

April 27, 2017

## Polish Weekly Review

**mBank Research**  
(macro/FI/FX analysis)

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### Table of contents

<b>Our view in a nutshell</b>	page 2
<b>Economics</b>	page 3
■ Fiscal update: Tax receipts are growing at a solid pace, focus should shift towards general government balance	
<b>Fixed income</b>	page 4
■ Heavy end of the week	
<b>Money market</b>	page 5
■ Following the macroeconomic story	
<b>FX market</b>	page 6
■ Spot – PLN – still sideways	
■ Options – EUR/PLN vols – dropped like a stone	

### Comment on the upcoming data and forecasts

This Friday, the CSO will release flash CPI data. We expect a slight drop in headline inflation, from 2.0% y/y in March to 1.9% y/y in April because of lower fuel and food (mainly vegetables) prices. Monday and Wednesday are public holidays in Poland, so domestic markets will be closed. On Tuesday, manufacturing PMI for April will be published. The index should stabilize at 53.5, following a similar pattern in most of CSO's business tendency indicators.

### Polish data to watch: April 28th to May 5th

Publication	Date	Period	mBank	Consensus	Prior
CPI y/y (%) <i>flash</i>	28.04	Apr	1.9	2.0	2.0
Manufacturing PMI (p.)	02.05	Apr	53.5	53.9	53.5

### 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	5/18/2017	1400	1.976	4/25/2017
5Y T-bond PS0422	5/18/2017	2300	2.862	4/25/2017
10Y T-bond DS0727	5/18/2017	2100	3.425	4/25/2017
30Y T-bond WS0447	-	2100	4.257	2/16/2017

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



#### Comment

Polish surprise index continues its upward trend after another positive surprise (unemployment rate), completing the picture of a terrific April. Next week, two releases can move the index – flash CPI (this Friday) and manufacturing PMI (Tuesday).

\* 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 (4.0% on average in 2017). We have frontrun a new wave of forecast upgrades for Poland. Recent data suggest even stronger growth this year.
- 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, while 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 benefitted 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 (e.g. 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 shifting its view towards ours) it should not change and Zloty may stay stronger.
- CHF risks could come back to the agenda once more as a joint conference of President Duda and NBP governor Glapinski was suggested. 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	3.8	2.7	4.0	3.9
CPI Inflation y/y (average %)	0.9	-0.1	-0.9	-0.6	2.1	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	7.2	6.6
Repo rate (end of period %)	2.50	2.00	1.50	1.50	1.50	2.25

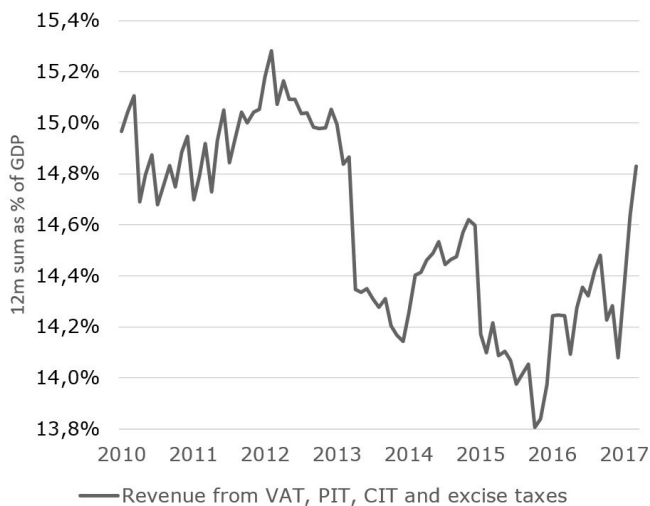
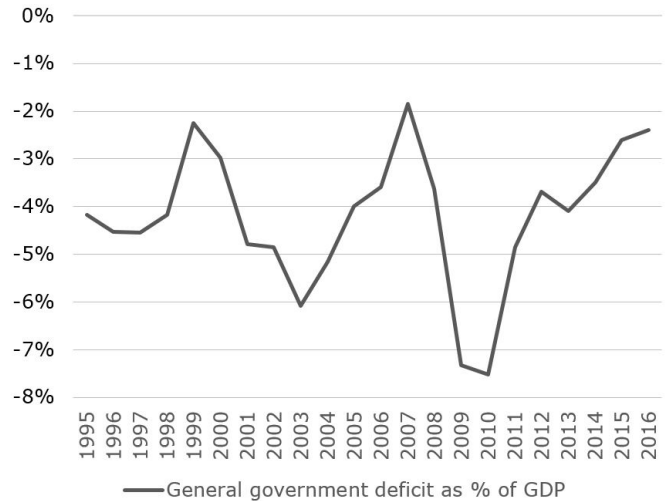
	2017	2017	2017	2017	2018	2018	2018	2018
	Q1 F	Q2 F	Q3 F	Q4 F	Q1 F	Q2 F	Q3 F	Q4 F
GDP y/y (%)	3.6	3.8	4.0	4.4	4.1	3.9	3.8	3.8
Individual consumption y/y (%)	4.3	4.2	4.2	4.0	4.0	3.8	3.8	3.8
Public Consumption y/y (%)	3.5	3.5	3.0	1.5	2.0	3.0	3.0	3.0
Investment y/y (%)	1.5	4.0	8.0	10.0	10.0	7.0	5.5	5.0
Inflation rate (% average)	2.0	2.1	2.3	2.0	2.1	2.2	2.3	2.4
Unemployment rate (% eop)	8.2	7.4	7.2	7.2	7.2	6.6	6.5	6.6
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)	2.01	2.10	2.20	2.25	2.30	2.35	2.40	2.45
10Y Polish bond yields (% eop)	3.49	3.60	3.70	3.80	3.90	4.00	4.10	4.20
EUR/PLN (eop)	4.23	4.25	4.22	4.20	4.20	4.20	4.20	4.20
USD/PLN (eop)	3.97	4.01	4.02	4.04	4.08	4.12	4.12	4.12

F - forecast

## Economics

### Fiscal update: Tax receipts are growing at a solid pace, focus should shift towards general government balance.

Recent fiscal data from Poland continued to come on the positive side. In the first quarter of 2017, tax revenues rose by 24% y/y, led by surging VAT revenues (+41%) and strong growth in other major categories (CIT +15% y/y; PIT +5% y/y; excise taxes +3%). The surge in VAT receipts is not a surprise and can be traced back to two factors we already covered in one of the previous reports, namely shifts in tax refunds towards December '16 as well as legislative changes that altered the frequency of VAT statements for enterprises. However, even if we account for the abovementioned factors, the trend in overall tax revenue collection remains positive and quite steep (see the graph below). Under conservative assumptions, one should expect tax revenues to outperform the Ministry's annual target by about 3-4% (i.e. 9-12 bn PLN). The expected payout of NBP profit (9 bn PLN above the MoF's original expectations) will compound on this and, overall, the annual deficit is expected to be ca. 20 bn PLN smaller than the statutory limit of 69 bn PLN.



As usual, this is not the full picture. For obvious and entirely correct reasons, economists are also interested in the broader measures of fiscal stance, namely the general government balance and debt figures. The former, as we have learned recently, has reached a multi-year high of -2.4% GDP in 2016, no small part due to significant cutbacks in public investment and record-high surpluses in the local government subsector. These factors will cease in 2017 and the overall swing (i.e. difference between this year's deficit and last year's surplus) in local government balance might even exceed 1% of GDP. It is unquestionably good news for the economy and we have been predicting this for many months. This will push the general government balance towards 3% of GDP, however not beyond it as the strong central government fiscal figures discussed above imply outperformance there. With real GDP growth possibly exceeding 4% this year (nominal GDP growth ca. 5.5%), PLN appreciation on year-end / year-end basis and interest expenditure in decline, we expect debt to GDP ratio to decline slightly this year.

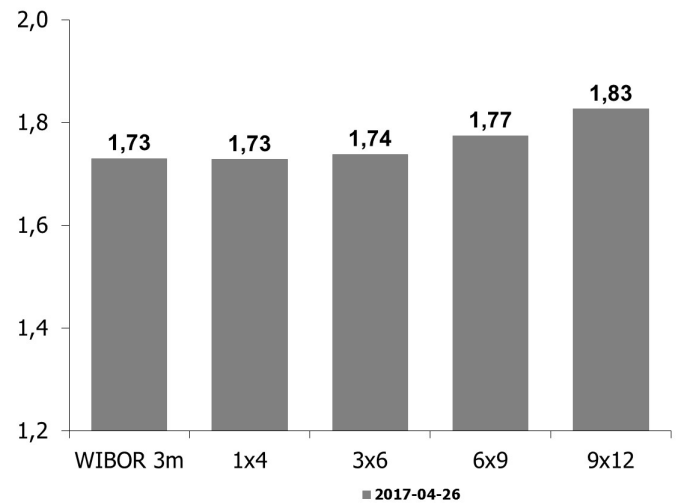
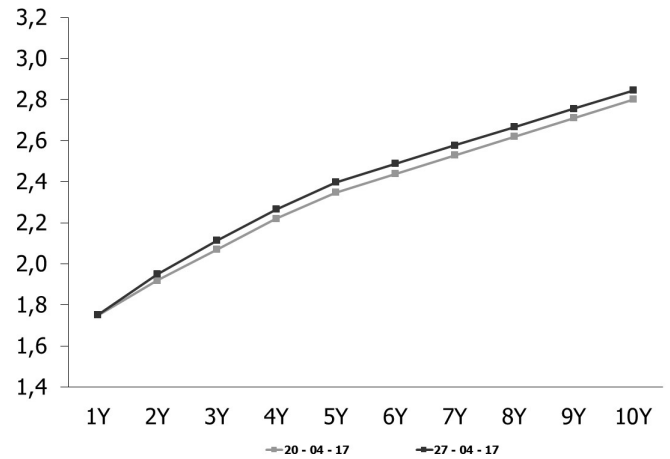
## Fixed income

### Heavy end of the week

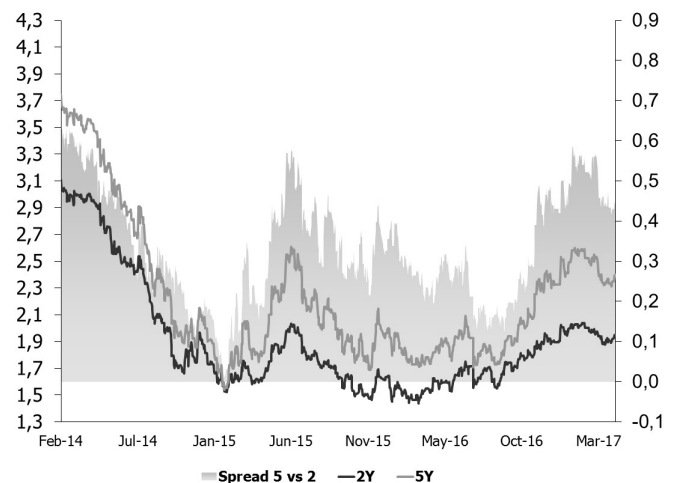
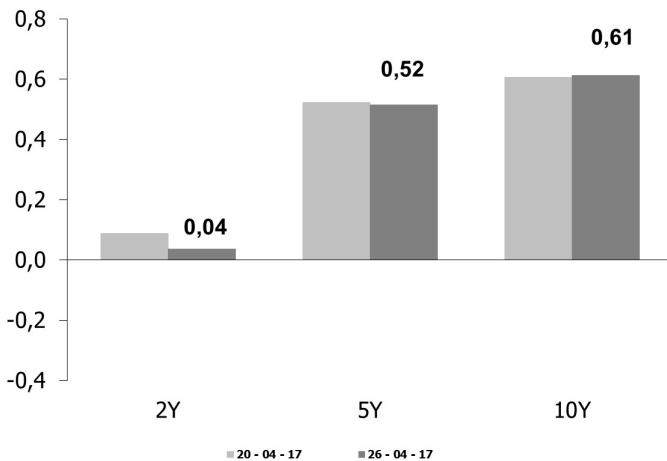
This week we had an auction. The Ministry of Finance sold OK0419/PS0422/DS0727/WZ1122/WZ0126. Bid to cover wasn't impressive, all the bids were covered, everyone is long now. It won't be easy to move yields lower. Since a long weekend is coming in Poland, people will try to close positions, it will be heavy.

The PS0422/DS0727 widened from 52 to 55, ASW PS0422/5y is at 47 bps and DS0727/10y is at 58 bps (both narrowed 2 bps). OK0419 is trading at 1.98% (3 bps up), PS0422 is trading at 2,85% (1 bp down) and DS0727 is trading at 3.42% (2 bps up).

IRS curve



Asset swaps





## Money market

### Following the macroeconomic story

Short rates are grinding a bit higher, following splendid macroeconomic data. The range of this move is limited, given the wide market consensus about rates staying low for an extended period of time.

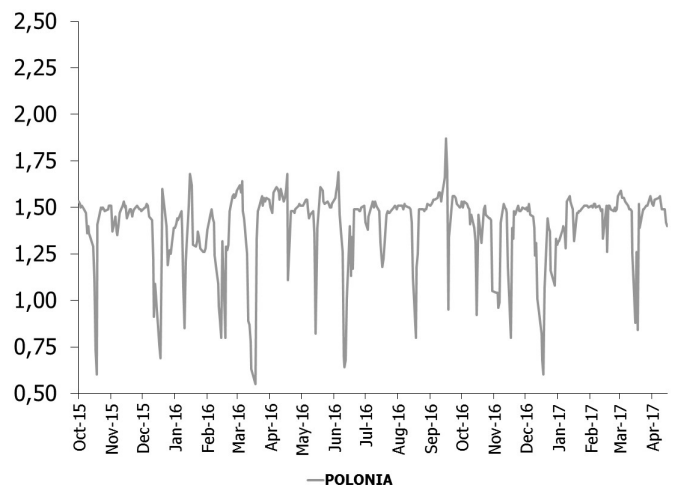
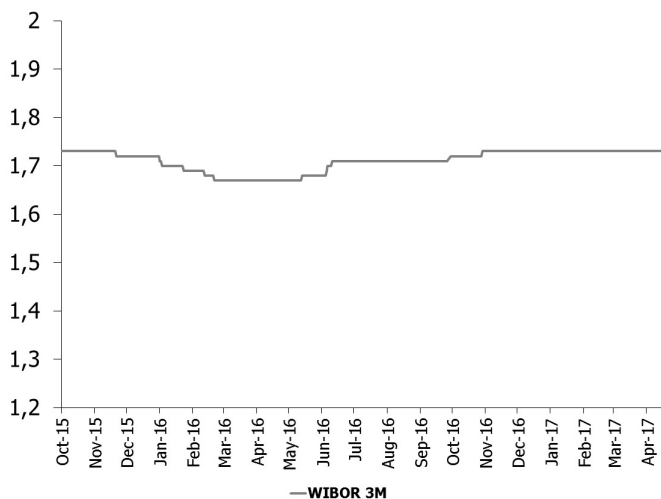
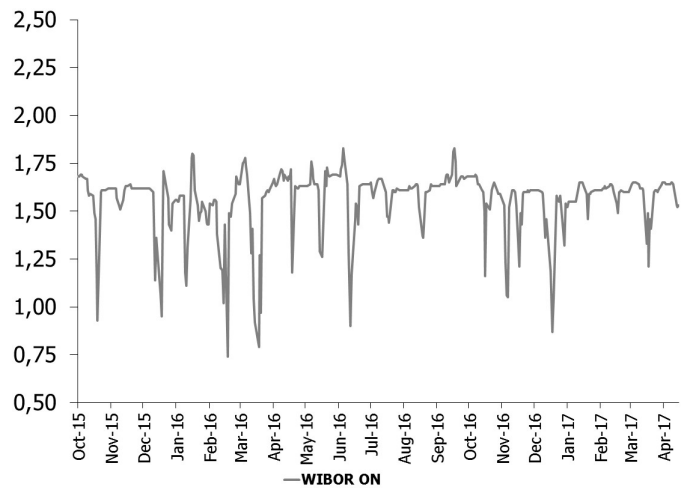
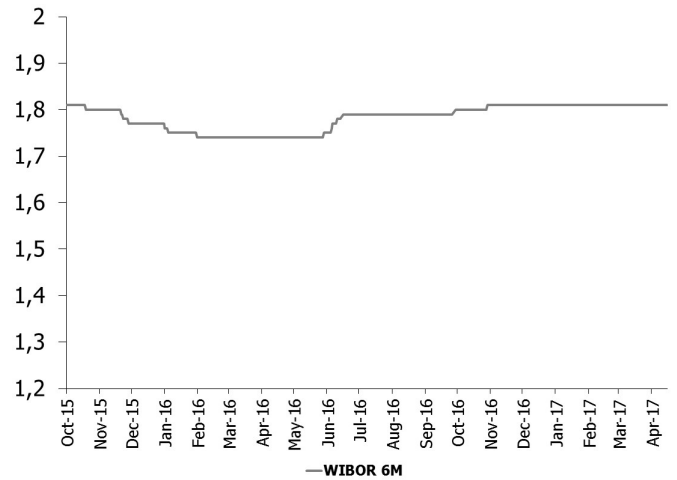
We still believe that with recent data pointing to much higher growth, there is an upside risk for the rates.

Last week was characterized by high volatility in overnight rates. They were moving in a wide, 1.00-1.50% range.

Ref rate vs Polonia averages:

30 day 4 bp

90 day 3 bp



## Forex

**Spot – PLN – still sideways** The removal (hopefully) of political risk coming from French elections cast a spell on Zloty. EUR/PLN opened sharply lower, the move was even more dramatic in USD/PLN. The lows of 4.2200 and 3.8550, respectively, were touched as a result. We are still hovering around these levels, with only minimal correction higher. Does this move have legs to extend PLN gains? Well, it is to be decided, the market is most likely already positioned (long PLN) for it, and that makes the risk/reward of being long PLN here much less compelling.

**EUR/PLN vols – dropped like a stone** 1 month EUR/PLN ATM MID dropped to 5.9% (0.9% lower), 3 months EUR/PLN are at 5.9% (0.7% lower), and finally 1 year is fixing at 6.9% (0.25% lower). The currency spread (difference of USD/PLN minus EUR/PLN) crashed in the front end, falling from 6% to 3.5%! This makes the 1 month USD/PLN the real victim of the events, it traded at 13.85%, 13.55% and 13.25% last week, only to be 10-ish offered now. The skew is tic better offered.

### Short-term forecasts

Main supports / resistances:

EUR/PLN: 4.18 / 4.28

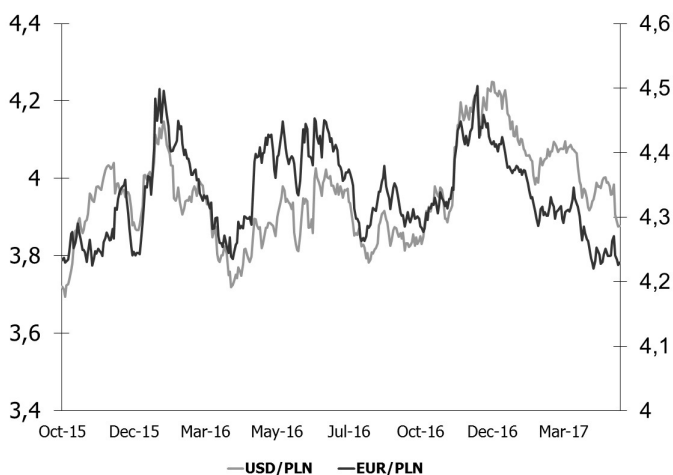
USD/PLN: 3.70 / 4.00

**Spot** Current position: Long EUR/PLN at 4.2250.

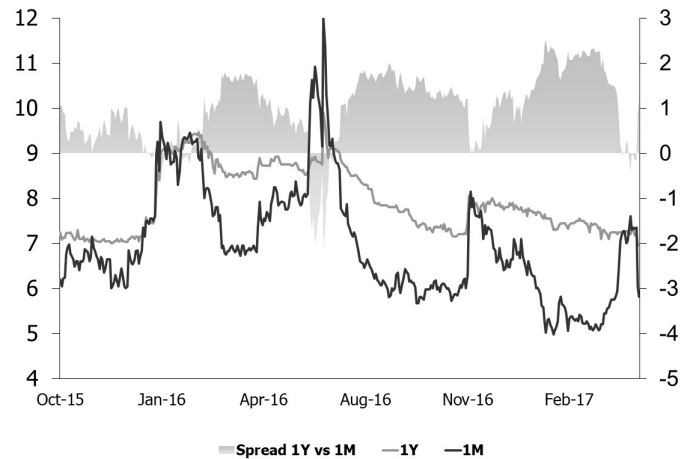
It is all about risk/reward. We don't see any imminent reasons to sell PLN, but the temptation of playing against the trend is rising. We are ready to add at 4.1850 with 4.1600 a firm stop. The hopes are to go back to 4.300 eventually. After the last set of positive data, we think the potential for positive surprises is really limited.

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

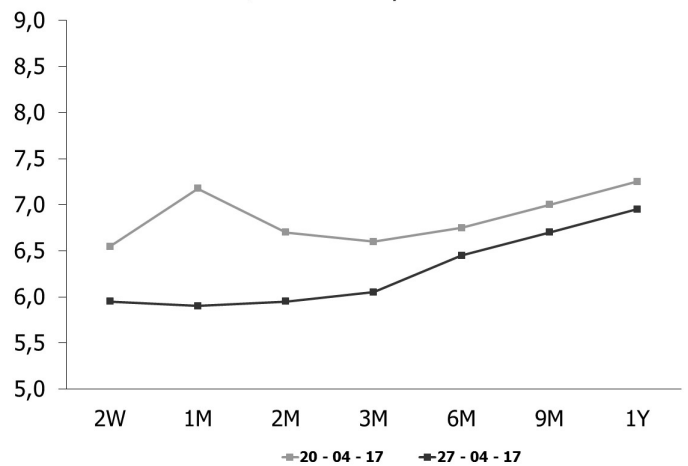
Our position got hit hard, when the vols reversed down on the back of market-friendly French elections results. Well, the milk has already spilled. The move down in vol was so big, that we are now at bids in 3 month EUR/PLN in the 5.80% region. We find that level attractive, and we would like to add some to our already long Vega exposure.



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
4/20/2017	1.74	1.73	1.85	1.71	2.07	1.75	1.73	1.74	1.76	1.81	1.87	1.85
4/23/2017	1.77	1.73	1.87	1.71	2.00	1.75	1.73	1.74	1.76	1.80	1.87	1.85
4/24/2017	1.72	1.73	1.81	1.71	1.97	1.75	1.73	1.74	1.77	1.82	1.87	1.86
4/25/2017	1.61	1.73	1.71	1.71	1.88	1.75	1.73	1.74	1.77	1.82	1.90	1.86
4/26/2017	1.79	1.73	1.89	1.71	2.07	1.75	1.73	1.74	1.77	1.83	1.91	1.86

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	4/6/2017	4/25/2019	96.06	1.99	900	2288	918
PS0422	4/6/2017	4/25/2022	97.11	2.87	1500	2255	1437
DS0727	4/6/2017	7/25/2027	91.95	3.44	1600	2552	1693

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0715	5Y IRS	PS0718	10Y IRS	DS1023
4/20/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
4/23/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
4/24/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
4/25/2017	1.750	1.474	1.635	1.638	1.990	2.290	2.447	2.985
4/26/2017	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	
4/20/2017	7.18	6.60	6.75	7.25	7.25	1.93	0.52	
4/23/2017	7.18	6.60	6.75	7.25	7.25	1.93	0.52	
4/24/2017	7.18	6.60	6.75	7.25	7.25	1.79	0.25	
4/25/2017	5.83	6.00	6.43	6.98	6.98	1.81	0.53	
4/26/2017	5.90	6.05	6.45	6.95	6.95	1.80	0.55	

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
4/20/2017	4.2631	3.9588	3.9788	3.6297	1.3617	0.1582
4/23/2017	4.2705	3.9841	3.9921	3.6517	1.3617	0.1585
4/24/2017	4.2410	3.9060	3.9267	3.5461	1.3602	0.1583
4/25/2017	4.2346	3.8873	3.9092	3.5190	1.3585	0.1579
4/26/2017	4.2255	3.8757	3.8982	3.4844	1.3553	0.1572

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