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Polish Weekly Review

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Comment on the upcoming data and forecasts

Next week starts with parliamentary election results, but it should not have any significant impact on economic policy (more details in the macro section). On Monday current account data will be published. We expect slowdown in both exports and imports (more profound than the consensus forecast) following the weak industrial production August reading. Next day final CPI will be published – flash estimate indicates the 2.6% reading (slowdown in food and fuel prices). It implies the core inflation of 2.3%. On Thursday employment (we expect stabilization of growth at 2.6% y/y) and average wage data (also stabilization, with weak manufacturing but still strong impact of services) will be published. Week ends with industrial production reading – after weak August in September it should increase by 6.0% y/y due to the positive working days difference, low base from the previous year and a possible shift in automotive production from August to September.

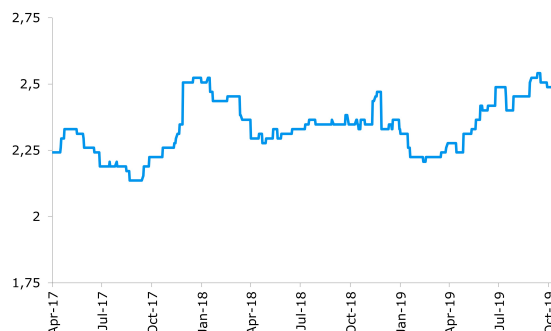
Polish data to watch: October 14th to October 18th

Publication	Date	Period	mBank	Consensus	Prior
Current Account Balance (m EUR)	14.10	Aug	-314	-543	-814
Exports	14.10	Aug	17650	17776	19239
Imports	14.10	Aug	17900	18200	19615
CPI final y/y (%)	15.10	Sep	2.6	2.6	2.9
Core inflation y/y (%)	16.10	Sep	2.3	2.3	2.2
Average Gross Wage y/y (%)	17.10	Sep	7.0	7.2	6.8
Employment y/y (%)	17.10	Sep	2.6	2.6	2.6
MPC Minutes	17.10				
Industrial Production y/y (%)	18.10	Sep	6.0	5.2	-1.3
PPI y/y (%)	18.10	Sep	0.6	0.5	0.7

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	11/7/2019	300	1.445	7/26/2019
5Y T-bond PS1024	11/7/2019	2000	1.823	7/26/2019
10Y T-bond DS1029	11/7/2019	1500	2.100	7/26/2019
30Y T-bond WS0447	11/7/2019	60	3.180	4/25/2019
5Y floater WZ0525	11/7/2019	2500	-	7/26/2019
10Y floater WZ0529	11/7/2019	2100	-	7/26/2019

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



Comment

There were no data releases this week so Polish surprise index has remained unchanged. Next week (with scheduled readings of inflation, industrial production, PPI and labor market data) can change it.

* 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 is set to slow down considerably next year. We have revised our 2020 forecasts from 4.0 to 3.2%. Waning effects of fiscal stimulus, unfavorable EU spending calendar, retrenchment of local government investment and weaker investment outlook are to blame. That being said, consumption will remain very resilient and this makes all the difference compared to 2011-2013 cycle.
- Core inflation is at multi-year high, but there is limited space for further acceleration. The pass-through from wages is working in services, but wage growth has stabilized there. In addition, deflation is likely to return to core consumer goods given the global environment.
- 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 risks are to the downside.
- This year's fiscal deficit is set to widen due to brisk expenditure growth. Next year's balanced budget proposal is not realistic given the already announced spending (pension bonus made permanent) and ambitious revenue targets. Actual deficit will be small, though.

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 more or less stable 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. However, slowdown is slowing down and as the risks for monetary policy are tilted to the downside, the same applies to PLN valuation.

mBank forecasts

	2015	2016	2017	2018	2019 F	2020 F
GDP y/y (%)	3.8	3.0	4.8	5.1	4.5	3.2
CPI Inflation y/y (average %)	-0.9	-0.6	2.0	1.6	2.4	3.1
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

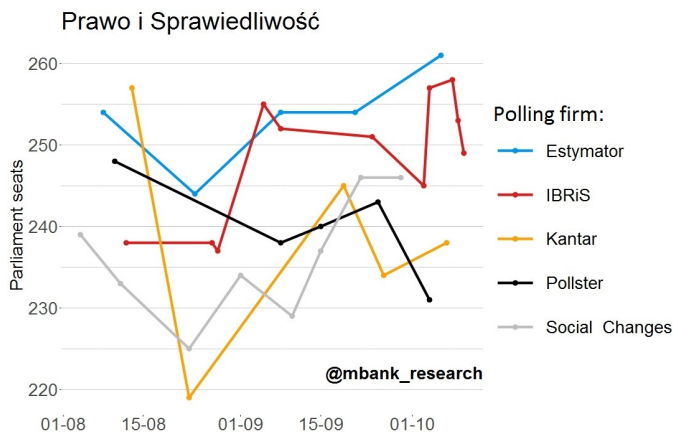
	2019	2019	2019	2019	2020	2020	2020	2020
	Q1	Q2	Q3 F	Q4 F	Q1 F	Q2 F	Q3 F	Q4 F
GDP y/y (%)	4.7	4.5	4.3	4.3	3.9	3.5	3.0	2.5
Individual consumption y/y (%)	3.9	4.4	4.6	5.0	4.6	4.2	3.4	2.8
Public Consumption y/y (%)	6.4	3.4	5.0	5.0	3.0	3.0	3.0	3.0
Investment y/y (%)	12.6	9.0	6.0	5.0	2.0	2.0	0.0	0.0
Inflation rate (% average)	1.2	2.4	2.8	3.3	3.7	3.2	2.7	2.7
Unemployment rate (% eop)	5.9	5.2	5.2	5.4	5.5	4.9	4.9	5.1
NBP repo rate (% eop)	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50
Wibor 3M (% eop)	1.72	1.72	1.72	1.72	1.72	1.72	1.72	1.72
2Y Polish bond yields (% eop)	1.69	1.61	1.52	1.51	1.55	1.55	1.55	1.55
10Y Polish bond yields (% eop)	2.84	2.39	2.00	1.95	2.10	2.24	2.27	2.30
EUR/PLN (eop)	4.30	4.24	4.37	4.35	4.35	4.40	4.40	4.40
USD/PLN (eop)	3.84	3.73	4.01	4.03	3.95	3.93	3.86	3.83

F - forecast

Economics

Before the parliamentary elections

This Sunday Polish parliamentary elections will be held. Exit polls will be known on Sunday evening, but for the exact number of parliamentary seats allocated to each party we will have to wait at least until Monday. Polls from the last few weeks indicate that maintaining the status quo is the most probable scenario.



According to our simulations, each poll published last month results in absolute majority for the governing Prawo i Sprawiedliwość (PiS) party (240 - 260 parliamentary seats, while 231 is the absolute majority threshold). Simulations also indicate that PiS would have to get less than 43% to lose the absolute majority and therefore increase the probability of coalition or opposition-led government.

The baseline scenario implies continuation of the current economic policy. It means that in the upcoming weeks the old-new government should pass the bills on 13th and 14th pension benefits and so-called small ZUS (lower contributions to the pension fund for micro-firms). One should also expect canceling the cap on pension contributions (now the basis is set on the level of 30 average wages) and changes in private pension funds. All those solutions were already announced by the government. Financial markets will consider the absolute majority for the governing party as a positive news (strong mandate and deficit control).

Alternative scenario, where PiS will need and find a coalition partner will result in higher uncertainty, but it should not change much the economic or fiscal policy. However the initial markets reaction will be negative. Another scenario, of the complete change of the government (for the opposition one), will result in the highest uncertainty. The new government, operating with a difficult cohabitation with the president, will have to provide a budget for the next year, without a number of key bills for the revenue side. Budget with sharply higher deficit can encourage the MPC to react, which will be easy to justify with inflation still elevated.

Fixed income

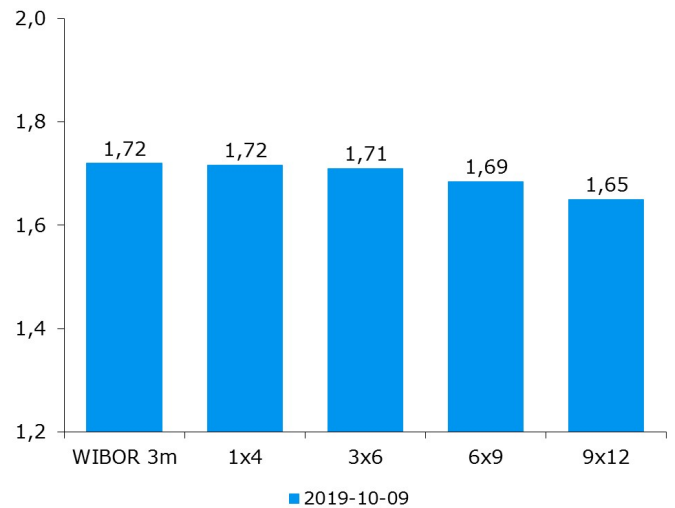
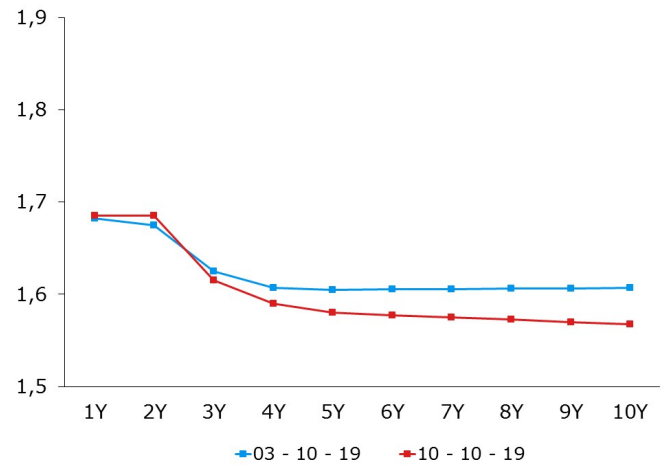
Calm week behind us

Last week was very calm, volatility was rather poor and investors' activity was low. Yield curve tends to flatten despite small bearish market and there is an interest to pay FRNs and ASWs.

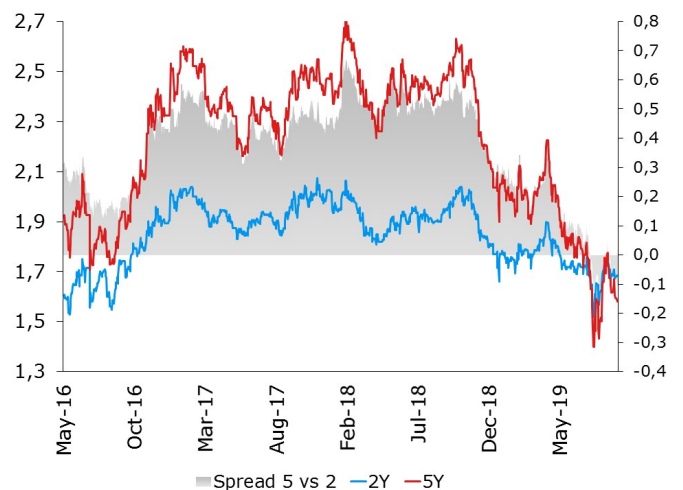
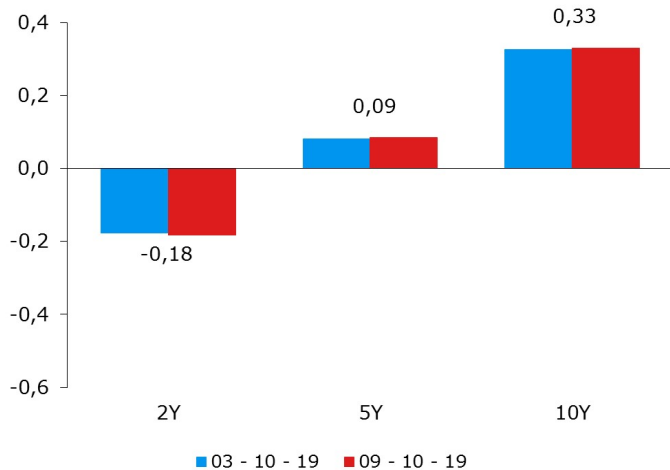
PS1024/5y is 3 bps, DS1029/10y is 30 bps. PS1024/DS1029 is 23 bps DS1029/Bund is 243 bps.

DS1021 is trading at 1.47% (no change), PS1024 is trading at 1.69% (no change) and DS1029 is trading at 1.92% (2 bps down).

IRS curve



Asset swaps

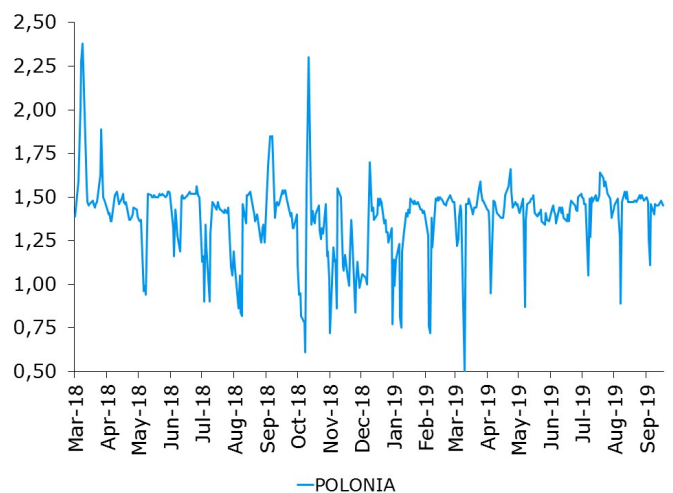
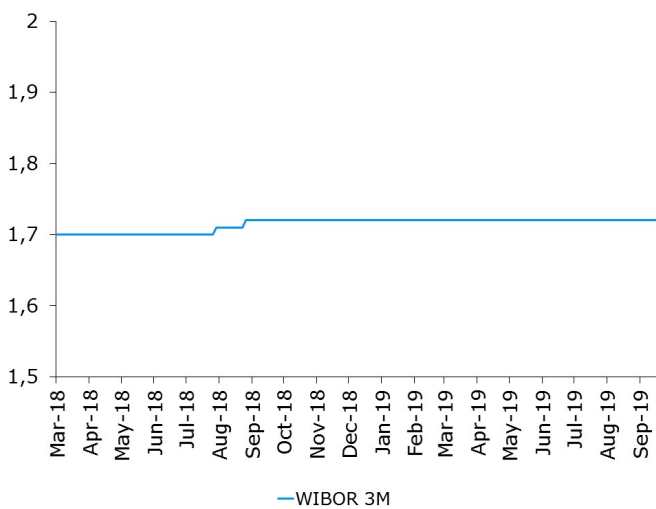
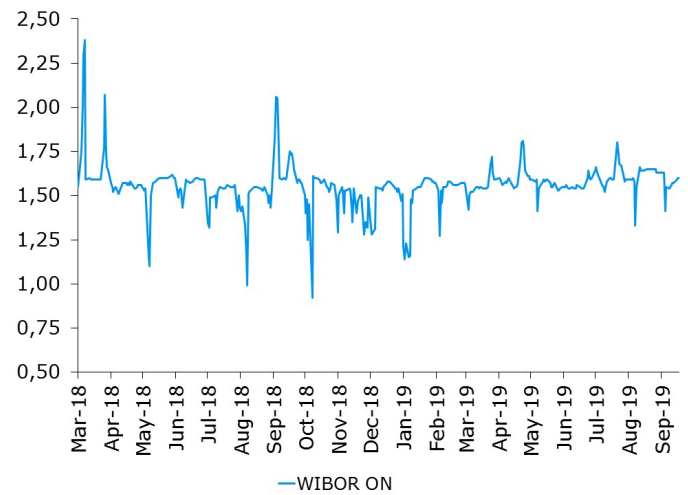
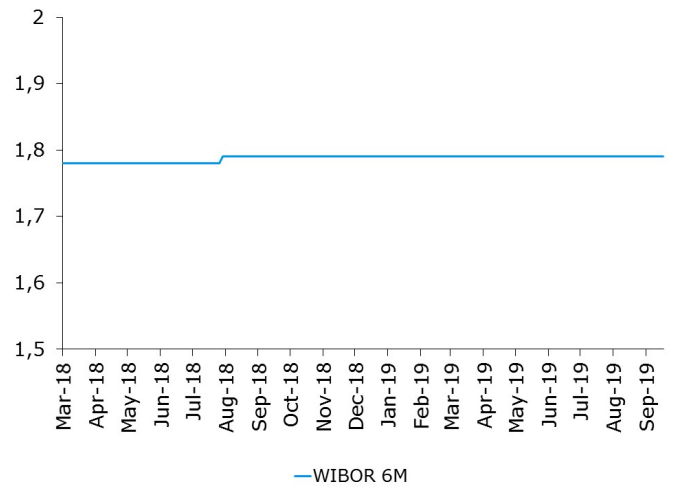




Money market

Stable week again

Overnight market was very stable again. On Friday's OMO banks bought PLN 86.7bn of 7-day bills when 91bn would have squared the market. We already forgot about any major move and additional OMO. There are two more regular operations this month, so do not expect a major drop in rates next week. In the end of the month we will have coupon payment of October's papers (recorded on October 23rd and paid on October 25th) and maturity of DS1019. It will be connected with a switching auction on October 25th. It could cause some move on overnight rate.



Forex

EURPLN – Consolidation phase for EUR/PLN After the long-awaited verdict of the ECJ on Swiss franc mortgages, Polish zloty gained and is currently significantly stronger than prior to ruling. EURPLN kept on meandering in the extremely tight range, 4.3185-4.3300, which itself is just in the middle of the new defined 4.30-4.34 range. Eventually, the ruling is likely to result in an increase in the number of court cases and, in consequence, pressure on the zloty. Besides we think that the zloty may again depreciate due to endless fears a global slowdown growth especially that prospect for progress in U.S.-China trade talks dimmed lately and concerns about "no-deal" Brexit intensified.

Opts: – EUR/PLN vols – dropped like a stone The tight range in EUR/PLN says all! Realized volatility is again on the move down. However, the drop of implied volatility seems to be exaggerated. 1 month ATM mid is today 4.25% (almost 0.2% lower), 3 months are at 4.25% (0.35% lower) and finally 1 year fixed at 4.7% (0.2% lower). The skew and the currency spread (difference between USD/PLN and EUR/PLN) are lower than one week ago.

Short-term forecasts

Main supports / resistances:

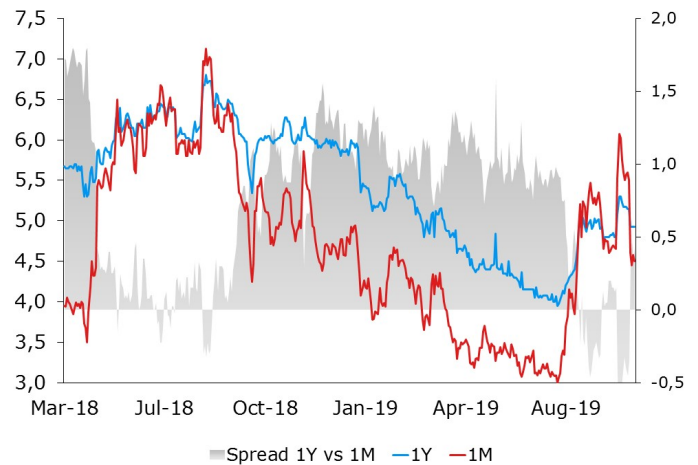
EUR/PLN: 4.3000 / 4.3600

USD/PLN: 3.8000 / 4.0000

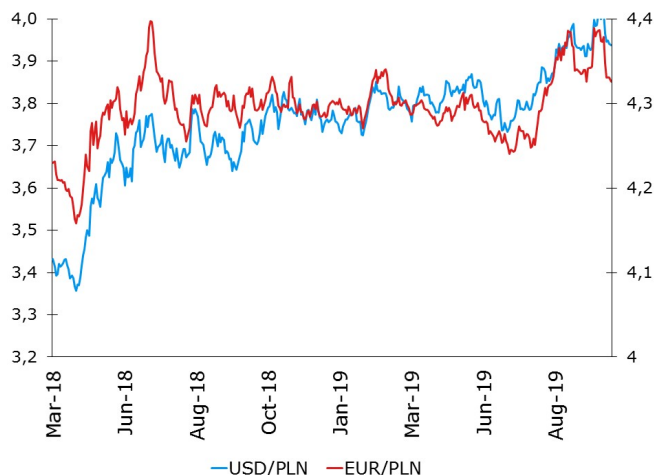
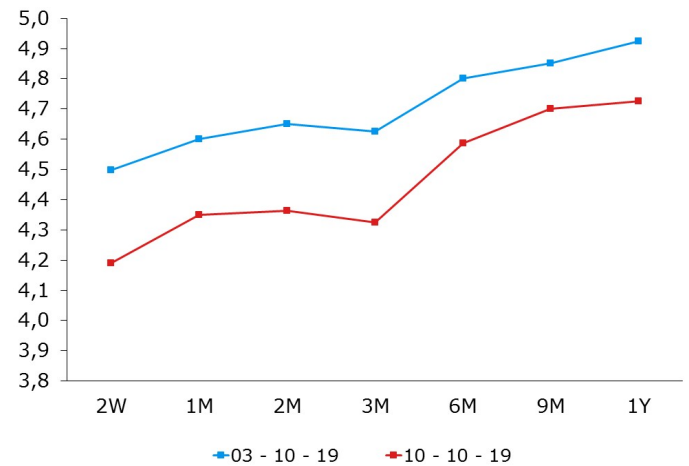
Spot – Current position: None. Buy on dips.

We don't have a position at the moment, but we are ready to buy on dips. The global market sentiment is getting worse, there are some local (autumn parliamentary elections) and global (trade war, Brexit) political risks. All this will probably stop further Zloty appreciation.

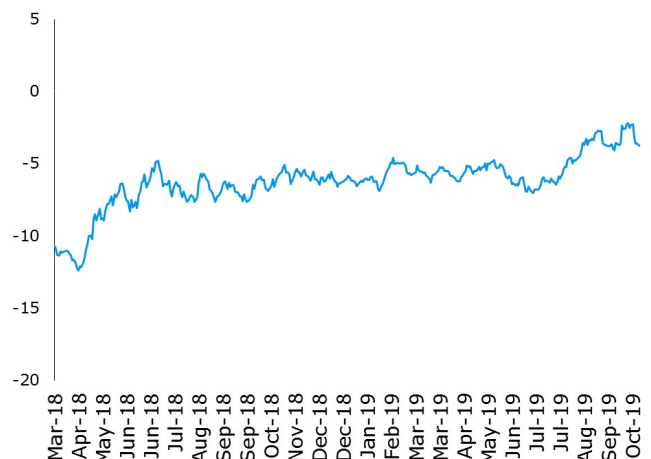
EURPLN volatility



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
10/3/2019	1.61	1.72	1.65	1.69	1.73	1.74	1.72	1.71	1.68	1.64	1.62	1.74
10/6/2019	1.85	1.72	1.82	1.69	1.89	1.74	1.72	1.71	1.68	1.65	1.60	1.75
10/7/2019	1.82	1.72	1.79	1.69	1.90	1.74	1.72	1.71	1.69	1.65	1.61	1.74
10/8/2019	1.72	1.72	1.69	1.69	1.78	1.74	1.72	1.71	1.68	1.64	1.60	1.75
10/9/2019	1.83	1.72	1.80	1.69	1.89	1.74	1.72	1.71	1.69	1.65	1.61	1.75

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
10/3/2019	1.740	1.242	1.675	1.498	1.605	1.686	1.607	1.933
10/6/2019	1.740	1.242	1.680	1.519	1.595	1.685	1.590	1.915
10/7/2019	1.740	1.204	1.685	1.496	1.590	1.644	1.585	1.889
10/8/2019	1.740	1.234	1.682	1.498	1.590	1.641	1.580	1.893
10/9/2019	1.740	1.244	1.685	1.502	1.580	1.665	1.568	1.897

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY
Date	1M	3M	6M	1Y	1M	1Y	1Y
10/3/2019	4.60	4.63	4.80	4.93	4.93	1.32	0.34
10/6/2019	4.45	4.53	4.70	4.93	4.93	1.32	0.34
10/7/2019	4.58	4.55	4.73	4.93	4.93	1.25	0.34
10/8/2019	4.50	4.53	4.73	4.93	4.93	1.24	0.35
10/9/2019	4.35	4.33	4.59	4.73	4.73	1.21	0.36

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
10/3/2019	4.3475	3.9652	3.9694	3.7024	1.3040	0.1687
10/6/2019	4.3311	3.9469	3.9588	3.6958	1.3027	0.1685
10/7/2019	4.3304	3.9498	3.9727	3.6957	1.3002	0.1681
10/8/2019	4.3310	3.9405	3.9714	3.6772	1.2967	0.1679
10/9/2019	4.3257	3.9382	3.9643	3.6711	1.2939	0.1677

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