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Polish Weekly Review

mBank Research
(macro/FI/FX analysis)

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Comment on the upcoming data and forecasts

On Monday CSO will publish final CPI data for May. We expect it to confirm flash reading at 1.9% y/y. First batch of monthly NBP's data will be published the day after. Core CPI should stabilize at 0.9% y/y. When it comes to balance of payment, we expect current account balance to remain deep below zero for another month in a row. Both exports and imports should drop significantly mainly due to seasonal pattern. NBP will publish money supply data on Wednesday – we expect M3 aggregate to rise only slightly to 6.5% y/y, because of base effect and after a large fall in corporate deposits. Thursday is a public holiday in Poland.

Polish data to watch: June 9th to June 16th

Publication	Date	Period	mBank	Consensus	Prior
CPI y/y (%) <i>final</i>	12.06	May	1.9	1.9	2.0
Core inflation y/y (%)	13.06	May	0.9	1.0	0.9
Current account (mio EUR)	13.06	Apr	-922	-70	-738
Exports (mio EUR)	13.06	Apr	15800	15642	17798
Import (mio EUR)	13.06	Apr	16200	15800	18016
Money supply M3 (%)	14.06	May	6.5	6.5	6.4

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	6/9/2017	250	1.905	5/18/2017
5Y T-bond PS0422	6/9/2017	1000	2.734	5/18/2017
10Y T-bond DS0727	6/9/2017	1000	3.289	5/18/2017
30Y T-bond WS0447	-	2100	4.257	2/16/2017

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



Comment

Unchanged, since MPC (just as expected) did not change interest rates. Next week is packed with releases, but surprisingly it has only one opportunity to move the index – final CPI.

* 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 front-run 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 benefited in lower rates environment among renewed EM inflows. Substantial improvement in fiscal position seems to be the most important factor for investors (compression of credit risks).
- Stronger GDP growth should underpin the zloty in the mid-term as it stays undervalued in real, effective terms.
- Although a technical correction is due from this levels, zloty-negative factors went to the background for the time being. Investors seem to share a benign view concerning the monetary policy in the euro zone and in the U.S. Therefore we would rather look for short-term zloty-negative factors in bursts of risk aversion triggered by non-economic news. The scope for correction is limited given rather benign macro outlook, though.

mBank forecasts

	2013	2014	2015	2016	2017 F	2018 F
GDP y/y (%)	1.4	3.3	3.8	2.7	4.1	3.9
CPI Inflation y/y (average %)	0.9	-0.1	-0.9	-0.6	2.0	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	6.7	6.0
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	Q2 F	Q3 F	Q4 F	Q1 F	Q2 F	Q3 F	Q4 F
GDP y/y (%)	4.0	4.2	4.2	4.2	4.1	3.9	3.8	3.8
Individual consumption y/y (%)	4.7	4.5	4.2	4.0	4.0	3.8	3.8	3.8
Public Consumption y/y (%)	1.0	3.5	3.5	3.5	2.0	3.0	3.0	3.0
Investment y/y (%)	-0.4	5.5	8.0	12.0	10.0	7.0	5.5	5.0
Inflation rate (% average)	2.0	1.9	2.1	2.1	2.1	2.2	2.3	2.4
Unemployment rate (% eop)	8.2	7.0	6.5	6.7	6.9	5.9	5.7	6.0
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	4.20	4.15	4.10	4.10	4.12	4.14	4.16
USD/PLN (eop)	3.97	3.75	3.77	3.87	3.94	4.00	4.02	4.00

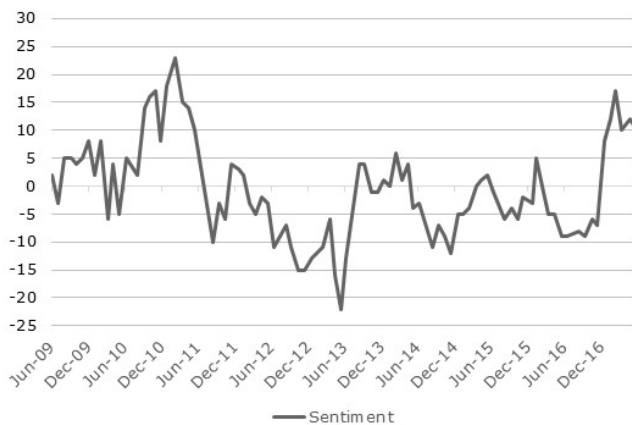
F - forecast

Economics

MPC: Rates unchanged... until 2018

Not only interest rates remained unchanged on June's meeting, but also Governor Glapinski expects them to remain at current levels for the whole 2018. Just as expected, MPC wording did not change significantly since last meeting (only 3 weeks before). According to the Council, Polish economy is on a sustainable growth path without any disequilibria. This thesis is supported by a "new" estimate of potential growth rate (as said during the conference), which is somewhere between 3% and 4%. So the Council only has to monitor, observe and keep an eye on the economy. By now it does not see anything worrying beside some lag in investment activity.

Traditionally we enclose our analysis of the sentiment enclosed in the statement. Not surprisingly it stabilized on a new, higher level.



Current MPC rhetoric is not only a result of an economic model which majority of MPC members believes in, but also a reaction to latest economic data: inflation stabilized (temporarily) with decent economic activity. Even after recent strengthening, the Zloty is in a medium-term perspective quite undervalued, which does give the Council additional reasons not to react. Polish Zloty (floating regime) could also be a buffer in case of a possible GDP acceleration – currency strengthening would be then an equivalent of monetary tightening.

In our opinion it will be extremely difficult to talk the Council out of this consensus. On the other hand, MPC is susceptible to economic data, especially when it comes to inflation and wages. Thus, even if the Council still ignores projected by NBP core inflation growth (far above 2% in 2019), a temporary acceleration of inflation coupled with persistent acceleration of wages could spark discussion about sooner-than-expected monetary tightening. Currently markets price-in first rate hikes only in 2019, so there is plenty of room to make interesting bet.

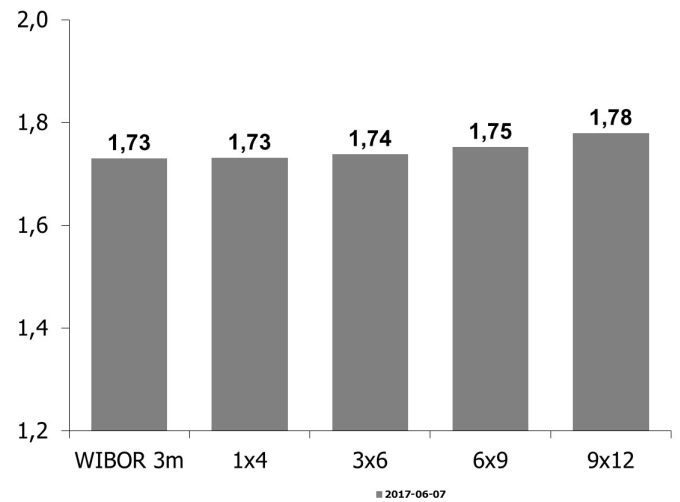
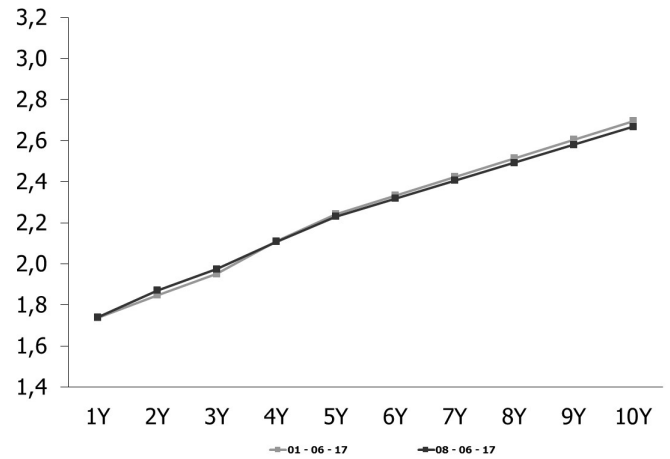
Fixed income

Nothing new, except an auction

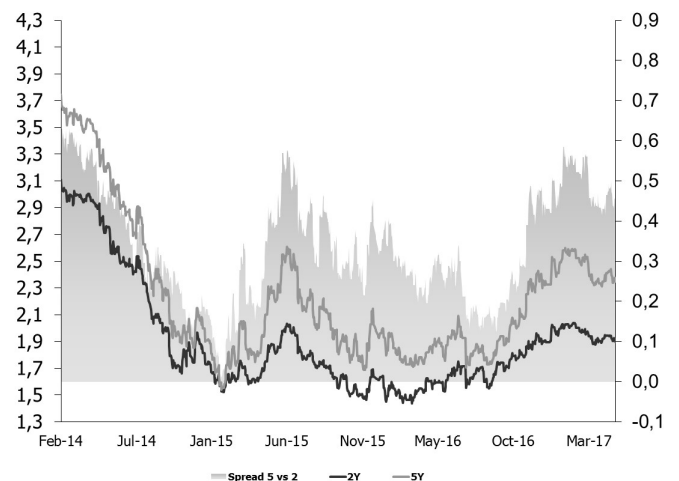
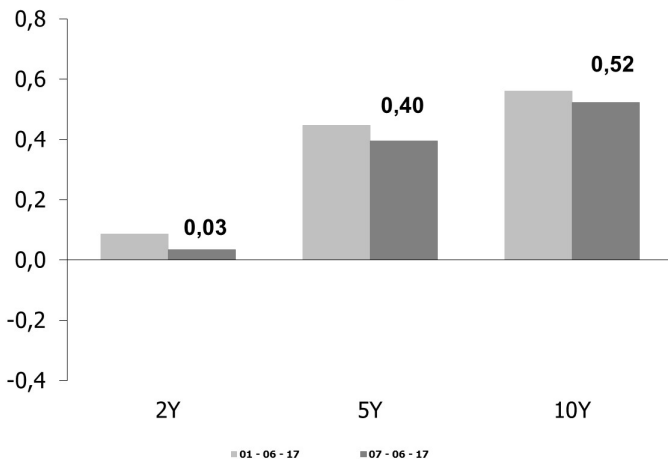
Tomorrow we will have a small auction, only 3 bio on the offer. MPC said nothing new. ECB said nothing new. We have happy buying again, and Polish bonds are the most attractive for everyone. There's no way we will finish this year at this levels, someone will take profit!

It was a boring week in Poland. Bund/DS0727 is 292bps today, it hasn't moved. The PS0422/DS0727 hasn't moved and is 58bps, ASW PS0422/5y is at 37bps and DS0727/10y is at 49bps, same as week ago. OK0419 is trading at 1/89% , PS0422 is trading at 2.62% (4bps down) and DS0727 is trading at 3.2% (4bps down).

IRS curve



Asset swaps



Money market

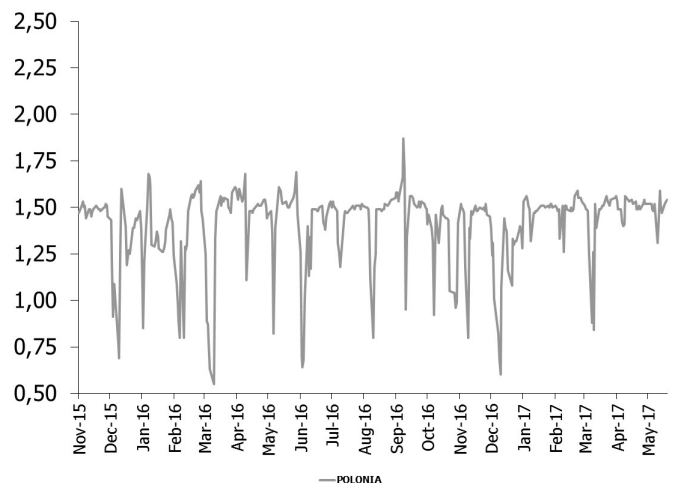
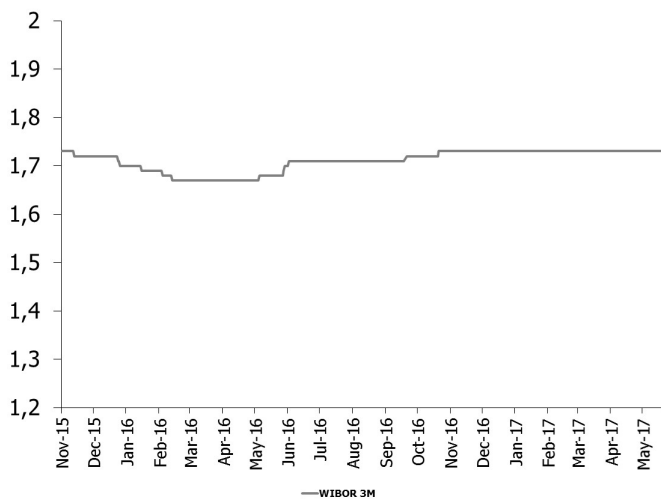
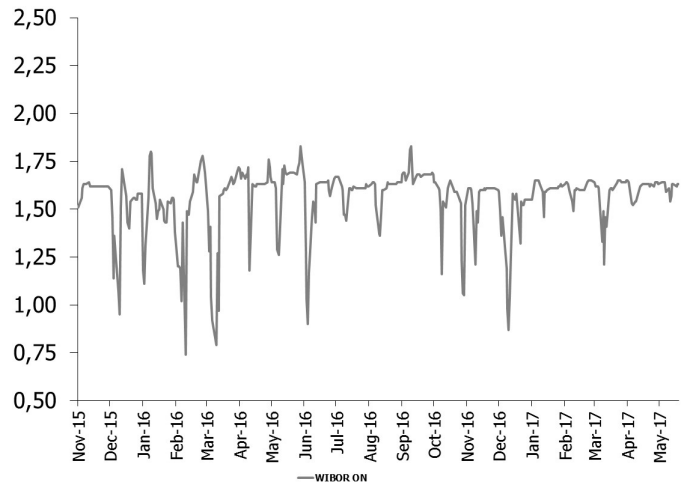
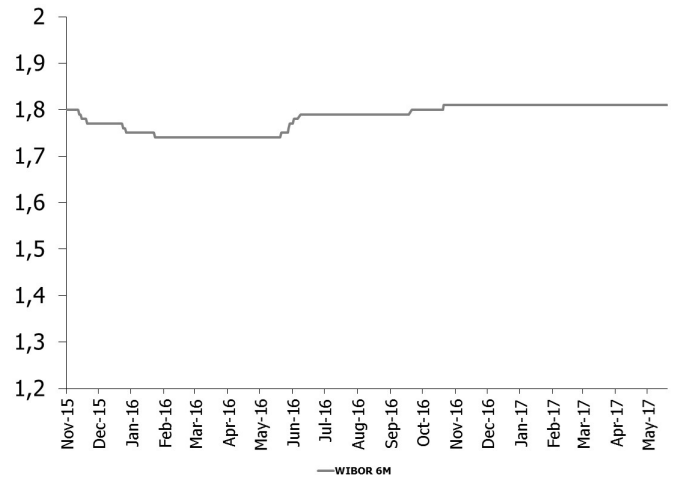
Central banks in the spotlight

Nothing new came from Polish MPC. They are still happy with current rates levels, seeing them as optimal in current economic environment. Governor Glapinski reiterated that in his opinion stable rates can extend through the whole 2018. That's broadly in line with current market pricing. The in comes to ECB, the Governing Council removed stance about chances of lowering rates in the future, apart from the fact that Governor Draghi sounded dovish as always. Next week we have FOMC decision, which might add some volatility to the markets.

Ref rate vs Polonia averages:

30 day -1 bp

90 day 2 bp



Forex

Spot – PLN – tic weaker but still in range EUR/PLN is still meandering in the well-known 4.17 – 4.22 range, but currently is closer to the upper limit. We are having small risk-off period, and the PLN is tic weaker as the result. Potentially more hawkish ECB, the fear of possible impeachment vows in USA and election in the UK are to be blamed for that. One may also add that technical 4.15-4.17 support zone, seems to be rock solid, and EUR/PLN was not able to break the lower bound for weeks. The momentum is still very weak, only a move above 4.23 would legitimize itself. We are still of the opinion of rangy, bit weaker PLN in the weeks to come.

EUR/PLN vols – tic lower Two main vol curves EUR/PLN and USDPLN have stopped sliding, for now. The main reason is the calendar, again. The market is trying to close shorts in Gamma before ECB/FOMC. 1 month EUR/PLN ATM is at 5.70% (0.05% lower), 3 months EUR/PLN are 5,85% (unchanged), and finally 1 year is fixing at 6.40% (0.05% lower). The currency spread (difference of USD/PLN minus EUR/PLN) is better bid, and the skew is roughly unchanged.

Short-term forecasts

Main supports / resistances:

EUR/PLN: 4.15 / 4.25

USD/PLN: 3.70 / 4.00

Spot Current position: Long EUR/PLN at 4.2250 and 4.1850.

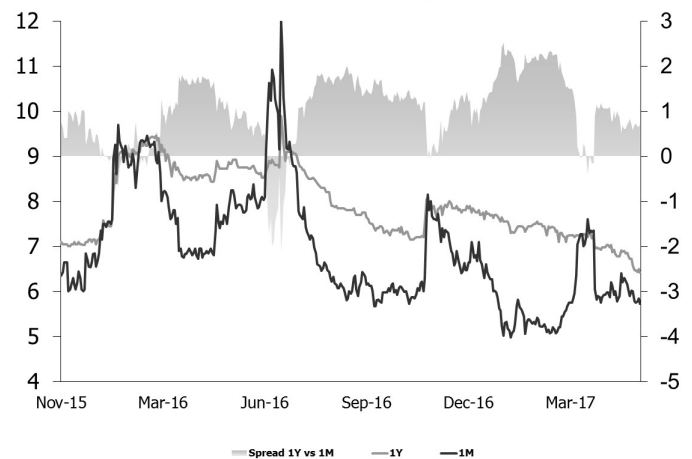
We are still long EUR/PLN, the position is back in the black (again). The price action is still not decisive and we are not holding our breath yet. It is still too early to call it a reverse in the trend. We need a convincing weekly close above 4.23/4.25 to make it look more serious. S/L is still placed at 4.1550 and first target is 4.2600 on the way to ideal target 4.30.

Options Vol – long 3 months and 9 months EUR/PLN.

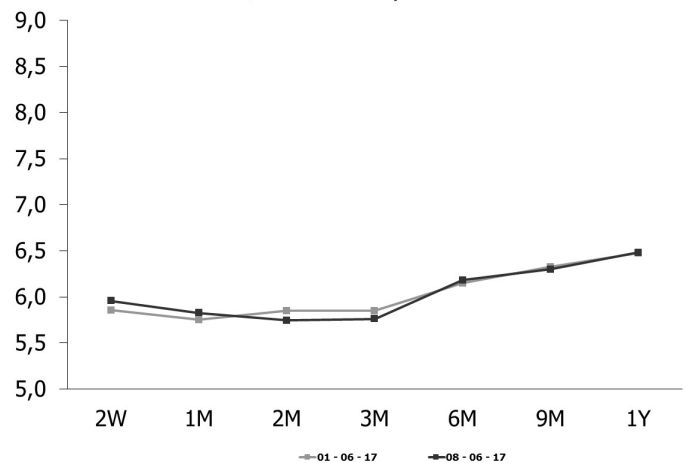
The slide in vols paused, but the realized volatility is still really low. One we got to be really lucky or skilled or both to cover the Theta bills with such a returns. We are keeping the position for the time being, but our time perspective (we wanted to get rid of that position before holidays) is shrinking.



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
6/1/2017	1.82	1.73	1.94	1.71	2.09	1.75	1.73	1.74	1.75	1.79	1.84	1.83
6/4/2017	1.61	1.73	1.71	1.71	1.75	1.75	1.73	1.74	1.75	1.77	1.80	1.82
6/5/2017	1.66	1.73	1.71	1.71	1.76	1.75	1.73	1.74	1.76	1.79	1.82	1.83
6/6/2017	1.69	1.73	1.79	1.71	1.95	1.75	1.73	1.74	1.75	1.78	1.82	1.84
6/7/2017	1.66	1.73	1.71	1.71	1.74	1.75	1.73	1.74	1.75	1.78	1.82	1.83

Last primary market rates							
Paper	Au. date	Maturity	Avg. price	Avg. yield	Supply	Demand	Sold
32W TB	2/22/2017	8/30/2017	99.21	1.50	700	1832	726
OK0419	5/18/2017	4/25/2019	96.43	1.91	250	990	253
PS0422	5/18/2017	4/25/2022	97.75	2.73	1000	2297	972
DS0727	5/18/2017	7/25/2027	93.25	3.29	1000	1454	990

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0715	5Y IRS	PS0718	10Y IRS	DS1023
6/1/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
6/4/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
6/5/2017	1.750	1.474	1.635	1.578	1.960	2.232	2.405	2.949
6/6/2017	1.750	1.474	1.635	1.638	1.990	2.290	2.447	2.985
6/7/2017	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
6/1/2017	5.75	5.85	6.15	6.48	6.48	1.88	0.57
6/4/2017	5.78	5.89	6.05	6.44	6.44	1.88	0.57
6/5/2017	5.85	5.81	6.15	6.50	6.50	1.90	0.49
6/6/2017	5.73	5.81	6.13	6.42	6.42	1.91	0.54
6/7/2017	5.83	5.76	6.18	6.48	6.48	1.90	0.54

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
6/1/2017	4.1834	3.7262	3.8378	3.3534	1.3604	0.1584
6/4/2017	4.1882	3.7323	3.8443	3.3459	1.3584	0.1591
6/5/2017	4.1781	3.7066	3.8471	3.3542	1.3580	0.1589
6/6/2017	4.1916	3.7250	3.8620	3.3948	1.3629	0.1592
6/7/2017	4.1943	3.7241	3.8662	3.4115	1.3593	0.1592

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