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Comment on the upcoming data and forecasts

Lazy week ahead of us. The only important release will be the Friday's current account. In result of mere debt payments and stable net transfers we expect a surplus to amount to 163m EUR (consensus: -230). Exports and imports are likely to decrease driven by seasonal factors. We forecast that the exports totaled to 12800m EUR, whereas the imports to 12150m EUR (consensus: 12478m and 12150m, respectively).

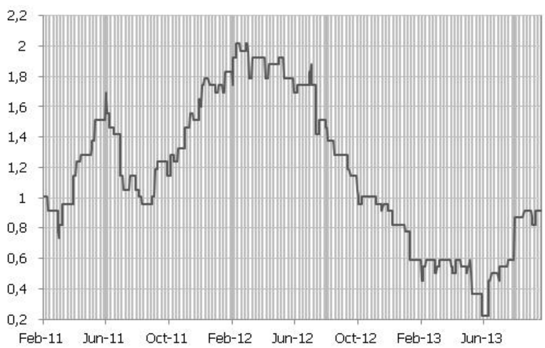
Polish data to watch: September 23th to 27th

Publication	Date	Period	BRE	Consensus	Prior
Exports (m EUR)	11.10	Sep	12800	12478	12952
Imports (m EUR)	11.10	Sep	12150	12150	12659
Current account (m EUR)	11.10	Sep	163.0	-229.9	-178.0

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Yield on the prev auction (%)	Prev auction
52 Week T-bills	-	3000	3.485	3/4/2013
2Y T-bond OK0116	-	5000	2.961	9/5/2013
5Y T-bond PS0718	-	3500	3.819	10/3/2013
10Y T-bond DS1023	-	3000	3.290	5/16/2013
20Y T-bond WS0429	-	150	3.464	5/16/2013

Reality vs analysts' expectations (surprise index* for Poland)



Comment

Unchanged as positive surprise in PMI index was not big enough and did not move the index (more in the Economics section). As current account data are too volatile and subject to revision, the index will remain on hold until real sphere data are released after 14th October.

* Surprise index presents in a synthetic way how the market was surprised by macroeconomic releases (it is constructed on daily basis as weighted average of differences between selected releases and Bloomberg forecast consensus).

Our view in a nutshell

Fundamentals

- Available data confirm that the long-awaited recovery began at the turn of Q2/Q3.
- The upswing is driven by a rebound in real income and recovering private consumption. Low rates trigger rotation in households assets towards overnight deposits. Given the scale of slack in investment (infrastructure in particular) and consumption, rebound generated this way may be initially moderate as measured by historical standards. Better business activity in the euro zone is going to strenghten the upswing trajectory, but we do not believe it is crucial for recovery to come at all.
- H2 is going to be substantially better than H1. Q3 already close to 1.5% and the possibility of exceeding 2% in Q4 monotonically rises. Such a growth is higher than current market consensus dominated by rather gloomy visions.
- Polish government committed to the convergence path, though in a very unorthodox and elastic way. The European Commission gave the government two additional years to bring the GG deficit down to 3%, and a budget amendment (at PLN +16 bn) was just passed. Furthermore, additional boost to public finances comes from the pension reform. This - along with the political cycle - opens room for fiscal stimulation. Formal acceptance of the EC (and overal trend of consolidation's fatigue) suggests the market should digest this information easily.
- We witnessed the steepest disinflation phase in Polish history. 0.2% inflation growth was the lowest in the cycle. Although inflation stays subdued, a new uptrend has began. We expect 1.5% by the end of the year and inflation target is going to be reached in mid 2014.
- Rebound in growth and inflation practically erases easing bias in MPC, as rates have been pun on hold at least until end-2013. We expect first rate hikes to materialize in late 2014 and think that NBP projections of both GDP and inflation for 2014 are be too pessimistic.

Financial markets

- Short term it is wise to stay constructive on Polish bonds due to (temporary) global reinstalation of QE-induced carry trades. However, unleashed volatility suggest the potential gains are rather limited which is consistent with the amount of risk foreign investors wish to hold in current circumstances.
- In the mid term Polish Local factors including economic upturn and liquidation of OFE assets suggest higher liquidity risk premium on Polish bonds. Global recovery and rising core yields will additionally adversely affect Polish bonds.
- Zloty capped by risk of NBP FX intervention. It should gradually strenghten on the back of cyclical recovery in Poland.

BRE forecasts

	2009	2010	2011	2012	2013F	2014F
GDP y/y (%)	1.6	3.9	4.5	1.9	1.3	3.2
CPI Inflation y/y (average %)	3.5	2.8	4.3	3.7	1.1	2.2
Current account (%GDP)	-1.6	-4.5	-4.9	-3.5	-1.9	-2.6
Unemployment rate (end of period %)	12.1	12.4	12.5	13.4	13.5	13.5
Repo rate (end of period %)	3.50	3.50	4.50	4.25	2.50	3.00

	2013 Q1	2013 Q2	2013 Q3 F	2013 Q4 F	2014 Q1 F	2014 Q2 F	2014 Q3 F	2014 Q4 F
GDP y/y (%)	0.5	0.8	1.6	2.1	2.6	3.0	3.4	3.7
Individual consumption y/y (%)	0.0	0.2	1.2	1.9	2.2	2.3	2.3	2.4
Public Consumption y/y (%)	-0.5	3.9	3.0	2.0	0.3	0.3	0.3	0.3
Investment y/y (%)	-2.0	-3.8	-1.0	1.0	1.5	2.5	3.5	4.5
Inflation rate (% average)	1.3	0.5	1.1	1.3	1.8	2.2	2.4	2.5
Unemployment rate (% eop)	14.3	13.2	13.0	13.5	13.9	12.7	12.5	12.9
NBP repo rate (% eop)	3.25	2.75	2.50	2.50	2.50	2.50	2.50	3.00
Wibor 3M (% eop)	3.39	2.73	2.70	2.70	2.70	2.70	2.70	3.20
2Y Polish bond yields (% eop)	3.19	3.07	3.10	3.20	3.30	3.30	3.30	3.30
10Y Polish bond yields (% eop)	3.94	4.34	4.80	5.00	5.00	5.10	5.20	5.50
EUR/PLN (eop)	4.18	4.33	4.20	4.10	4.05	3.95	3.90	3.90
USD/PLN (eop)	3.26	3.32	3.13	3.08	3.11	3.15	3.20	3.25
F - forecast								

Economics

The first week of October brought us surprisingly strong PMI release, a further sign of a forthcoming recovery in Polish economy. The surprise was mainly due to unexpected increase in employment, which indicates a brighter future for polish labour market. Wednesday's MPC meeting was a non-event. Everything went according to the plan, as rates remained unchanged and a quasi-forward guidance was maintained. Our baseline scenario (accelerating growth and stable interest rates) is materializing itself.

MPC's decision - rates unchanged. How to handle two-month-long forward guidance?

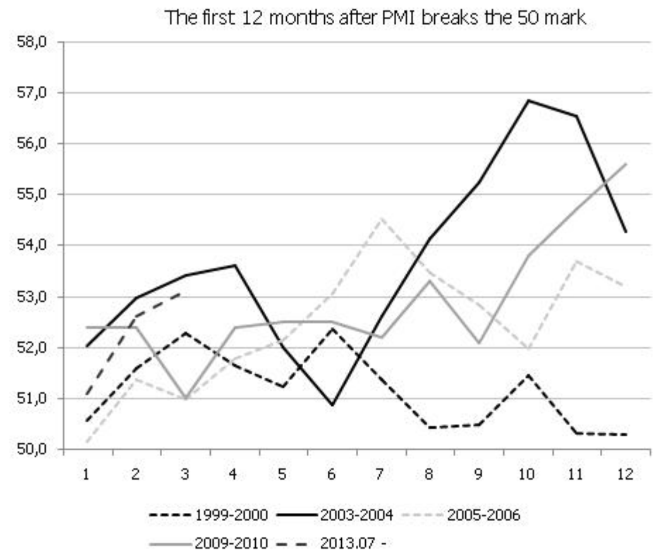
Both the decision and the official statement were non-events. The rate remain unchanged at 2.5% and the MPC maintained its forward guidance (i.e. a clue for what path of future interest rates one should expect). In the statement the committee stressed that the view on global economy is becoming increasingly optimistic noticing also a first signs of an upswing in the Polish economy. During the press conference Governor Belka expressed his opinion that he expects a gradual recovery of a mediocre pace. It was also confirmed that the inflationary pressures remain subdued.

Governor Belka didn't comment on a speculation of extending forward guidance. However, he stressed that he himself as well as some other MPC members share the opinion that the rates should remain unchanged till the second half of 2014. Overall impression of the statement is rather dovish. Belka indicated that the forward guidance can be adjusted after November inflation projection. Interestingly, the Economic Institute has recently conducted a course on forward guidance that aimed to explain this tool to the MPC members. This could indicate that the MPC is still reconsidering whether such a policy is appropriate in the present environment and in Poland's situation. Most likely the MPC will extend the forward guidance to the second half of 2014 as to actually shape rate expectations (current wording is utterly impotent in this regard) or will back out of this policy in a subtle way.

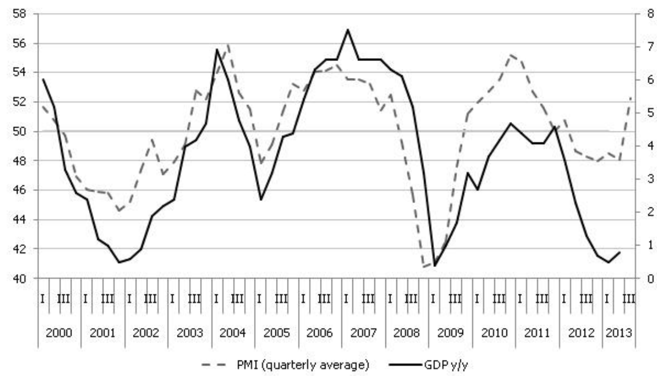
The dovish words of Governor Belka moved the market rates down a few bps. In our view NBP's analysts will be positively surprised by the dynamics of forthcoming recovery in Poland. We forecast annual GDP growth rate to amounts to 3.1% in 2014. Additionally, we expect the CPI to accelerate and reach the inflation target in the first half of 2014. In effect, the markets can start pricing in aggressive rate hikes, as it was the case in the past in similar circumstances. We think that the MPC may delay the rate hikes until the second half of 2014 in order to avoid adverse effects of premature policy tightening. Having said that, we recommend to set up PAY positions at the turn of the year.

September PMI surprises on the positive side - but only because of employment

In September Polish manufacturing PMI increased to 53.1 pts. from 52.6 in last month. Both the consensus and our forecast were rather conservative (52.3 and 52.4 respectively) as a result of a slight decrease of its European counterparts. Nevertheless after the first three months of the recovery the PMI is on impressive levels, even in comparison with relatively good period of 2009 and 2010 (see graph below).



Abovementioned negative external factors are mirrored in the slight decrease of production subindex (a fall from 56.6 to 55.8) and a decelerating growth rate of the new orders. The above-consensus-reading results from unexpectedly dynamic growth in the employment subindex, which reached the highest level since 2007. It confirms the beginning of an uptrend in the labour market and suggests a positive y/y growth rate of employment as soon as at the end of current year. Those developments support our optimistic view on the strength of the Polish labour market.



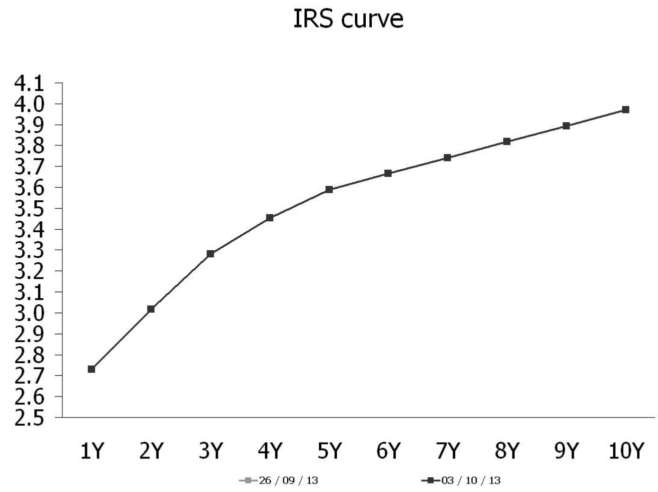
In Q3 PMI have averaged to 52.3 pts. vs. 48.1 pts. noted between April and June. Having in mind that there is no straightforward relation between PMI and GDP growth, the recent high levels of the former indicate, however, that current consensus underestimates the GDP growth rate in Q3. According to our estimates yearly dynamics in Q3 is likely to exceed 1.5%.

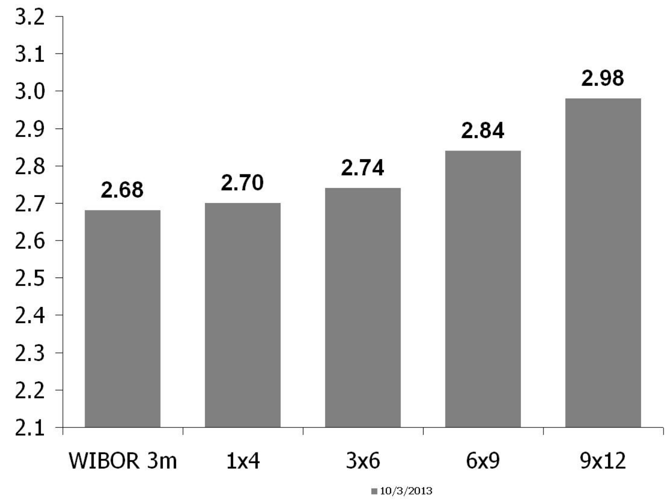
Fixed income

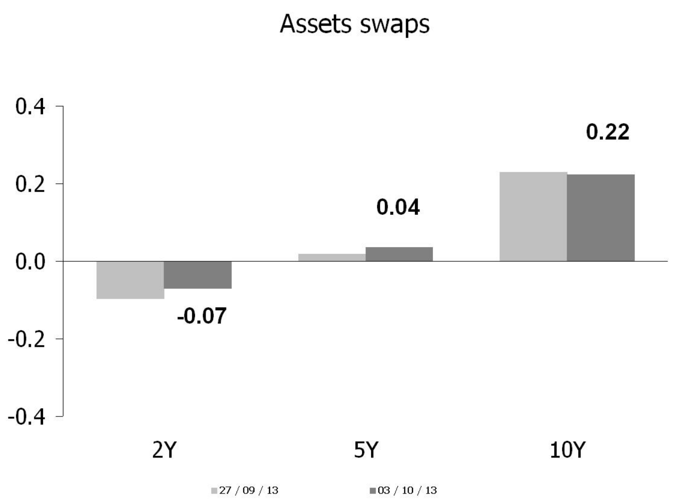
Waiting for the outcome of the US budget conflict

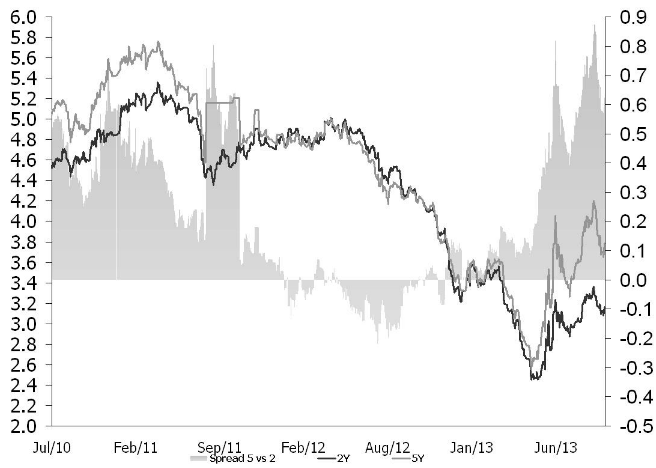
Market is stuck waiting for the results of U.S. budget conflict. Outcome of current negotiations will definetly determine the direction in which financial markets will follow. To be honest, at current levels we do not see clear value in 5-10 year tenors. Possible result creates one-off scenario either of ways with equal payoff, by our judgement. So, spending cuts or not - the choice is yours.

But we still see value in buying 2-3Y bonds which provide decent carry (about 70-80 bps) and with such value stay in the range of interests of local banks. On the other hand, we believe (and hope) that economic revival is inevitable and we see opportunity in paying IRS forwards - 1Y1Y and 2Y2Y especially. Both trade ideas combined create a hedge portfolio with likely positive payoff.





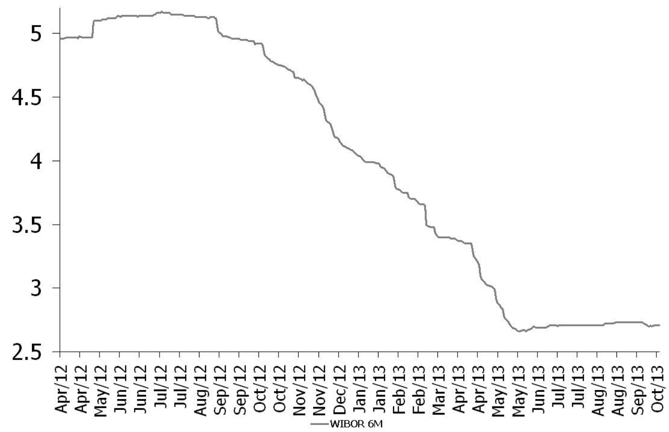


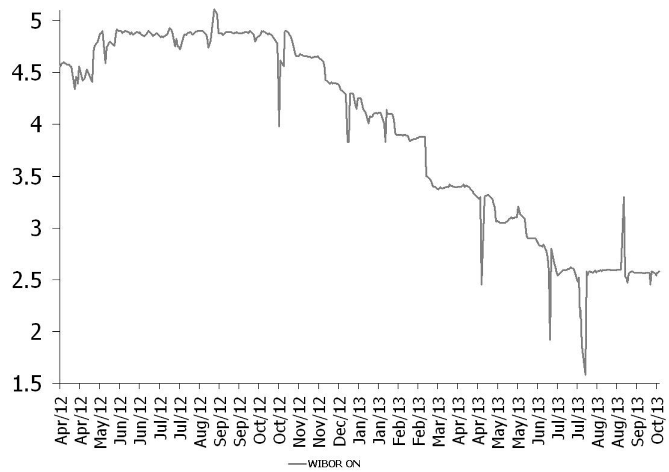


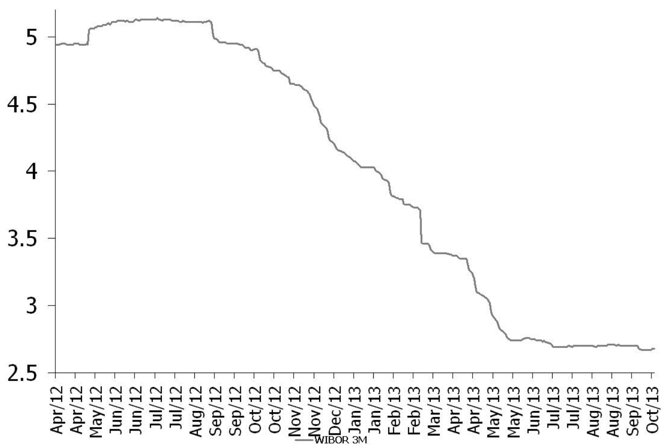
Money market

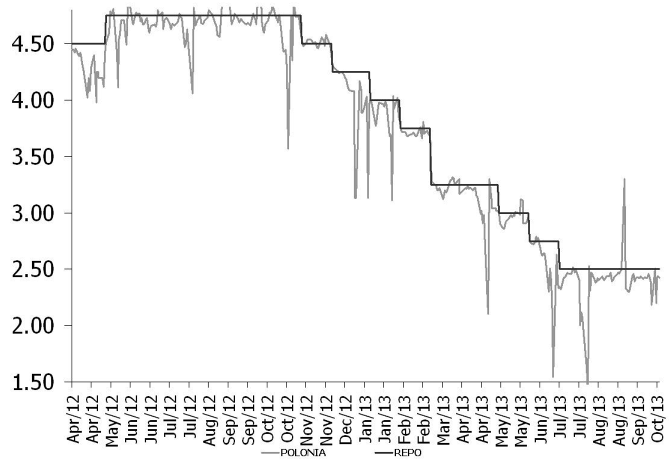
Relatively expensive week ahead Easy end of the reserve settlement period with short term drop of CoC at the beginning of the new one. It was however sterilised by the extra OMO operation (we were betting on no operation due to the beginning of the period) bringing back shortest rates to the main rate level. Today's OMO was well overbid even though the offer was larger then expected to square the market. This should imply a relatively expensive week.

No local data, US on constant watch On hold on longer rates waiting for any driver. We follow the US government shutdown and debt ceiling debate for possible information, since no local market data is being published next week.









Forex

PLN tic stronger On Monday 30th of September we were expecting the PLN buying from the government agent, because of so called „Farmer Fixing". Last year it was an event, and PLN got stronger roughly 9 figures in 2 days, this year it was not a case. The government flow was seen only occasionally and never in size. The EUR/PLN was moving in really tight range 4.1950/4.2400, and PLN eventually drifted to tic stronger levels. The weak USD is generally helping the ZĹ‚oty appreciation trend, and US problems are not really a reason for a global risk off. At least not yet.

Volslower The PLN is only marginally stronger. But the falling realized volatility was the main reason why the EUR/PLN vols and the frontend in particular was so much offered. The 1 month ATM EUR/PLN fixed today at 7.5% (0.6% lower than last Friday), 3 months are 7.8% (0.4% lower), and 1 year is lower only by 0.2% to 8.9%. The Skew was also tic better offered and the currency spread was neutral.

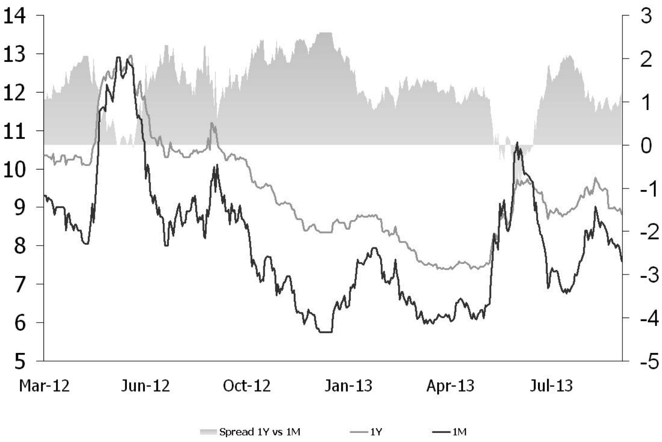
Short-term forecasts

SPOT Main supports / resistances:
EUR/PLN: 4.1900 / 4.2400
USD/PLN: 3.0500 / 3.3000

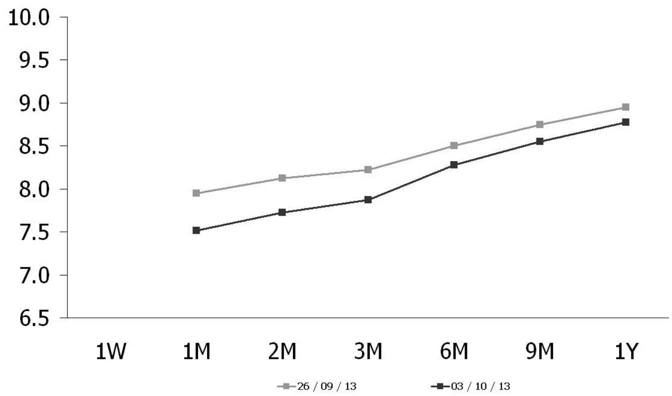
Short EUR/PLN We are still short EUR/PLN 4.2300 but we are moving stop down to 4.2400 and we still hope for a retest of 4.1450 low. The price action is a bit disappointing, but we see no reason to change this view as of yet. The PLN is appreciating gently. The USD weakening trend is positive for PLN. The momentum is clearly not there, but because the stop is relatively close, we stick to the position.

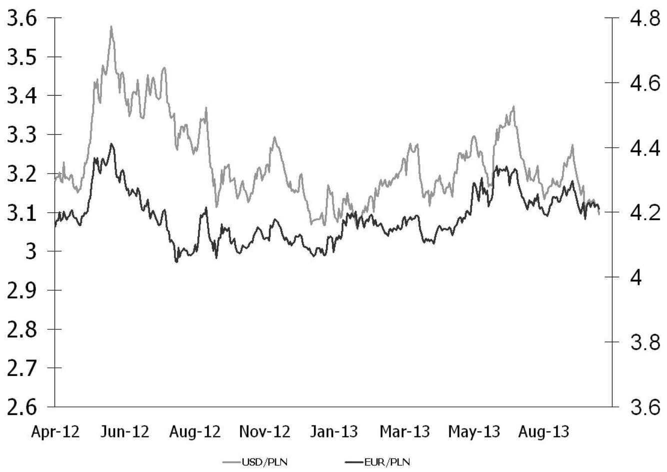
Derivatives The volatility is sharply lower on the FOMC news, with the big risk for PLN postponed for the time being. We don't see a lot of value in the EUR/PLN vol curve at the moment. We see the wild swings in spot but that's a post FOMC shock, but we will most likely be back soon to low realized volatility. The short term (up to 4 months) EUR/PLN is still rather a sell, but to a smaller degree then last week. Similar situation with the skew and currency spread.

EURPLN volatility



EUR/PLN volatility curve





Bias from the old parity (%)

Market prices update

Money market rates (mid close)								FRA rates (mid close)				
Date	FXSW 3M	WIBOR 3M	FXSW 6M	WIBOR 6M	FXSW 1Y	WIBOR 1Y	1x4	3x6	6x9	9x12	12x15	6x12
9/27/2013	2.29	2.67	2.44	2.60	2.74	2.65	2.69	2.75	2.85	2.99	3.19	2.98
9/30/2013	2.29	2.67	2.43	2.61	2.74	2.65	2.72	2.75	2.84	2.99	3.16	2.95
10/1/2013	2.28	2.67	2.45	2.61	2.74	2.65	2.72	2.76	2.85	2.98	3.16	2.96
10/2/2013	2.30	2.68	2.46	2.61	2.76	2.65	2.71	2.75	2.83	2.97	3.15	2.94
10/3/2013	2.37	2.68	2.48	2.61	2.62	2.65	2.70	2.74	2.84	2.98	3.17	2.95

Last primary market rates							
Paper	Au. date	Maturity	Avg. price	Avg. yield	Supply	Demand	Sold
52W TB	5/30/2011	5/30/2012	95.57	4.58	600	2667	505
OK0114	8/10/2011	1/25/2013	89.58	4.58	5000	4934	1889
PS1016	10/19/2011	10/25/2016	98.44	5.11	3600	11200	3638
DS1021	7/21/2011	10/25/2021	99.53	5.80	3000	5608	3000

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0715	5Y IRS	PS0718	10Y IRS	DS1023
9/27/2013	2.650	2.809	3.163	3.066	3.785	3.804	4.190	4.420
9/30/2013	2.650	2.825	3.158	3.067	3.780	3.877	4.185	4.495
10/1/2013	2.650	2.847	3.155	3.057	3.775	3.876	4.185	4.449
10/2/2013	2.650	2.779	3.133	3.050	3.741	3.790	4.146	4.416
10/3/2013	2.650	2.677	3.140	3.070	3.780	3.816	4.190	4.414

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY
Date	1M	3M	6M	1Y	1M	1Y	1Y
9/27/2013	8.04	8.23	8.49	8.91	8.91	2.91	0.78
9/30/2013	8.00	8.23	8.48	8.93	8.93	2.91	0.78
10/1/2013	7.88	8.08	8.43	8.98	8.98	2.86	0.80
10/2/2013	7.60	7.88	8.28	8.81	8.81	2.82	0.75
10/3/2013	7.51	7.88	8.28	8.78	8.78	2.87	0.76

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
9/27/2013	4.2310	3.1328	3.4506	3.1758	1.4107	0.1649
9/30/2013	4.2163	3.1227	3.4500	3.1905	1.4129	0.1641
10/1/2013	4.2230	3.1170	3.4512	3.1800	1.4248	0.1642
10/2/2013	4.2231	3.1212	3.4488	3.2067	1.4217	0.1647
10/3/2013	4.2105	3.0951	3.4310	3.1647	1.4224	0.1646

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