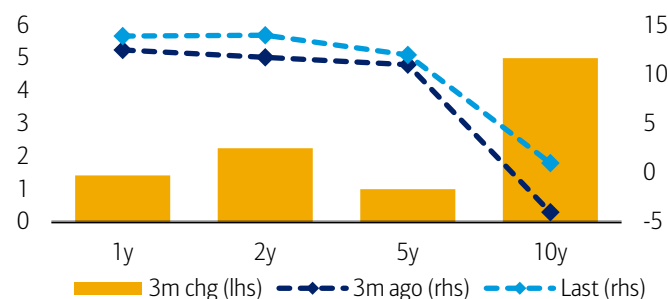


Source: BofA Global Research, Bloomberg

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Exhibit 15: Term structure of basis swaps (bps)

Long end moving higher



Source: BofA Global Research, Bloomberg

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Volatility surface USD/ZAR

Exhibit 16: Current implied volatilities

Upward sloping

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	13.04	13.07	13.50	14.42	15.59
3m	13.11	13.17	13.63	14.67	16.01
6m	13.85	14.01	14.60	15.91	17.59
1y	14.27	14.37	14.86	16.17	18.00

Source: BofA Global Research

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Exhibit 17: 3m z-scores of implied volatilities

Changes over time

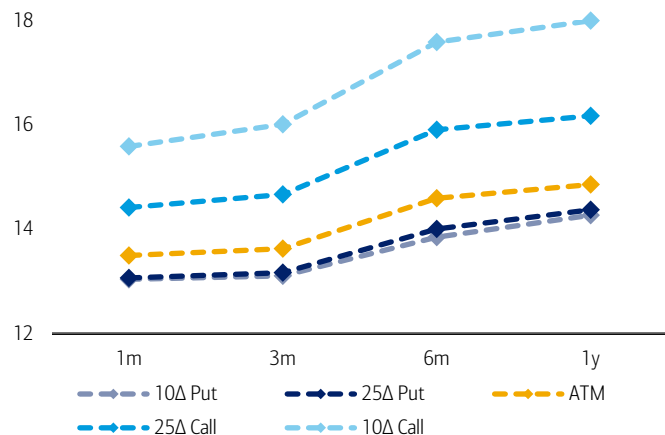
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-0.4	-0.3	-0.3	-0.3	-0.4
3m	-1.1	-1.0	-1.0	-1.1	-1.2
6m	-1.7	-1.3	-0.9	-0.7	-0.7
1y	-2.8	-2.3	-1.8	-1.7	-1.7

Source: BofA Global Research

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Exhibit 18: Term structures of implied volatilities

Upward sloping

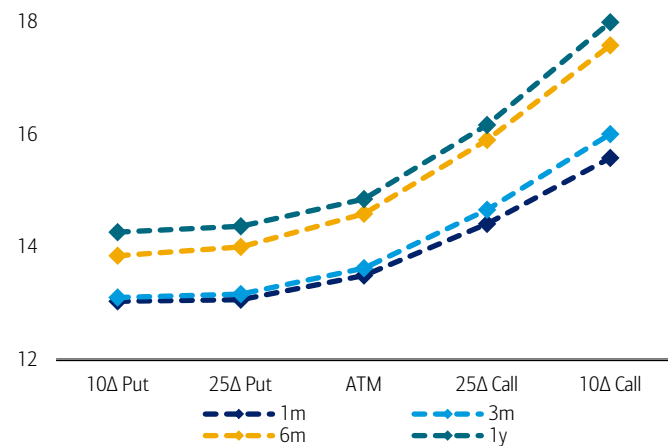


Source: BofA Global Research

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Exhibit 19: Implied volatility smiles

Implied vol smiles are somewhat skewed



Source: BofA Global Research

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Türkiye: weaker FX in line with forwards

Zumrut Imamoglu

MLI (UK)

zumrut.imamoglu@bofa.com

Mikhail Liluashvili

MLI (UK)

mikhail.liluashvili@bofa.com

View: TRY to be stronger than forwards imply against EUR

We are bullish TRY against the EUR in the short term as we do not expect any cuts in 2024. We see 5-10% real TRY appreciation this year. However, we are neutral on TRY FX against the USD due to stronger dollar outlook, significant external financing needs and upside risks to inflation. These factors are likely to be offset partly by TRY support from the official sector, leading to an orderly depreciation in line with forwards in Q1 and Q2.

Key macro developments: The CBRT held the policy rate constant but gave a message that the current monetary stance will be maintained for a long time or could be tightened further if needed. We think that additional hikes are possible in 2Q, depending on the demand side pressures from wage increases and additional FX demand from locals. While hikes are not our baseline, we do not expect cuts this year either as we expect inflation to be 40% at year-end and see risks on the upside. In the inflation report press conference and its statement, the CBRT made it clear that the monthly inflation trend is what is important. Hence, cut expectations based on a drop in the headline due to base effects are not realistic, in our opinion.

Bank loan growth is still subdued, although there has been some acceleration lately. Private banks' appetite to grow is high while public bank lending has been relatively muted. We do not observe high credit growth pre-local elections as we did before elections last May. Hence, we believe this time is different. The CBRT made it clear in its last statement that real appreciation in the currency was key to disinflation. We believe this could alleviate any jump concerns in the FX. We see c.5-10% real appreciation this year – a sharper decrease in the CA deficit than expected could support more than this.

The CBRT made changes to reserve requirements and started to pay interest on some conditional on FX-protected account conversions. Since then, reserve losses have slowed, TRY liquidity in the onshore market has tightened and TRY deposit rates (up to 3 months) have increased to 52%. FX-protected accounts continue to slowly decrease.

Valuations: TRY FX is significantly overvalued on our long-term CA-based model

Positioning: investors are net short TRY FX, particularly hedge funds

Risks to our view: Geopolitical risks, higher oil price

Upcoming risk events: February inflation (March 4), CBT meeting (March 21).

Corporate hedging: we do not recommend hedging through forwards, given the high implied yields and our neutral view

Rates: higher – too much easing is priced in for the next 12 months

Exhibit 20: USD/TRY forecasts vs forwards

We expect USD/TRY at 40 by the end of 2024

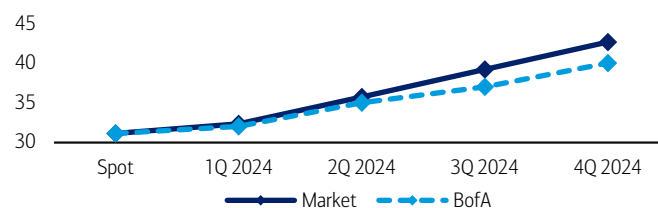
Spot	current 31.12	chg (diff) +0.86	Forward	
Period	current	chg (diff)	current	chg (diff)
1Q 2024	32.00	-	32.34	-0.19
2Q 2024	35.00	-	35.72	-0.10
3Q 2024	37.00	-	39.20	+0.04
4Q 2024	40.00	-	42.66	+0.02

Source: BofA Global Research, Bloomberg

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Exhibit 21: USD/TRY forecasts

Our forecast path is aligned with forwards



Source: BofA Global Research, Bloomberg

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Cross currency basis USD/TRY

Exhibit 22: USD/TRY xccy basis

1y xccy basis at 51bp

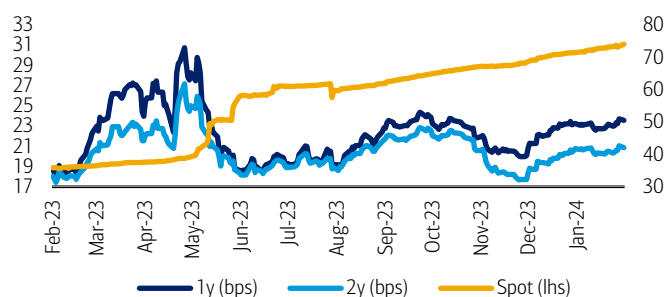
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	51.00	1.7	5.9	15.6	33.4		73.0	46.5	4.2	30.3	6.6	0.5
2y	42.69	1.7	1.5	9.2	31.4		61.8	41.2	3.0	21.9	6.3	0.3
5y	33.55	1.5	-0.3	4.0	25.9		48.4	33.2	2.4	17.0	5.8	0.1
10y	29.01	1.1	-0.5	2.6	23.1		41.4	28.9	2.2	16.1	4.6	0.0

Note: ● : current value; ◇ : 1y average. The z-score measures the distance between the current value and the mean in standard deviation units. Source: BofA Global Research, Bloomberg

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Exhibit 23: Short-term basis swaps vs USD/TRY spot

Xccy basis flattish

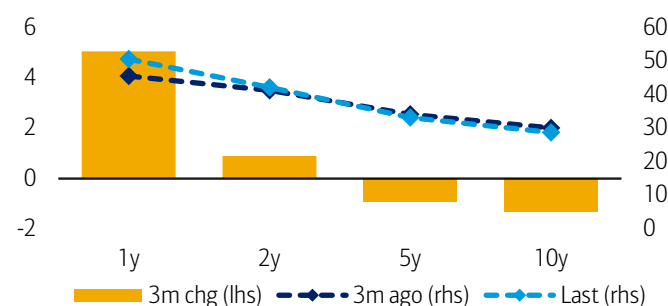


Source: BofA Global Research, Bloomberg

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Exhibit 24: Term structure of basis swaps (bps)

Short end moving higher



Source: BofA Global Research, Bloomberg

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Volatility surface USD/TRY

Exhibit 25: Current implied volatilities

Upward sloping

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	7.20	6.20	6.36	8.20	10.86
3m	10.04	9.31	10.19	13.31	17.46
6m	13.13	12.70	14.11	18.45	24.28
1y	17.52	17.13	18.64	24.13	31.92

Source: BofA Global Research

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Exhibit 26: 3m z-scores of implied volatilities

Changes over time

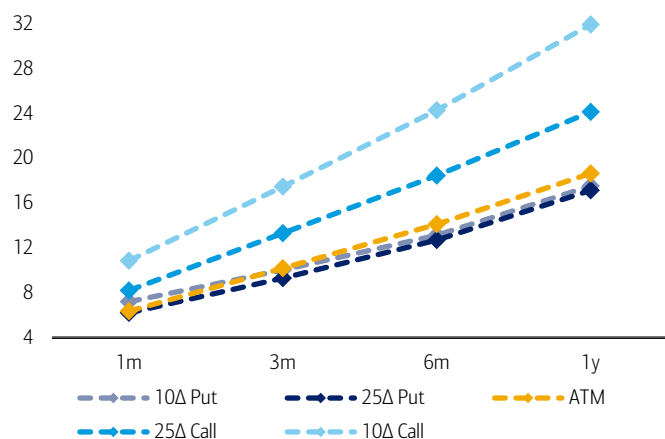
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-1.0	-1.0	-1.0	-1.2	-1.1
3m	-1.3	-1.3	-1.4	-1.5	-1.4
6m	-1.6	-1.5	-1.6	-1.7	-1.6
1y	-2.0	-1.9	-1.9	-2.0	-1.9

Source: BofA Global Research

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Exhibit 27: Term structures of implied volatilities

Upward sloping

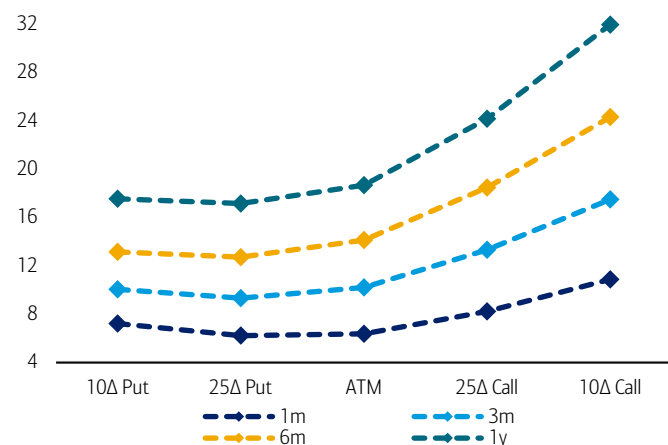


Source: BofA Global Research

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Exhibit 28: Implied volatility smiles

Implied vol smiles are somewhat skewed



Source: BofA Global Research

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Israel: conflict-driven FX

Zumrut Imamoglu

MLI (UK)

zumrut.imamoglu@bofa.com

Mikhail Liluashvili

MLI (UK)

mikhail.liluashvili@bofa.com

View: binary nature of risks leads to neutral view

Political and geopolitical risks are crucial for the ILS outlook. US equities and the broader dollar also matter for USD/ILS, but their importance has declined, in our view.

Key macro developments: Inflation in January surprised on the downside again at 2.6%, close to the upper bound of the target range. Tradables inflation decreased to 1.5% and non-tradables inflation excluding housing, fruits and vegetables fell to 2.3%. Nevertheless, the BOI held its base rate at 4.5%, in line with our forecast, and it kept its guidance unchanged. It still sees cuts over the rest of the year to be moderate and gradual. We expect the BOI to deliver the second cut in April unless inflation surprises on the upside. Overall, we see the year-end base rate at 3.5%. The bank said in its statement that “the constraints on activity in the construction industry, a depreciation of the shekel, and fiscal behavior” are the main risks to inflation.

Data points to some revival in the economy since the conflict started but economic activity still remains below pre-war levels. While demand recovers gradually, supply side limitations continue in sectors like housing and agriculture. Developments in the Red Sea add to supply side concerns and pose risk to transportation costs.

The budget deficit widened to 4.8% in January due to increased defence spending and a slowdown in the economy and is expected to be 6.6% in 2024, according to the new budget proposal. Moody’s downgraded Israel’s credit rating recently and other rating agencies are likely to follow. We don’t think fiscal policy will be an inflationary concern at this level, however, the general trajectory of the debt to GDP ratio will be watched closely.

Valuations: ILS FX remains undervalued on our current account model

Positioning: hedge funds are marginally short ILS, while RMs are long

Risks to our view: political noise, US equity performance

Upcoming risk events: CPI (15 March), BoI meeting (8 April).

Corporate hedging: no strong views

Rates: receiver bias as the cutting cycle has already started

Exhibit 29: USD/ILS forecasts vs forwards

We expect USD/ILS at 3.55 by the end of 2024

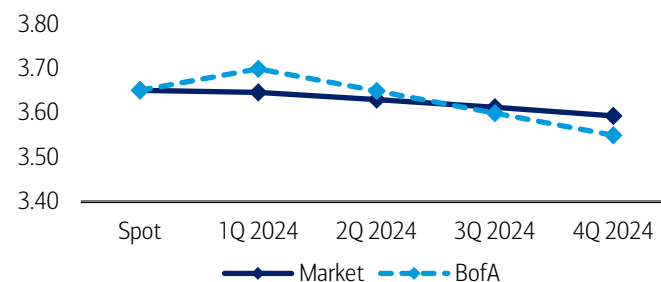
Spot	current 3.65	chg (diff) -0.107		
	Forecast		Forward	
Period	current	chg (diff)	current	chg (diff)
1Q 2024	3.70	-	3.65	-0.103
2Q 2024	3.65	-	3.63	-0.103
3Q 2024	3.60	-	3.61	-0.104
4Q 2024	3.55	-	3.59	-0.107

Source: BofA Global Research, Bloomberg

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Exhibit 30: USD/ILS forecasts

Our forecast path is below forwards in the long term



Source: BofA Global Research, Bloomberg

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Cross currency basis USD/ILS

Exhibit 31: USD/ILS cross currency basis

1y xccy basis at -69bp

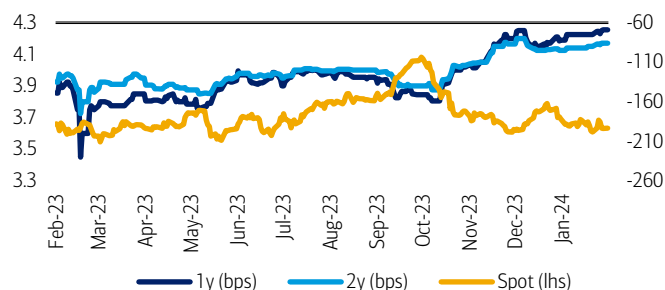
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	-69.00	6.0	47.0	69.0	-230.0		-69.0	-129.1	13.8	99.6	4.5	2.0
2y	-86.00	4.0	28.0	45.0	-175.0		-80.0	-122.2	7.9	57.2	2.8	1.9
5y	-106.00	-2.0	0.0	14.0	-136.0		-83.0	-113.5	4.3	31.0	-5.3	0.7
10y	-109.00	-3.0	-3.0	6.0	-131.0		-86.0	-113.0	3.9	28.3	-5.6	0.4

Note: ● : current value; ◇ : 1y average. The z-score measures the distance between the current value and the mean in standard deviation units. Source: BofA Global Research, Bloomberg

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Exhibit 32: Short-term basis swaps vs USD/ILS spot

Xccy basis flat

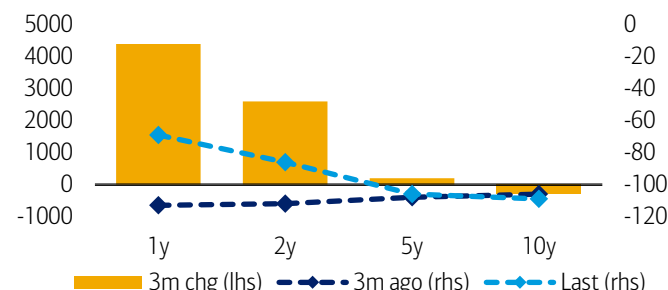


Source: BofA Global Research, Bloomberg

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Exhibit 33: Term structure of basis swaps (bps)

Short end moving higher



Source: BofA Global Research, Bloomberg

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Volatility surface USD/ILS

Exhibit 34: Current implied volatilities

Flattish

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	9.98	9.79	10.11	11.04	12.31
3m	9.36	9.24	9.65	10.72	12.12
6m	9.27	9.12	9.52	10.69	12.25
1y	9.24	9.10	9.50	10.75	12.40

Source: BofA Global Research

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Exhibit 35: 3m z-scores of implied volatilities

Changes over time

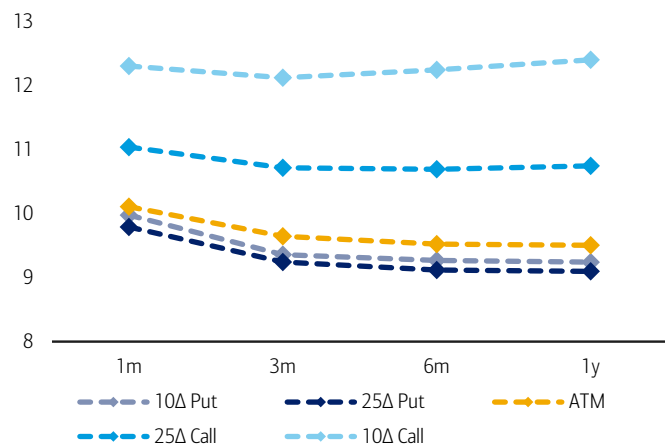
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-1.1	-0.8	-0.7	-0.8	-1.0
3m	-2.3	-2.0	-1.7	-1.8	-1.9
6m	-2.5	-2.4	-2.1	-2.0	-2.0
1y	-2.9	-2.8	-2.6	-2.3	-2.1

Source: BofA Global Research

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Exhibit 36: Term structures of implied volatilities

Flattish

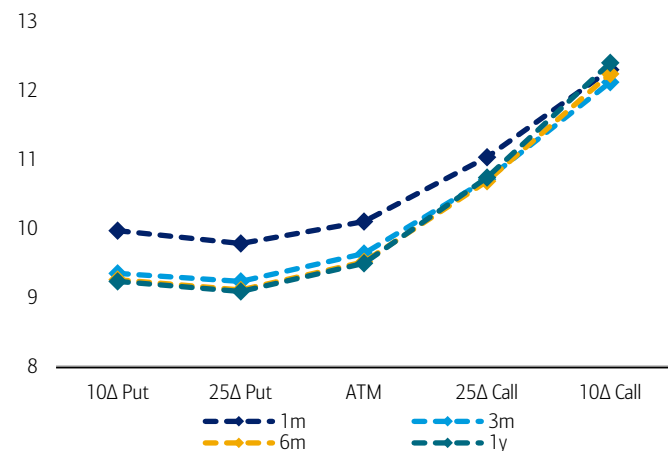


Source: BofA Global Research

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Exhibit 37: Implied volatility smiles

Implied vol smiles are skewed



Source: BofA Global Research

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Czechia: neutral view on FX

Mai Doan

MLI (UK)

mai.doan@bofa.com

Mikhail Liluashvili

MLI (UK)

mikhail.liluashvili@bofa.com

View: easing to drive CZK weaker in line with forwards

The CZK is likely to be under pressure in Q1/Q2 to depreciate as the market focuses on the cutting cycle and the dollar remains strong. From H2, a higher EUR/USD and strong BoP position should help the koruna appreciate against the euro.

Key macro developments: Much faster disinflation in January argues in favour of faster rate cuts, but a cautious Czech National Bank (CNB) means that it's a close call between 75bp vs 50bp in the upcoming meetings. For now, we keep our baseline of 50bp steps in line with the Board's preference, but expect a continuous easing cycle rather than a pause at 4%. The base rate will likely end 2024 at 3.50% (from our previous call of 4%) and reach the terminal level of 3% (no change) by early 2025.

Following the January CPI downside surprise, we expect inflation to slightly undershoot the 2% target by 3Q before picking up slightly in 4Q on base effects. Headline inflation at 2.3% in January, and core at 2.9% were well below the CNB's forecasts of 3% and 3.8%, respectively, and now well within the 2%±1% target tolerance band. Meanwhile, wage pressures appear to be easing. Monthly wage growth in the industrial sector has been trending lower, now c.6%, which is much closer to the neutral level of around 5%.

Activity data continue to paint a weak macro picture. Retail sales ex-auto have barely picked up and consumer confidence has not improved as much as for peers. Auto output has recovered, but demand is increasingly a constraint to production. The share of firms reporting this as an issue has been rising steadily in recent quarters to c.47%, comparable to levels at the onset of past crises (2008, 2012, 2020).

The macro case to move to 75bp rate cuts is strong, but the CNB Board may still want to keep a cautious approach to prove themselves to the public as 'inflation hawks'. We currently look for 50bp cut clips until the rate has fallen closer to 4%, when we think the CNB will move more cautiously in 25bp steps. Our baseline remains that the CNB rate will reach the 3% long-held neutral estimate by early 2025. At this stage we do not see the need for the CNB to go below neutral. This could change if the external backdrop, particularly German growth, worsens from here.

Valuations: the CZK is undervalued on our current account model

Positioning: the market is likely to be net short CZK

Main risks to our view: slower cutting cycle, stronger-than-expected USD

Upcoming risk events: CNB decisions (20 March, 2 May)

Corporate hedging: we do not recommend hedging in the short term

Rates: lower/steeper – the market underprices cutting cycles

Exhibit 38: EUR/CZK forecasts vs forwards

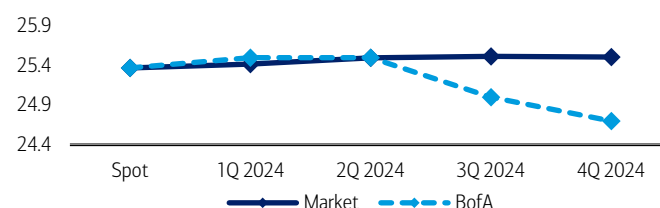
We expect EUR/CZK at 24.7 by the end of 2024

Spot	current 25.4	chg +0.50	Forward	
	Forecast		current	chg
Period	current	chg	current	chg
1Q 2024	25.5	+0.60	25.4	+0.43
2Q 2024	25.5	+0.50	25.5	+0.42
3Q 2024	25.0	+0.20	25.5	+0.38
4Q 2024	24.7	+0.10	25.5	+0.34

Source: BofA Global Research, Bloomberg

Exhibit 39: EUR/CZK forecasts

Our forecast path is below forwards in the long term



Source: BofA Global Research, Bloomberg

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Cross currency basis EUR/CZK

Exhibit 40: EUR/CZK cross currency basis

1y basis at -40.5bp

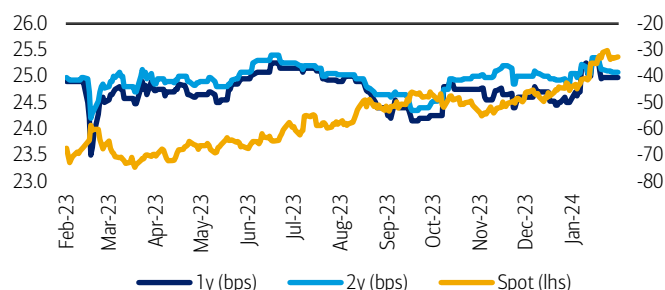
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	-40.50	0.0	5.0	1.3	-70.0		-34.5	-45.4	4.5	32.7	1.1	0.9
2y	-38.50	-1.8	2.0	5.5	-56.0		-32.6	-41.4	3.1	22.5	0.4	0.7
5y	-32.50	0.0	-3.0	2.5	-46.0		-23.5	-31.5	2.7	19.7	-1.4	-0.3
10y	-22.50	-0.1	0.0	-3.5	-27.7		-13.5	-19.4	2.4	17.5	-1.5	-0.9

Source: BofA Global Research, Bloomberg

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Exhibit 41: Short-term basis swaps vs EUR/CZK spot

Xccy basis stays flat

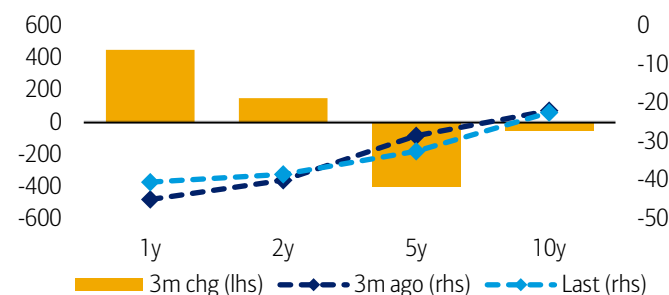


Source: BofA Global Research, Bloomberg

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Exhibit 42: Term structure of basis swaps (bps)

Short end moving higher



Source: BofA Global Research, Bloomberg

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Volatility surface EUR/CZK

Exhibit 43: Current implied volatilities

Flattish

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	5.21	4.94	4.93	5.29	5.86
3m	4.96	4.71	4.78	5.26	5.98
6m	4.83	4.57	4.66	5.22	6.03
1y	4.80	4.48	4.57	5.23	6.19

Source: BofA Global Research

BofA GLOBAL RESEARCH

Exhibit 44: 3m z-scores of implied volatilities

Changes over time

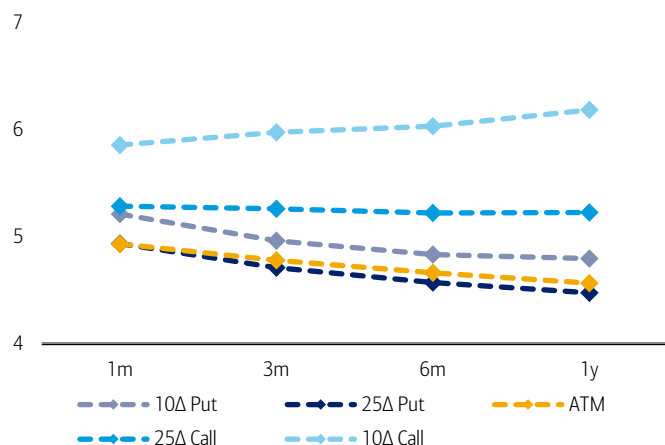
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	+0.8	+0.6	+0.1	-0.6	-1.2
3m	+0.2	+0.4	-0.1	-0.8	-1.2
6m	-0.6	-0.4	-0.7	-1.1	-1.3
1y	-0.9	-0.8	-1.0	-1.3	-1.5

Source: BofA Global Research

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Exhibit 45: Term structures of implied volatilities

Flattish

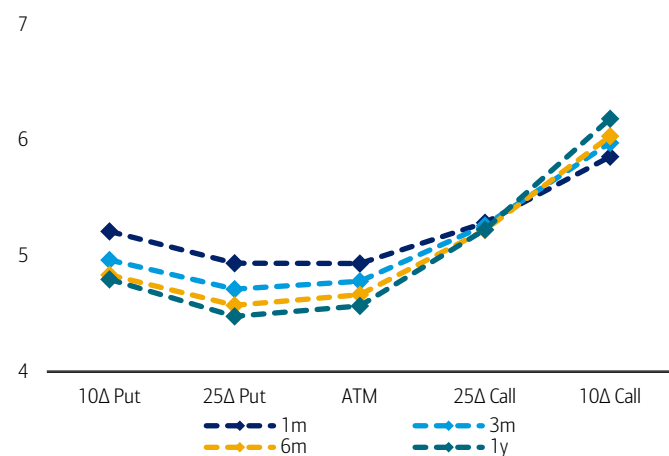


Source: BofA Global Research

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Exhibit 46: Implied volatility smiles

Implied vol smiles are somewhat skewed



Source: BofA Global Research

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Hungary: weaker in line with forwards

Mai Doan

MLI (UK)

mai.doan@bofa.com

Mikhail Liluashvili

MLI (UK)

mikhail.liluashvili@bofa.com

View: focus on growth means a weaker forint

Longer term, we expect HUF depreciation as policy focuses more on growth and 2026 elections, but some support to the forint from a weaker USD from H2.

Key macro developments: Despite sharp disinflation in 1Q, we maintain that the policy rate will fall to 5.5% by YE2024. Under Governor Matolcsy, whose term lasts until early March 2025, the National Bank of Hungary (NBH) will keep a cautious approach amid justified concerns about inflation and HUF stability. So the acceleration to 100bp rate cut step will likely be limited to the next 2-3 months, with the central bank keeping the guidance that rates will fall to 6-7% by mid-year. The government is likely content with this, as such levels of base rate allow more effective subsidised lending initiatives. The 2025 outlook is more uncertain with a change in governor, with the MPC likely holding a more dovish bias consistent with the government's preparation for 2026 elections. We think the base rate could fall to 4% next year. The idea of a "high pressure" economy favoured by EconMin implies the need for HUF depreciation in the longer term.

Headline CPI slowed much faster than expected to 3.8% yoy in January from 5.5% in December. Base effects will continue to be favourable in the next three months, so the trough is likely close to the 3% target. But we are cautious about underlying processes. Services inflation momentum has been stuck at c.8% saar for two months. Unit labour cost is well over 10%, with wage growth unlikely slowing to single-digit rates. Demand pressures will come back amid the government's efforts to revive growth, particularly household consumption. Consumer confidence has shot up recently, together with a higher intention for major purchases, as real wage growth improved sharply.

The EU funds outlook seems more positive than in 2023, though the process is not smooth sailing with various conditions for delivery. After unblocking c.EUR10bn of cohesion funds in late 2023, Hungary may get the green light from the EU to access recovery funds in late 1Q/2Q. While high-level politics is key to disbursement, we perceive good progress on Hungary's side in delivering the milestones and targets, and a more conciliatory approach from the EU. The first RRP payment would bring EUR1.7bn, which is in the budget for this year.

Valuations: the HUF looks undervalued on our current account model

Positioning: investors are net long HUF

Main risks to our view: more hawkish NBH, significantly weaker dollar

Upcoming risk events: NBH decisions (26 Mar, 23 Apr), EU RRP decision (late 1Q/2Q)

Corporate hedging: we recommend hedging vs HUF weakness

Rates: no strong views at the moment

Exhibit 47: EUR/HUF forecasts vs forwards

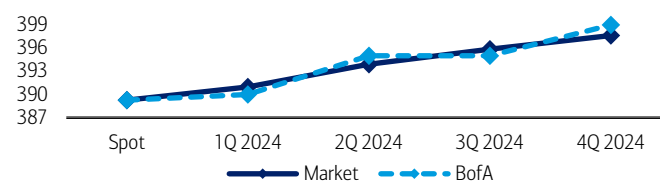
We expect EUR/HUF at 399 by the end of 2024

Spot	current	chg		
	389.3	+3.00		
	Forecast		Forward	
Period	current	chg	current	chg
1Q 2024	390	-	391	+1.12
2Q 2024	395	-	394	+1.33
3Q 2024	395	-	396	+1.50
4Q 2024	399	-	398	+1.56

Source: BofA Global Research, Bloomberg

Exhibit 48: EUR/HUF forecasts

Our forecast path is above forwards



Source: BofA Global Research, Bloomberg

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Cross currency basis EUR/HUF

Exhibit 49: EUR/HUF cross currency basis

1y basis at -27bp

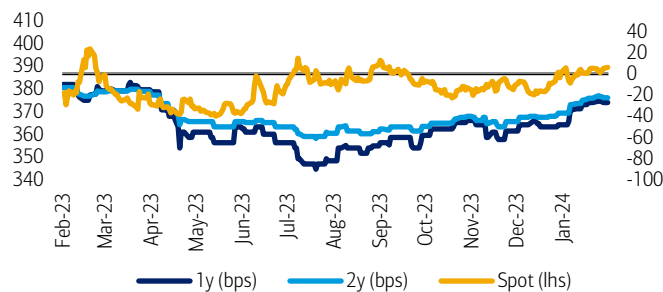
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	-27.0	0.0	17.0	-17.0	-90.0		-8.0	-49.3	7.4	53.2	2.2	1.1
2y	-22.5	0.5	17.5	-9.5	-61.0		-13.0	-40.2	3.8	27.3	2.5	1.3
5y	-14.8	1.2	20.2	2.7	-39.8		-14.3	-29.6	2.1	15.0	4.0	1.9
10y	-10.4	3.6	14.6	9.2	-35.0		-9.5	-22.8	4.2	30.0	2.7	3.0

Source: BofA Global Research, Bloomberg

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Exhibit 50: Short-term basis swaps vs EUR/HUF spot

Xccy basis stays flat

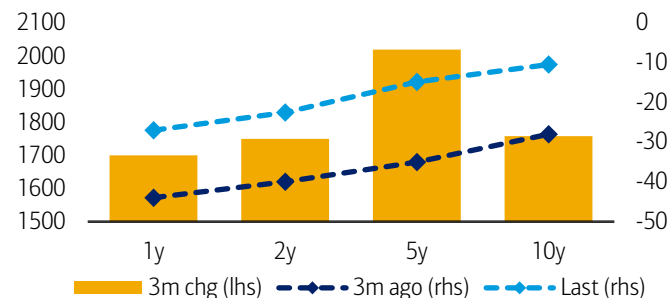


Source: BofA Global Research, Bloomberg

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Exhibit 51: Term structure of basis swaps (bps)

Belly moving higher



Source: BofA Global Research, Bloomberg

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Volatility surface EUR/HUF

Exhibit 52: Current implied volatilities

Upward sloping

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	5.89	5.71	6.01	6.86	7.96
3m	6.12	6.09	6.66	7.89	9.37
6m	6.52	6.43	7.04	8.48	10.22
1y	6.80	6.77	7.51	9.22	11.25

Source: BofA Global Research

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Exhibit 53: 3m z-scores of implied volatilities

Changes over time

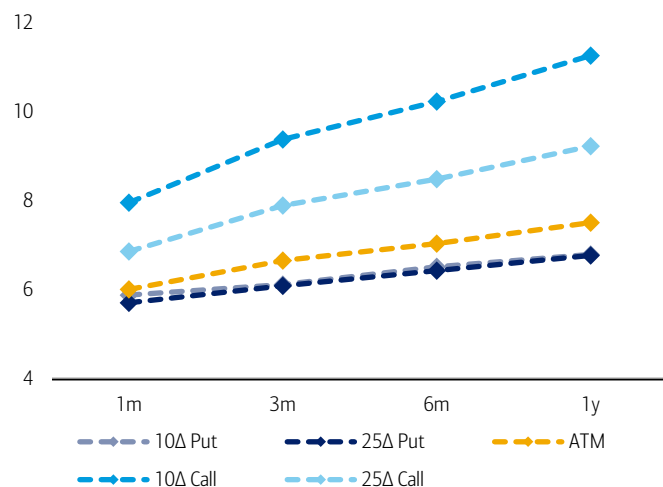
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-1.9	-2.1	-2.4	-2.6	-2.8
3m	-2.0	-2.1	-2.2	-2.3	-2.4
6m	-1.9	-2.0	-2.1	-2.1	-2.2
1y	-1.7	-1.8	-1.9	-2.1	-2.2

Source: BofA Global Research

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Exhibit 54: Term structures of implied volatilities

Upward sloping

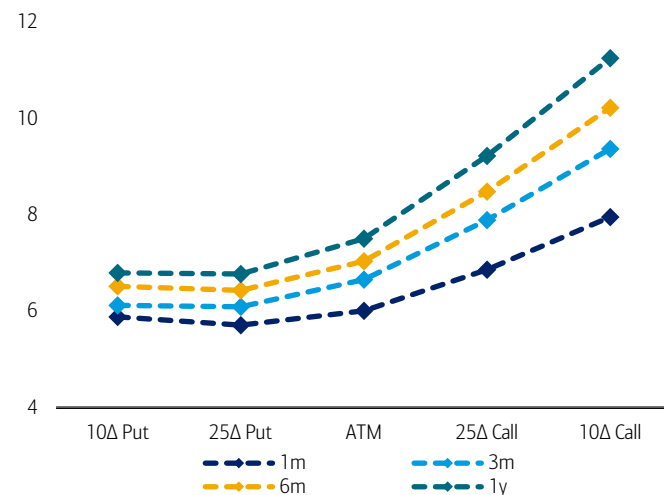


Source: BofA Global Research

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Exhibit 55: Implied volatility smiles

Implied vol smiles are somewhat skewed



Source: BofA Global Research

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Fair value Compass model

Exhibit 56: Compass FX fair value model

Fair value assessments from the long-term perspective (based on current account methodology)

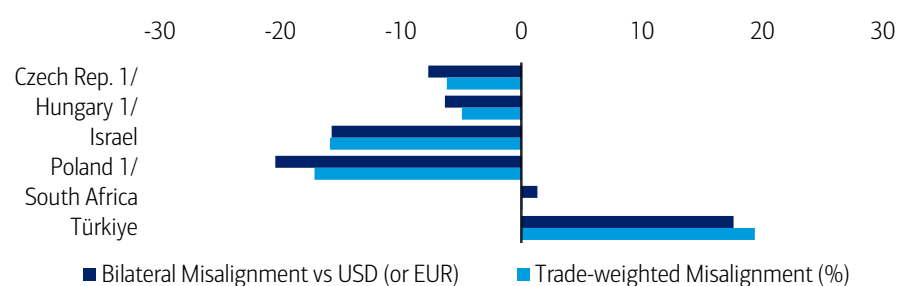
	Fair Value vs USD (or EUR)	Spot vs USD (or EUR)	Bilateral Misalignment vs USD (or EUR)	Trade-weighted Misalignment (%)
EEMEA			(5.2)	(4.1)
Czech Rep. 1/	23.55	25.37	(7.7)	(6.2)
Hungary 1/	366	389	(6.4)	(4.9)
Israel	3.14	3.63	(15.7)	(15.9)
Poland 1/	3.58	4.31	(20.4)	(17.2)
South Africa	19.48	19.22	1.3	0.1
Türkiye	37.79	31.14	17.6	19.3

Source: BofA Global Research. Last updated 27 February 2024. *against EUR

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Exhibit 57: Compass FX % misalignment

Türkiye and South Africa overvalued from a long-term perspective



Note: Please also see GEMs Viewpoint 'EM currencies now cheapest since 2009', 31 March 2020 for more info.

Source: BofA Global Research. Last updated 27 February 2024. 1/ against EUR

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EEMEA FX forecasts

Exhibit 58: EEMEA FX forecasts

End-of-period

EEMEA	Spot	1Q 2024		2Q 2024		3Q 2024		4Q 2024		1Q 2025		2Q 2025		3Q 2025	
		F'cst	Fwd	F'cst	Fwd	F'cst	Fwd	F'cst	Fwd	F'cst	Fwd	F'cst	Fwd	F'cst	Fwd
EUR/CZK	25.3	25.5	25.4	25.5	25.4	25.0	25.5	24.7	25.5	24.4	25.5	24.2	25.5	24.0	25.4
EUR/HUF	389.3	390	391	395	394	395	396	399	398	387	400	375	402	362	404
EUR/PLN	4.31	4.30	4.32	4.25	4.34	4.23	4.36	4.20	4.39	4.20	4.42	4.20	4.45	4.20	4.47
EUR/RON	4.97	5.01	4.98	5.02	5.00	5.04	5.03	5.05	5.05	5.13	5.08	5.21	5.11	5.28	5.14
USD/AED	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67
USD/EGP	30.9	30.9	39.6	45.0	47.9	47.0	50.2	50.0	52.5	52.0	55.1	54.0	57.8	56.0	60.6
USD/ILS	3.62	3.70	3.62	3.65	3.61	3.60	3.59	3.55	3.57	3.50	3.55	3.50	3.53	3.45	3.52
USD/KWD	0.31	0.30	0.31	0.30	0.31	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30
USD/KZT	450	420	454	420	463	420	472	420	480	420	489	420	498	420	509
USD/NGN	1544	1520	1557	1530	1601	1540	1653	1550	1701	1500	1754	1500	1803	1500	1853
USD/QAR	3.65	3.64	3.65	3.64	3.65	3.64	3.65	3.64	3.66	3.64	3.66	3.64	3.67	3.64	3.67
USD/SAR	3.75	3.75	3.75	3.75	3.75	3.75	3.76	3.75	3.76	3.75	3.76	3.75	3.76	3.75	3.77
USD/TRY	31.15	32.0	32.3	35.0	35.7	37.0	39.2	40.0	42.7	42.0	46.0	44.0	49.0	45.0	52.1
USD/UAH	38.3	40.0	38.3	40.0	38.3	40.0	38.3	40.0	38.3	40	38.3	40	38.3	40	38.3
USD/ZAR	19.1	19.0	19.2	19.2	19.3	18.5	19.5	18.0	19.7	17.9	19.8	18.0	20.0	18.2	20.2

Source: BofA Global Research, Bloomberg

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Special Disclosures

Some of the securities discussed herein should only be considered for inclusion in accounts qualified for high risk investment.



Disclosures

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Research Analysts

David Hauner, CFA >>

EEMEA Cross Asset Strategist
MLI (UK)
david.hauner@bofa.com

Mikhail Liluashvili

EEMEA Local Markets Strategist
MLI (UK)
mikhail.liluashvili@bofa.com

Mai Doan

CEE/Israel Economist/Strategy
MLI (UK)
mai.doan@bofa.com

Zumrut Imamoglu

Turkey & Israel Economist
MLI (UK)
zumrut.imamoglu@bofa.com

Tatonga Rusike

Sub-Saharan Africa Economist
MLI (UK)
tatonga.rusike@bofa.com

Vladimir Osakovskiy >>

EEMEA Macro/Equity Strategist
Merrill Lynch (DIFC)
vladimir.osakovskiy@bofa.com

Jean-Michel Saliba

MENA Economist/Strategist
MLI (UK)
jean-michel.saliba@bofa.com

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