



argued that the positive effects from a weaker exchange rate on the economy were outweighing negative effects on demand. Combined with global disinflation, the Czech Republic's large negative output gap continues to advocate further policy easing, with the CNB's focus in turn likely to remain on ways of making policy more expansive.

Meanwhile global disinflation is complicating the policy outlook in much of the rest of EMEA FX. In Israel, Poland and Turkey output gaps are largely non-existent, with domestic credit growth and/or house prices edging higher. In these markets, further rate reductions would not necessarily support demand since the slowdown was/is due to weak sentiment and a poor external environment. Moreover, more rate cuts could also fuel further inflows into the domestic bond market, with foreigners already increasingly long local rates.

Here central banks are instead drawn into a growing dilemma: reduce rates and risk adding to domestic imbalances/'pockets' of domestic overheating, or 'accept' that slow growth is primarily due to a poor external backdrop something monetary policy is not equipped to address.

The FX implication: In real terms, we think it is all but inevitable that these currencies will appreciate. What monetary authorities can do is to decide if most of that appreciation will come through nominal appreciation or higher domestic inflation. We maintain long core views in ILS, PLN and TRY.

**Trades:**

Buy a 3m EURHUF call with strike at 300 and KO at 320 for 55bps. Spot ref 293.60. Vanilla 3m call at 300 costs 1.50%.

Buy a 3m USD/TRY put, with a strike 1.79 for 0.46% of notional. Spot ref 1.81.

Maintain short USD/ILS. We are long a 3m USD/ILS put with a strike at 3.50 for 0.17% (spot ref: 3.68) from the EMEA Daily Compass on March 11-. Little to prevent further grind lower to 2011 lows around 3.40, stop @ 3.73.

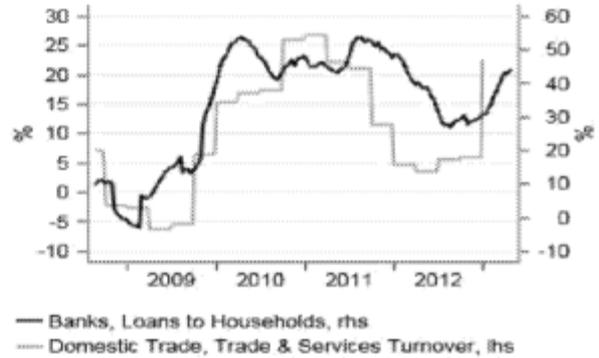
Target a continued gradual grind higher in PLN/CZK. Target 6.400, stop @ 6.10.

Buy a 3m USD/ZAR call with a 9.20 strike and KO at 9.65 for 32bps. Spot ref 9.12. Vanilla 3m call at 300 costs 2.76%.

[Risks: Maximum loss for long option trades is the premium; risks detailed in FX Blueprint report]

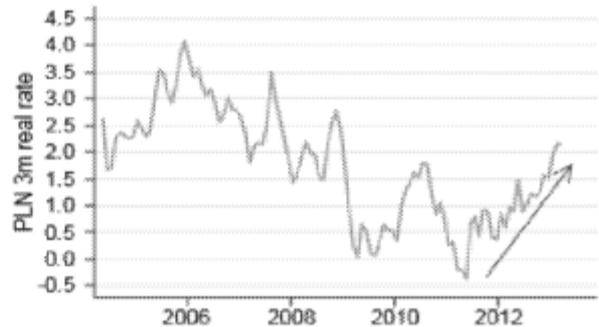
Henrik Gullberg, London, [REDACTED]

Figure 4: Turkey, credit leading domestic demand higher again.



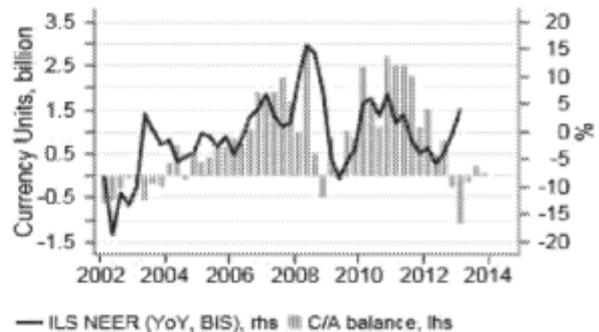
Source: Deutsche Bank

Figure 5: NBP are cutting, but real rates are PLN supportive.



Source: Deutsche Bank

Figure 6: ILS rallying ahead of C/A improvement



Source: Deutsche Bank