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## Polish Weekly Review

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### Comment on the upcoming data and forecasts

Week starts with manufacturing PMI for March (Monday). We expect a visible rise in the index (to 55.5 pts.) based on surging economic sentiment in the euro zone. On Wednesday, the Monetary Policy Council will decide about interest rates, however one should not expect changes. The post-meeting statement and the tone of the press conference should be broadly unchanged from the previous month – the Council is set to remain optimistic but its optimism regarding the economy will not translate into greater hawkishness.

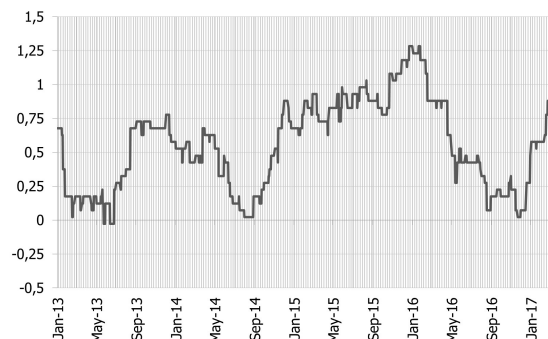
### Polish data to watch: April 3rd to April 7th

Publication	Date	Period	mBank	Consensus	Prior
Manufacturing PMI (p.)	03.04	Mar	55.5	54.6	54.2
MPC decision (%)	05.04	Apr	1.50	1.50	1.50

### Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Yield on the prev auction (%)	Prev auction
(29–37/52) Week T-bills	-	700	1.500	2/22/2017
2Y T-bond OK1019	4/6/2017	200	2.049	3/23/2017
5Y T-bond PS0422	4/6/2017	2000	2.945	3/23/2017
10Y T-bond DS0727	4/6/2017	1000	3.568	3/23/2017
30Y T-bond WS0447	-	2100	4.257	2/16/2017

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



### Comment

Big negative surprise in the CPI, and the result is a long-overdue correction in our surprise index. Only the PMI can surprise next week.

\* 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

- The economy accelerated in Q4 and at the beginning of the year, suggesting that the recovery in investment is proceeding faster than anticipated. Because of this we have decided to raise our growth forecasts, to 3.6% in Q1 (prev. 3.1%) and 4.0% on average in 2017 (prev. 3.4%).
- Boosted by statistical base effects, weak PLN, food price hikes and commodity price spike, headline inflation breached 2% and will fluctuate within the target band. While the market and the MPC is focused on base effects and flat CPI in the second half of the year, the case of accelerating core inflation is strengthening. Stellar employment performance shows no respite but wage growth remains moderate. Such equilibrium is unsustainable. If 2007 and 2008 are taken as guidance, wages are ready to take off this year as current demand for labor meets limited supply.
- MPC stays calm and waits rises in headline inflation out carrying steady message of stable rates. Such rhetoric can stay in place for some months. However, as trend in core inflation emerges as evident and labor market strengthen further, the case for rate hikes is set to strengthen as well. All we need is a small change in MPC's wording to make rate expectations wander somewhat more freely.
- Solid labor market performance and prospect for faster growing wages support PIT and VAT revenue from consumption. With much higher headline inflation already in place (deflationary 2016!), further improvements in tax income seem a safe bet for 2017 even without any stringent assumptions on the efficiency of tax collection.

### Financial markets

- Zloty benefited in lower rates environment among renewed EM inflows. Although a technical correction is due from this levels, zloty-negative factors went to the background for the time being (ECB hikes). Remember that Fed hikes were recently a factor discouraging substantial strengthening but not a reason for a weaker zloty per se. With stronger GDP growth (market seems to be upgrading its view towards ours) it should not change and zloty may stay stronger.
- CHF risks are set to come back to the agenda once more within 2 weeks as joint conference of president Duda and NBP governor Glapinski is looming. However, we expect the conference to be long on words and short on actions. More precisely, rather nothing more than spread regulation and threats of using higher capital weights in SREP process.

### mBank forecasts

	2013	2014	2015	2016	2017 F	2018 F
GDP y/y (%)	1.4	3.3	3.9	2.8	4.0	3.9
CPI Inflation y/y (average %)	0.9	-0.1	-0.9	-0.6	2.2	2.3
Current account (%GDP)	-1.2	-2.1	-0.6	-0.6	-0.9	-1.1
Unemployment rate (end of period %)	13.4	11.4	9.8	8.3	7.8	7.3
Repo rate (end of period %)	2.50	2.00	1.50	1.50	1.50	2.25

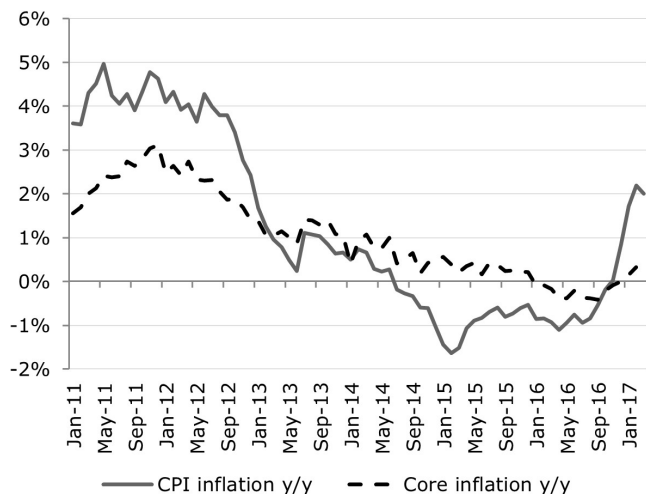
	2017	2017	2017	2017	2018	2018	2018	2018
	Q1 F	Q2 F	Q3 F	Q4 F	Q1 F	Q2 F	Q3 F	Q4 F
GDP y/y (%)	3.6	3.8	4.0	4.4	4.1	3.9	3.8	3.8
Individual consumption y/y (%)	4.3	4.2	4.2	4.0	4.0	3.8	3.8	3.8
Public Consumption y/y (%)	3.5	3.5	3.0	1.5	2.0	3.0	3.0	3.0
Investment y/y (%)	1.5	4.0	8.0	10.0	10.0	7.0	5.5	5.0
Inflation rate (% average)	2.1	2.4	2.4	1.9	2.1	2.2	2.3	2.4
Unemployment rate (% eop)	8.5	7.9	7.5	7.8	8.0	7.4	7.1	7.3
NBP repo rate (% eop)	1.50	1.50	1.50	1.50	1.50	1.75	2.00	2.25
Wibor 3M (% eop)	1.73	1.73	1.73	1.73	1.73	1.98	2.23	2.48
2Y Polish bond yields (% eop)	2.15	2.20	2.25	2.30	2.30	2.35	2.40	2.45
10Y Polish bond yields (% eop)	3.90	3.95	4.00	4.05	4.10	4.15	4.20	4.25
EUR/PLN (eop)	4.30	4.25	4.25	4.20	4.20	4.20	4.20	4.20
USD/PLN (eop)	4.06	4.01	4.05	4.04	4.08	4.12	4.12	4.12

F - forecast

## Economics

### CPI corrects on lower food prices

According to the flash estimate, Polish CPI fell to 2.0% from 2.2% y/y in February. We need to wait for the details until the middle of the month. However, we expect lower food prices to be the main cause of this fall. Pattern of lower vegetable prices seen in Western Europe countries (Spain, Germany) and Poland (on the marketplaces) found its way into CSO data.



In the next month we see a possibility of further downward correction of food prices seen in last few months, which should result in stabilization of CPI at around 2%. However, fuel and food prices are volatile enough to generate surprises and gyrations from upward trend in inflation. When it comes to core inflation, we expect it to continue growing steadily, driven by trajectories of real sphere processes (labour market, economic growth).

March CPI flash inflation is in line with recent sentiment on other European markets (inflation in the euro zone also surprised on the downside). In our opinion this is only a correction in the upward trend, which should persist in the following months fueled by real sphere data (pushing also core inflation upwards). Thus, we see a limited scope of further unpricing of rate hikes (in US, Eurozone and of course Poland – when it comes to the latter, we are only few basis points from the moment where there will be no rate hikes prices in 2018).

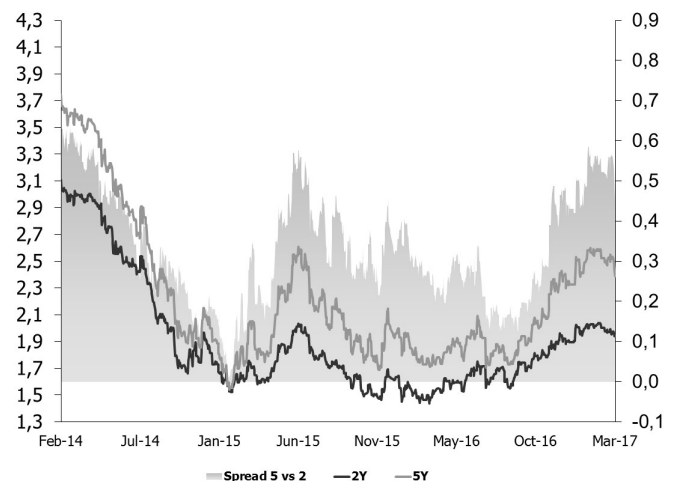
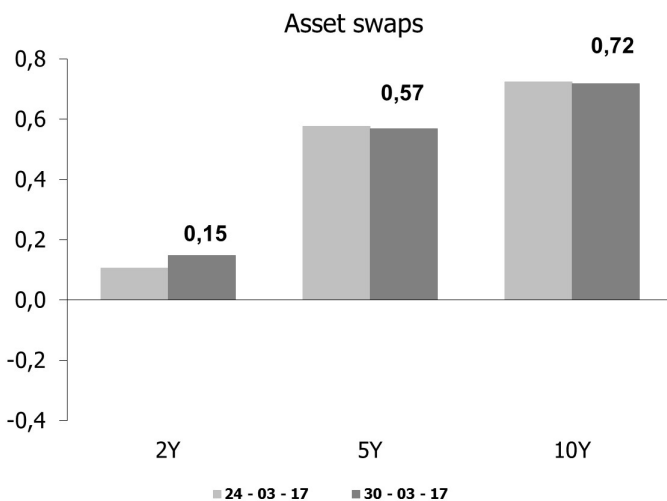
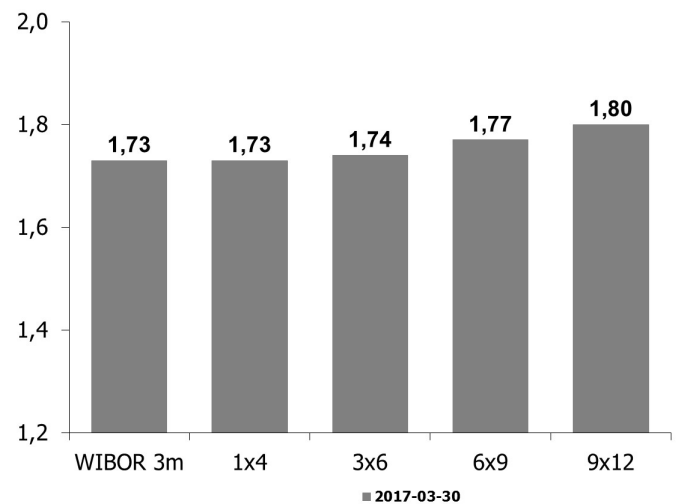
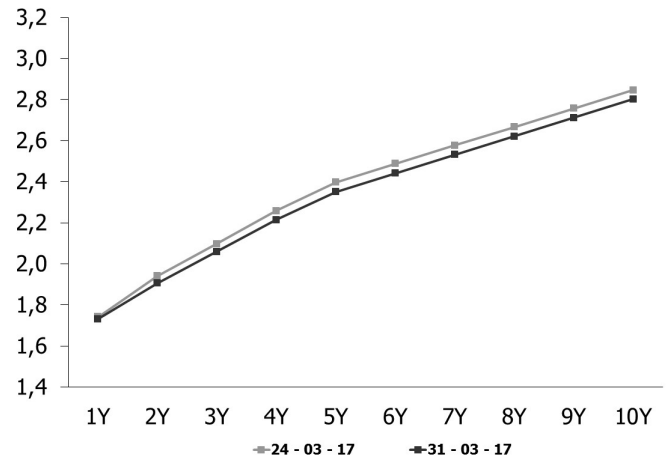
## Fixed income

### Curve even flatter

Next week we have an auction. The Ministry of Finance is selling OK0419/PS0422/DS0727/WZ1122/WZ0126. We expect good supply in April, 13-16 bn. Yields are at this year's lows, BUND/DS0727 is trading at 318bps. Curve is very flat and it's hard to expect it to flatten more.

The PS0422/DS0727 spread has narrowed from 60 to 58, ASW PS0422/5y is at 51bps and DS0727/10y is at 65bps. OK0419 is trading at 1.99% (4bps down), PS0422 is trading at 2.92% (3bps down) and DS0727 is trading at 3.5% (5bps down).

IRS curve



## Money market

### Cheap month end

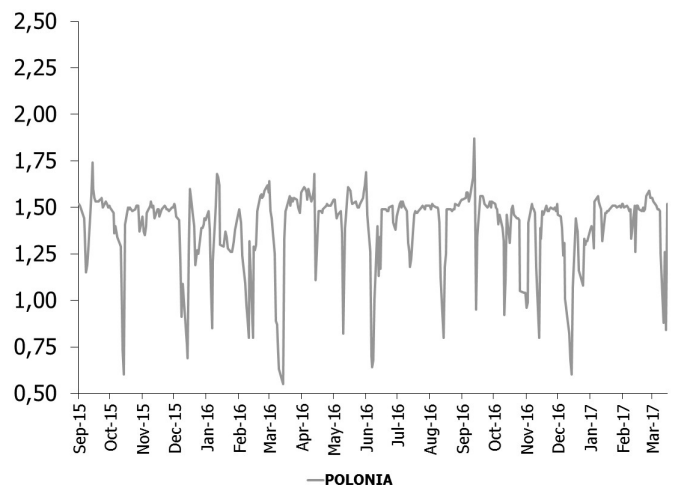
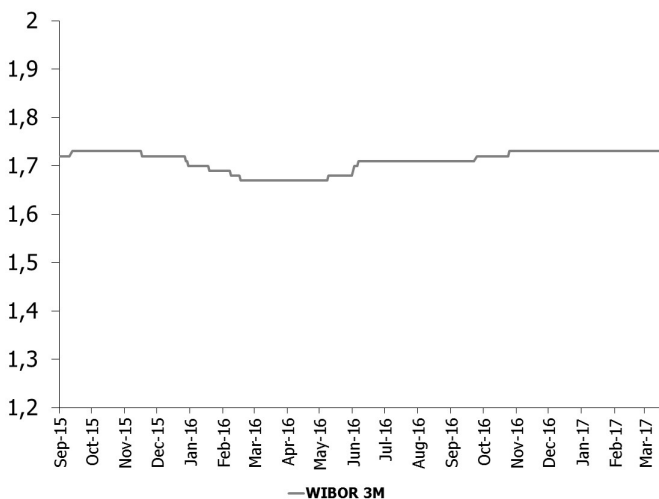
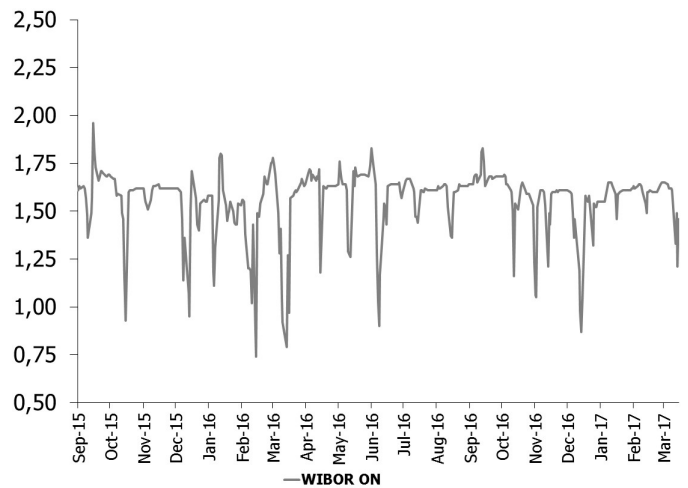
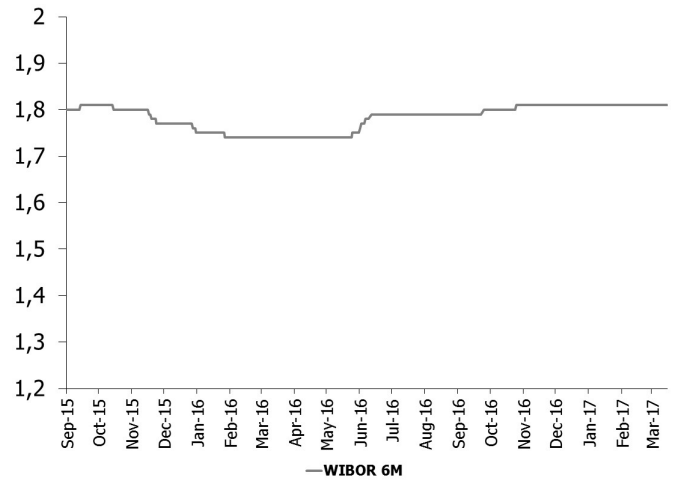
Recent bullish sentiment on POLGBs lost some of its steam last week. Yields fell only marginally with 2y IRS touching 1.935%. Today's lower than expected CPI print shouldn't have a big impact as the broad consensus for Polish rates is no changes for an extended period of time. Would be happy to pay front end rates if they fall further and erase rate hike odds for two years.

Favourable calendar effects in March resulted in cheap month end. Our monthly average widens 3 bp to 1.46%. This is more or less where we see average overnight funding in the medium term. Unfortunately, April ends on Friday, on the same day as reserve period which reduces chances for cheap end. On the other hand, we have Easter holidays incoming, which should act in the quite opposite direction.

Ref rate vs Polonia averages:

30 day 4 bp

90 day 8 bp



## Forex

**Spot – Stronger again** EUR/PLN has broken the 4.25-4.27 support zone and set fresh YTD low at 4.2100. The „risk on” train is still running, fueled by the positive investment sentiment. The next possible EUR/PLN target to the downside is 4.1850 and the former support at 4.25-4.27 is now acting as the resistance. We have to respect the price action and the fact that inflows into polish assets continue. Nevertheless, we are a bit skewed to fade PLN spikes, and bit skeptical in PLN having much more room to flourish.

**EUR/PLN vols – Front end vols tic higher** The French elections are supporting the front end vols, (already included in 1 month). As the consequence, the front end was well supported. 1 month EUR/PLN ATM is paid at 5.8% (0.4% higher), 3 month EUR/PLN are 6.3% (unchanged) and, finally, 1 year is fixing at 7.1% (0.1% lower). The currency spread (difference between USD/PLN and EUR/PLN) is bit lower in the back end. The skew is roughly unchanged.

### Short-term forecasts

Main supports / resistances:

EUR/PLN: 4.18 / 4.28

USD/PLN: 3.85 / 4.05

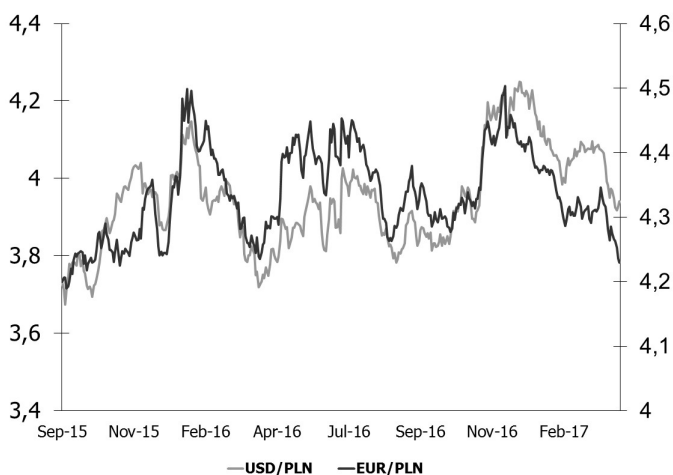
**Spot** Position: Sidelined.

The longs in EUR/PLN at 4.2930 and at 4.2600 both were stopped out at 4.235.

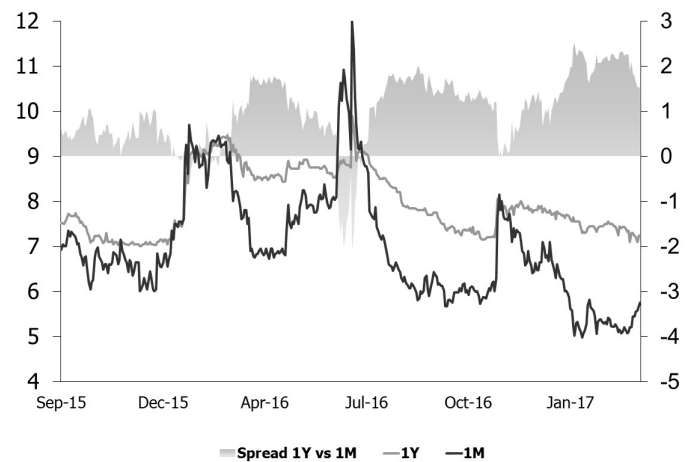
We have to respect the market price action. We haven't expected the downside trend to be that strong. We are sidelined at the moment, we still are more keen to fade the Zloty strength, but the entry level has to be picked carefully. Currently the drop to 4.17-4.19 in EUR/PLN would be a fresh signal to dip our toe in the water again.

**Options** Vol – Long 9 month EUR/PLN vol.

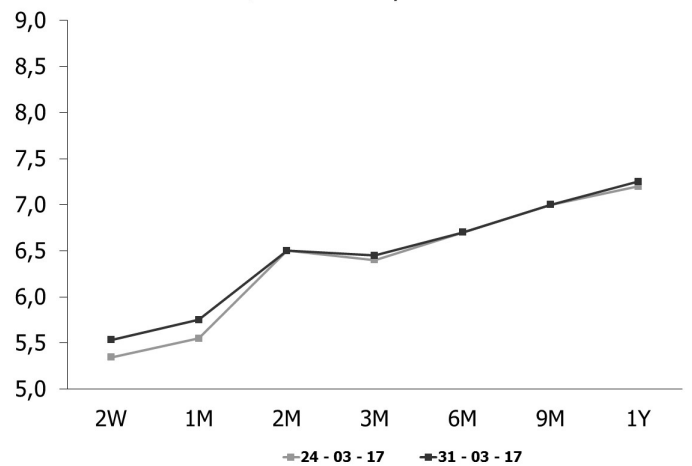
We are keeping the backend long as an outright long position. We see French elections as good enough reason to be long vol at current levels. We are encouraged by the fact that the backend vols are holding well even with a current low realized volatility.



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
3/24/2017	1.65	1.73	1.65	1.71	1.65	1.75	1.73	1.74	1.76	1.82	1.88	1.84
3/27/2017	1.72	1.73	1.84	1.71	2.04	1.75	1.74	1.74	1.76	1.80	1.88	1.83
3/28/2017	1.73	1.73	1.79	1.71	1.82	1.75	1.73	1.74	1.77	1.81	1.88	1.84
3/29/2017	1.54	1.73	1.66	1.71	1.89	1.75	1.74	1.74	1.76	1.80	1.88	1.82
3/30/2017	1.72	1.73	1.84	1.71	2.06	1.75	1.73	1.74	1.77	1.80	1.87	1.84

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
OK0419	1/5/2017	4/25/2019	94.88	2.32	1000	2825	990
PS0422	1/5/2017	4/25/2022	95.62	3.16	1500	2880	1570
DS0727	1/5/2017	7/25/2027	89.20	3.76	1500	2787	1544

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0715	5Y IRS	PS0718	10Y IRS	DS1023
3/24/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
3/27/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
3/28/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
3/29/2017	1.750	1.474	1.635	1.638	1.990	2.290	2.447	2.985
3/30/2017	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	1Y
3/24/2017	5.55	6.40	6.70	7.20	7.20	1.79	0.46	0.46
3/27/2017	5.58	6.40	6.69	7.19	7.19	1.79	0.46	0.46
3/28/2017	5.58	6.40	6.69	7.19	7.19	1.77	0.57	0.57
3/29/2017	5.75	6.45	6.75	7.25	7.25	1.78	0.51	0.51
3/30/2017	5.75	6.45	6.70	7.25	7.25	1.78	0.51	0.51

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
3/24/2017	4.2658	3.9481	3.9839	3.5529	1.3788	0.1579
3/27/2017	4.2630	3.9259	3.9843	3.5592	1.3756	0.1578
3/28/2017	4.2529	3.9169	3.9730	3.5380	1.3745	0.1574
3/29/2017	4.2360	3.9265	3.9543	3.5386	1.3670	0.1567
3/30/2017	4.2292	3.9402	3.9538	3.5487	1.3643	0.1565

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