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## Polish Weekly Review

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### Table of contents

#### Our view in a nutshell

#### Economics

- Polish GDP soft patch is real

#### Fixed income

- Steepener

#### Money market

- Spillovers

#### FX market

- Spot – PLN is on fire
- Options – EUR/PLN vols – gapped higher

page 2

page 3

page 4

page 5

page 6

### Comment on the upcoming data and forecasts

Week starts on Monday with CSO's real sphere data. Unfavorable working days difference and base effects imply that industrial production fell slightly on a yearly basis in October. When it comes to construction-assembly production we see a slight upward move of yearly index, which is a result of low base and working days effect. Producer prices yearly dynamics should also rise insignificantly driven by higher coke prices. Retail sales seems to be the only bright spot among other releases. We expect strong figure based on rebound in durable goods category as well as cold and wet October being a driving force for clothing sales. Thursday's Minutes would pass almost unnoticed. Week ends on Friday with release of CSO's Statistical Bulletin. It would contain details of November's publication with composition of Polish GDP for Q3. According to preliminary MFLSP estimates, unemployment rate fell further in October, however we still see a risk of higher figure based on lagged effect of economic slowdown in sectors vulnerable to seasonal effects.

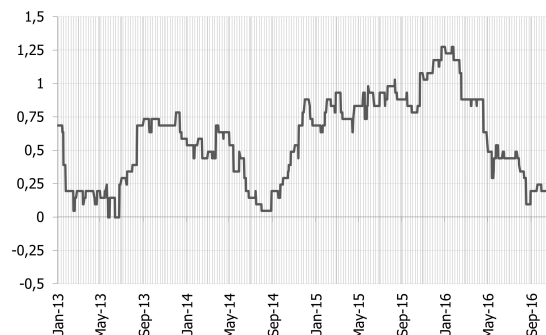
### Polish data to watch: November 21th to November 25th

Publication	Date	Period	mBank	Consensus	Prior
Industrial production y/y (%)	21.11	Oct	-0.1	1.1	3.2
Construction production y/y (%)	21.11	Oct	-14.7	-15.8	-15.3
PPI y/y (%)	21.11	Oct	0.3	0.4	0.2
Retail sales y/y (%)	21.11	Oct	5.4	4.1	4.8
MPC Minutes	24.11	Nov			
Unemployment rate (%)	25.11	Oct	8.3	8.2	8.3

### Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Yield on the prev auction (%)	Prev auction
(32/37/52) Week T-bills	-	1500	1.350	3/14/2016
2Y T-bond OK1018	12/15/2016	2000	1.742	10/6/2016
5Y T-bond PS0722	-	4000	2.499	11/17/2016
10Y T-bond DS0727	12/15/2016	4000	3.098	10/6/2016
15Y T-bond WS0428	-	200	3.027	7/7/2016

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



#### Comment

Polish manufacturing PMI staggered markets coming well below market consensus. Surprise index moved down by a few points, and we see it at current levels throughout the next week, since the MPC will not change rates.

\* 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

- 500+ programme is set to support private consumption in 2016. Despite weak Zloty, exports growth ground into a halt. Public infrastructure outlays have shifted towards 2017, and private investment seems to be locally, negatively affected by spillovers from public investment gap, lower absorption of EU funds and political uncertainty. Hence, we expect 2-3 quarters of sub-3% growth.
- Current GDP growth is sufficient to keep inflation and credit risk in check. Globally, low to moderate growth amid low commodity prices is set to further underpin deflationary environment. Headline inflation is going to slowly rise only on the back of statistical base.
- Rate cuts are still a possibility (but MPC is very unwilling to ease and global trend is for tightening). We expect the MPC to finally acknowledge downside risks for Polish GDP growth.

### Financial markets

- Global reflation trades weakened the Zloty by raising risk-free rates and encouraging capital outflows from EM assets. Due to the weakness in exports and country risks still present, we expect Zloty to remain weak for the time being.
- The prevailing event risk for PL assets, the CHF conversion, moved to the background, as its details are unlikely to be announced soon.
- Stronger dollar and upcoming Fed hike (December) hold in check any strengthening of Polish zloty.

### mBank forecasts

	2012	2013	2014	2015	2016 F	2017 F
GDP y/y (%)	1.6	1.4	3.3	3.9	2.7	3.2
CPI Inflation y/y (average %)	3.7	0.9	-0.1	-0.9	-0.6	1.3
Current account (%GDP)	-3.7	-1.3	-2.0	-0.1	-0.7	-0.9
Unemployment rate (end of period %)	13.4	13.4	11.4	9.8	8.7	8.1
Repo rate (end of period %)	4.25	2.50	2.00	1.50	1.50	1.25

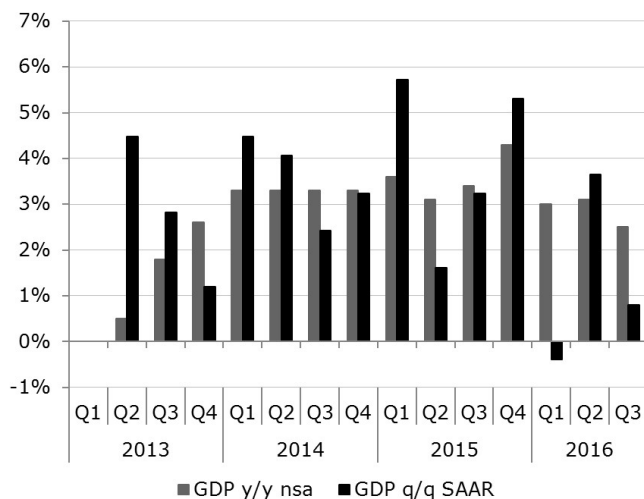
	2016	2016	2016	2016	2017	2017	2017	2017
	Q1	Q2	Q3 F	Q4 F	Q1 F	Q2 F	Q3 F	Q4 F
GDP y/y (%)	3.0	3.1	2.5	2.0	2.8	3.1	3.4	3.5
Individual consumption y/y (%)	3.2	3.3	3.8	4.6	4.6	4.0	3.8	3.5
Public Consumption y/y (%)	4.4	4.4	4.0	2.0	3.6	3.5	2.4	2.4
Investment y/y (%)	-1.8	-4.9	-6.5	-3.0	0.0	3.5	6.0	6.0
Inflation rate (% average)	-0.9	-0.9	-0.8	0.2	1.3	1.4	1.2	1.1
Unemployment rate (% eop)	9.9	8.7	8.3	8.7	8.9	8.2	7.8	8.1
NBP repo rate (% eop)	1.50	1.50	1.50	1.50	1.25	1.25	1.25	1.25
Wibor 3M (% eop)	1.67	1.71	1.71	1.71	1.44	1.44	1.44	1.44
2Y Polish bond yields (% eop)	1.45	1.65	1.76	1.80	1.70	1.60	1.60	1.70
10Y Polish bond yields (% eop)	2.84	2.91	2.92	3.60	3.50	3.40	3.50	3.50
EUR/PLN (eop)	4.24	4.38	4.30	4.50	4.45	4.35	4.25	4.25
USD/PLN (eop)	3.73	3.94	3.82	4.21	4.20	4.14	4.05	4.05

F - forecast

## Economics

### Polish GDP soft patch is real

According to the flash estimate, Polish GDP rose in third quarter only by 2.5% y/y, while quarterly dynamics fell to sluggish 0.2%. Given market consensus (2.9%) and even our more down to earth forecast (2.7%), those number are undeniably a disappointment. We still need to wait till next Friday for final composition, nevertheless we expect that consumption rose by 4% y/y, investment fell by 6-7% yearly what net exports had not significant impact.



As we have heralded for long, economic growth pace is slowing more abruptly than analysts expected. We think that even if rebound in EU funds-based investment will be enough to put growth back above the 3% threshold in H2 2017, global environment still poses a threat. Deflationary environment and low growth in Europe could negatively affect Polish exports, while possible escalation of EM problems would be problematic for exports diversification outside EU. We do not see any inflationary pressure in medium term, thus rate hikes in Poland are definitely off the table for a long period of time.

Today's negative surprise could also influence economic sentiment among enterprises and put an end to overoptimistic MPC comments about state of Polish economy, eventually resulting in much more dovish statements. We have already seen first reactions, some members already acknowledged possible need for discussion about rate hikes (Zyzynski) or do not exclude possible monetary easing (Hardt's "never say never"). When it comes to next few quarters, we do not see significant rebound in GDP growth (expect sub 3% GDP reading in Q4 2016 and Q1 2017). This was already noted by the government, deputy PM Morawiecki expects EU fund-based investment to start even on the turn of first and second quarter of 2017.

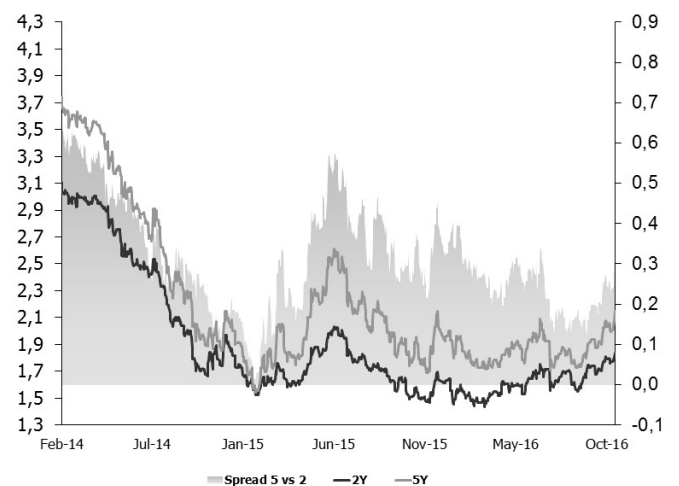
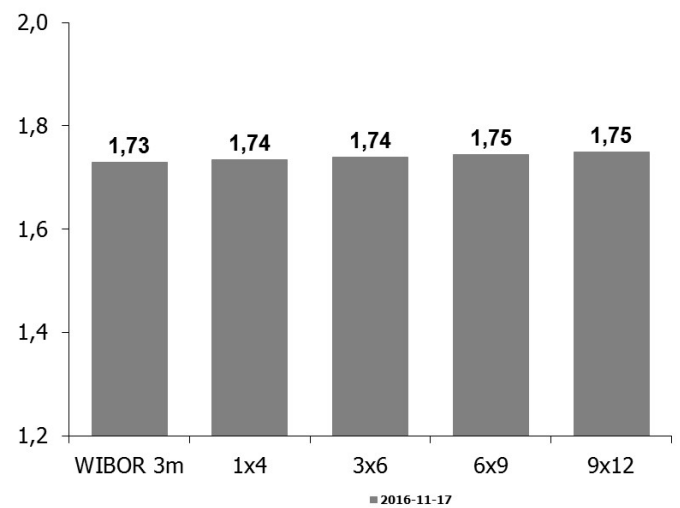
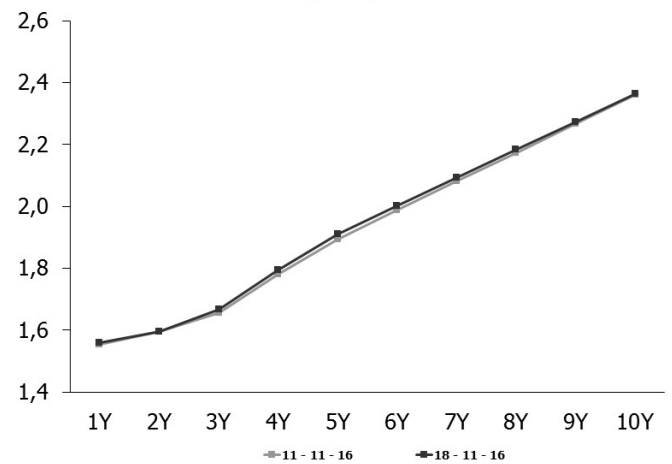
## Fixed income

### Steepener

Ministry of Finance sold PS0422 2.9 bio, WZ0122 0.3bio, WZ0126 0.46 bio this week. We saw uncovered demand on floater. After the auction market was too heavy and sell flow put bond prices down. Spread PS0721 / DS0726 moved to record level at from 60/58 to 72/70bps. DS0726/DS0727 spread stuck at 7/6. Since last Thursdays we have global sell off bonds. DS0726 jumped from 3.15% to 3.65% and PS0721 from 2.67% to 2.90%. ASW currently are wider PS0721 / 5y 46/44.

Latest Polish GDP figure (2.5% y/y) confirmed no chance to rate hike in 2017. Next primary auction will be ca 15th of December.

IRS curve



## Money market

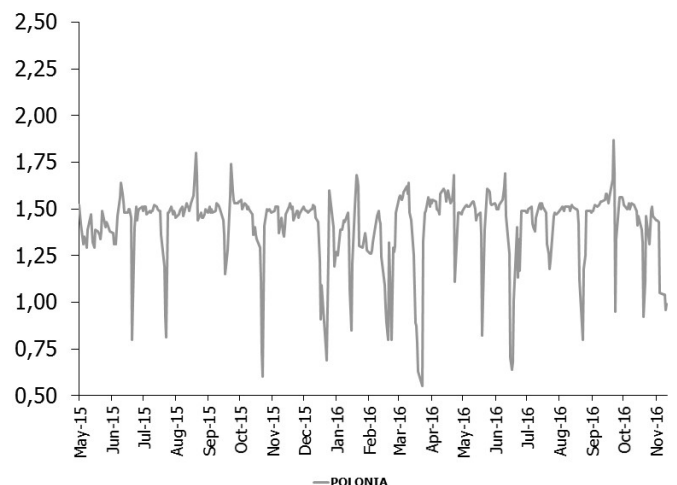
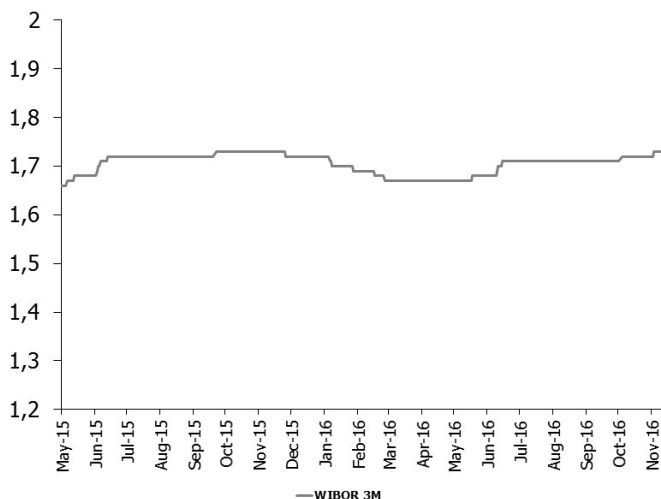
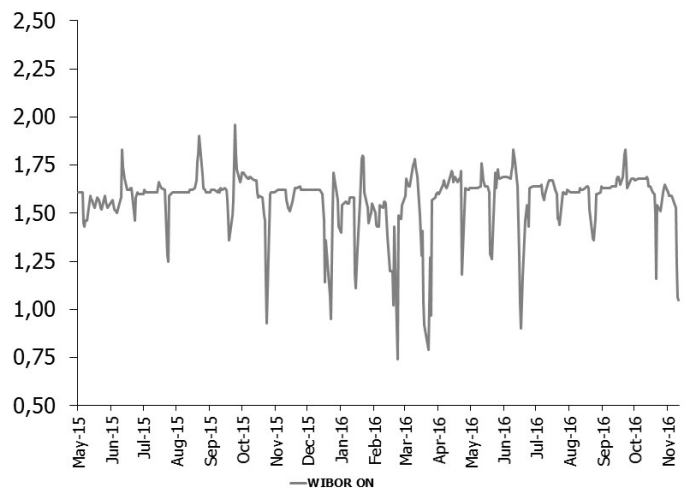
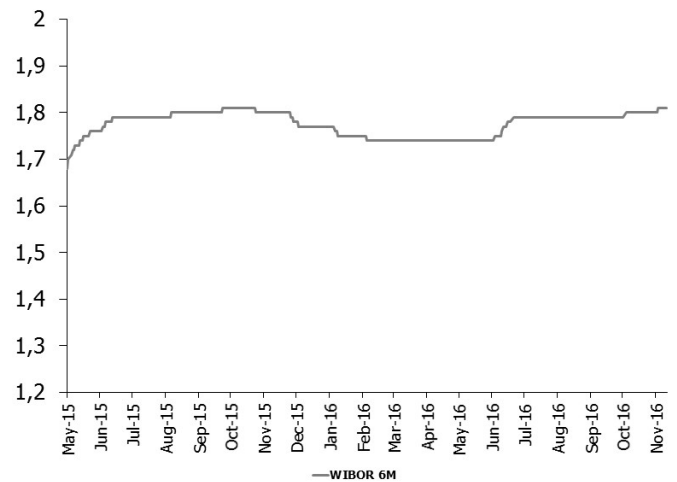
### Spillovers

Armageddon came through bond markets across the world and POLGBs were not spared. Volatility not seen in many months took us to 3.70% on DS0726. Bond curve steepened massively as short end was shielded by weak Q3 GDP print and banking tax related demand. When the dust settles market players may remind themselves about weak economic data (GDP, PMI, CPI) and revive rate cut expectations.

Overnight rates have been very low for the whole week. We would blame a long 8-day OMO as well as "panic" on the bond market which have caused liquidity desks to take safe stance.

Ref rate vs Polonia averages:

30 day: 18 bp (+12)  
 90 day: 8 bp (+4)



## Forex

**Spot – PLN is on fire** EUR/PLN has finally broken out of its 4.2950-4.3450 mini range and spiked to 4.4615, as a result of Trumpflation fears. The move in USD/PLN was even more dramatic as it has moved from 3.8430 (post Trump low), to 4.2100 high. The PLN basket is significantly weaker as a result, with PLN longs liquidation adding fuel to the move. Domestic factor is not really helping, with GDP number much weaker than market consensus. We think the new range of 4.38-4.48 is, in establishing itself, but the risk of a final leg higher is still high. The air is thin for EUR/PLN above 4.50 (visited briefly this year, immediately after Brexit).

**Options – EUR/PLN vols gapped higher** The risk off is in full swing. The vols gapped higher with vengeance. 1 month EUR/PLN is now 7.8% mid (1.8% higher), 3 month EUR/PLN are 7.4% (1.25% higher) and finally 1 year is 7.8% (0.7% higher). The currency spread (USD/PLN vol minus EUR/PLN vol) spiked by almost 1.5% from 4.25 to 5.75 roughly. That makes the USD/PLN vol the ultimate winner of the move. Skew is also better bid.

### Short-term forecasts

Main supports / resistances:

EUR/PLN: 4.38 / 4.53

USD/PLN: 3.90 / 4.30

**Spot Position:** None.

Good things come to those who wait. Our longs EUR/PLN from 4.3170 and 4.2870, were cashed at 4.3900 and 4.4200.

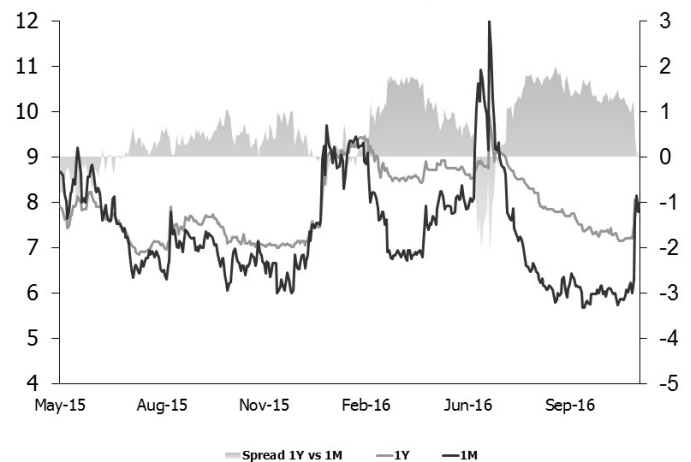
We have been keeping longs in EUR/PLN for several weeks, at we were quite close to stop loss at several occasions. The US president elect has finally delivered the spark that put PLN on fire. We are quite puzzled, what is next from here. Especially USD/PLN move is maybe bit exaggerated, but we think it is too early to catch the falling knife (Zloty), at the moment. Sidelined.

**Options** Selectively long Vega

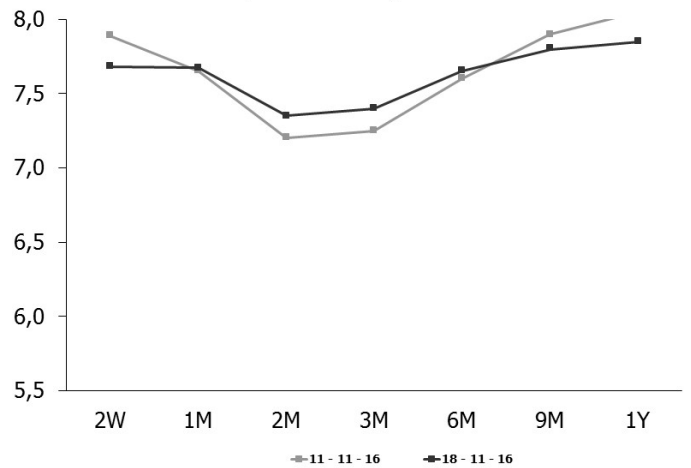
We have closed half of our long Vega EUR/PLN position. The scale of the jump in vols, was just too tempting. The currently increased volatility is likely to persist, but with proximity of Christmas, we assumed it would be prudent. We are trimming potential theta bills for the rest of the year.



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
11/11/2016	2.04	1.73	2.08	1.71	2.12	1.75	1.73	1.74	1.74	1.77	1.79	1.82
11/14/2016	2.15	1.73	2.18	1.71	2.20	1.75	1.74	1.75	1.76	1.79	1.85	1.88
11/15/2016	2.09	1.73	2.12	1.71	2.14	1.75	1.73	1.73	1.74	1.74	1.77	1.81
11/16/2016	1.95	1.73	1.97	1.71	2.00	1.75	1.74	1.75	1.75	1.76	1.79	1.83
11/17/2016	1.96	1.73	2.00	1.71	2.05	1.75	1.74	1.74	1.75	1.75	1.80	1.83

Last primary market rates							
Paper	Au. date	Maturity	Avg. price	Avg. yield	Supply	Demand	Sold
32W TB	3/14/2016	11/30/2016	99.04	1.35	1500	1757	1692
OK1018	10/6/2016	10/25/2018	96.54	1.74	2000	4838	2448
PS0421	8/18/2016	7/25/2021	98.31	2.11	3500	4968	3844
DS0727	10/6/2016	7/25/2027	94.57	3.10	4000	5916	4359

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0715	5Y IRS	PS0718	10Y IRS	DS1023
11/11/2016	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
11/14/2016	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
11/15/2016	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
11/16/2016	1.750	1.474	1.635	1.638	1.990	2.290	2.447	2.985
11/17/2016	1.750	1.474	1.635	1.525	2.000	2.269	2.460	2.964

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY
Date	1M	3M	6M	1Y	1M	1Y	1Y
11/11/2016	7.65	7.25	7.60	8.05	8.05	2.38	0.64
11/14/2016	8.15	7.50	7.95	8.10	8.10	2.38	0.64
11/15/2016	7.80	7.30	7.63	7.95	7.95	2.39	0.64
11/16/2016	8.00	7.45	7.80	7.95	7.95	2.39	0.65
11/17/2016	7.68	7.40	7.65	7.85	7.85	2.49	0.71

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
11/11/2016	4.3424	3.9856	4.0351	3.7538	1.4166	0.1608
11/14/2016	4.3892	4.0805	4.0998	3.7830	1.4188	0.1624
11/15/2016	4.4098	4.0837	4.1046	3.7731	1.4229	0.1632
11/16/2016	4.4345	4.1380	4.1268	3.7792	1.4278	0.1640
11/17/2016	4.4386	4.1375	4.1372	3.7938	1.4324	0.1639

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