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Polish Weekly Review

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Comment on the upcoming data and forecasts

On Tuesday NBP will publish the new Inflation Report with lower Polish GDP forecasts and slightly higher inflation projections (more details in macroeconomic section). The same day, current account data for September will be published. We expect a positive trade balance (Exports of 19800m EUR and Imports 19600m EUR) – a good signal for Polish exports can come from the production of other transport equipment which September result was much better than expected. On Thursday GDP for Q3 will be published. We expect it to grow by 4.3% y/r (investments 7% and consumption 4.2%). Final inflation should confirm the flash reading (2.5% y/y), which results in core inflation of 2.4 - 2.5% (our forecast is 2.5% but in fact, it is at the knife's edge)

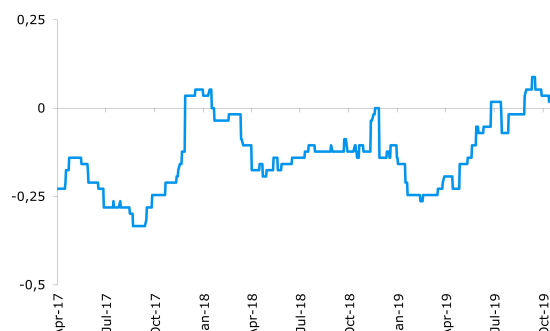
Polish data to watch: November 8th to November 15th

Publication	Date	Period	mBank	Consensus	Prior
Current Account Balance (m EUR)	13.11	Sep	160	-218	-606
Exports (m EUR)	13.11	Sep	19800	19313	17646
Imports (m EUR)	13.11	Sep	19600	19248	17701
GDP <i>flash</i> y/y (%)	14.11	Q3	4.3	4.1	4.5
CPI <i>final</i> y/y (%)	14.11	Oct	2.5	2.5	2.5
CPI core y/y (%)	15.11	Oct	2.5	2.5	2.4

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	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

Even though PMI reading surprised negatively (45.6 pts. vs consensus forecast of 48.1), it was not enough to move the surprise index. Next week, possible surprise can be result of current account, GDP and inflation readings.

* 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. 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. Our revised 2020 forecasts call for 3.2% y/y growth.
- 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 and the lagged relationship with local manufacturing wages.
- 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. The revised budget will show a small deficit. General government deficit will remain low as local governments are set to cut investment considerably.

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 slowdown and as the risks for monetary policy are tilted to the downside, the same applies to PLN valuation. Breakeven exchange rates for exporters are, however, moving steadily higher with rising labor costs and that puts an ever-higher floor on EURPLN. No durable appreciation in current circumstances.

mBank forecasts

	2015	2016	2017	2018	2019 F	2020 F
GDP y/y (%)	3.8	3.1	4.9	5.1	4.5	3.2
CPI Inflation y/y (average %)	-0.9	-0.6	2.0	1.6	2.4	2.6
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	5.3
Repo rate (end of period %)	1.5	1.5	1.5	1.5	1.5	1.5

	2019 Q1	2019 Q2	2019 Q3 F	2019 Q4 F	2020 Q1 F	2020 Q2 F	2020 Q3 F	2020 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	3.0	3.3	2.6	2.2	2.3
Unemployment rate (% eop)	5.9	5.2	5.1	5.5	5.6	5.0	5.0	5.3
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	1.71	1.71	1.71	1.71	1.71
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	3.95	3.95	3.93	3.86	3.83
F - forecast								

Economics

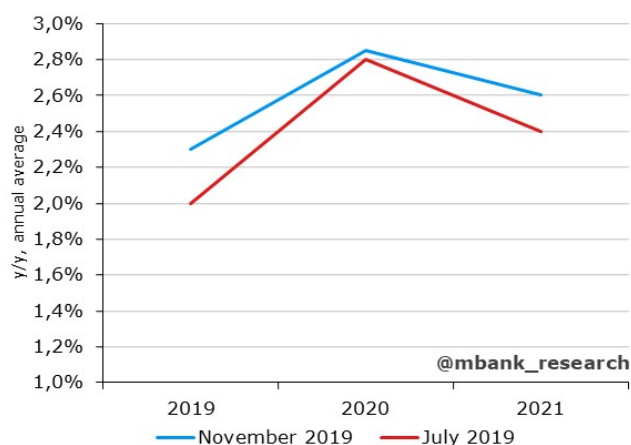
Status quo in monetary policy

There were no surprises at yesterday's MPC meeting. Interest rates remain stable and - according to governor Glapinski - they will probably not change until the end of his term. In this context, everything has remained unchanged. MPC claims that decreasing growth is mainly the effect of external factors, where the German economy is the most important one. It seems, that without a significant improvement in Europe, the MPC will not believe neither in change of the GDP trajectory nor in inflationary pressure in the medium term.

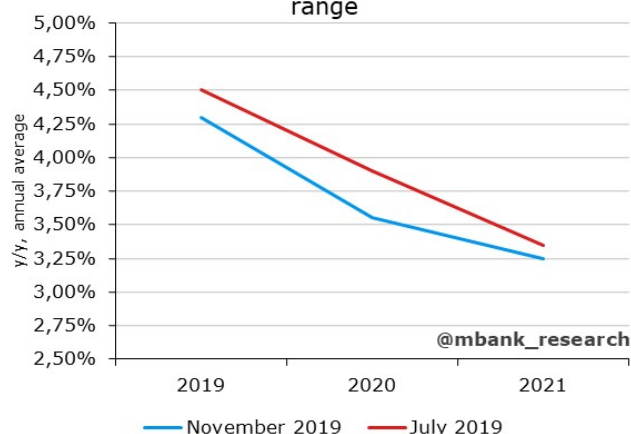
The latest inflation forecasts were slightly raised despite lower GDP dynamics. But inflation is still close to target, while in 2020 - when the NBP assumes an 8 increase in electricity price (here we hope to know further details after presentation of Inflation Report next Tuesday) - inflation is on average still below 3.5% in annual terms. For now, the projection is quite conservative, but the MPC still follows its well-known path. If someone sees the analogy with November 2018 it is a good example.

rate cuts. Glapinski, asked about the possible direction of interest rate changes (when MPC will need to change them), pointed to higher probability of a cut. It means, that stories about no space of loosening the policy with the repo rate, are not treated as important ones in the MPC itself, and there will always be room for a slight correction if needed.

CPI projection: midpoint of central range



GDP growth projection: midpoint of central range



Hence, in the baseline scenario, the MPC will not change interest rates. However, the balance of risks is shifted towards loosening monetary policy if GDP growth surprises negatively. It seems that the threshold for MPC (it is the estimate of governor Glapinski) is well below 3%. But MPC is not closed to interest

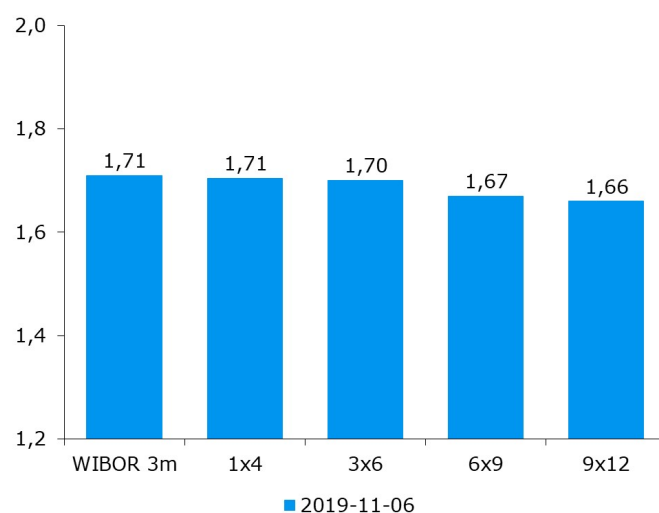
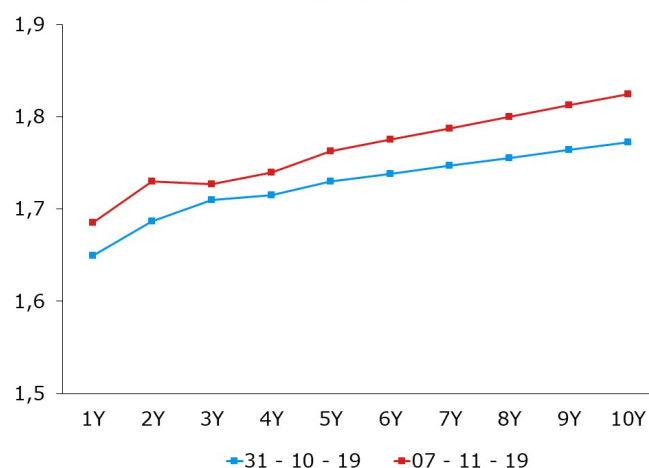
Fixed income

It is really hard to sink POLGBs

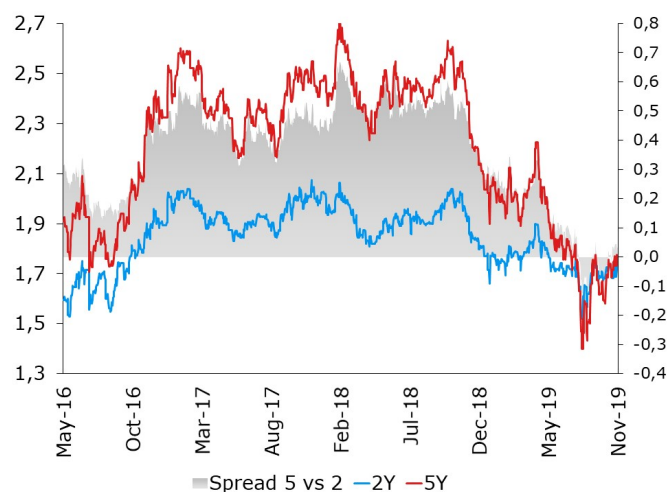
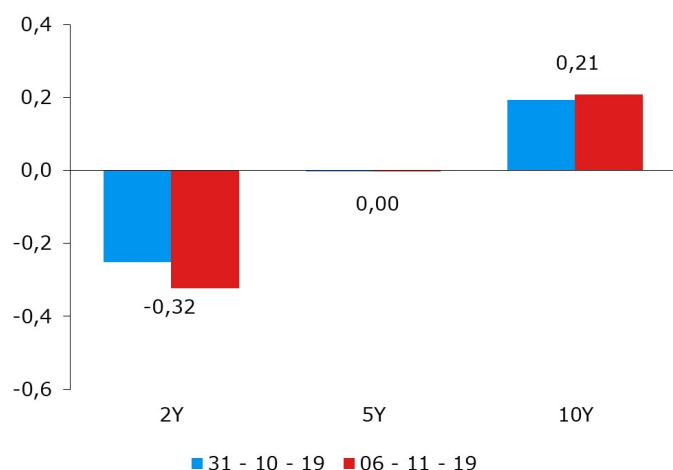
Today we had one of the smallest auction in recent years, Ministry of Finance switched only 2.8bn bonds, demand amounted to 4.3bn which resulted in decent (1.5x) bid to cover ratio. During last days we performed much better than core markets and small auction may contribute to even narrower spread vs bund. PS1024/5y is -4, DS1029/10y is 15bps. PS1024/DS1029 is 26bps DS1029/Bund is 230bps.

DS1021 is trading at 1.37% (5bps down), PS1024 is trading at 1.76% (3bps up) and DS1029 is trading at 2.02% (4bps up).

IRS curve



Asset swaps



Money market

Rising core rates expose local tops

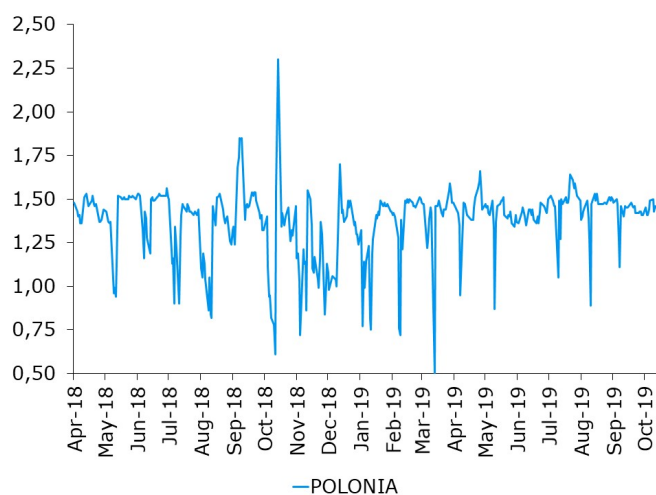
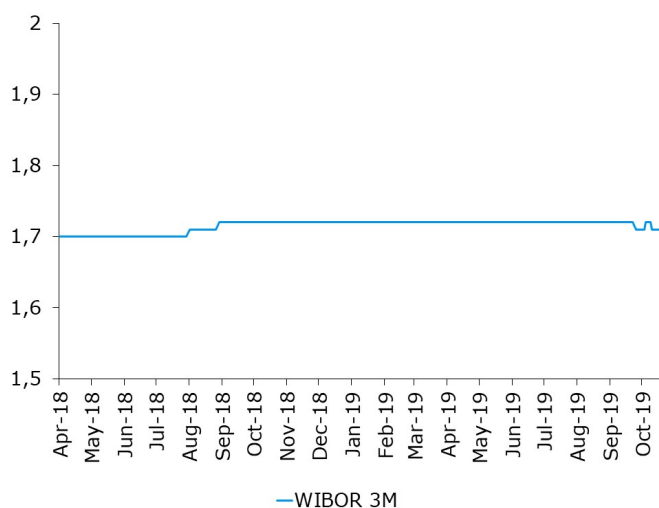
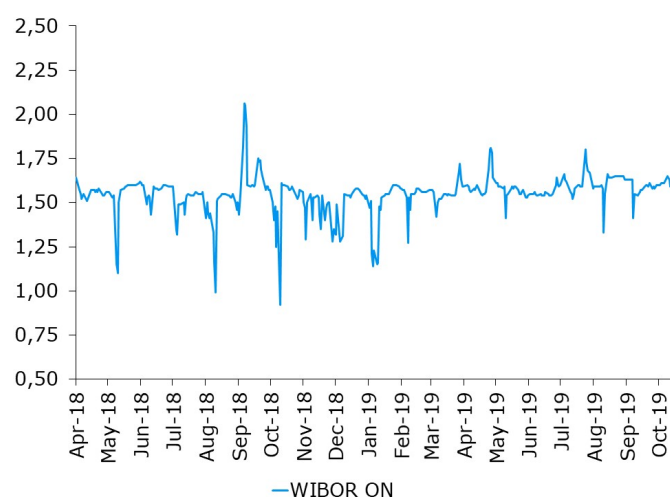
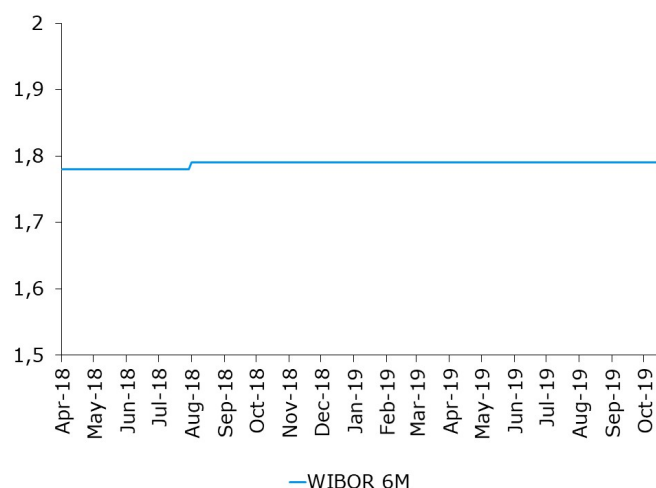
Polish rates are knocking again to upper band of current range. With core yields rising significantly we are holding quite well. It seems like the story for negative yields is gone for now. And upper band of the range might be in trouble.

Cash stable recently around 1.50. Next week we expect same.

Ref rate vs Polonia averages:

30 day 6 bp

90 day 5 bp



Forex

Spot - EUR/PLN - Trade wars - main topic on the market.

Trade war still is the crucial factor for global investment sentiment. During the last days, global market mood was a good as a result of news about the progress of US-China talks and better than expected October ISM non-manufacturing in the US. The zloty gained, benefiting from signs Beijing and Washington are approaching a trade deal (with hopes for at least partial truce). On the other hand, disappointing data was published from the Polish economy, (i.e. Poland's manufacturing PMI strongly declined). Finally, the Polish zloty remained relatively stable in ranges: EURPLN 4.2505-4.2740 and USDPLN 3.8030-3.8580. All in all, it was comparatively good week for the Zloty.

Opts: EUR/PLN vols - tic higher. Slightly weaker PLN, and positioning were the reasons, why the vols kept on creeping higher. The gains are cosmetic, and we need higher realized volatility and/or weaker PLN to support that gains. 1 month EUR/PLN ATM is traded today at 3.7% (0.3% higher than week ago). 3 months EUR/PLN are 3.75% (0.15% higher) and finally 1 year is 4.35% (0.1% higher). The skew is roughly higher than week ago, while the currency spread (difference of USD/PLN minus EUR/PLN) is lower.

Short-term forecasts

Main supports / resistances:

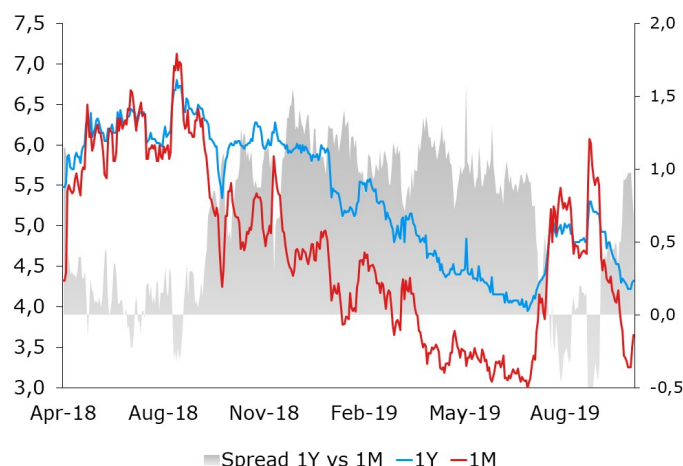
EUR/PLN: 4.2500 / 4.3000

USD/PLN: 3.7500 / 3.9500

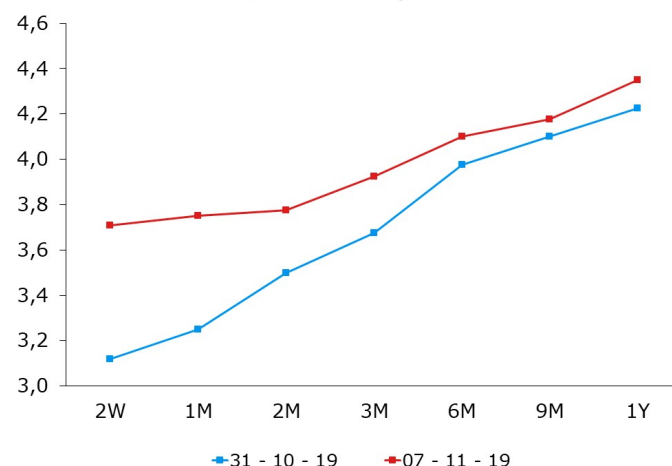
Current position: long EUR/PLN.

According to our trade idea we are long EURPLN at 4.27 (on average) with 4.24 stop and hopes to revisit 4.30. This week, the market has tested local support zone at 4.25. Overall, we still believe in range trading in EUR/PLN. Our strategy is unchanged, playing the range 4.25-4.30, ideally from the short PLN side.

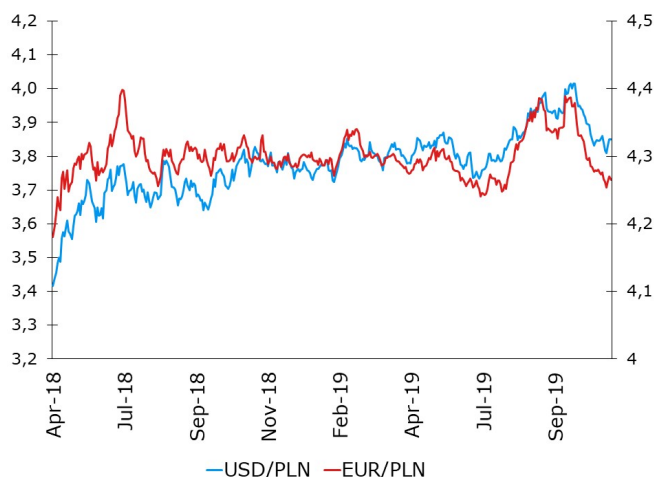
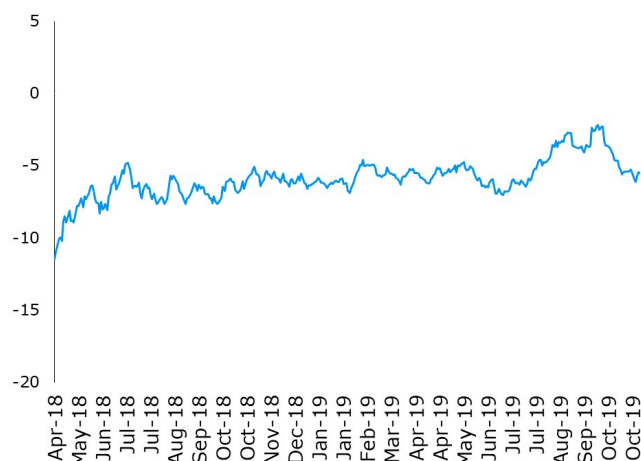
EURPLN volatility



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
10/31/2019	1.86	1.71	1.88	1.69	1.90	1.74	1.71	1.70	1.69	1.65	1.61	1.77
11/3/2019	1.86	1.71	1.88	1.69	1.91	1.74	1.71	1.70	1.68	1.64	1.61	1.76
11/4/2019	1.85	1.71	1.87	1.69	1.92	1.74	1.71	1.70	1.68	1.66	1.63	1.75
11/5/2019	1.73	1.71	1.76	1.69	1.83	1.74	1.71	1.71	1.68	1.66	1.63	1.75
11/6/2019	1.84	1.71	1.88	1.69	1.93	1.74	1.71	1.70	1.67	1.66	1.63	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
10/31/2019	1.740	1.059	1.687	1.436	1.730	1.728	1.773	1.965
11/3/2019	1.740	1.059	1.687	1.436	1.730	1.728	1.773	1.965
11/4/2019	1.740	1.016	1.717	1.515	1.735	1.735	1.798	1.970
11/5/2019	1.740	0.858	1.732	1.405	1.775	1.760	1.843	2.011
11/6/2019	1.740	0.873	1.730	1.408	1.763	1.762	1.825	2.033

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY	
Date	1M	3M	6M	1Y	1M	1Y	1Y	
10/31/2019	3.25	3.68	3.98	4.23	4.23	1.05	0.40	
11/3/2019	3.25	3.60	3.93	4.23	4.23	1.05	0.40	
11/4/2019	3.49	3.80	3.95	4.30	4.30	1.01	0.42	
11/5/2019	3.65	3.85	4.05	4.33	4.33	1.01	0.42	
11/6/2019	3.75	3.93	4.10	4.35	4.35	1.06	0.42	

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
10/31/2019	4.2617	3.8174	3.8681	3.5247	1.2921	0.1671
11/3/2019	4.2617	3.8174	3.8681	3.5247	1.2921	0.1671
11/4/2019	4.2539	3.8099	3.8567	3.5156	1.2970	0.1667
11/5/2019	4.2631	3.8308	3.8669	3.5189	1.2954	0.1670
11/6/2019	4.2697	3.8497	3.8778	3.5332	1.2883	0.1673

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