

August 22, 2019

Polish Weekly Review

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Comment on the upcoming data and forecasts

Tomorrow M3 data will be published – we do not expect any significant changes compared to the previous months (forecasting 9.1% y/y growth). Next Friday, Statistics Poland will publish final GDP reading for 2Q with its components. According to flash estimate Q2 GDP growth slowed down to 4.4% y/y from 4.7% in the 1st quarter. We forecast slight acceleration (compared to Q1) in private consumption (from 3.9 to 4.1%) and moderately lower investment growth (down from 12.6 to 8-8.5%). Public consumption likely offered strong support for GDP growth (about 6.0%). Exports data suggest a positive net exports contribution (+0.4 pp.), which could be countered by the negative change in inventories (-0.6 or even -1 pp.). On the same day flash CPI reading for August will be published (final forecast with a more detailed comment will be provided in the next weekly report). We do not, however, expect a significant deviation from July's reading of 2.9% y/y.

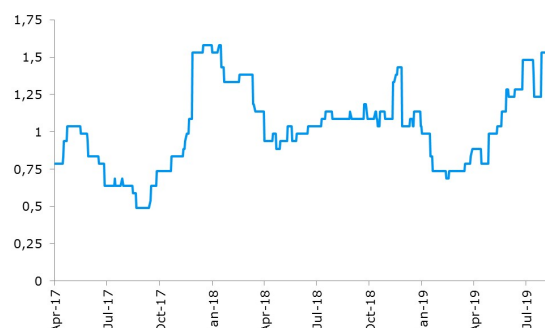
Polish data to watch: August 23rd to August 30th

Publication	Date	Period	mBank	Consensus	Prior
M3 y/y (%)	23.08	Jul	9.1	9.5	9.3
GDP y/y final (%)	30.08	Q2	4.4	4.4	4.7
CPI y/y flash (%)	30.08	Aug			2.9

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	9/5/2019	300	1.445	7/26/2019
5Y T-bond PS1024	9/5/2019	2000	1.823	7/26/2019
10Y T-bond DS1029	9/5/2019	1500	2.100	7/26/2019
30Y T-bond WS0447	9/5/2019	60	3.180	4/25/2019
5Y floater WZ0525	9/5/2019	2500	-	7/26/2019
10Y floater WZ0529	9/5/2019	2100	-	7/26/2019

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



Comment

There were no major surprises in macro releases published last two weeks (final inflation confirmed the flash reading, GDP in line with market consensus as well as labor market, production and retail sales data). Until next Friday surprise index should also remain unchanged.

* 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. Additionally, private investment finally arrived and fiscal stimulus will hit consumers' wallets in the second half of the year. However, the protracted weakness in external demand and problems in the construction sector are forcing us to downgrade our GDP growth forecasts. The economy will grow by 4.6% this year (prev. 5.0%) and 4.0% in 2020 (unchanged).
- Core inflation is projected to rise steadily. The combination of high food prices and base effects are set to push inflation above target in the year's end. The issue of electricity prices will make its comeback in January. Therefore, inflation might accelerate even further at the beginning of 2020.
- The MPC is now talking about holding rates steady through 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. The on-going rise in inflation may generate some noise from MPC members, though. It is more likely to be on the dovish side.
- This year's fiscal deficit is set to widen due to brisk expenditure growth. Nevertheless, revenue growth remains solid and fiscal policy will likely be tightened after the elections. Polish fiscal story remains positive.

Financial markets

- Global growth worries, strong dollar and thin liquidity are a toxic combination for the PLN. The result was marked weakening in recent weeks. The worst is over in our view.
- We see stronger PLN along the way. New wave of global monetary easing makes Polish rates relatively higher and the economy is holding very well given the global slowdown of economic activity.

mBank forecasts

	2015	2016	2017	2018	2019 F	2020 F
GDP y/y (%)	3.8	3.0	4.8	5.1	4.6	4.0
CPI Inflation y/y (average %)	-0.9	-0.6	2.0	1.6	2.4	3.0
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	5.4	5.1
Repo rate (end of period %)	1.5	1.5	1.5	1.5	1.5	1.5

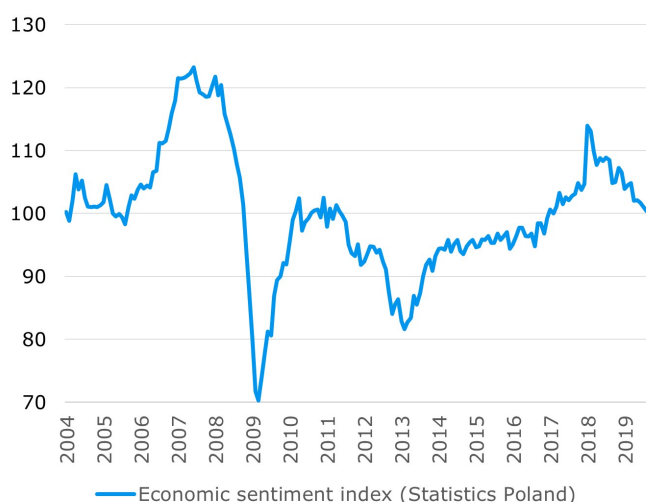
	2018 Q1	2018 Q2	2018 Q3	2018 Q4	2019 Q1	2019 Q2 F	2019 Q3 F	2019 Q4 F
GDP y/y (%)	5.2	5.3	5.2	4.9	4.7	4.4	4.5	4.8
Individual consumption y/y (%)	4.6	4.8	4.4	4.2	3.9	4.1	4.4	4.7
Public Consumption y/y (%)	4.5	4.5	5.2	4.7	6.4	6.4	6.4	6.4
Investment y/y (%)	9.6	6.0	11.3	8.2	12.6	8.5	7.5	6.5
Inflation rate (% average)	1.5	1.7	1.9	1.4	1.2	2.4	2.8	3.0
Unemployment rate (% eop)	6.6	5.9	5.7	5.9	5.9	5.2	5.2	5.4
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	1.61	1.52	1.52
10Y Polish bond yields (% eop)	3.18	3.22	3.24	2.83	2.84	2.39	2.00	2.20
EUR/PLN (eop)	4.21	4.37	4.28	4.29	4.30	4.24	4.20	4.20
USD/PLN (eop)	3.42	3.74	3.69	3.74	3.84	3.73	3.68	3.62
F - forecast								

Economics

Weak July data prompted us to lower our 2019 GDP forecast, but overall scenario is unchanged

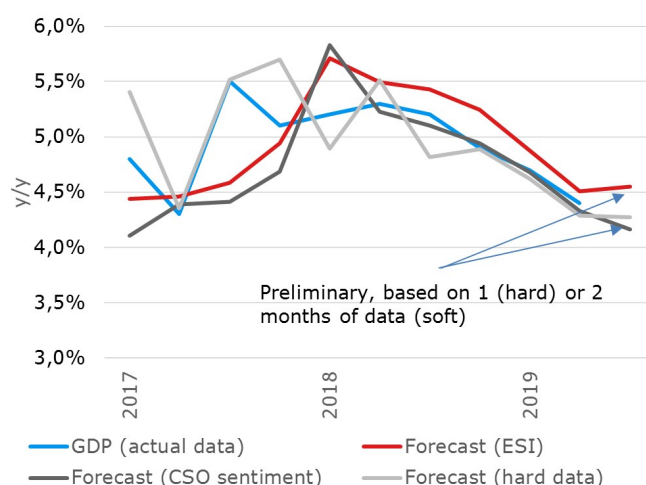
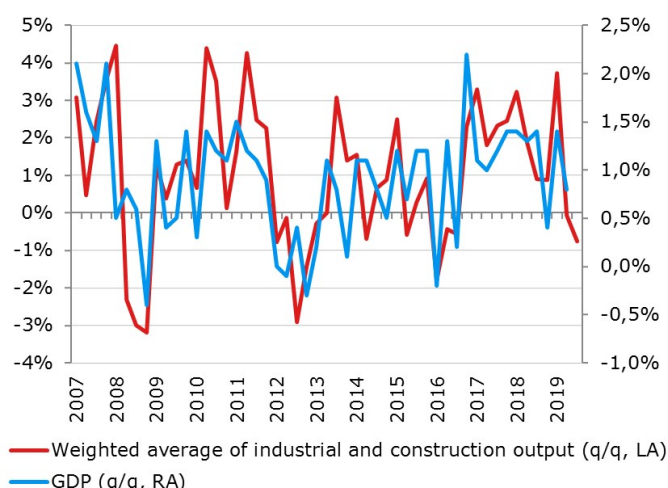
Forecast revisions are generally procyclical (positive in up-swings, negative in downturns), it should not be surprising that it's been some time since we last downgraded our GDP growth forecasts for Poland. The last time this happened to our current-year forecasts was in 2017. However, circumstances are forcing us to cut our GDP forecasts for 2019 moderately. We now forecast the Polish economy to grow by 4.6% this year (prev. 5.0%). The overall story is unchanged, though. Strong domestic demand, led by private and public consumption and private investment, will shield the Polish economy from the worst effects of the global slowdown. As a result, Poland is set to outperform the euro area by one of the widest margins in history. Below you can find the brief summary of our thinking.

First, Poland has never been completely immune from the slowdown in external demand. GDP growth peaked at the turn of 2017 and 2018 and business sentiment peaked in January 2018. Since then, broad business sentiment indicators have been in a gentle downtrend (see the graph below). As we repeatedly noted, this is a much more accurate measure of activity than the Polish PMI. Currently, the indicators suggest that GDP growth slowed down to 4.2-4.4% in the third quarter.

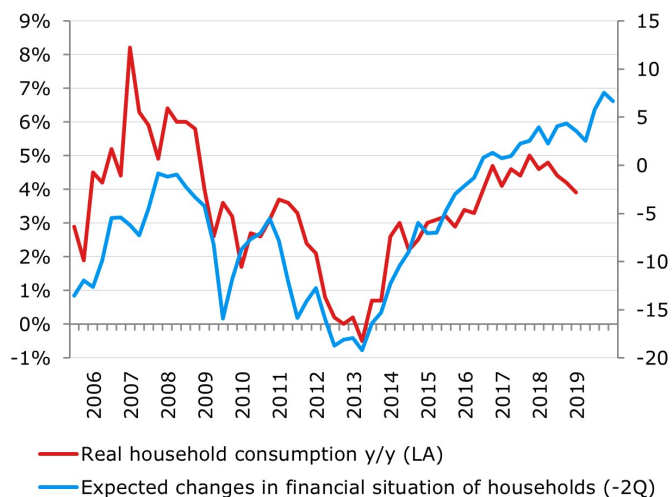


Second, hard data on economic activity have turned for the worse in June, with multi-year lows in industrial and construction output growth. At the time, we pointed out one-off factors (timing of schoolyear end, working day count, heat wave) that played the decisive role in reducing working time and dampening activity and suggested that July data will bring a decisive rebound. This, however, happened only partially and all main real activity indicators fell short of our expectations: industrial output accelerated from -2.7 to 5.8% y/y (mBank: 7.2% y/y); construction output accelerated from -0.7 to 6.6% y/y (mBank: 10.9% y/y); retail sales from 3.7 to 5.7% y/y (mBank: 7.5% y/y). We conclude that there is some genuine weakness in real activity, which can be traced back to weak external demand and waning public investment surge. As a result, Q3 started on a negative note (see the graph below) and the momentum of Polish economy has dropped to a fresh 3-year low. While next two months are likely to improve on this performance, GDP growth is unlikely

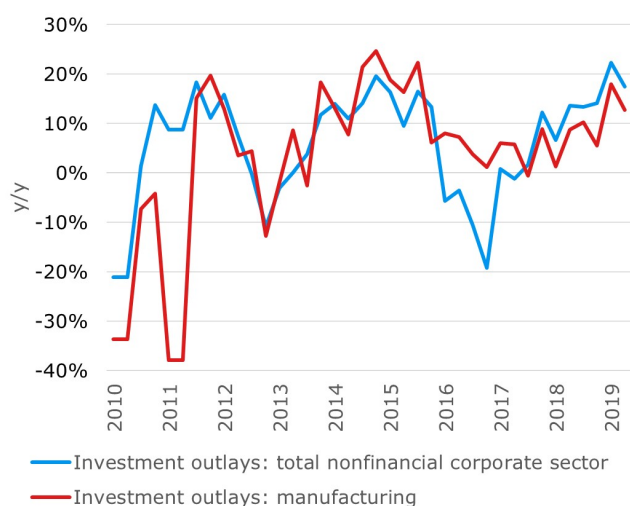
to be materially different from Q2's figure of 4.4% y/y.



Third, the strongest part of the Polish economy is still the consumer. His (or her) behavior also holds the key to the overall performance of the economy in the second half of the year. Fresh consumer sentiment data indicate that households continue to assess their financial situation positively and their optimism is hovering slightly below all-time high. As one of the few truly leading indicators, consumer sentiment points to acceleration in household consumption in the second half of the year. The main reason seems to be the fiscal stimulus (expanded child subsidy programme and PIT rate cut) that will be hitting the consumers' wallets soon. Two consecutive disappointments in retail sales data do not change our view on the matter and we should note that: (1) retail sales slowed only marginally from 2017/18 highs; (2) spending on services was an important driver of recent consumer boom and as such is not included in retail sales figures.



Last but not least, the recovery in private investment is continued in Q2. Total investment of nonfinancial corporations rose by 17.5% y/y in Q2 (down slightly from Q1's 22.3% y/y) and sectors dominated by private enterprises performed well – the largest of them, manufacturing, clocked a 13% increase in investment. Private investment cycles are typically quite long and that bodes well for this year's investment growth. Firms' activity will cushion the slowdown in public investment.



Fixed income

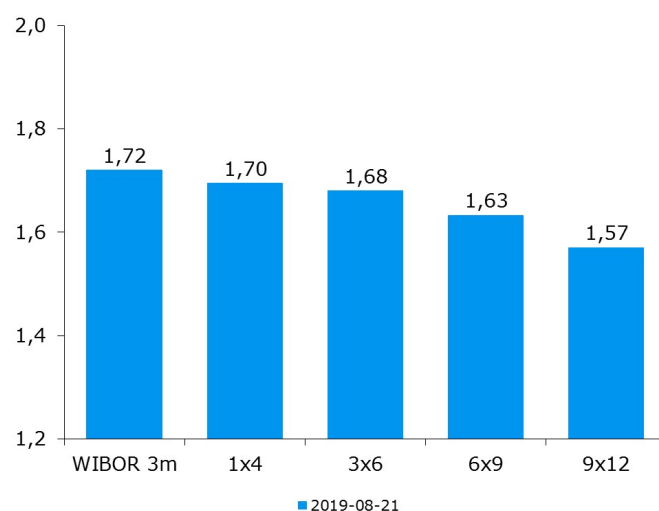
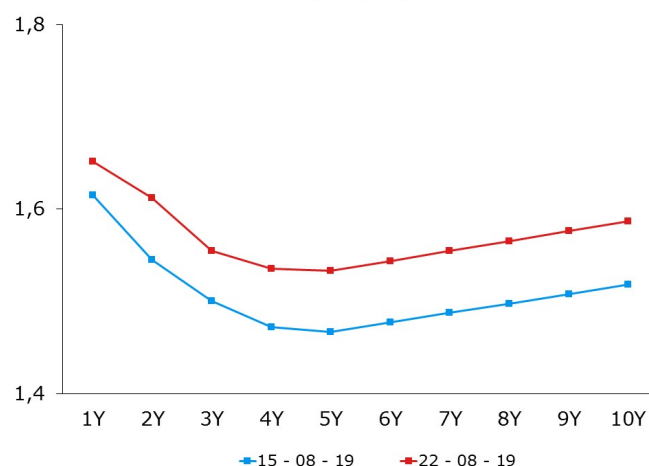
Rollercoaster

After the recent rollercoaster we came back to more normal levels. We touched 1.70% on DS1029, 1.55% on PS1024, 10y IRS traded at 1.42% and 5y IRS at 1.37% (all-time lows!). As the move down was very rapid, the way back is even more dynamic. Yields are consequently very low, but now, after the correction, there is room for a move in any direction. This weekend will give us guidance for coming weeks, as we have the Jackson Hole symposium and G-7 summit.

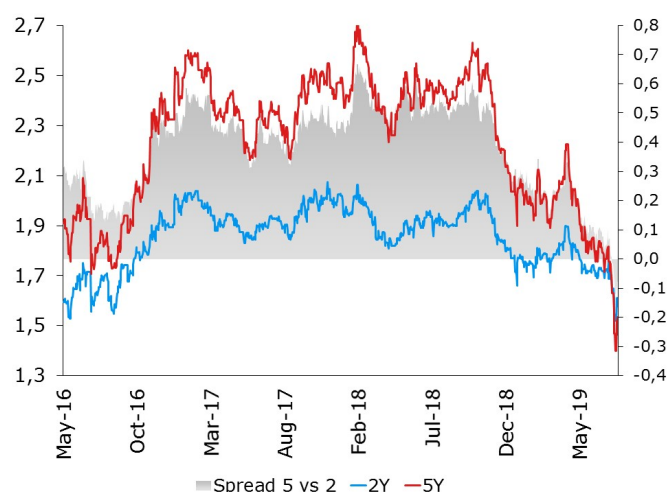
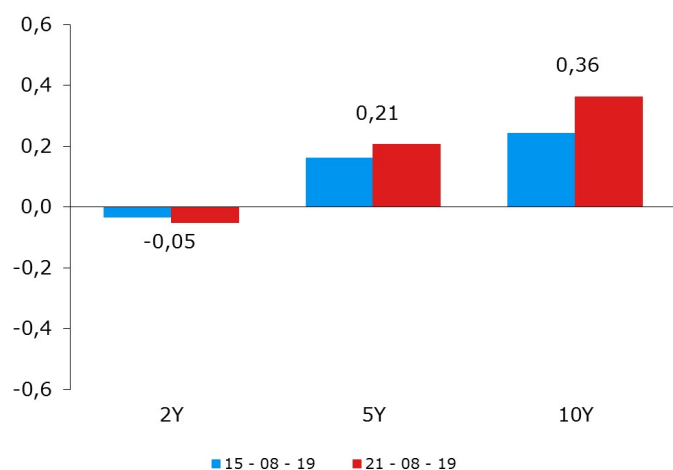
PS1024/5y is 20 bps, DS1029/10y is 38 bps. PS1024/DS1029 is 20 bps DS1029/Bund is 262 bps.

DS1020 is trading at 1.35% (10 bps up), PS1024 is trading at 1.80% (1 bps up) and DS1029 is trading at 2.00% (1 bps up).

IRS curve



Asset swaps



Money market

What goes down must go up

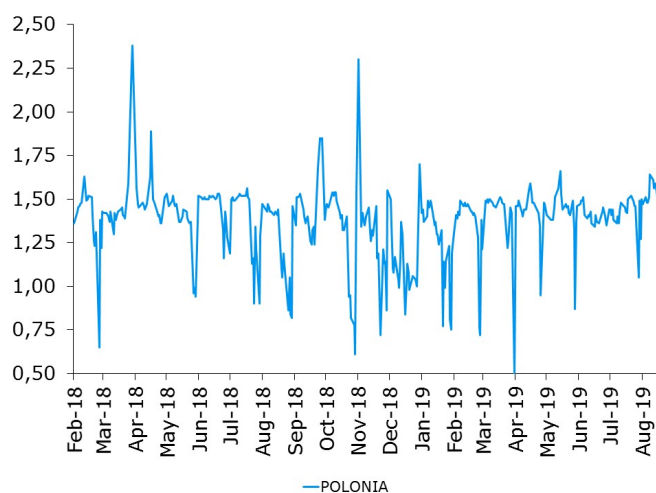
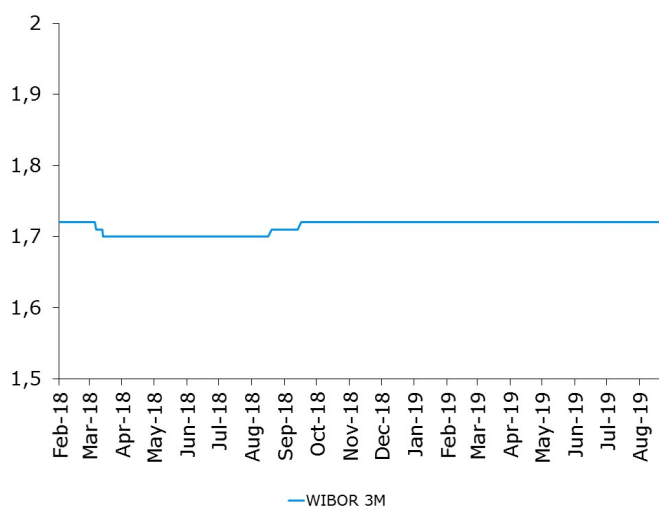
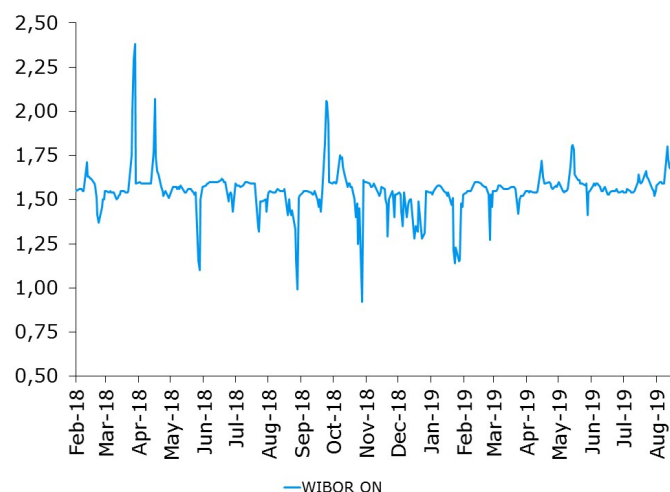
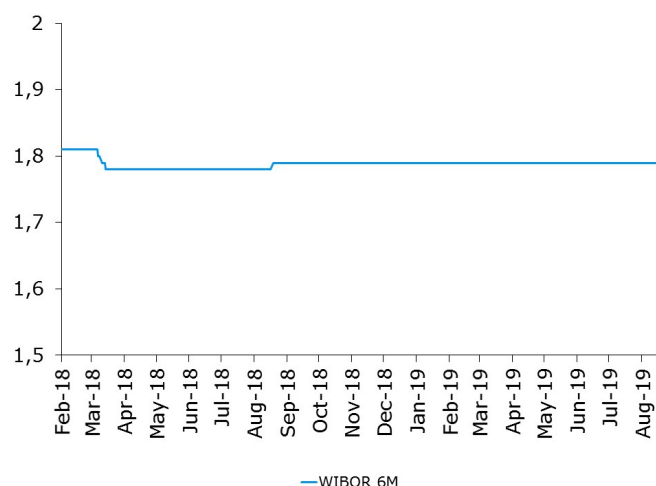
Polish yield curve is a rollercoaster. At first, we got to all-time lows on swaps. There was totally zero liquidity and stop losses pushed 5y swap rate down to 1.4%. This week, we've had a sharp reversal with MPC minutes showing there was a hike motion on last meeting. Previously the 2y swap was pricing a cut and now we've seen a sharp move higher. The WIBOR is currently at 1.79% while 2y is trading around 1.66%.

Market was left with cash surplus, so we were trading slightly below 1.50%. Next week we have end of the reserve period, so stay focused.

Ref rate vs Polonia averages:

30 day 6 bp

90 day 8 bp



Forex

Spot – PLN on fire – waiting for news from Jackson Hole

Stronger USD and worries over global recession have provided the needed spark for PLN to start the weakening spiral. EUR/PLN, from the lazy scrambling to the top of old range, spiked to 3.3950. In fairness, this high in EUR/PLN happened on August 15th, which was a public holiday in Poland, and the thin liquidity was adding fuel to the move, which looked really exaggerated. So nothing surprising that next day, it corrected lower to 4.33ish, which now acts as a support. Global economic outlook is not too optimistic. Expectations for further monetary easing globally are rising. Thus, in our opinion, the zloty should remain in new, higher range: 4.34/4.39. This Friday the central bankers' conference in Jackson Hole starts. Powell's speech, whether and how it relates to Trump's pressure for greater interest rate cuts, recession worries and Brexit news are main events that may result in a volatility spike.

Opts – EUR/PLN volatility higher again The Vols are higher and that is not a surprise – realized volatility exploded. Last time buyers of gamma were very active on the market, so especially the beginning of the EURPLN volatility curve is higher than two weeks ago. EUR/PLN 1 month ATM mid is 5.4% today (1.3% higher), 3 month is at 5.15% (1.0% higher) and, finally, 1 year fixed at 5.0% (0.6% higher). The skew was a little higher, while the currency spread (difference between USD/PLN and EUR/PLN) is at the same level as a week ago.

Short-term forecasts

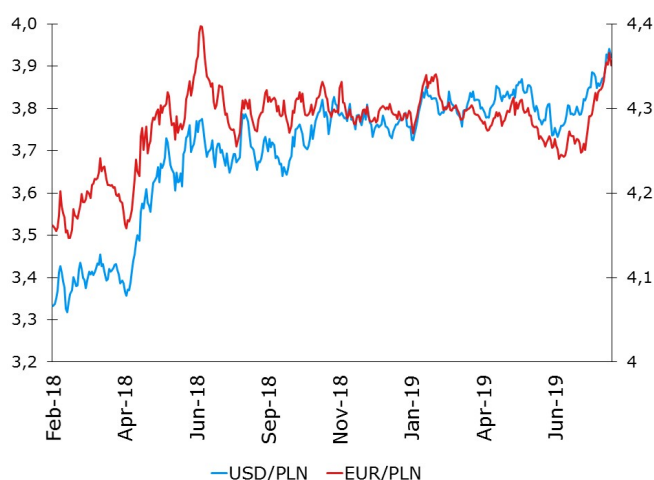
Main supports / resistances:

EUR/PLN: 4.3400 / 4.3900

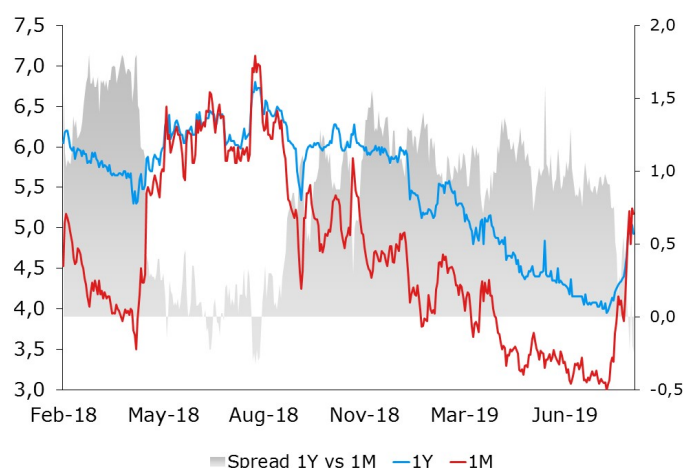
USD/PLN: 3.7000 / 4.0000

Spot – Current position: None. Buy on dips.

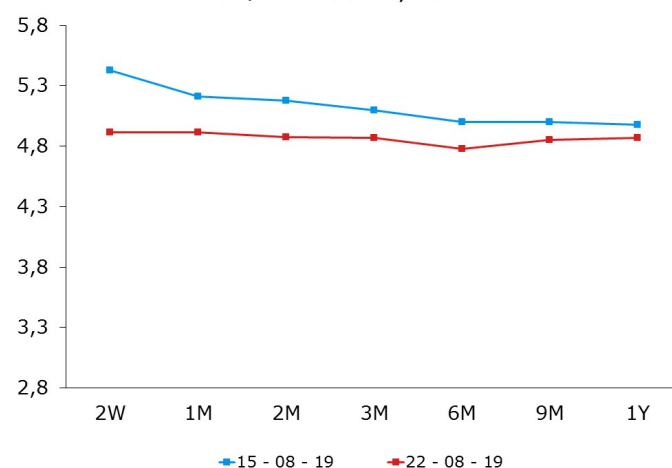
Shorts in EUR/PLN from 4.3075 were stopped at 4.35. We don't have a position at the moment, but we are ready to buy on dips. Global sentiment is changing, some local political risk appears (Autumn parliamentary elections, the ruling of European Court of Justice on Swiss loans), which combined with dovish monetary stance of the MPC is likely to result in further Zloty depreciation.



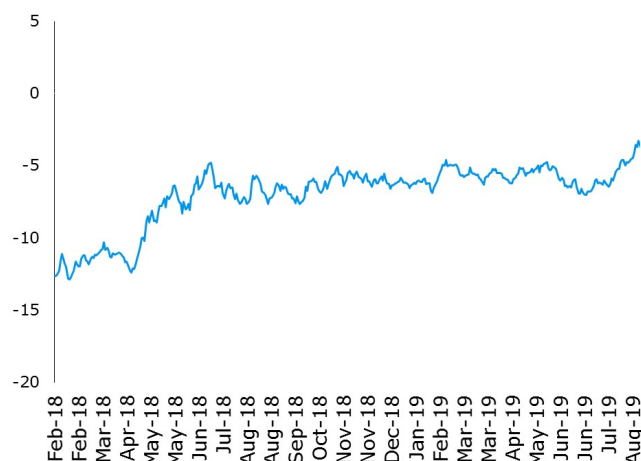
EURPLN volatility



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
8/15/2019	1.71	1.72	1.73	1.69	1.77	1.75	1.70	1.67	1.60	1.53	1.42	1.63
8/18/2019	1.95	1.72	1.84	1.69	1.89	1.75	1.70	1.67	1.59	1.52	1.46	1.62
8/19/2019	1.62	1.72	1.62	1.69	1.68	1.75	1.71	1.70	1.64	1.58	1.50	1.67
8/20/2019	1.53	1.72	1.54	1.69	1.62	1.75	1.72	1.69	1.61	1.55	1.47	1.64
8/21/2019	1.66	1.72	1.66	1.69	1.74	1.75	1.70	1.68	1.63	1.57	1.50	1.66

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	7/26/2019	5/25/2021	97.42	1.45	300	625	300
PS1024	7/26/2019	10/25/2024	102.10	1.82	2000	2330	1500
DS1029	7/26/2019	10/25/2029	105.91	2.10	1500	2248	1511

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0720	5Y IRS	PS0423	10Y IRS	WS0428
8/15/2019	1.750	1.224	1.545	1.511	1.467	1.628	1.518	1.760
8/18/2019	1.750	1.236	1.520	1.489	1.398	1.478	1.425	1.721
8/19/2019	1.750	1.240	1.610	1.561	1.520	1.708	1.580	1.873
8/20/2019	1.750	1.243	1.575	1.511	1.463	1.665	1.513	1.848
8/21/2019	1.750	1.286	1.612	1.561	1.533	1.739	1.587	1.950

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY	
Date	1M	3M	6M	1Y	1M	1Y	1Y	
8/15/2019	5.21	5.10	5.00	4.98	4.98	1.51	0.52	
8/18/2019	4.80	4.98	4.85	4.90	4.90	1.51	0.52	
8/19/2019	5.24	5.07	4.98	5.04	5.04	1.51	0.50	
8/20/2019	5.17	5.00	4.90	4.93	4.93	1.51	0.52	
8/21/2019	4.92	4.87	4.78	4.87	4.87	1.50	0.51	

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
8/15/2019	4.3463	3.8890	3.9924	3.6536	1.3436	0.1683
8/18/2019	4.3543	3.9281	4.0093	3.6953	1.3399	0.1688
8/19/2019	4.3519	3.9199	4.0071	3.6778	1.3373	0.1689
8/20/2019	4.3656	3.9408	4.0227	3.7023	1.3339	0.1693
8/21/2019	4.3513	3.9210	4.0014	3.6805	1.3293	0.1687

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