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Polish Weekly Review

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Comment on the upcoming data and forecasts

Tomorrow industry and construction data for October data will be published. Due to unfavorable working day count (0 vs. +1 y/y in the previous month) we expect activity to slow down, especially in industry. At the same time Statistics Poland's business sentiment indicators for November will be published. On Monday retail sales reading will be published. We do not expect any breakthrough in car sales; food sales and non specialized stores should go better after weak September; warm October means low dynamics in clothing and footwear category. Next day NBP will publish M3 aggregate (we expect 9.0% y/y due to high base in household and social funds deposits). On Wednesday unemployment rate will be published (our estimate 5.0%). Week ends with publication of final GDP in Q3 (flash reading at 3.9% y/y) and flash CPI for November – more details in the next weekly review.

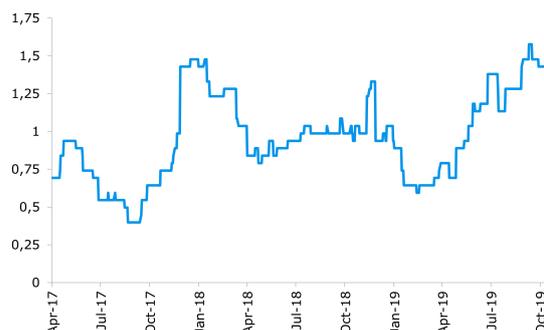
Polish data to watch: November 22nd to November 29th

Publication	Date	Period	mBank	Consensus	Prior
Business confidence	22.11	Nov			
Industrial output y/y (%)	22.11	Oct	1.8	2.5	5.6
PPI y/y (%)	22.11	Oct	0.2	0.3	0.4
Construction output y/y (%)	22.11	Oct	5.1	6.2	7.6
Retail sales y/y (%)	25.11	Oct	3.7	4.3	4.3
M3 y/y (%)	26.11	Oct	9.0	9.4	9.4
Unemployment rate (%)	27.11	Oct	5.0	5.1	5.1
GDP y/y (%)	29.11	Q3	3.9	3.9	3.9
CPI y/y (%)	29.11	Nov			2.5

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	12/13/2019	300	1.445	7/26/2019
5Y T-bond PS1024	12/13/2019	2000	1.823	7/26/2019
10Y T-bond DS1029	12/13/2019	1500	2.100	7/26/2019
30Y T-bond WS0447	12/13/2019	60	3.180	4/25/2019
5Y floater WZ0525	12/13/2019	2500	-	7/26/2019
10Y floater WZ0529	12/13/2019	2100	-	7/26/2019

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



Comment

Index remains unchanged - even though labor market data did surprise to the downside, readings were close to the market consensus. In the upcoming days, the remainder of the monthly set of Polish data will be published, so surprise index can change.

* 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 slowing down 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	4.3	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	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	4.0	3.9	3.9	3.6	3.0	2.5
Individual consumption y/y (%)	3.9	4.4	4.1	4.8	4.6	4.2	3.4	2.8
Public Consumption y/y (%)	6.4	3.4	3.0	5.0	3.0	3.0	3.0	3.0
Investment y/y (%)	12.6	9.0	5.5	4.0	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

No major changes to economic policies after the elections

This week the Polish Prime Minister commenced his second term with a traditional speech outlining the priorities of the new government. There were no surprises. First and foremost, the government will focus on implementing its pre-election promises: the so called 13th and 14th pensions (the later from 2021 on) and tweaks in social security contributions from small entrepreneurs. In addition, major strategic investment projects (e.g. Solidarity Transport Hub, Via Baltica) will continue. However, this suggests that no additional stimulus measures are currently planned and the fiscal policy stance is deemed as appropriate given the available forecasts. The overarching goal of economic policy in the next four years is maintaining a 2-3 p.p. lead in GDP growth over the Euro Area. This lies squarely within the historical norm.

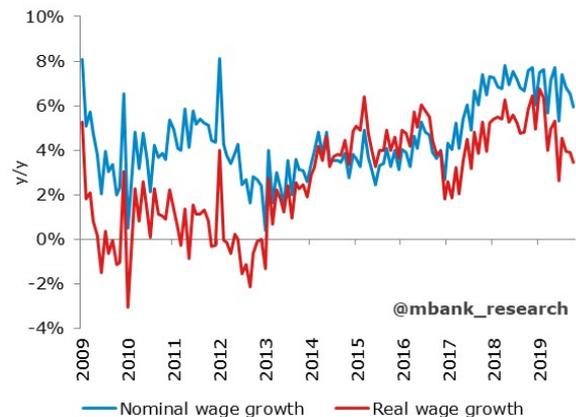
Several small-scale measures were announced and all of them can be seen as targeting the supply side: female labor supply will be boosted by support for part-time and telework; a drive towards deregulation and/or better and simpler regulation (including the tax code) was also announced; improvements in the quality of vocational education are presumably also aimed at the supply side. In addition, corporate investment will be encouraged, be it via faster depreciation for tax purposes, unspecified investment grants or the so called "Estonian-style CIT" (shift from gross profit to distributed profit taxation) for SMEs. The latter is arguably the only completely new measure mentioned in the PM's speech. Empirical evidence suggests that this policy has an immaterial impact on corporate investment, but improves corporate liquidity and survival rates in recessions (the beleaguered SME sector would certainly welcome it). The budgetary cost was earmarked at roughly PLN 3 bn. The plans for minimum wage hike were not mentioned in the speech.

Lack of a detailed action plan (it is customary to outline such a plan for the first 100 days of the cabinet) suggests that economic policy mix will be refined during the term. From the macroeconomic and market perspectives the speech did not bring any material new information. Over the short term, the 2020 budget (the government scrapped its plans to lift the social security contribution cap in favor of excise tax hikes and higher 5G auction proceeds, and proposed off-budget financing of the 13th pension to comply with the expenditure rule) continues to be the major story, while the key macro questions are about next year's consumption and public investment trajectories.

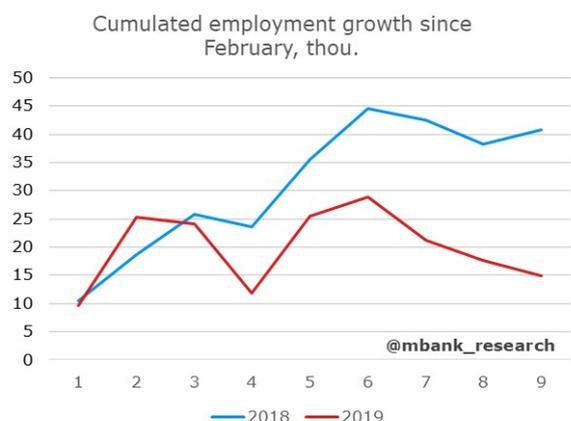
Slowdown in wages fits the trend, but its scale in October is artificially overblown by base effects in mining.

Wage growth in October slowed down to 5.9% y/y, in line with our forecast (but below the market consensus at 6.2% y/y). The most probable cause is a dent in wage growth in mining sector triggered by a base effect. Moreover, there could be slight working day effect in some sectors. But, as every month, these are only our estimates - for confirmation we need to wait till Wednesday. This reading fits the trend of a slight slowdown in wage growth. Next months (apart from a rebound in January result-

ing from the increase of the minimum wage) should bring further slowdown, which is in line with the employment data – lower labor demand will result in lower wage pressure.



Employment in the enterprise sector slowed down to 2.5% y/y, below our forecast (2.6%). In monthly terms it is the third month with a decline. Since Spring, labor demand is looking much weaker than a year ago. The reasons remain the same – supply constraints and business cycle (it results in lower labor demand, this effect is probably gathering pace). We can only repeat our expectations of further employment slowdown. It is also consistent with forecast of slower private consumption growth. Although consumers now are more willing and able to smooth consumption over time (due to social transfers that are considered a part of a permanent income), lower income growth should translate to slower consumption (but at smaller scale than in the alternative world, without additional elements of permanent income we just mentioned).



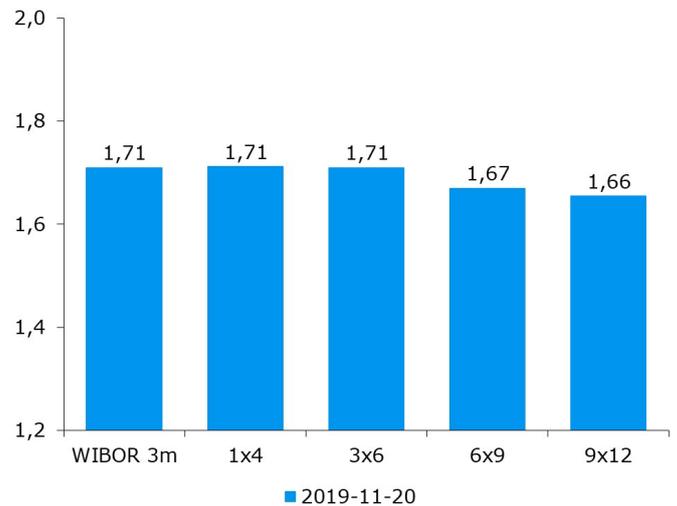
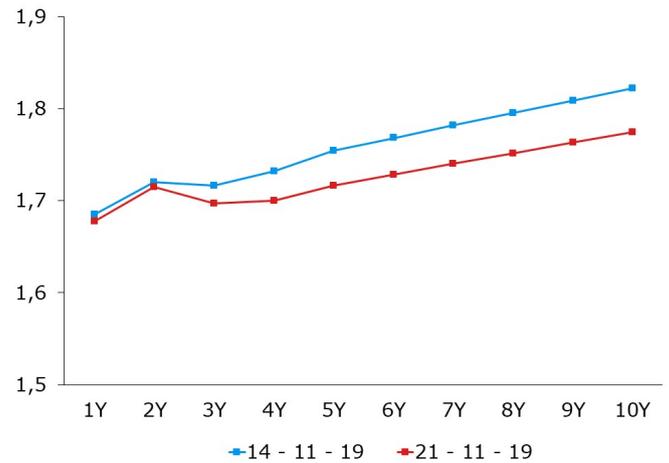
Fixed income

Small auction today, one more left this year

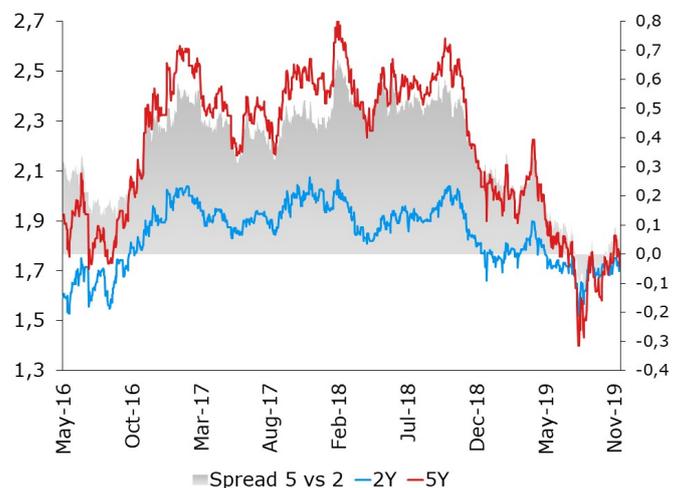
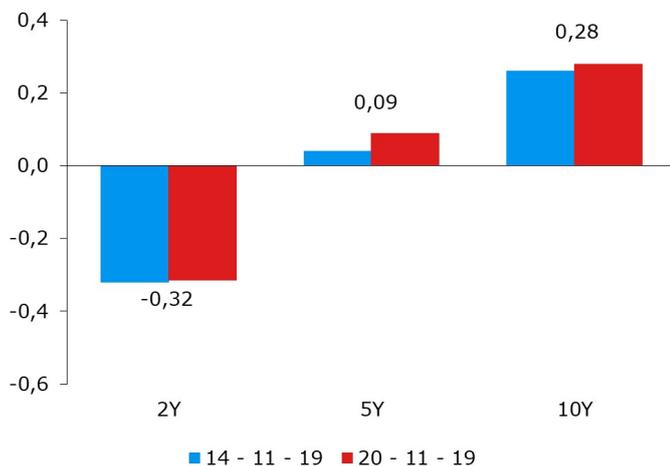
It was a quiet week. Yields were moving in narrow range, DS1029 was traded between 2.05-2.10%. People are tired with this year, so everyone is happy when volatility disappears. Today Ministry sold PLN 4.2 bn and it does not seem to be enormous volume but rather small size. There is only one auction left this year. Till the end of year we should see flows from banking books and they usually buy 2-5yr bonds. Longer bonds are closely following core markets.

PS1024/5y is 5 bps, DS1029/10y is 26 bps. PS1024/DS1029 is 28 bps. DS1029/Bund is 241 bps. DS1021 is trading at 1.38% (1 bps up), PS1024 is trading at 1.79% (1 bps up) and DS1029 is trading at 2.07% (1 bps up).

IRS curve



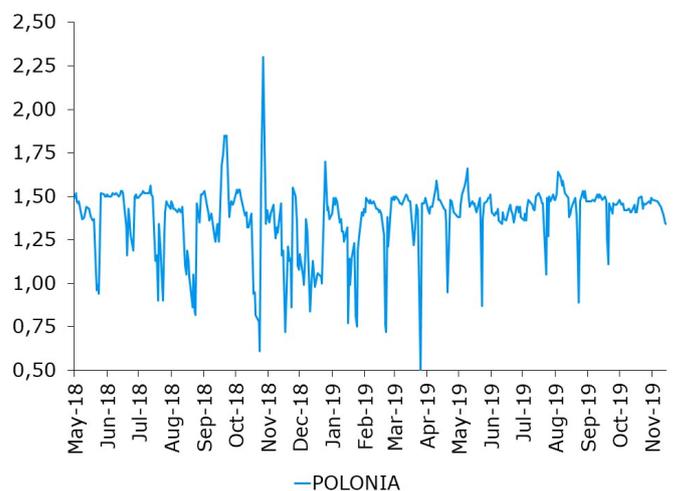
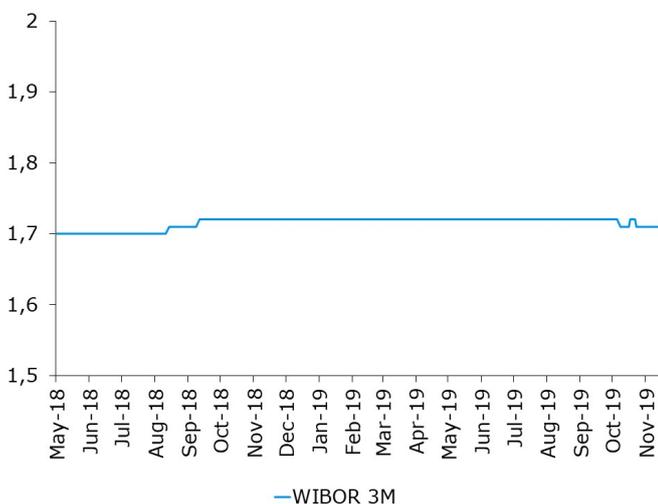
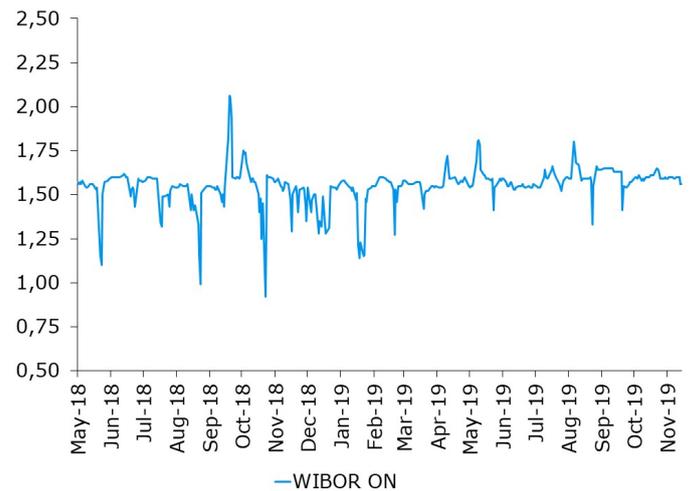
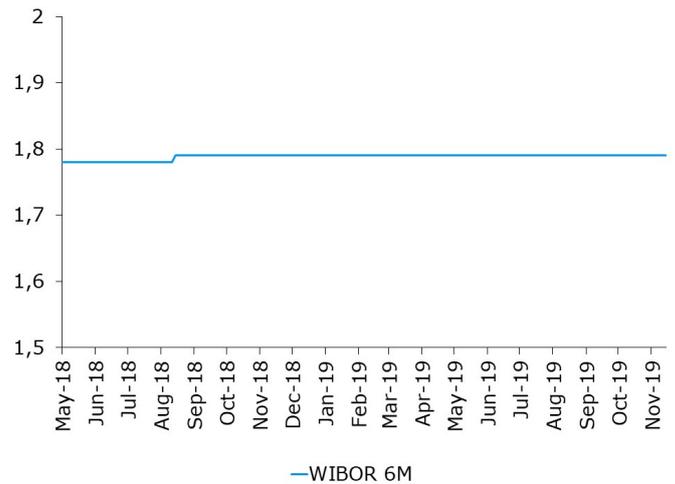
Asset swaps



Money market

Stable and cheap overnight cash

Overnight cash was little cheaper this week with Polonia below 1.50% (reached 1.35% on Wednesday). On Friday's OMO banks bought PLN 77.5 bn bills out of 88 bn offered. This week we had coupon payments of November's papers (WZ1122, WZ0524, WZ0525, WZ0528 and WZ1129; recorded on November 20th and paid on November 25th) and additionally today we had the second to last switch auction this year. It was not as big as traders expected, but banks bought a bit more than PLN 4 bn. This caused a sell-off in the switching bonds. Next week will be the last one of the mandatory reserve period (with ends on 1st of December coming on Sunday). We do not see any reason for next week to be extremely cheap, so rates should hover around this week's levels.



Forex

Spot - EUR/PLN - higher in the range Signs of progress on a U.S.-China trade deal? The main focus is still the trade talks between Beijing and Washington. The U.S. Senate bill backing Hong Kong protesters could complicate progress towards a preliminary trade deal. China condemned the US Senate's efforts to support protesters for democracy. During the last days, the Polish Zloty has stayed stable and fluctuated in a narrow range. It looks like it may still be influenced by signals from the global markets.

Options - EUR/PLN vol falling down It was again a very calm week on the options market. Most of the action was in short term gamma covering big events in December (GB election, ECB, FED decision) - 1m ATM were paid around 4.0%. The rest of the curve were relatively stable. Finally today 1 month EUR/PLN ATM is at 3.75% (0.20% lower than week ago), 3 months EUR/PLN are 3.75% (0.2% lower) and 1 year is 4.3% (0.05% lower). The skew is roughly higher than week ago, while the currency spread (difference between USD/PLN and EUR/PLN) is at the same level.

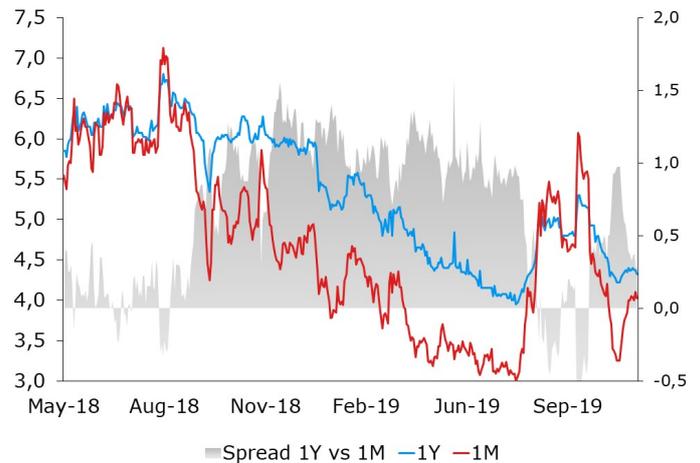
Short-term forecasts

Main supports / resistances:
 EUR/PLN: 4.2500 / 4.3000
 USD/PLN: 3.7500 / 3.9500

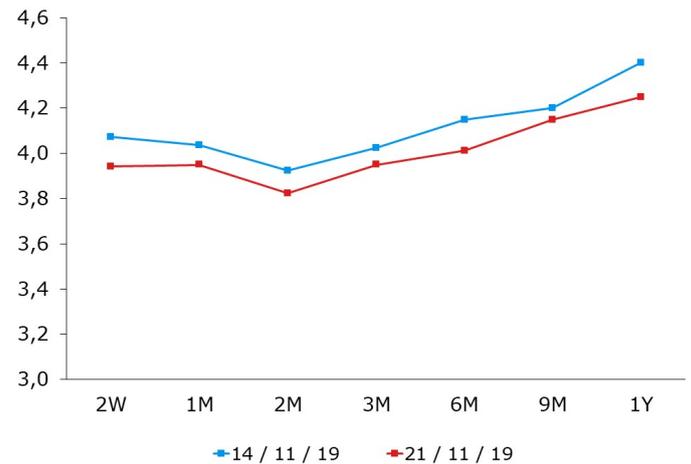
Current position: None.

We don't have a position at the moment, but are ready to reverse our position to the short EUR/PLN above 4.30. We still believe in 4.25-4.30 range trading in EUR/PLN, and don't expect to break out that range any time soon.

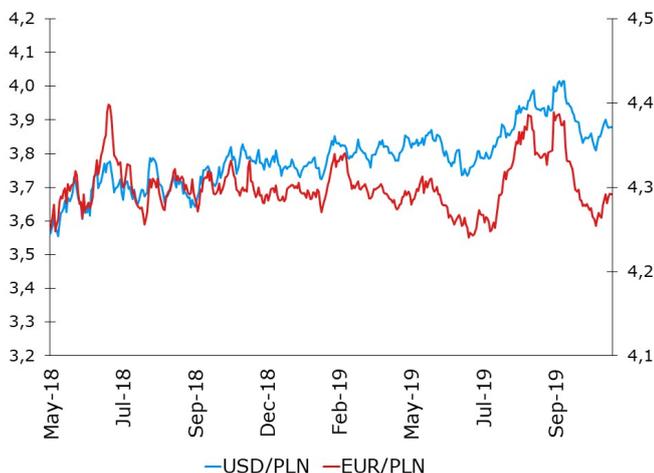
EURPLN volatility



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
11/14/2019	1.92	1.71	1.91	1.69	1.95	1.74	1.71	1.71	1.69	1.65	1.61	1.77
11/17/2019	1.91	1.71	1.89	1.69	1.95	1.74	1.71	1.71	1.69	1.68	1.63	1.77
11/18/2019	1.91	1.71	1.90	1.69	1.96	1.74	1.71	1.71	1.69	1.65	1.62	1.77
11/19/2019	1.86	1.71	1.86	1.69	1.88	1.74	1.71	1.70	1.69	1.65	1.63	1.76
11/20/2019	2.00	1.71	1.99	1.69	1.99	1.74	1.71	1.71	1.67	1.66	1.63	1.77

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
11/14/2019	1.740	0.797	1.720	1.399	1.755	1.794	1.822	2.082
11/17/2019	1.740	0.798	1.735	1.399	1.787	1.828	1.853	2.100
11/18/2019	1.740	0.792	1.697	1.401	1.773	1.825	1.814	2.095
11/19/2019	1.740	0.884	1.735	1.416	1.765	1.831	1.830	2.095
11/20/2019	1.740	0.851	1.715	1.400	1.717	1.806	1.775	2.055

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY
Date	1M	3M	6M	1Y	1M	1Y	1Y
11/14/2019	4.04	4.03	4.15	4.40	4.40	1.01	0.42
11/17/2019	4.00	3.98	4.18	4.38	4.38	1.01	0.42
11/18/2019	4.10	3.98	4.15	4.38	4.38	1.01	0.42
11/19/2019	4.03	3.95	4.13	4.33	4.33	1.01	0.42
11/20/2019	3.95	3.95	4.01	4.25	4.25	1.01	0.43

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
11/14/2019	4.2916	3.9011	3.9501	3.5920	1.2859	0.1680
11/17/2019	4.2807	3.8848	3.9206	3.5744	1.2793	0.1673
11/18/2019	4.2884	3.8767	3.9133	3.5565	1.2787	0.1675
11/19/2019	4.2928	3.8786	3.9113	3.5654	1.2818	0.1680
11/20/2019	4.2917	3.8792	3.9126	3.5775	1.2878	0.1681

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