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## Polish Weekly Review

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### Comment on the upcoming data and forecasts

Week begins with NBP's official core inflation data. After last Friday's detailed CPI data, we are forecasting 0.3% growth (slightly below our original forecast). On Wednesday GUS will publish monthly data from the labor market. While employment is set to remain boring, with y/y growth stuck at 1.0%, some variation is expected with respect to wage growth. According to our forecasts, wage growth likely slowed down in October, mainly due to high statistical base in manufacturing, construction and support services. Thursday's data on industry and trade will also show slowing economic activity in October: here the main culprit is a negative working day effect. Nominal retail sales was also dragged down by low food and fuel prices, in our view. Last but not least, very low statistical base in energy prices likely boosted annual PPI growth.

### Polish data to watch: November 16th to November 20th

Publication	Date	Period	mBank	Consensus	Prior
Core CPI y/y (%)	16.11	Oct	0.3	0.3	0.2
Average gross wage y/y (%)	18.11	Oct	3.1	3.6	4.1
Employment y/y (%)	18.11	Oct	1.0	1.0	1.0
Sold industrial output y/y (%)	19.11	Oct	1.5	2.5	4.1
PPI y/y (%)	19.11	Oct	-2.3	-2.5	-2.9
Retail sales y/y (%)	19.11	Oct	-0.8	0.5	0.1

### Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Yield on the prev auction (%)	Prev auction
52 Week T-bills	-	3000	3.485	3/4/2013
2Y T-bond OK0717	11/19/2015	1000	1.770	10/29/2015
5Y T-bond PS0720	11/19/2015	3000	2.317	10/29/2015
10Y T-bond DS0726	11/19/2015	2000	3.076	10/29/2015
15Y T-bond WS0428	-	20	2.092	3/12/2015

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



#### Comment

Flash GDP came out close to market consensus and hence did not impact our surprise index. Next week is all about labor market, industry and trade data – plenty of opportunities for the index to move in both directions.

\* 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

- GDP growth is set to stay close to 3% per annum.
- Downside risks prevail near term. However, until only selected business tendency indicators are decreasing, Poland is expected to escape a deeper slowdown. Exports is going to be weaker due to international developments, investment activity may be negatively affected by the unanticipated fall of future demand. At the same time consumption is to maintain 3% growth (labor market is tight, households have resources to smooth consumption over time). The schedule for infrastructure spending suggests a steep path of outlays from the turn of 2015/2016 onwards. At this stage it is more likely that outlays will be postponed for later part of 2016.
- Given the schedule of infrastructure spending and stable consumption growth, many years of economic expansion are still our baseline scenario for the Polish economy. The upswing can be flatter than we historically got used to but longer. Such an outcome almost guarantees that the likelihood of bottlenecks in the economy is small.
- 3% growth is sufficient to keep inflation and credit risk in check. Global headwinds and low commodity prices are set to further underpin deflationary environment. Headline inflation is going to slowly rise only on the back of statistical base.
- We expect lower rates in 2016 as the new MPC is set to be more responsive for weaker environment amid global trends for monetary stimulation. Moreover, the new parliament is set to have inclination towards selecting more dovish MPC members.

### Financial markets

- Polgbs – near term still neutral (cash). Rate cuts are already priced in, uncertainty surrounding fiscal policy is still an issue, bonds are sensitive to potential monetary tightening in the US.
- We think that POLGBs may still have potential mid-term as monetary stimulus (ECB) is waiting in the wings and the new government is likely to push for easier monetary policy that ultimately will be delivered. Ultimately, we think fiscal worries will prove overdone.
- Pro-active ECB stance should be enough to shield the zloty from sharp depreciation in case of higher risk aversion. We see zloty stronger mid-term on solid growth story and differentiation flows. Political risk and potential for easier monetary policy may linger for some days. However, as much of it has already been consumed, we neutralize our outlook and opt for more balanced trading around 4.20.

### mBank forecasts

	2011	2012	2013	2014	2015F	2016 F
GDP y/y (%)	5.0	1.6	1.3	3.3	3.3	3.1
CPI Inflation y/y (average %)	4.3	3.7	0.9	-0.1	-0.8	1.5
Current account (%GDP)	-4.9	-3.5	-1.3	-1.2	-0.6	-1.0
Unemployment rate (end of period %)	12.5	13.4	13.4	11.5	10.0	8.9
Repo rate (end of period %)	4.50	4.25	2.50	2.00	1.50	1.00

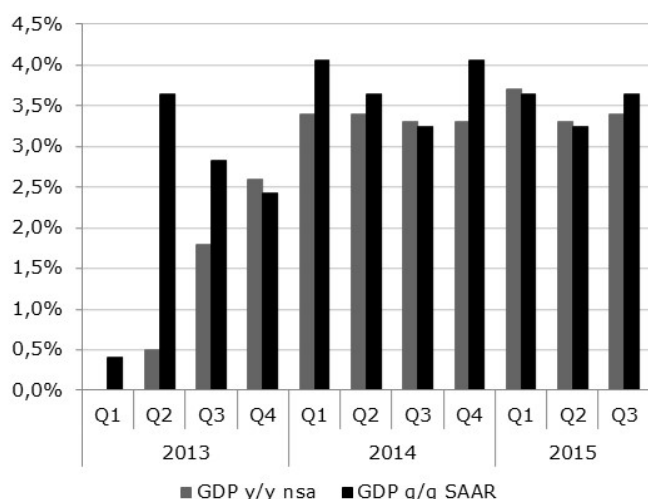
	2015 Q1	2015 Q2	2015 Q3 F	2015 Q4 F	2016 Q1 F	2016 Q2 F	2016 Q3 F	2016 Q4 F
GDP y/y (%)	3.6	3.3	3.1	3.1	3.0	3.0	3.1	3.2
Individual consumption y/y (%)	3.1	3.0	3.0	3.2	3.2	3.3	3.2	3.0
Public Consumption y/y (%)	3.3	2.4	2.5	1.5	1.5	1.5	1.5	1.5
Investment y/y (%)	11.4	6.4	6.5	5.5	4.5	6.5	7.0	7.0
Inflation rate (% average)	-1.4	-0.9	-0.7	-0.3	0.5	0.6	0.5	0.9
Unemployment rate (% eop)	11.5	10.2	9.7	10.0	10.6	9.4	8.9	9.0
NBP repo rate (% eop)	1.50	1.50	1.50	1.50	1.25	1.00	1.00	1.00
Wibor 3M (% eop)	1.65	1.72	1.73	1.70	1.44	1.20	1.20	1.20
2Y Polish bond yields (% eop)	1.61	1.99	1.76	1.45	1.35	1.35	1.35	1.35
10Y Polish bond yields (% eop)	2.31	3.31	2.84	2.70	2.50	2.50	2.50	2.50
EUR/PLN (eop)	4.07	4.19	4.25	4.15	4.15	4.15	4.15	4.15
USD/PLN (eop)	3.80	3.76	3.80	3.92	3.99	4.07	4.07	4.03

F - forecast

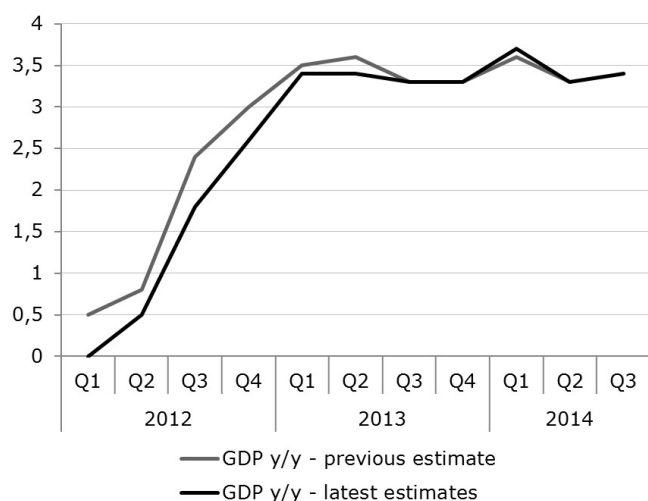
## Economics

### Flash GDP suggests stable growth in the coming quarters

According to the flash estimate, GDP grew by 3.4% y/y in the third quarter, slightly above market expectations and our forecast. The seasonally adjusted data suggest that the economy grew by 0.9% q/q, right in the middle of last two years' range of 0.8-1.0%.



The data is roughly consistent with predictions from models based on high frequency data (3.2-3.3% y/y). We ourselves have assumed a lower growth rate, mainly due to lower consumption growth (marked deceleration in real retail sales) and small rebound in investment after the weak second quarter. In current circumstances we cannot assess whether our assumptions were correct. The low (and negative) contribution from net exports could well be matched by an increase in inventories (to be expected if a slowdown in demand was not anticipated by consumers and businesses – this is precisely what business tendency indicators showed) or faster public consumption growth.

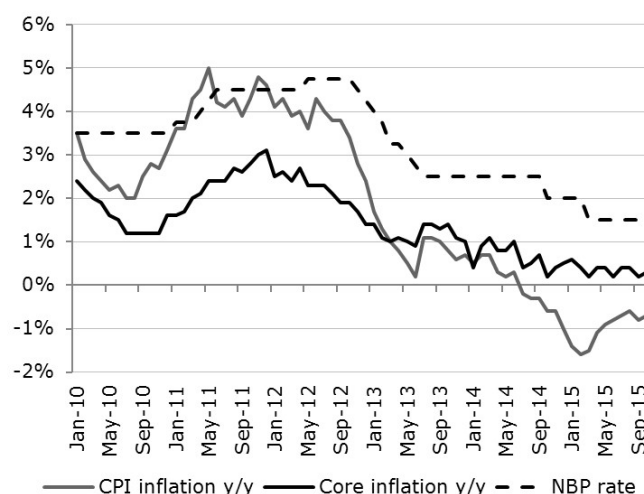


In the coming quarters we still expect a stable GDP growth path. Initial GDP estimates from GUS often point to such a path. Only later do we learn that business cycle fluctuations were more pronounced; take a look at 2013 Q1 for instance – after more than

two years we have just learned that the economy stagnated on annual basis (vs. +0.5% y/y previously estimated). That does not mean that there is a slowdown and GUS is (so far) unable to show it in GDP data. On the contrary – we simply want to clarify that with monthly data coming up still on a weaker side (uncertainty, sluggish global growth, relatively strong zloty), the economy is set to cruise along a flat trajectory. Not fast enough to change the current status quo in inflation and interest rate forecasts.

### Sixteenth month of deflation

Final reading of inflation came slightly lower than the flash one, at -0.7%, as we initially expected. Therefore, October marked the sixteenth consecutive month with annual negative price growth.



As for the breakdown, food prices went slightly up by 0.3% m/m, reflecting to some degree the lagged effects of higher prices in September. Overall, however, food prices growth was almost normal and local drought effects petered out. Fuel prices went down by 2.2% m/m. Core prices came out low. It was sufficient to raise core inflation from 0.2% to 0.3% but price momentum stays stubbornly low. Trends in food prices, fuels and absolute lack of domestic inflation pressure imply that saying goodbye to low inflation will take a little longer and 2016 will still be marked by inflation hovering barely above zero.

The moment price growth turns positive is going to fall in December or January. November is likely to see inflation at -0.3% y/y. It is of minor importance for monetary policy, though. Interest rate cut expectations hinge on new MPC nominees (dovish) amid slow global economy, low inflation and considerations concerning European monetary policy synchronization. Our forecast assumes 50pb cuts, which are already priced in. In our opinion, volatility of the short end of the yield curve is set to be rather low. Only big time events can turn rate cuts expectations around.

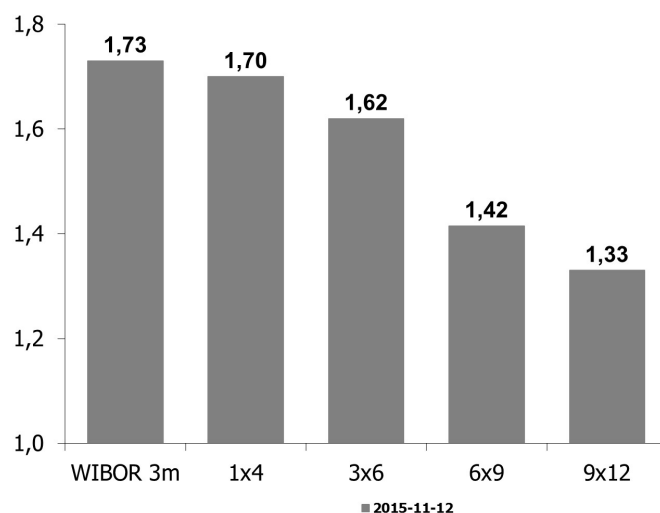
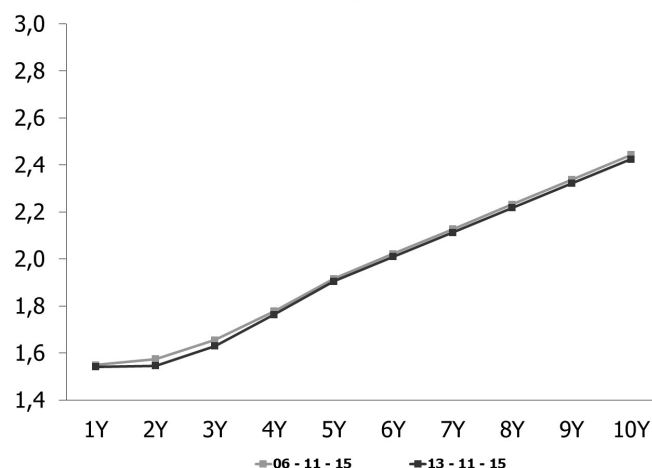
## Fixed income

### Rollercoaster

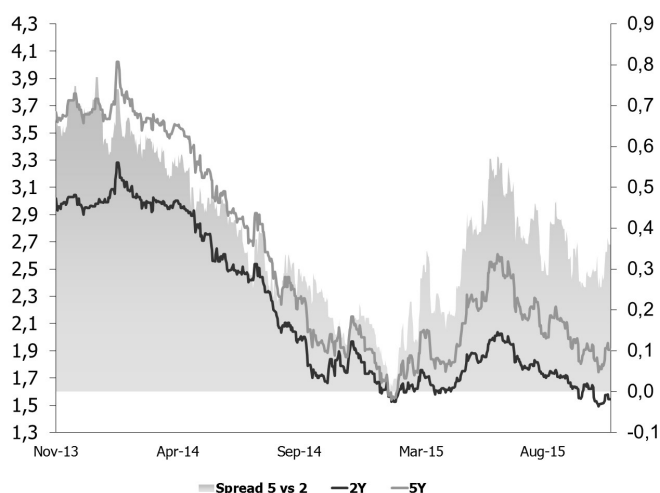
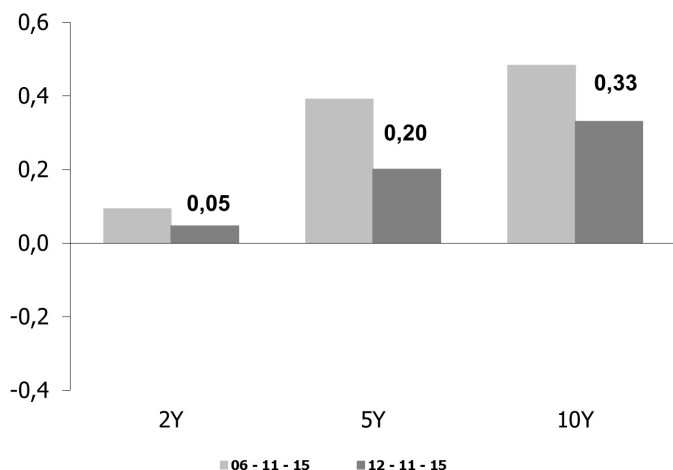
After better than expected non-farm payrolls data last week, Polish 5y IRS touched 2.00%. That seemed to be a previous peak together with 55-day moving average level. Unable to break that resistance, the market became more sensitive to any weaker global data that finally led to unexpected fallback to the October lows. The downtrend seemed to be fueled also by the broadly speculated lower GDP reading (around 3.1%). Surprisingly, the data came out much stronger and that drop in yields have found its support.

We feel like riding on a rollercoaster for the last couple of weeks and do not expect any significant change in trading mood in the near future especially as the market is heading to the end of a financial year. Moreover, the market seemed to fully price in the 2016 monetary easing so we would not see any further value in receiving almost anything on a curve. We would prefer to look for a short term value on a yield curve for a time being. The current risk – reward scenario looks favorable for paying rates.

IRS curve



Asset swaps



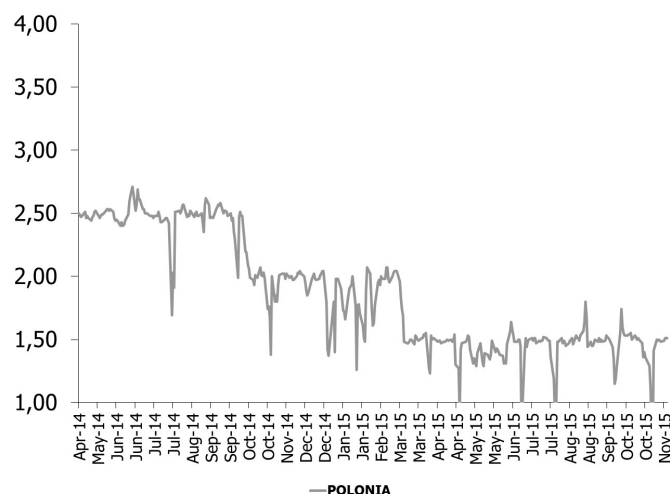
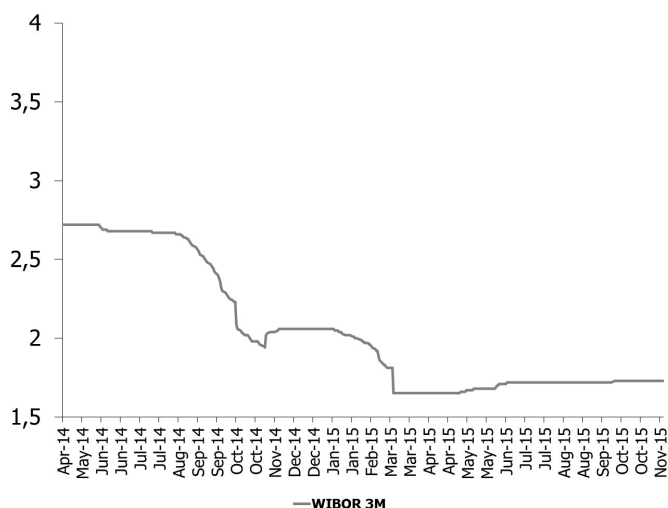
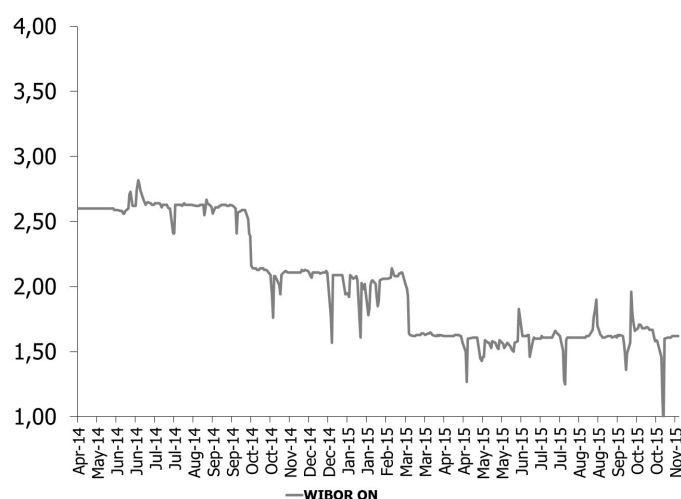
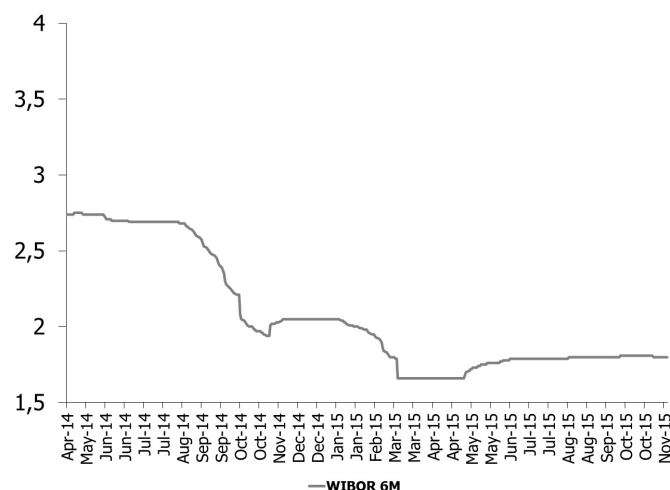
## Money market

### Stable week behind us

Stable week on the cash market. Polonia fluctuated around 1.50 for the whole week.

After last Friday's, the NFP whole curve moved up, even the shortest end. 9x12 FRA moved to 1,40, 6x9 to 1,48. As market stabilized, rates have started to fall since Monday, reaching 1,35 and 1,41 on Thursday, discounting almost 50 bps rate cuts in 2016. Situation looks the same on the OIS market. 1Y OIS is now around 1,25.

We suggest buying the whole front end (FRAs and OISs) as rate cuts are still not certain. Hedge it by cheap (in our opinion) short bonds (especially OK0717 looks interesting with yield around 1,58).



## Forex

**PLN – even stronger** EUR/PLN moved from 4.2750 (last Monday's high) to 4.2070 low this week on market expectations that the new government would scale back its pre-election (fiscally costly) promises together with the extension of the ECB QE program. On Friday EUR/PLN bounced off the lows up to 4.2460 where we started to see sellers. The elections has removed some political uncertainty, but we still need to wait and see what the first decisions of the freshly constituted government will be. Some of the projects, like the financial transactions tax or the Presidential CHF loan bill, are quite market-shaking. We still believe in the rangy nature of EUR/PLN, currently 4.20-4.32.

**Options – Consolidation** It was a very calm week on the options market. The positive correlation between spot and the level of volatilities didn't work. Spot PLN was stronger but implied volatilities stood firmly unchanged as though market was awaiting the mammoth events in December (ECB and FOMC decision). EUR/PLN implied volatilities are at the same levels as a week before: 1 month EUR/PLN ATM is this Friday 6.5%, 3 months are 6.6%, and finally 1 year is 7.1%. The Skew was roughly unchanged. The currency spread (difference between USD/PLN vol and EUR/PLN vol) was traded at the levels as week before – ca. 5.0%.

## Short-term forecasts

Main supports / resistances:

EUR/PLN: 4.20 / 4.32

USD/PLN: 3.70 / 4.00

**Position** Spot – long EUR/PLN .

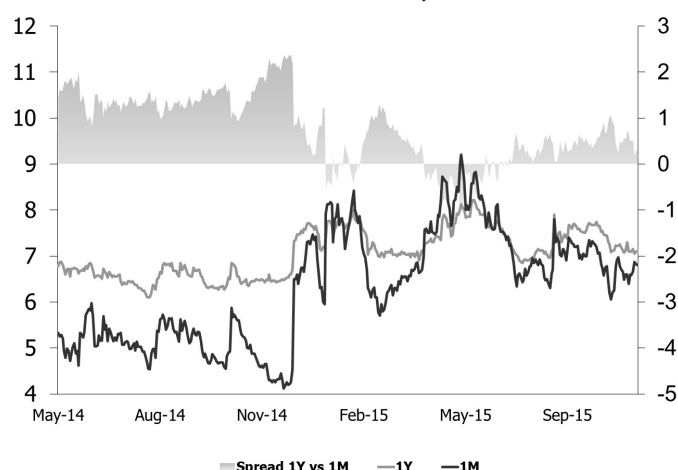
We added at 4.22 to our long position from previous week, so finally we are long at average 4.23 with a stop below 4.20 and hopes to revisit 4.28/4.29. Our central scenario is still to play the rangy nature of EUR/PLN. Nevertheless the political risks are clearly looming on the horizon and that supports short PLN positions.

## Options – we are long 1 year Vega against 3 months (Vega neutral)

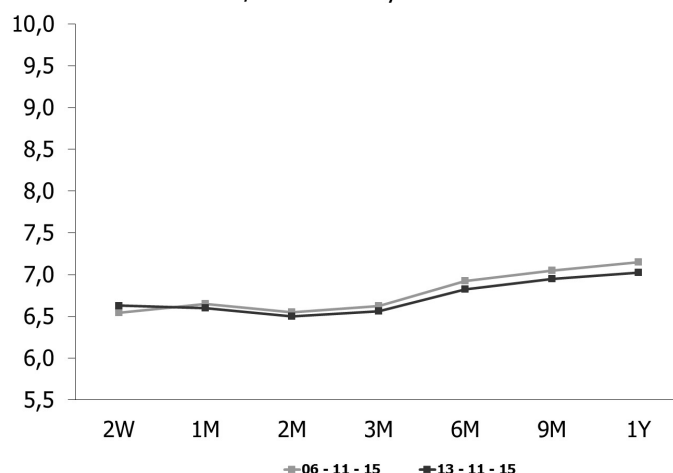
We are of the opinion that party that have won the elections would act more prudent as they will be taking full responsibility for the country. Hence, that would temper some of its promises and Poland's generally healthy fundamentals will prevail. The looser fiscal conditions may influence us negatively in the future and that is the reason to be long 1 year ATM.



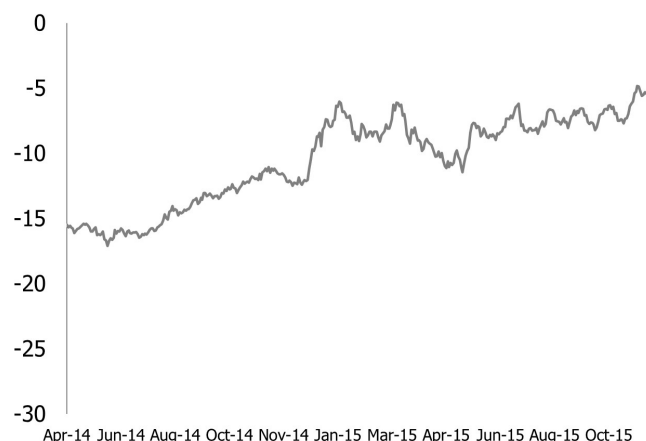
EURPLN volatility



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
11/5/2015	1.78	1.73	1.69	1.70	1.71	1.73	1.70	1.62	1.46	1.37	1.39	1.46
11/9/2015	1.78	1.73	1.82	1.70	1.71	1.73	1.71	1.63	1.48	1.40	1.44	1.49
11/10/2015	1.78	1.73	1.83	1.70	1.72	1.73	1.70	1.62	1.45	1.37	1.41	1.47
11/11/2015	1.68	1.73	1.63	1.70	1.68	1.73	1.70	1.62	1.45	1.37	1.41	1.47
11/12/2015	1.76	1.73	1.83	1.70	1.72	1.72	1.70	1.62	1.42	1.33	1.34	1.43

Last primary market rates							
Paper	Au. date	Maturity	Avg. price	Avg. yield	Supply	Demand	Sold
52W TB	3/4/2013	8/28/2013	98.33	3.49	3000	7324	3084
OK0716	4/23/2014	7/25/2016	93.51	3.02	800	2136	836
PS0719	5/8/2014	7/25/2019	99.25	3.41	4000	5807	4075
DS1025	6/5/2014	7/25/2025	94.90	3.82	2000	2743	1693

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0715	5Y IRS	PS0718	10Y IRS	DS1023
11/5/2015	1.730	1.612	1.531	1.621	1.835	2.170	2.372	2.808
11/9/2015	1.730	1.626	1.580	1.689	1.956	2.314	2.486	2.948
11/10/2015	1.730	1.632	1.545	1.621	1.905	2.181	2.425	2.845
11/11/2015	1.730	1.632	1.545	1.621	1.905	2.181	2.425	2.845
11/12/2015	1.720	1.623	1.545	1.592	1.905	2.106	2.425	2.755

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY	
Date	1M	3M	6M	1Y	1M	1Y	1Y	
11/5/2015	6.59	6.58	6.83	7.10	7.10	1.93	0.50	
11/9/2015	6.88	6.55	6.75	7.05	7.05	1.93	0.50	
11/10/2015	6.83	6.73	6.88	7.10	7.10	1.91	0.50	
11/11/2015	6.80	6.73	6.88	7.10	7.10	1.93	0.50	
11/12/2015	6.60	6.56	6.83	7.03	7.03	1.92	0.50	

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
11/5/2015	4.2306	3.8925	3.9062	3.1940	1.3462	0.1564
11/9/2015	4.2651	3.9605	3.9464	3.2058	1.3538	0.1578
11/10/2015	4.2485	3.9570	3.9435	3.2133	1.3557	0.1571
11/11/2015	4.2485	3.9570	3.9435	3.2133	1.3557	0.1571
11/12/2015	4.2245	3.9434	3.9263	3.2054	1.3537	0.1563

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