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Polish Weekly Review

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Comment on the upcoming data and forecasts

On Tuesday the NBP will publish balance of payments data for March. Like the consensus, we expect a slight narrowing in both current account and trade deficits. However, we forecast much stronger monthly increases in both imports and exports. On Wednesday Statistics Poland will publish flash GDP and final CPI data. The former is likely to show a small decline in annual GDP growth rate – our forecast is a bit more optimistic than market consensus (4.7 v.s 4.4% y/y), but consistent with monthly data and the pan-European pattern of positive surprises in real-sphere data in Q1 (we elaborate on that in the Economics section). CPI data will confirm the flash release of 2.2% y/y and shed more light on the sources of the surprise. On Wednesday afternoon the MPC will end its two-day meeting and announce its monetary policy decisions. Interest rates will be kept on hold and the Council is very unlikely to alter its stance due to stronger inflationary pressures. The recent increases in the CPI will likely be waved off as modest, externally induced and negative for consumer disposable income and consumption (a negative supply shock). Therefore, the NBP governor will continue to sound very dovish. Next Thursday the NBP will publish official core inflation indices. Based on the details of April flash CPI we estimate inflation excluding food and energy to have increased from 1.4 to 1.8% y/y.

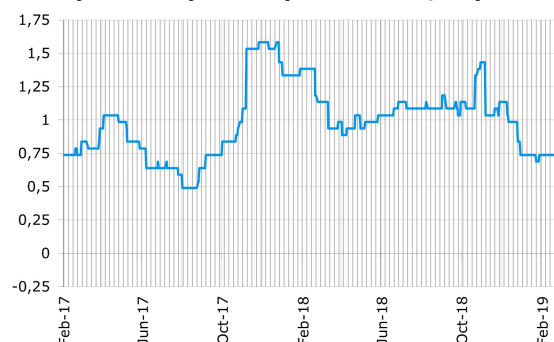
Polish data to watch: May 10th to May 17th

Publication	Date	Period	mBank	Consensus	Prior
Current account (m EUR)	14.05	Mar	-1232	-1001	-1386
Exports (m EUR)	14.05	Mar	20100	19603	18324
Imports (m EUR)	14.05	Mar	21200	20480	19651
Flash GDP y/y (%)	15.05	Q1	4.7	4.4	4.9
Final CPI y/y (%)	15.05	Apr	2.2	2.2	2.2
MPC decision (%)	15.05	May	1.50	1.50	1.50
Core CPI y/y (%)	16.05	Apr	1.8	1.4	1.4

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Yield on the prev auction (%)	Prev auction
T-bill	-	700	1.500	2/22/2017
2Y T-bond OK0521	6/13/2019	1000	1.598	4/25/2019
5Y T-bond PS0424	6/13/2019	1800	2.224	4/25/2019
10Y T-bond DS1029	6/13/2019	1000	2.890	4/25/2019
30Y T-bond WS0447	6/13/2019	60	3.180	4/25/2019
5Y floater WZ0524	6/13/2019	1000	-	4/25/2019
10Y floater WZ0528	6/13/2019	1000	-	4/25/2019

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



Comment

Sharply up after last week's inflation surprise. Next week has two important macro releases: flash GDP and final CPI. Both could move the index again.

* 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

- Polish economy continues to show great resilience to global slowdown and Polish consumers seem unfazed by pretty much anything. We are forecasting 2019 growth at 4.5% y/y and 2020 growth at 4.0% y/y. Recent data proved our earlier revisions to be prescient.
- Core inflation is projected to rise steadily. Meat prices (ASF in China; abruptly increased demand for pork), along with considerable increases in fuel prices (May, June) are set to push inflation beyond NBP target already in 2019.
- The MPC is now talking about holding rates steady until 2021 (the end of most members' term) and – given the overall environment (both global and local factors) – we concur. We don't expect any rate changes in Poland in the foreseeable future, although the rise in inflation may generate some noise from MPC members.
- Increased government transfers and lower taxes presented in February found new sources of financing (revamp of the pension system) and only moderate GG deficits along with falling debt/GDP ratio are secured. Fiscal story returned to positive path in an unambiguous way.

Financial markets

- The PLN proved to be exceptionally resilient in recent months: neither the increase in global rates, nor their subsequent decline and violent repricing of monetary policy expectations managed to break it out of the narrow, 2.5% range vis-a-vis the euro.
- Fiscal stimulation is both a blessing and a curse for the PLN. Over the short term, fiscal stimulus and expectations of a monetary offset should be PLN-positive. New wave of forecast revisions and dovish central banks globally also support PLN strength. However, if no monetary offset arrives and the economy begins to overheat, weaker currency is the only rebalancing mechanism left. For this scenario to play out we need to see inflation. Lots of inflation. With CPI much below 2.5% (for now) the story appeals on to speculative minds.

mBank forecasts

	2015	2016	2017	2018	2019 F	2020 F
GDP y/y (%)	3.8	3.0	4.8	5.1	4.5	4.0
CPI Inflation y/y (average %)	-0.9	-0.6	2.0	1.6	2.4	2.9
General government balance (%GDP)	-2.7	-2.2	-1.4	-0.2	-0.7	-1.1
Current account (%GDP)	-0.6	-0.5	0.2	-0.6	-1.2	-1.4
Unemployment rate (end of period %)	9.8	8.2	6.6	5.9	5.5	4.9
Repo rate (end of period %)	1.5	1.5	1.5	1.5	1.5	1.5

	2018	2018	2018	2018	2019	2019	2019	2019
	Q1	Q2	Q3	Q4	Q1 F	Q2 F	Q3 F	Q4 F
GDP y/y (%)	5.2	5.3	5.2	4.9	4.6	4.5	4.5	4.4
Individual consumption y/y (%)	4.6	4.8	4.4	4.2	4.2	4.1	4.5	4.9
Public Consumption y/y (%)	4.5	4.5	5.2	4.7	4.4	4.2	4.0	4.0
Investment y/y (%)	9.6	6.0	11.3	8.2	5.0	5.0	4.0	3.0
Inflation rate (% average)	1.5	1.7	1.9	1.4	1.2	2.5	2.8	3.0
Unemployment rate (% eop)	6.6	5.9	5.7	5.9	5.9	5.4	5.3	5.5
NBP repo rate (% eop)	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50
Wibor 3M (% eop)	1.70	1.70	1.72	1.72	1.72	1.72	1.72	1.72
2Y Polish bond yields (% eop)	1.49	1.63	1.56	1.35	1.69	1.33	1.35	1.37
10Y Polish bond yields (% eop)	3.18	3.22	3.24	2.83	2.84	2.85	2.96	3.12
EUR/PLN (eop)	4.21	4.37	4.28	4.29	4.30	4.30	4.25	4.25
USD/PLN (eop)	3.42	3.74	3.69	3.74	3.84	3.77	3.70	3.66

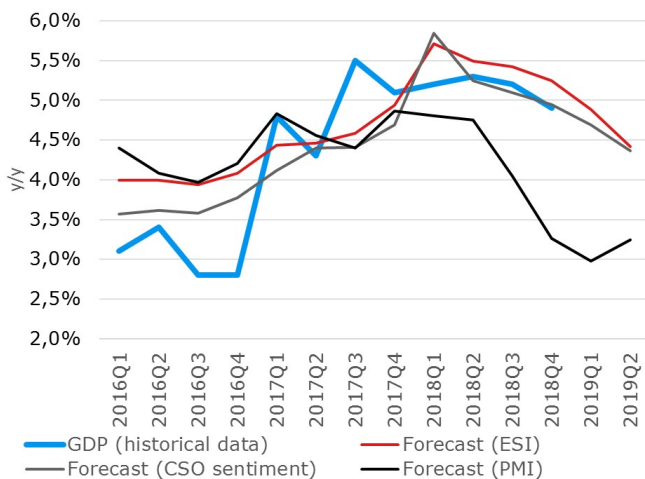
F - forecast

Economics

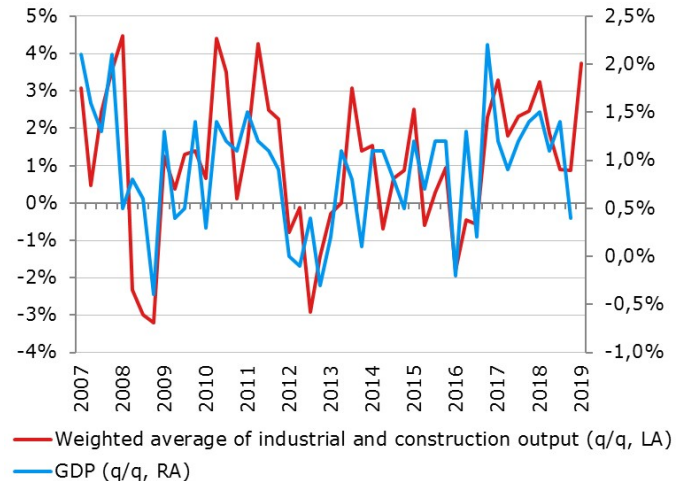
A preview of Q1 GDP

On Wednesday Statistics Poland will publish the flash estimate of Q1 GDP. While some slowdown in annual terms is in order, we believe that the Q1 GDP growth rate will be barely lower than Q4's figure (4.9% y/y). Our fairly optimistic forecast stands at 4.7% y/y (consensus: 4.4% y/y). There are several arguments favoring the upside in Q1 GDP.

First, all monthly indicators suggest that the economy has continued to grow at a fast pace. Our models based on monthly real activity point to a 4.6% growth. However, soft indicators (apart from the PMI which is unreliable in these matters) suggest an upside to these numbers. The range of estimates based on ESI and a similar indicator published by Statistics Poland lies even further to the north (4.7-4.9% y/y). Our final forecast is a compromise between soft and hard data.



Second, this optimism is a sea change from what we suggested at the beginning of the year. However, since the economy has maintained very strong momentum in Q1, our estimates must have been revised steadily upward. Consider that industrial output rose by 3.2% q/q (best quarter since 2006) and construction output advanced by a respectable 5.5% q/q. Weighted average growth of these two sectors was the highest since 2011. As a result, one must expect GDP to grow by more than 1% q/q in Q1, easily making up for the poor Q4 (+0.4% q/q) and matching the result from the first three months of 2018 (1.5% q/q). Hence, base effects will not dampen GDP growth.



Third, Poland has not been the only country in Europe where hard data surprised to the upside in Q1. In fact, the pattern of stronger-than-expected output growth is a pan-European one. German industrial production has only been the latest in the sequence of positive surprises. That pertains to GDP figures as well, and CEE should not be immune to this trend.

The composition of growth in Q1 will not be known until May 31st. However, we can make some educated guesses. Household consumption likely slowed down from 4.3 to 4.1% y/y, which could have been compensated by faster public consumption growth. We forecast investment growth at a hefty 7.5% y/y. With net exports being a drag on growth, buildup in inventories is needed to balance the overall figure. Finally, we should note that it is too early to draw any firm conclusions about the second quarter – very strong monthly figures forecast for April (our estimates: retail sales at 11.3% y/y, construction output at 23% y/y and industrial production at 9.5% y/y) are at odds with the marked deterioration in business sentiment last month (see the first graph). More data is needed, but since the announcement of the fiscal package, Q2 has shaped up to be the weakest in the year. Meanwhile, let's focus on Q1 GDP.

Fixed income

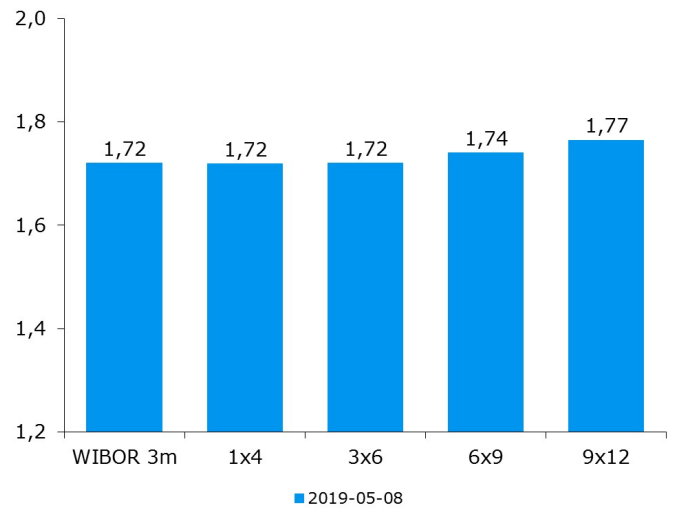
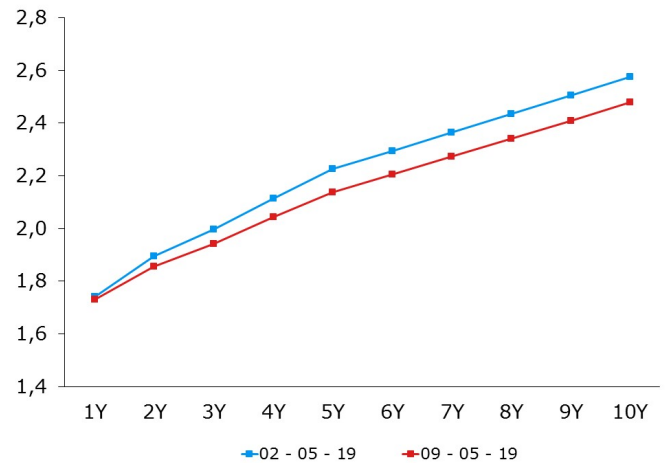
The Yield, or There and Back Again

After weeks of quiet market, we have finally seen some move on Polish rates. CPI was a bit higher than market expected so we moved 15bps on 1/e bonds. The second mover was the US-China meeting, and Trump's comments that moved yields on core markets by 10-15 bps lower. POLGBs stick with the Bund now so yields came back from the last peak. In the end we are a bit higher in yields.

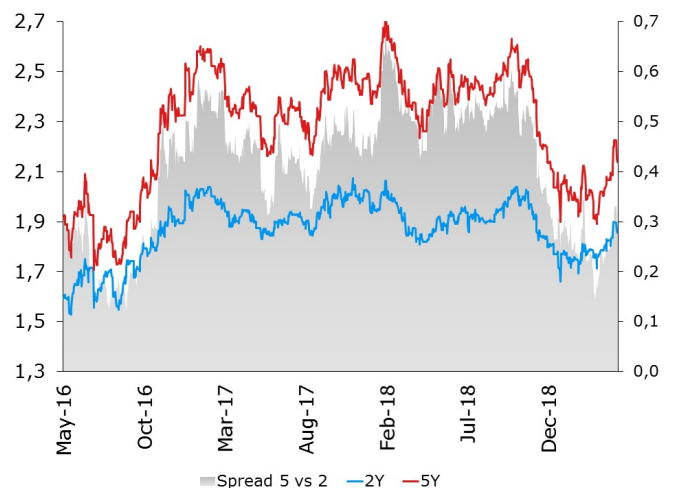
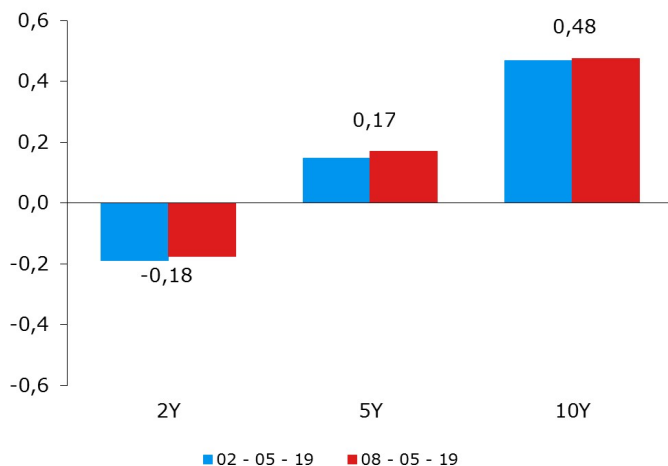
PS0424/5y is 15 bps, WS0428/10y is 36 bps. PS0424/WS0428 is 55 bps. WS0428/Bund is 290 bps.

DS1020 is trading at 1.56% (7 bps up), PS0424 is trading at 2.29% (6 bp up) and WS0428 is trading at 2.84% (3 bps up).

IRS curve



Asset swaps



Money market

Volatility Strikes Back

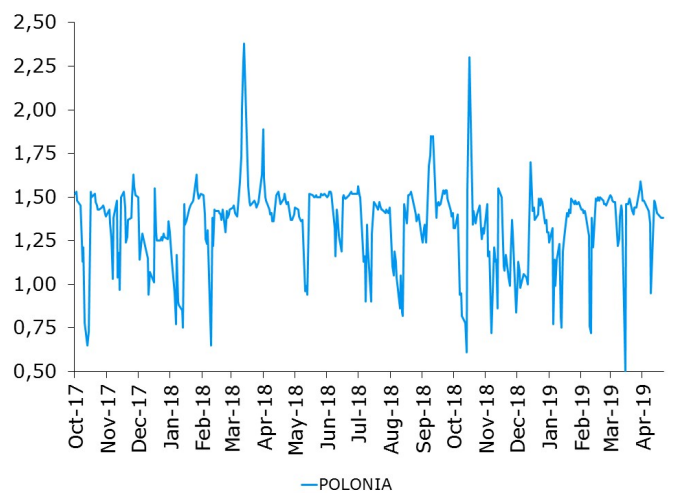
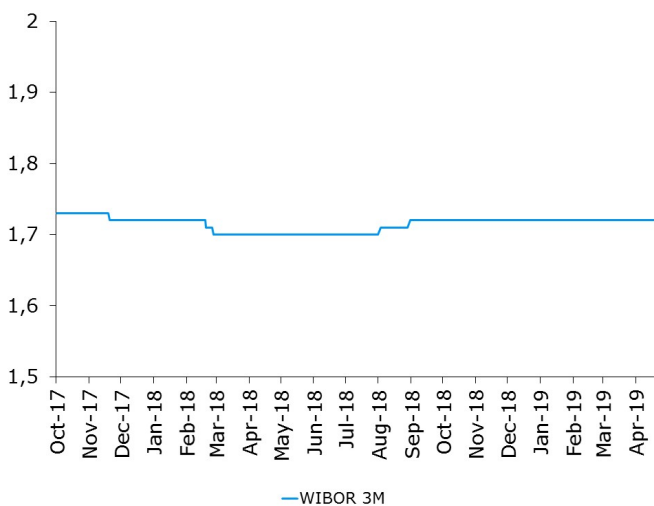
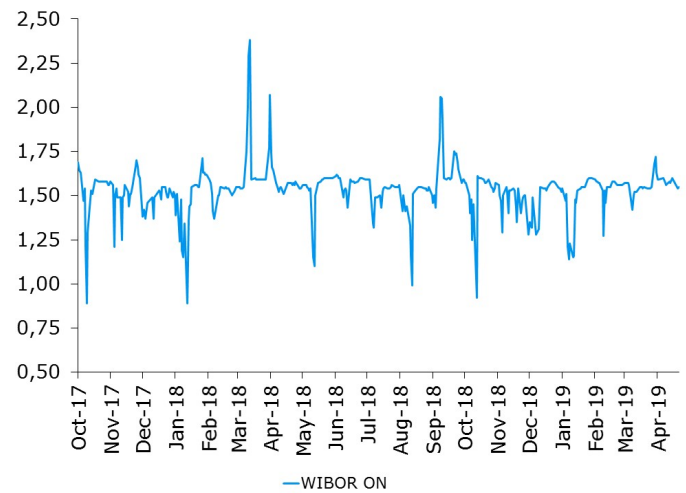
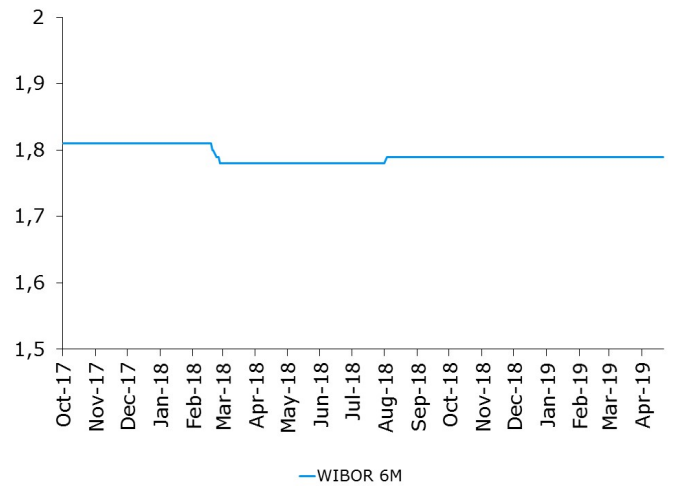
We had some volatility on the market since the last weekly report. That was due to the upside surprise in CPI reading. The figure came out at 2.2% vs 1.8% expected, fueling some expectation for future rate hikes. Swaps topped last week with 2y trading as high as 1.94% and 5y at 2.24%. Since then, core market developments have started to outweigh the local story and we fell to pre-CPI levels. Markets fell a bit in risk-off mode, therefore ASWs are widening a bit, core yields are falling in tandem with stocks. Worse global sentiment is partially due to US-China trade talks escalation.

Cash stable at the beginning of the month. We expect getting closer to 1.50% next week.

Ref rate vs Polonia averages:

30 day 10 bp

90 day 16 bp



Forex

Spot - EUR/PLN - higher in the range This week the backdrop remained weak for Zloty as risk aversion gripped broader markets amid concerns that the US-China trade conflict could escalate. The EUR/PLN spiked to 4.30 from the lazy trading just above the 4.27 support. Finally, it corrected lower during that day, to 4.29-ish. We are still firmly in the wider 4.26-36 range and our strategy to play that range still applies.

Options - implied volatility stable Realized volatility is still on the move down but implied volatility seems to have found its equilibrium at current levels as the curve has not changed much for weeks. 1 month EUR/PLN atm is today at 3.4% (unchanged from last week), 3 month is at 3.65% (unchanged), 1 year is at 4.4% (0.15% lower). The currency spread (difference between USD/PLN and EUR/PLN vol) increased by 0.3%, following higher EUR/USD volatility.

Short-term forecasts

Main supports / resistances:

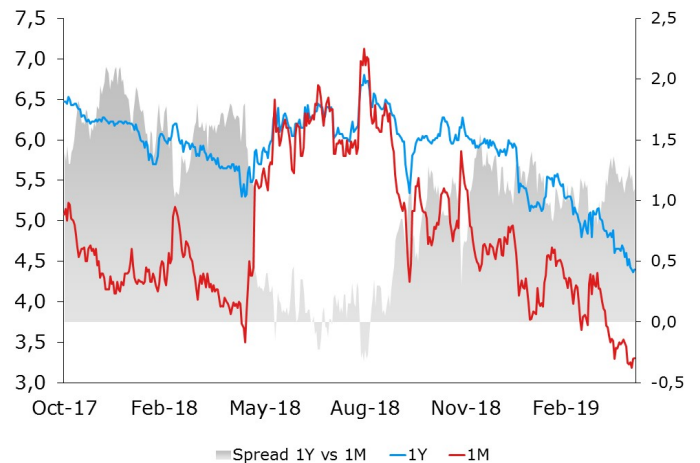
EUR/PLN: 4.2600 / 4.3400

USD/PLN: 3.6000 / 3.9000

Spot - long EUR/PLN at 4.2750

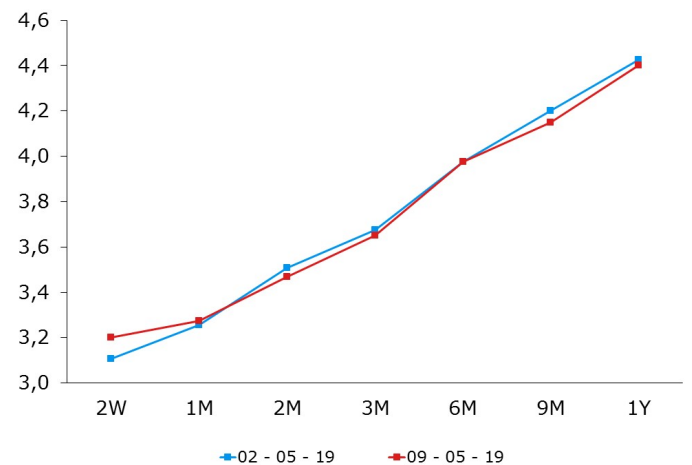
We are ready to add to the position at 4.2400 with stop at 4.2250 and hopes to revisit 4.33. It is a technical / opportunistic trade, as we are looking for the 4.26-4.34 range to hold.

EURPLN volatility



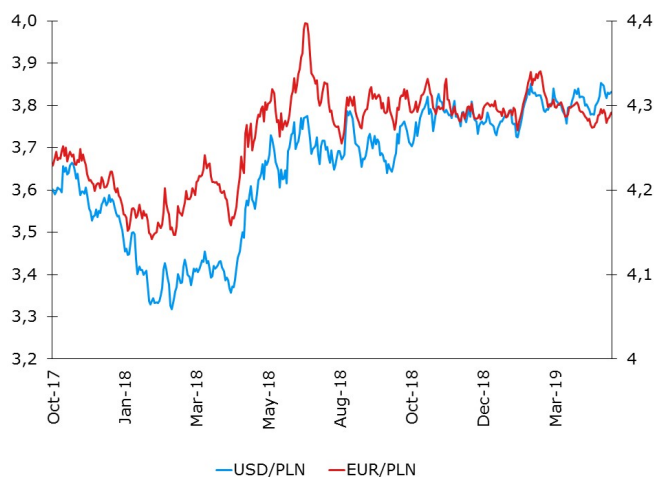
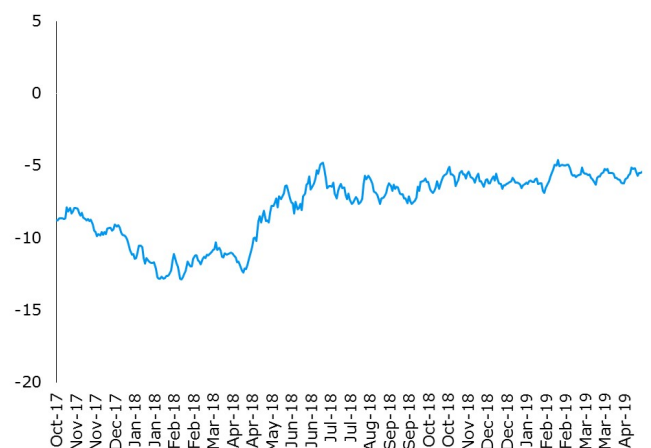
Spread 1Y vs 1M — 1Y — 1M

EUR/PLN volatility curve



02 - 05 - 19 — 09 - 05 - 19

Bias from the old parity (%)



USD/PLN — EUR/PLN

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
5/2/2019	1.70	1.72	1.78	1.69	1.93	1.77	1.72	1.73	1.75	1.79	1.83	1.84
5/5/2019	1.72	1.72	1.80	1.69	1.95	1.77	1.72	1.74	1.75	1.78	1.83	1.83
5/6/2019	1.69	1.72	1.76	1.69	1.92	1.77	1.72	1.73	1.75	1.79	1.83	1.83
5/7/2019	1.59	1.72	1.67	1.69	1.84	1.77	1.72	1.73	1.75	1.77	1.80	1.82
5/8/2019	1.68	1.72	1.75	1.69	1.92	1.77	1.72	1.72	1.74	1.77	1.80	1.82

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
OK0521	4/25/2019	5/25/2021	96.77	1.60	1000	1260	1010
PS0424	4/25/2019	4/25/2024	101.28	2.22	1800	2766	1896
DS1029	4/25/2019	10/25/2029	98.72	2.89	1000	1598	923

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0720	5Y IRS	PS0423	10Y IRS	WS0428
5/2/2019	1.770	1.608	1.895	1.705	2.225	2.373	2.575	3.043
5/5/2019	1.770	1.608	1.895	1.705	2.225	2.373	2.575	3.043
5/6/2019	1.770	1.604	1.895	1.705	2.225	2.359	2.575	3.024
5/7/2019	1.770	1.588	1.865	1.675	2.152	2.324	2.493	2.985
5/8/2019	1.770	1.563	1.855	1.678	2.137	2.308	2.478	2.953

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY
Date	1M	3M	6M	1Y	1M	1Y	1Y
5/2/2019	3.26	3.68	3.98	4.43	4.43	1.40	0.51
5/5/2019	3.19	3.59	3.98	4.40	4.40	1.40	0.51
5/6/2019	3.30	3.59	3.98	4.36	4.36	1.40	0.50
5/7/2019	3.30	3.65	3.98	4.40	4.40	1.40	0.51
5/8/2019	3.28	3.65	3.98	4.40	4.40	1.40	0.51

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
5/2/2019	4.2795	3.8177	3.7480	3.4231	1.3198	0.1669
5/5/2019	4.2795	3.8177	3.7480	3.4231	1.3198	0.1669
5/6/2019	4.2847	3.8313	3.7649	3.4604	1.3238	0.1666
5/7/2019	4.2858	3.8278	3.7583	3.4620	1.3226	0.1666
5/8/2019	4.2914	3.8325	3.7654	3.4793	1.3226	0.1668

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