

# The EEMEA FX Strategist

## Plant a hedge

### Carry is nice, but low vol = good hedge

Carry trades are popular for a reason, but rates vol is now at the lowest levels since end-January when we reached the first EM frenzy this year. If our Fed call (another two hikes) is correct, rates vol is likely to mean-revert higher around the July FOMC. We like adding hedges here, such as long USD/ILS and long USD/ZAR. The best EEMEA carry trades remain CZK and HUF, though with the caveat that the latter is very crowded.

**PLN (bearish):** a potential cut in October when inflation is still elevated should make the zloty weaker than forwards imply in Q2 and Q3.

**ZAR (bearish):** worsening of loadshedding is likely to drive the rand weaker in the next few months; we see USDZAR lower than forwards by the end of this year.

**TRY (neutral):** we expect orderly depreciation. High inflation and a significant current account deficit remain concerns. High carry and a tightening of liquidity conditions should provide some support for the currency.

**CZK (bullish):** a credible central bank with substantial reserves should drive the CZK stronger in the medium term; crowded positioning is becoming a concern.

**ILS (neutral):** the binary nature of the political outlook means we are neutral the ILS, but we think it has room to depreciate in the next few weeks.

**HUF (bullish):** an improving BoP because of falling gas prices, coupled with high carry, should support the forint over the forecast horizon; stretched positioning is a risk.

#### Exhibit 1: EEMEA FX forecasts for the next four quarters

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

Currency	View/bias	Spot	Forecasts			
			3Q '23	4Q '23	1Q '24	2Q '24
EUR/PLN	bearish	4.45	4.65	4.55	4.51	4.48
USD/ZAR	bearish	18.16	19.0	18.0	17.6	17.5
USD/TRY	neutral*	23.68	25.0	26.0	27.0	28.5
USD/ILS	neutral*	3.60	3.6	3.6	3.5	3.5
EUR/CZK	bullish	23.77	23.8	23.5	23.4	23.3
EUR/HUF	bullish	374	375.0	370.0	368.0	365.0

#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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20 June 2023

### GEM FI & FX Strategy EEMEA

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

**David Hauner, CFA >>**  
EEMEA Cross Asset Strategist  
MLI (UK)  
+44 20 7996 1241  
david.hauner@bofa.com

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

**Vladimir Osakovskiy >>**  
EEMEA Macro/Equity Strategist  
Merrill Lynch (DIFC)  
+971 4 425 8291  
vladimir.osakovskiy@bofa.com

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

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

[See Team Page for List of Analysts](#)

EEMEA is Emerging Europe, Middle East and Africa

Fed is Federal Reserve

FX is foreign exchange

BoP is balance of payments

USD is US dollar

SOE is state-owned enterprise

Vol is volatility

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Refer to important disclosures on page 16 to 18.

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Timestamp: 20 June 2023 08:37AM EDT

# Poland: bearish in Q3

**Mai Doan**

MLI (UK)

mai.doan@bofa.com

**Mikhail Liluashvili**

MLI (UK)

mikhail.liluashvili@bofa.com

## View: EURPLN should go higher than forwards imply

We expect higher EURPLN than forwards imply in Q3 2023 as the NBP is likely to cut in October and positioning is becoming long PLN. Real rates in Poland remain low (even without a cut), which is also a headwind for the zloty, in our view.

**Key macro developments:** Inflation likely heading towards single digits in the autumn will provide the NBP with the excuse to cut rates before the October elections. Inflation is the number-one topic for voters, but the PiS administration will claim victory early, when inflation is below 10%, to bolster its campaign. The NBP can argue that ex-ante real rates are positive based on the new projections in the July Inflation Report, and deliver a 25bp rate cut to 6.50% in October, as long as the PLN is strong.

We don't think this will mark the start of a swift easing cycle. Inflation will be sticky in high single-digit rates, in our view, with fiscal policies clearly pro-inflationary next year. We see headline inflation at over 8% at YE2023E and averaging around 6% in 2024E. The base rate may thus fall to 5.50% by YE2024E from 6.50% at YE2023E. This baseline assumes a continuation of the NBP's current dovish approach under another PiS government. The NBP would be likely to take a more hawkish stance if the opposition wins, in which case rates will likely be stable. The PLN performance will be an important factor for the rates outlook. The government remains in favour of a stable/strong PLN, and appears comfortable with EUR/PLN in a 4.50-4.60 range to balance the need to tame inflation without hurting competitiveness.

The ruling PiS is carefully planning its policies so as not to upset the disinflation trends until the October vote, but the 2024 fiscal looks set to be expansionary. The main parties are trying to maximise their chances for the 2023 elections, and 2024 brings local and European elections, so any fiscal consolidation is unlikely.

Financing in 2023 is comfortable even with the recent upward budget revision, with the borrowing requirement raised by c.1.4% of GDP. Around 75% of financing needs for this year have been funded. Meanwhile, the current account has improved more quickly than expected, solidifying the basic balance surplus at c.3% of GDP.

**Valuations:** the PLN is overvalued from both a CA (long-term) perspective and on our BEER (short-term) model

**Positioning:** the market is marginally net long the PLN

**Risks to our views:** weaker broader dollar, no cuts from the NBP in 2023

**Upcoming risk events:** NBP decisions (6 July, 6 Sep, 4 Oct)

**Corporate hedging:** we recommend hedging against PLN weakness in the short term

### Exhibit 2: EUR/PLN forecasts vs forwards

We expect EUR/PLN at 4.48 by the end of Q2 24

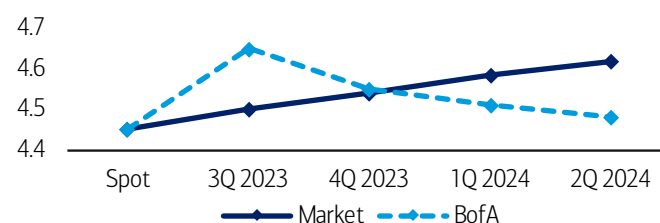
Spot	current 4.45	chg (diff) -0.05		
	Forecast		Forward	
Period	current	chg (diff)	current	chg (diff)
3Q 2023	4.65	-	4.50	-0.06
4Q 2023	4.55	-	4.54	-0.07
1Q 2024	4.51	-	4.59	-0.07
2Q 2024	4.48	-	4.62	-0.07

Source: BofA Global Research, Bloomberg

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### Exhibit 3: EUR/PLN forecasts

Our forecast path is below forwards in the long term



Source: BofA Global Research, Bloomberg

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## Cross currency basis EUR/PLN

### Exhibit 4: EUR/PLN cross currency basis

1y xccy basis at 89.0bp

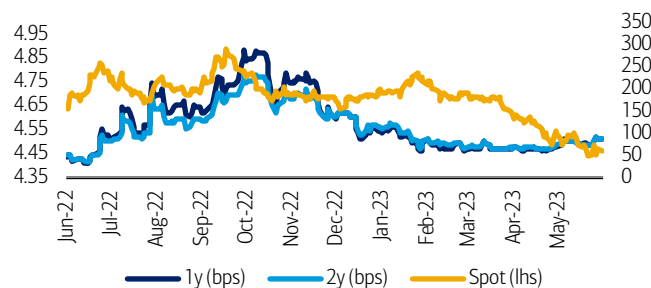
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	89.00	17.0	27.0	46.0	32.5		287.5	123.1	25.4	183.4	2.4	-0.5
2y	89.00	16.5	25.0	43.0	35.5		235.0	113.2	19.8	143.1	2.6	-0.5
5y	87.50	13.0	13.5	39.5	39.5		188.0	105.7	14.2	102.1	1.8	-0.5
10y	90.00	13.0	8.0	29.0	52.0		185.5	107.2	13.3	95.6	1.5	-0.5

Note: = up; = down. 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 basis stays flat

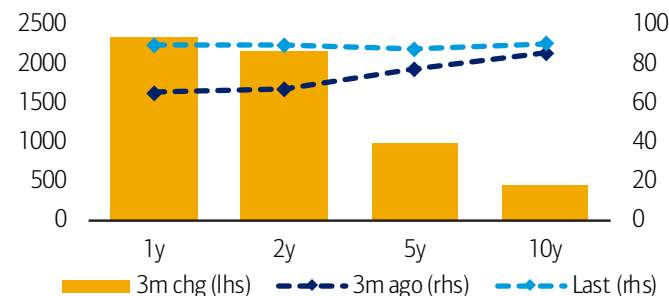


Source: BofA Global Research, Bloomberg

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### Exhibit 6: Term structure of basis swaps (bps)

Short end moving higher



Source: BofA Global Research, Bloomberg

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## Volatility surface EUR/PLN

### Exhibit 7: Current implied volatilities

Close to flat

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	6.21	6.02	6.55	7.92	9.68
3m	6.19	6.03	6.62	8.13	10.04
6m	6.38	6.20	6.81	8.45	10.53
1y	6.53	6.32	6.92	8.62	10.81

Source: BofA Global Research

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### Exhibit 8: 3m z-scores of implied volatilities

Changes over time

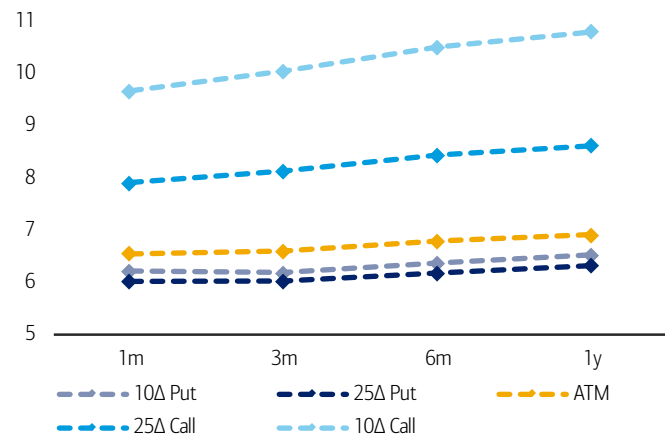
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	+0.3	+0.5	+0.6	+0.6	+0.5
3m	-0.1	+0.2	+0.2	+0.1	-0.1
6m	-1.1	-0.6	-0.3	-0.4	-0.5
1y	-1.9	-1.5	-1.1	-1.0	-0.9

Source: BofA Global Research

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### Exhibit 9: Term structures of implied volatilities

Close to flat

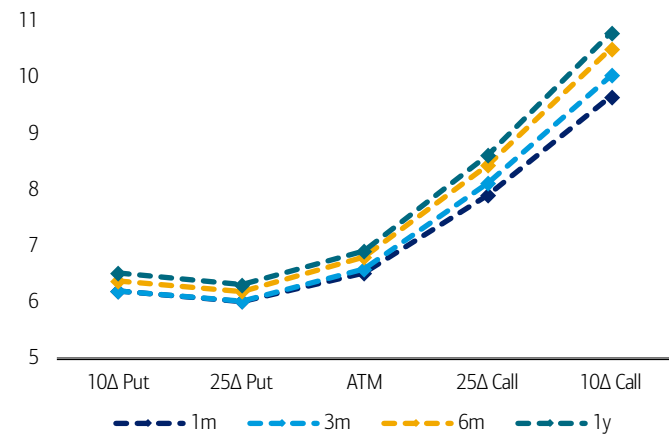


Source: BofA Global Research

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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: more loadshedding

**Tatonga Rusike**

MLI (UK)

tatonga.rusike@bofa.com

**Mikhail Liluashvili**

MLI (UK)

mikhail.liluashvili@bofa.com

## View: more weakness in the next 3 months

Loadshedding is likely to be an important driver of USDZAR in the short term. We think winter in South Africa will bring higher stages of loadshedding and, hence, a weaker rand as Stage 3 loadshedding is unsustainable, in our view.

**Key macro developments:** 1Q 2023 GDP printed 0.4% quarter on quarter seasonally adjusted (0.2% year on year), from a revised -1.1% contraction in 4Q 2022. The positive print means South Africa avoided slipping into a technical recession. We revised up our 2023E real GDP growth to 0.5% from 0.1% previously. The revision is largely a statistical bounce following a better-than-expected 1Q 23 outcome. We assume no contraction in the coming quarters but subdued quarter-on-quarter positive growth. The 1Q 2023 current account balance was -ZAR66.2bn relative to a revised -ZAR155.3bn deficit (previously a -ZAR174bn deficit) in 4Q 22, seasonally adjusted. As a % of GDP it is -1% in 1Q 23 relative to -2.3% in 4Q 22. A higher risk premium is now being applied to the ZAR amid increased loadshedding and geopolitical tensions.

The 1Q 23 current account deficit was a positive surprise compared to our expectation of a current account deficit similar to 4Q 22. The main swing factor in this print is the trade in goods and services account, which swung into a surplus (ZAR43bn) from a deficit in 4Q (-ZAR54bn). Annualised exports were higher in 1Q compared to 4Q, particularly gold receipts. Overall, our view remains that the current account is weakening on lower exports from coal and rhodium – the two biggest export earners since 2021. Coal prices are more than 50% down, while volumes are also weak. Rhodium volumes (a precious metal) are also down 30%. Despite a surge in gold prices and iron ore in 2023, this will not offset the losses from coal and rhodium. The overall non-seasonally adjusted trade balance remains in deficit year to date, partly because of the large trade deficit posted in January. On the other hand, some moderate increases in imports from higher petroleum products and from solar panels related to offsetting effects of power cuts. We estimate a current account deficit of -2.7% of GDP in 2023.

**Valuations:** the ZAR is significantly undervalued on our BEER model and overvalued on our FEER model

**Positioning:** investors are short the rand, but much less than at the beginning of June

**Risks to our view:** a weaker USD, less severe loadshedding

**Upcoming risk events:** SARB meeting (20 July), BRICS summit in August

**Corporate hedging:** we recommend hedging against rand weakness in the short term

### Exhibit 11: USD/ZAR forecasts vs forwards

We expect USD/ZAR at 17.5 by the end of Q2 24

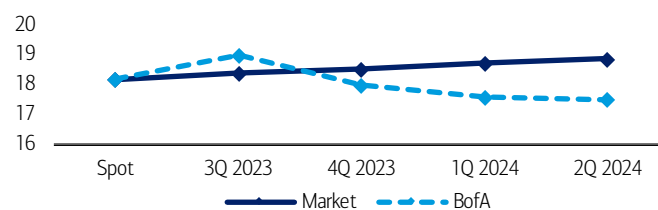
Spot	current	chg (diff)		
	18.18	-1.63		
Period	Forecast		Forward	
	current	chg (diff)	current	chg (diff)
3Q 2023	19.00	+1.00	18.4	-1.67
4Q 2023	18.00	+1.00	18.5	-1.70
1Q 2024	17.60	+0.40	18.7	-1.75
2Q 2024	17.50	-	18.9	-1.80

Source: BofA Global Research, Bloomberg

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### Exhibit 12: USD/ZAR forecasts

Our forecast path is below forwards in the long term



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 51.0bp

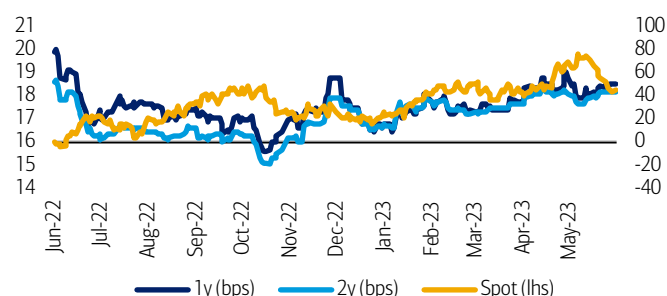
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	51.00	3.0	23.5	-28.0	-8.0		80.0	30.1	10.2	73.3	1.7	1.4
2y	43.00	-1.0	18.0	-11.5	-18.3		53.5	20.7	6.7	48.0	1.8	1.4
5y	35.50	0.0	6.5	12.0	-10.0		48.0	16.0	5.6	40.4	0.6	1.2
10y	11.00	-0.5	0.0	13.0	-22.0		32.0	-1.5	6.0	43.5	-1.4	0.9

Note: = up; = down. 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 in the middle range

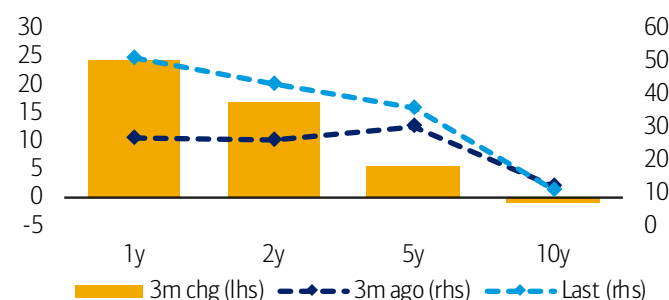


Source: BofA Global Research, Bloomberg

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### Exhibit 15: Term structure of basis swaps (bps)

Short end moving higher



Source: BofA Global Research, Bloomberg

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## Volatility surface USD/ZAR

### Exhibit 16: Current implied volatilities

Slightly upward sloping

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	13.28	13.14	13.75	15.29	17.28
3m	13.89	13.87	14.56	16.27	18.50
6m	14.55	14.56	15.18	16.84	19.06
1y	15.12	15.09	15.52	16.99	19.16

Source: BofA Global Research

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### Exhibit 17: 3m z-scores of implied volatilities

Changes over time

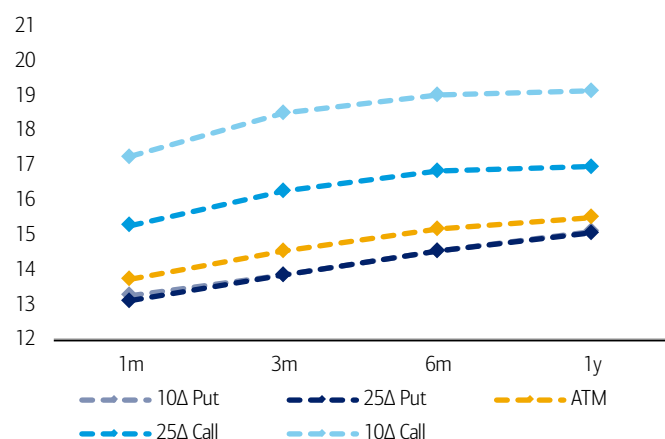
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-1.6	-1.7	-1.5	-1.2	-0.9
3m	-2.1	-1.9	-1.5	-1.0	-0.6
6m	-2.2	-1.8	-1.3	-0.8	-0.5
1y	-1.2	-1.3	-1.3	-1.1	-0.9

Source: BofA Global Research

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### Exhibit 18: Term structures of implied volatilities

Slightly upward sloping

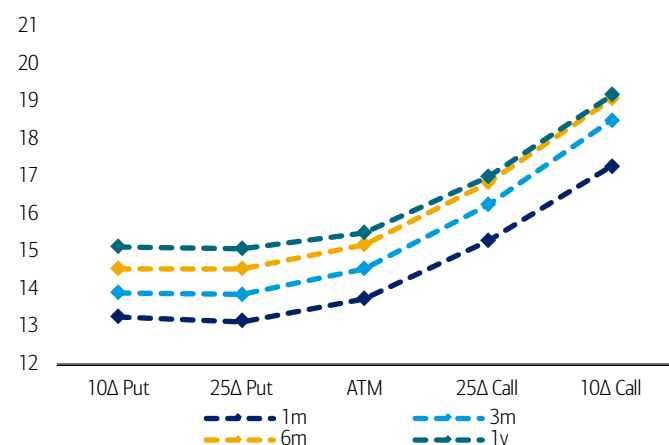


Source: BofA Global Research

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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 TRY, close to forwards

**Zumrut Imamoglu**

MLI (UK)

zumrut.imamoglu@bofa.com

**Mikhail Liluashvili**

MLI (UK)

mikhail.liluashvili@bofa.com

## View: neutral TRY FX

We are neutral on TRY FX due to significant external financing needs, risks to the inflation outlook, and negative net international FX reserves. These factors are likely to be partially offset by support to the TRY from the official sector leading to an orderly depreciation.

**Key macro developments:** Pressure on reserves and the current account balance still imply a weaker TRY. Gross reserves have recovered only slightly since the election by \$1.3bn despite a depreciation of c.17%. Usable FX reserves increased to \$14.8bn from \$11.1bn and gold reserves were \$42bn. A rate decision on Thursday and how much the authorities will change the regulations and controls will be key to shape expectations. However, an increase in the minimum wage of around 25-30% would weigh on exporters and they could continue to demand weaker TRY.

Relaxing the regulations, especially those that require banks to convert FX deposits to TRY deposits, could push TRY deposit rates down from the current level of 40-45% and create retail FX demand. FX-protected account participation has calmed recently, and this could weaken further with looser regulations. Good news on the demand side is that consumer loan growth has slowed significantly since the elections as we expected, even without a rate hike. State bank lending is at a slower pace and consumer loan rates have hit 40%. However, it will take more tightening to stabilize the TRY and inflation dynamics.

**Valuations:** TRY is undervalued on our BEER model and still overvalued on our current account model

**Positioning:** investors are net short TRY FX

**Risks to our view:** Ukraine-Russia conflict escalation, higher-than-expected energy prices.

**Upcoming risk events:** June inflation (July 3), CBT meeting (June 22)

**Corporate hedging:** we do not recommend hedging through forwards given the high implied yields

### Exhibit 20: USD/TRY forecasts vs forwards

We expect USD/TRY at 28.5 by the end of Q2 24

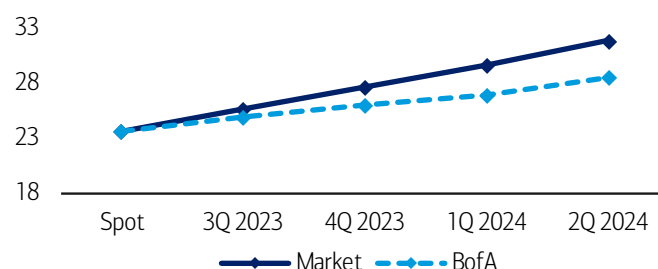
Spot	current 23.62	chg (diff) +3.68	Forward	
Period	current	chg (diff)	current	chg (diff)
3Q 2023	25.00	+1.50	25.60	+1.19
4Q 2023	26.00	+1.00	27.65	+0.59
1Q 2024	27.00	+1.00	29.70	+0.05
2Q 2024	28.50	+1.00	31.88	-0.38

Source: BofA Global Research, Bloomberg

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### Exhibit 21: USD/TRY forecasts

Our forecast path is below 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 1761bp

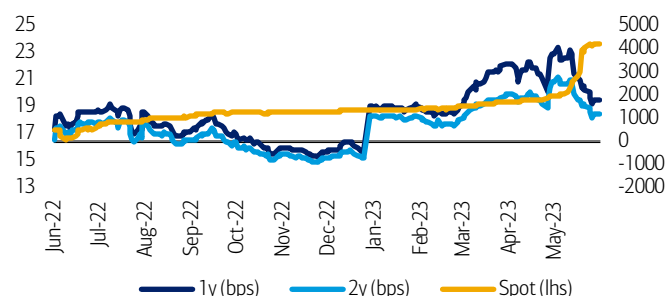
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	1760.75	-455.3	267.2	1050.7	-657.6		4077.3	1145.6	461.0	3324.0	-1.3	0.5
2y	1171.41	-331.5	270.9	878.9	-883.8		2793.8	601.1	356.6	2571.7	-1.1	0.6
5y	719.96	-148.2	366.6	543.7	-824.6		1710.9	268.8	269.8	1945.8	-0.6	0.7
10y	498.71	-114.4	337.3	341.4	-751.4		1302.6	157.3	221.3	1595.5	-0.4	0.7

Note: = up; = down. 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 going down

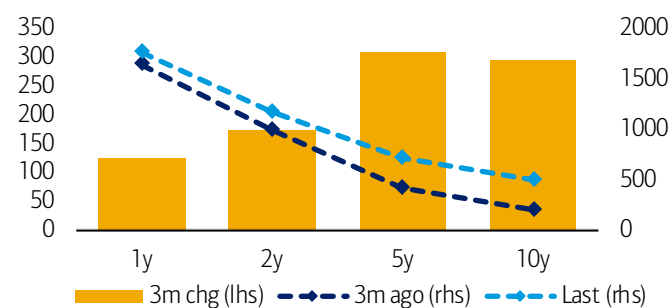


Source: BofA Global Research, Bloomberg

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### Exhibit 24: Term structure of basis swaps (bps)

Long 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	29.98	31.18	35.90	45.68	57.19
3m	29.87	31.37	36.18	47.37	60.66
6m	31.17	33.50	38.00	49.50	64.33
1y	35.70	37.52	41.05	54.02	73.38

Source: BofA Global Research

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### Exhibit 26: 3m z-scores of implied volatilities

Changes over time

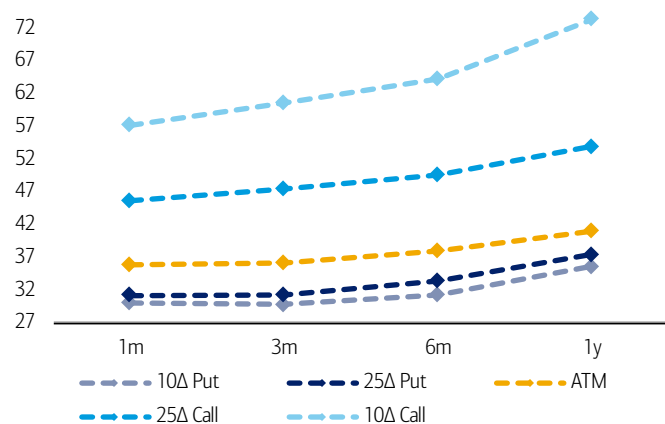
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	+0.4	+0.3	+0.4	+0.5	+0.5
3m	-0.1	-0.2	-0.1	+0.1	+0.3
6m	+0.4	+0.2	+0.2	+0.3	+0.4
1y	+0.9	+0.4	+0.2	+0.3	+0.9

Source: BofA Global Research

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### Exhibit 27: Term structures of implied volatilities

Upward sloping

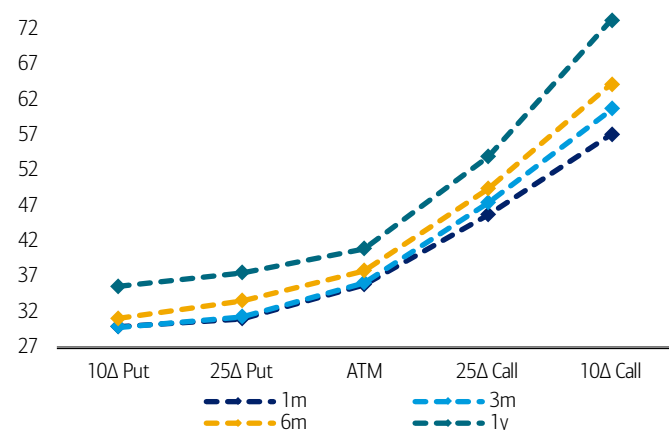


Source: BofA Global Research

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### Exhibit 28: Implied volatility smiles

Implied vol smiles are somewhat skewed



Source: BofA Global Research

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# Israel: it is all about the judiciary reform

**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

USDILS performance is still at the mercy of political risks and to some extent US equities. Anecdotal evidence suggests that locals hedge ILS strength much less now when they buy US equities. This means that judiciary reform and, to some extent, the broader dollar are becoming more important drivers than before.

**Key macro developments:** May inflation surprised on the downside and decreased to 4.6% yoy vs. 5% consensus. The drop in the tradables inflation was the major driver, going down from 4.1% to 3.5%. Clothing and furniture were the main contributors to the decrease in mom inflation. Meanwhile, services inflation remained high at 5.3%, down from 5.4% the previous month. The increase in house prices mom kept its pace at 0.5%.

We expect the Bank of Israel (BOI) to hold the key rate at 4.75% at the July meeting and we don't see any further hikes unless inflation data surprises on the upside or ILS depreciates further than 3.70-3.75 levels. Uncertainty around judicial reform is still the main risk to the exchange rate, rather than economic data.

GDP growth in 1Q was revised up to 3.1% from 2.5%, still pointing to a mild slowdown in the economy. The upward revision in the investments component was the main driver. However, investments still contracted qoq and decreases in exports were deeper than estimated previously. 1Q growth data is still in line with our expectation of 2.5% growth in 2023. The budget was approved by the Knesset at the end of May and the planned total spending remained the same as expected – at a 5.3% increase over last year. The BOI and Ministry of Finance estimate the deficit at the end of the year to be 0.9% while we see it at 2% since we expect a 5% drop in tax revenues this year.

**Valuations:** ILS FX remains undervalued on our current account and BEER models

**Positioning:** investors are net long ILS FX

**Risks to our view:** political noise, better-than-expected performance of US equities

**Upcoming risk events:** CPI (15 July), BoI meeting (10 July)

**Corporate hedging:** we do not recommend any hedging given the binary outcome for the currency depending on political developments

### Exhibit 29: USD/ILS forecasts vs forwards

We expect USD/ILS at 3.45 by the end of Q2 24

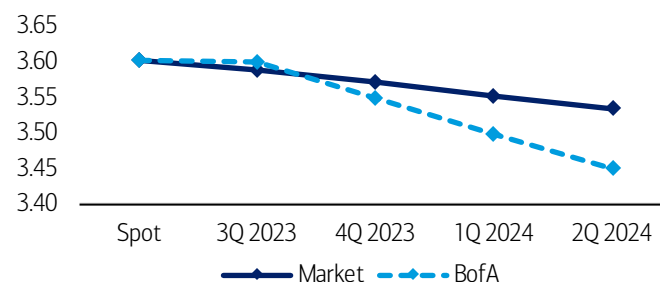
Spot	current 3.60	chg (diff) -0.128		
	Forecast		Forward	
Period	current	chg (diff)	current	chg (diff)
3Q 2023	3.60	-	3.59	-0.120
4Q 2023	3.55	-	3.57	-0.119
1Q 2024	3.50	-	3.55	-0.122
2Q 2024	3.45	-	3.53	-0.128

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

BofA GLOBAL RESEARCH



## Cross currency basis USD/ILS

### Exhibit 31: USD/ILS cross currency basis

1y xccy basis at -144bp

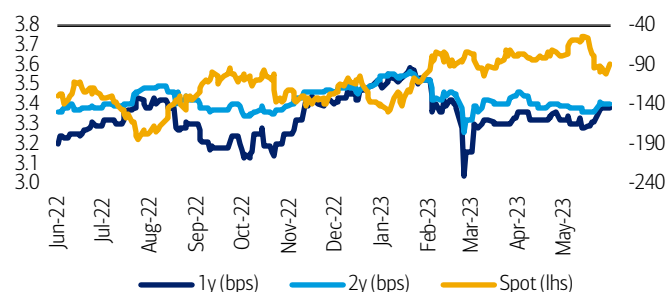
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	-144.00	18.0	56.0	46.0	-230.0		-93.0	-155.1	16.4	118.1	1.9	0.4
2y	-138.00	11.5	22.0	11.0	-175.0		-98.0	-133.4	9.2	66.5	0.4	-0.3
5y	-122.00	3.0	13.0	-10.0	-136.0		-99.0	-119.4	4.5	32.4	0.5	-0.3
10y	-122.00	2.0	8.0	-23.5	-131.0		-98.5	-116.3	4.3	30.8	0.4	-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 32: Short-term basis swaps vs USD/ILS spot

Xccy basis at the upper end of the historical range

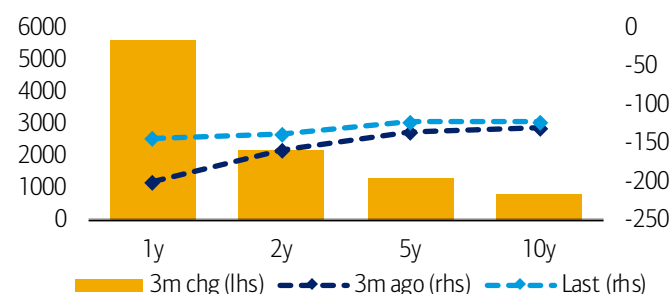


Source: BofA Global Research, Bloomberg

BofA GLOBAL RESEARCH

### 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

Slightly downward sloping

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	10.43	10.15	10.48	11.55	13.02
3m	10.25	10.01	10.36	11.46	12.95
6m	10.04	9.86	10.24	11.36	12.86
1y	9.71	9.56	9.97	11.21	12.84

Source: BofA Global Research

BofA GLOBAL RESEARCH

### Exhibit 35: 3m z-scores of implied volatilities

Changes over time

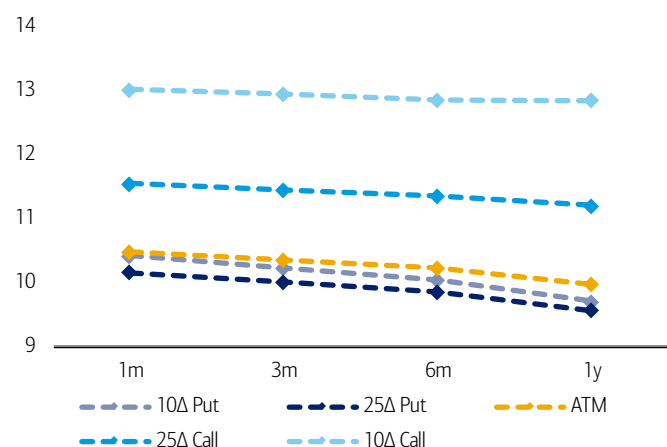
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-0.7	-0.6	-0.7	-0.8	-0.9
3m	-0.5	-0.4	-0.5	-0.6	-0.9
6m	-0.4	-0.2	-0.2	-0.5	-0.9
1y	-0.5	+0.1	+0.3	-0.1	-0.6

Source: BofA Global Research

BofA GLOBAL RESEARCH

### Exhibit 36: Term structures of implied volatilities

Slightly downward sloping

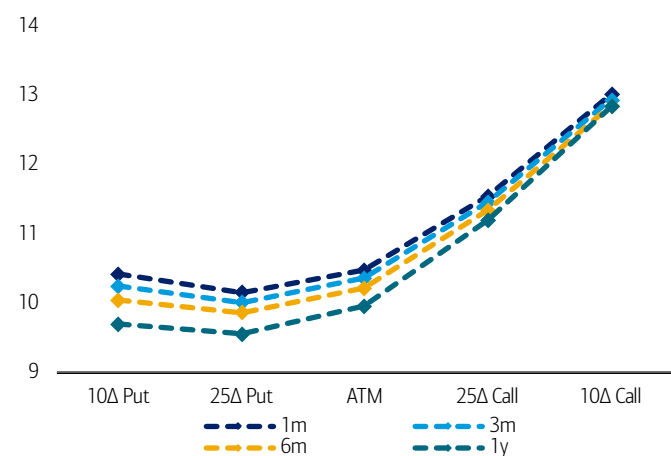


Source: BofA Global Research

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### Exhibit 37: Implied volatility smiles

Implied vol smiles are skewed



Source: BofA Global Research

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# Czechia: appreciation trend for CZK

**Mai Doan**

MLI (UK)

mai.doan@bofa.com

**Mikhail Liluashvili**

MLI (UK)

mikhail.liluashvili@bofa.com

## View: CZK to outperform forwards

Starting from Q3, a weakening US dollar and a credible central bank with significant reserves should drive the CZK stronger. However, positioning in the CZK is becoming crowded and valuations do not look very attractive.

**Key macro developments:** The market is keen to price in the CNB cutting soon, as sequential inflation is slowing quickly and domestic demand remains weak, but we think the central bank is still focused on the headline yoy growth rate as an important factor for inflation expectations. Since the May meeting, the hawkish arguments for rate hikes have clearly eased. The June meeting may thus see a 5-2 or 6-1 vote to hold rates, from 4-3 in May. But the prospects of high single-digit headline rates this year, together with a tight labour market, should continue to make the CNB uncomfortable to start thinking about easing soon. We see the first rate cut in February 2024, barring any major negative shocks, which could lead to a move in late 2023. We keep our YE2024 policy rate forecast at 4%.

While headline inflation has been falling steadily, the Board members are likely concerned about ability to strictly deliver the 2% target in 2024 after several years of overshooting. These concerns are driven by the recent renewed tightening in the labour market and strong corporate profitability, which likely strengthens employees' bargaining power for a material pay rise to compensate for high inflation in the past year. With YE inflation likely having important implications for wage negotiations, we do not think the CNB will opt to cut rates in 4Q.

The CNB maintains its preference for a strong CZK, though it has not intervened for several months. The hawkish split of votes, while unlikely to lead to a rate hike, should help the central bank to support the CZK as a quick channel to disinflation. The CZK is also cushioned by the recent quick turnaround in the current account, which improved by more than 1% of GDP in the first three months of the year.

**Valuations:** the CZK is overvalued on the FEER model and fairly valued on our BEER model

**Positioning:** the market is net long the koruna

**Main risks to our view:** a stronger-than-expected broader dollar

**Upcoming risk events:** CNB decisions (21 Jun, 3 Aug, 27 Sep, 2 Nov)

**Corporate hedging:** we recommend hedging vs CZK strength

### Exhibit 38: EUR/CZK forecasts vs forwards

We expect EUR/CZK at 23.3 by the end of Q2 24

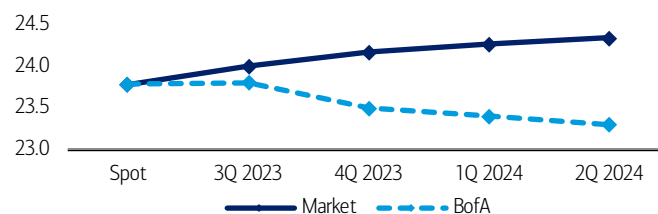
Spot	current 23.8	chg +0.17		
	Forecast		Forward	
Period	current	chg	current	chg
3Q 2023	23.8	-	24.0	+0.12
4Q 2023	23.5	-	24.2	+0.11
1Q 2024	23.4	-	24.3	+0.08
2Q 2024	23.3	-	24.3	+0.04

Source: BofA Global Research, Bloomberg

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### Exhibit 39: EUR/CZK forecasts

Our forecast path is below forwards



Source: BofA Global Research, Bloomberg

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## Cross currency basis EUR/CZK

### Exhibit 40: EUR/CZK cross currency basis

1y basis at -43bp

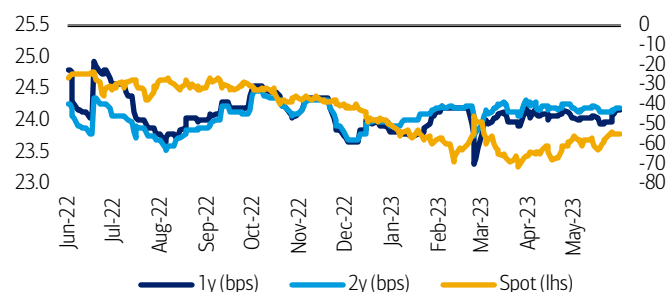
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	-43.00	5.0	16.9	-23.5	-70.0		-18.0	-44.7	6.3	45.1	2.3	0.2
2y	-41.50	2.0	12.0	0.5	-62.7		-33.0	-45.7	4.5	32.8	0.6	0.7
5y	-34.00	-1.5	8.8	15.0	-64.9		-30.0	-42.2	4.5	32.4	-0.4	0.9
10y	-20.50	-3.5	7.0	19.5	-63.3		-15.5	-31.1	4.5	32.6	-1.5	0.8

Source: BofA Global Research, Bloomberg

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

Xccy basis at the middle of the historical range

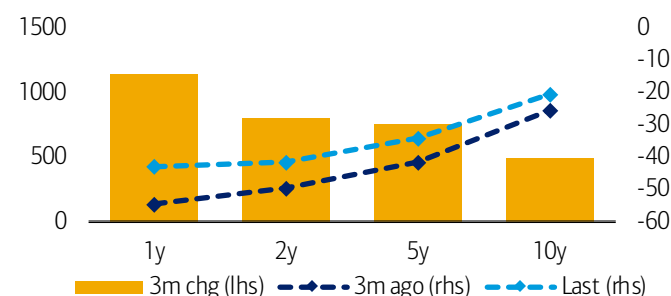


Source: BofA Global Research, Bloomberg

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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

Slightly upward sloping

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	4.40	4.20	4.48	5.31	6.43
3m	4.23	4.03	4.42	5.53	6.96
6m	4.20	4.01	4.47	5.73	7.34
1y	4.23	4.03	4.51	5.88	7.63

Source: BofA Global Research

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### Exhibit 44: 3m z-scores of implied volatilities

Changes over time

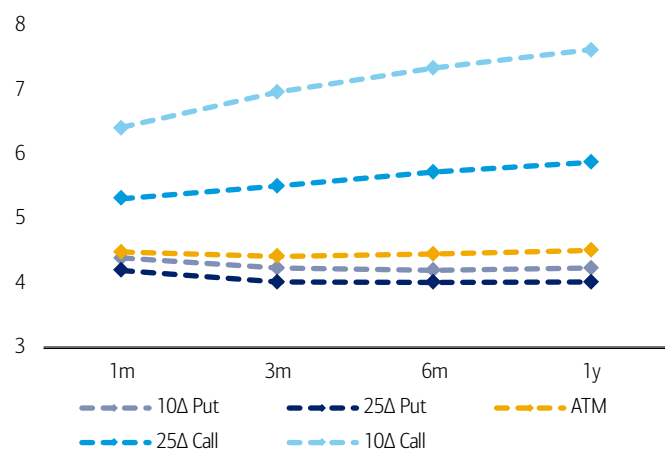
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-1.1	-1.1	-1.1	-1.0	-1.0
3m	-1.6	-1.6	-1.5	-1.4	-1.3
6m	-1.7	-1.7	-1.6	-1.5	-1.4
1y	-1.7	-1.6	-1.5	-1.4	-1.4

Source: BofA Global Research

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### Exhibit 45: Term structures of implied volatilities

Slightly upward sloping

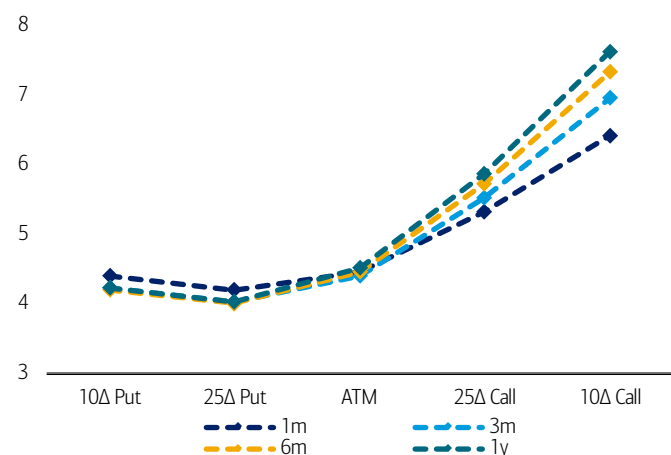


Source: BofA Global Research

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### Exhibit 46: Implied volatility smiles

Implied vol smiles are somewhat skewed



Source: BofA Global Research

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# Hungary: still bullish, positioning is a risk

**Mai Doan**

MLI (UK)

mai.doan@bofa.com

**Mikhail Liluashvili**

MLI (UK)

mikhail.liluashvili@bofa.com

## View: positioning is a key obstacle to further appreciation

The forint should be supported by an improving balance of payments position and high carry. The NBH is likely to cut only cautiously making sure that the forint does not weaken much. However, positioning is crowded and can be an obstacle to a spot appreciation in the short term.

**Key macro developments:** Hungarian assets should enjoy further support from government measures to support local demand for government bonds, though foreign investors are increasingly worried about positioning and waning carry. The macro and financing backdrop has improved significantly this year, but Hungary is not yet out of the woods as inflation remains high and the process to unlock EU funds, while on track, is demanding (disbursement likely delayed to early 2024, with government officials recently downplaying the needs for this funding). This implies the need for a continuation of very prudent policies. The NBH's first phase of the cutting cycle from May is strongly related to a stable HUF, and the second phase from the autumn to positive real rates. The government will likely stay firm on the fiscal consolidation path, as surging interest costs and a tense relationship with the EU bring tough constraints.

The NBH will likely cut the overnight deposit rate in 100bp steps to reach the base rate level at 13% by September. We expect a more gradual path when it comes to cutting the base rate from 13%. We keep our YE2023E policy rate at 11.5% and YE2024E at 6.5%. This profile reflects the NBH's preference for positive ex-ante and ex-post real rates to provide carry support for the HUF and to tame inflation.

Inflation remains elevated but there are some signs for optimism that would support the first phase of a rate normalisation path. Headline CPI will benefit from base effects, which would cut inflation by at least 1.5pp in the rest of year, with nearly 4pp in September. The goods sector should see further pass-through of lower PPI inflation to CPI inflation, particularly in non-durables where there is a big lag.

The financing backdrop is favourable. FinMin has covered 50% of the borrowing plan. The new regulation on banks and investment funds, together with the NBH's rate cuts, should promote demand for local bonds in the near term. But the longer-term outlook is not smooth sailing given a tight budget, EU funds delay, and NBH tapering from 2024.

**Valuations:** the HUF looks overvalued on BEER and FEER models, but valuation is just one of the metrics we look at

**Positioning:** investors are net long HUF and positioning is crowded

**Main risks to our view:** rising European gas prices or significant delay of EU funds

**Upcoming risk events:** NBH decision (25 Jul, 29 Aug), RRP payment request (4Q)

**Corporate hedging:** we recommend hedging vs HUF strength

### Exhibit 47: EUR/HUF forecasts vs forwards

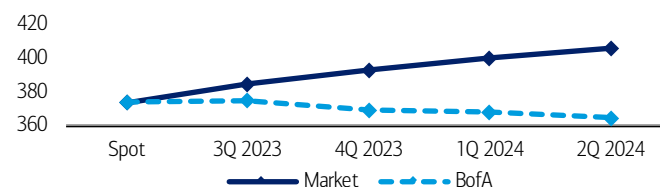
We expect EUR/HUF at 365 by the end of Q2 24

Spot	current	chg		
	373.7	+1.18		
Period	Forecast		Forward	
	current	chg	current	chg
3Q 2023	375	-	385	-1.70
4Q 2023	370	-	393	-1.93
1Q 2024	368	-	400	-2.42
2Q 2024	365	-	406	-2.99

Source: BofA Global Research, Bloomberg

### Exhibit 48: EUR/HUF forecasts

Our forecast path is below 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 -65bp

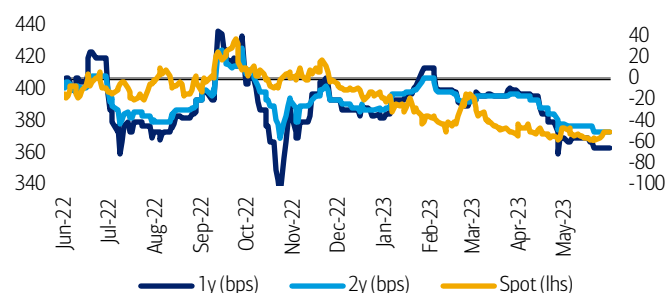
Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	-65.0	0.0	-45.0	-56.0	-110.0		45.0	-24.8	17.5	126.0	-6.9	-1.6
2y	-50.0	0.0	-29.0	-40.5	-56.0		29.0	-20.4	9.8	71.0	-7.9	-1.8
5y	-35.0	0.0	-17.0	-26.4	-35.0		8.3	-14.3	3.9	28.2	-3.4	-2.2
10y	-26.6	0.0	-6.8	-18.1	-26.6		10.5	-11.4	3.0	21.3	-2.4	-1.7

Source: BofA Global Research, Bloomberg

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

Xccy basis flat

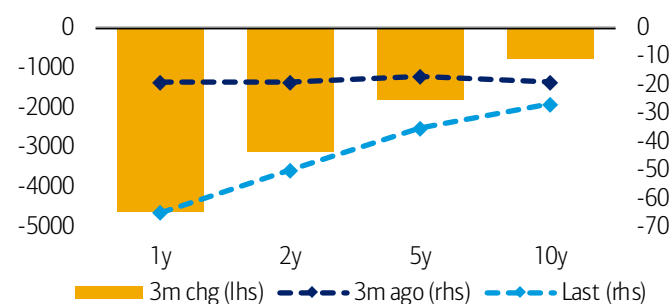


Source: BofA Global Research, Bloomberg

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### Exhibit 51: Term structure of basis swaps (bps)

Short end moving lower



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	7.17	7.07	7.77	9.37	11.29
3m	8.02	7.92	8.72	10.62	12.89
6m	8.69	8.69	9.62	11.70	14.16
1y	9.22	9.40	10.44	12.67	15.23

Source: BofA Global Research

BofA GLOBAL RESEARCH

### Exhibit 53: 3m z-scores of implied volatilities

Changes over time

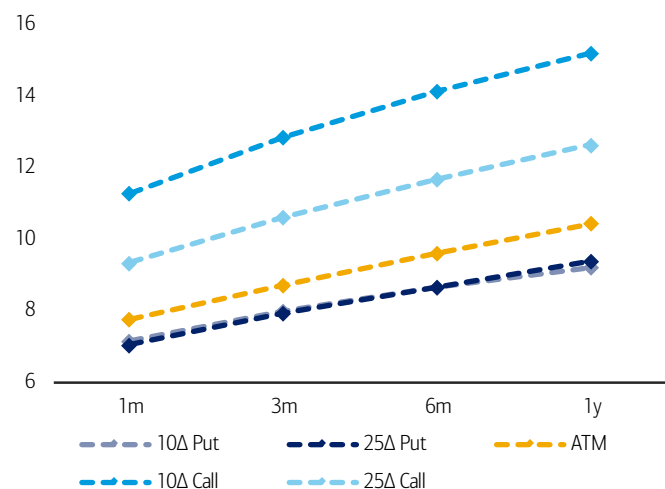
	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	-1.6	-1.6	-1.6	-1.7	-1.7
3m	-1.6	-1.6	-1.7	-1.8	-1.8
6m	-1.7	-1.6	-1.7	-1.8	-1.9
1y	-1.6	-1.6	-1.7	-1.7	-1.8

Source: BofA Global Research

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### Exhibit 54: Term structures of implied volatilities

Upward sloping

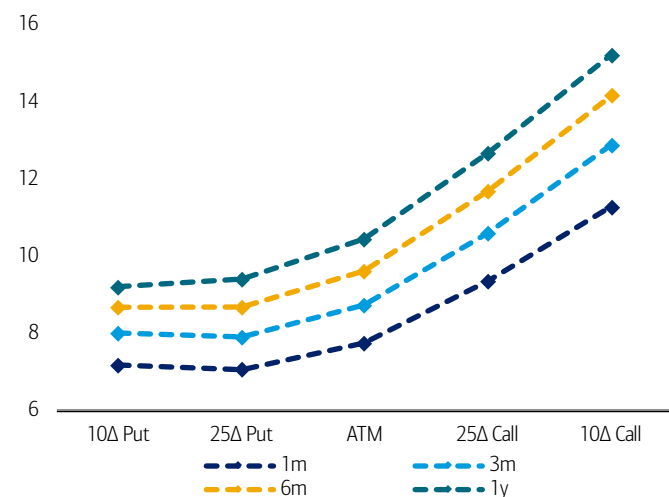


Source: BofA Global Research

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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 models: BEER & Compass

## Exhibit 56: EEMEA FX BEER model results

Majority of EM continues to be overvalued in the short term

Country	Fair Value vs. USD (*or EUR)	Spot vs USD (*or EUR)	Bilateral Misalignment (%)
			(5.0)
Czech Rep.*	23.79	23.78	0.0
Hungary*	394.64	373.45	5.4
Israel	3.36	3.60	(7.0)
Poland*	4.97	4.45	10.5
South Africa	16.55	18.18	(9.8)
Türkiye	20.48	23.68	(15.6)

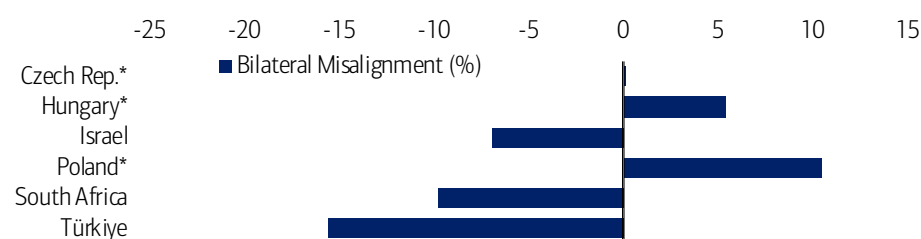
Note: Please also see Emerging Insight 'Energy shock: when BEER diverges from FEER (EEMEA FX)', 23 Oct 2022 for more info.

Source: BofA Global Research

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## Exhibit 57: Currency misalignments vs. BEER fair values

Israel, South Africa and Türkiye underweight



Note: Please also see Emerging Insight 'Energy shock: when BEER diverges from FEER (EEMEA FX)', 23 Oct 2022' for more info.

Source: BofA Global Research

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## Exhibit 58: Compass FX fair value model

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

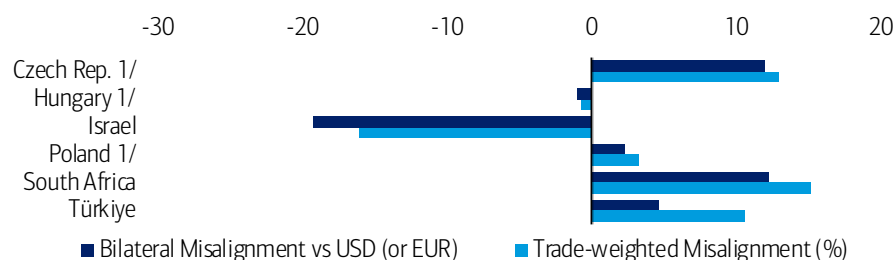
	Fair Value vs USD (or EUR)	Spot vs USD (or EUR)	Bilateral Misalignment vs USD (or EUR)	Trade- weighted Misalignment (%)
<b>EEMEA</b>			<b>3.5</b>	<b>6.9</b>
Czech Rep. 1/	27.01	23.77	12.0	13.0
Hungary 1/	370	374	(1.0)	(0.8)
Israel	3.02	3.60	(19.2)	(16.2)
Poland 1/	4.56	4.45	2.3	3.2
South Africa	20.71	18.17	12.3	15.1
Türkiye	24.83	23.68	4.6	10.6

Source: BofA Global Research. Last updated 16 Jun 2023. \*against EUR

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## Exhibit 59: Compass FX % misalignment

Israel and South Africa undervalued 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 16 Jun 2023. \*against EUR

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# EEMEA FX forecasts

## Exhibit 60: EEMEA FX forecasts

End-of-period

	Spot	3Q 2023		4Q 2023		1Q 2024		2Q 2024		3Q 2024		4Q 2024		1Q 2025	
		F'cst	Fwd	F'cst	Fwd	F'cst	Fwd	F'cst	Fwd	F'cst	Fwd	F'cst	Fwd	F'cst	Fwd
<b>EEMEA</b>															
EUR/CZK	23.8	23.8	24.0	23.50	24.2	23.4	24.3	23.3	24.3	23.2	24.4	23.0	24.5	22.9	24.5
EUR/HUF	373.7	375	385	370	393	368	400	365	406	363	411	360	416	358	419
EUR/PLN	4.45	4.65	4.49	4.55	4.53	4.51	4.57	4.48	4.61	4.44	4.64	4.40	4.67	4.38	4.70
EUR/RON	4.96	5.05	5.00	5.09	5.03	5.13	5.06	5.17	5.09	5.21	5.13	5.25	5.17	5.28	5.21
USD/AED	3.67	3.68	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.67	3.68	3.67	3.68
USD/EGP	30.9	31.0	33.1	39.0	35.5	39.5	38.0	40.0	40.2	41.0	42.2	42.0	44.3	43.0	46.4
USD/ILS	3.60	3.60	3.59	3.55	3.57	3.50	3.55	3.45	3.54	3.40	3.52	3.30	3.50	3.27	3.49
USD/KWD	0.31	0.28	0.31	0.28	0.30	0.28	0.30	0.28	0.30	0.28	0.30	0.28	0.30	0.28	0.30
USD/KZT	447	440	461	430	471	420	481	420	491	420	503	420	515	420	530
USD/NGN	657	660	666	670	677	680	688	700	698	700	709	700	720	700	731
USD/QAR	3.65	3.64	3.65	3.64	3.66	3.64	3.66	3.64	3.67	3.64	3.67	3.64	3.68	3.64	3.68
USD/SAR	3.75	3.75	3.76	3.75	3.76	3.75	3.76	3.75	3.76	3.75	3.76	3.75	3.77	3.75	3.77
USD/TRY	23.66	25.0	25.7	26.0	27.8	27.0	29.9	28.5	32.1	29.5	34.4	30.5	36.7	31.0	39.3
USD/UAH	36.9	40.0	36.9	40.0	36.9	40.0	36.9	40.0	36.9	40.0	36.9	40.0	36.9	40.0	36.9
USD/ZAR	18.2	19.0	18.4	18.0	18.5	17.6	18.7	17.5	18.9	17.0	19.1	17.5	19.3	17.8	19.5

Source: BofA Global Research, Bloomberg

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## Research Analysts

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**David Hauner, CFA** >>  
EEMEA Cross Asset Strategist  
MLI (UK)  
[david.hauner@bofa.com](mailto:david.hauner@bofa.com)

**Mikhail Liluashvili**  
EEMEA Local Markets Strategist  
MLI (UK)  
[mikhail.liluashvili@bofa.com](mailto:mikhail.liluashvili@bofa.com)

**Mai Doan**  
CEE/Israel Economist/Strategy  
MLI (UK)  
[mai.doan@bofa.com](mailto:mai.doan@bofa.com)

**Zumrut Imamoglu**  
Turkey & Israel Economist  
MLI (UK)  
[zumrut.imamoglu@bofa.com](mailto:zumrut.imamoglu@bofa.com)

**Tatonga Rusike**  
Sub-Saharan Africa Economist  
MLI (UK)  
[tatonga.rusike@bofa.com](mailto:tatonga.rusike@bofa.com)

**Vladimir Osakovskiy** >>  
EEMEA Macro/Equity Strategist  
Merrill Lynch (DIFC)  
[vladimir.osakovskiy@bofa.com](mailto:vladimir.osakovskiy@bofa.com)

**Jean-Michel Saliba**  
MENA Economist/Strategist  
MLI (UK)  
[jean-michel.saliba@bofa.com](mailto:jean-michel.saliba@bofa.com)

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