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Polish Weekly Review

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Table of contents

Our view in a nutshell

Economics

■ Inflation outlook: business as usual

Fixed income

■ Where have all the flows gone?

Money market

■ Very low liquidity

FX market

■ Spot – Zloty stable, but the tariff deadline on December 15th looms

■ Opts – EUR/PLN vols – trading water

Comment on the upcoming data and forecasts

A busy week ahead of us. This Friday, Statistics Poland will publish detailed CPI data for November. The breakdown of the flash estimate (2.6% y/y) suggested a knife-edge reading, with high likelihood of an upward revision, to 2.7% y/y. Core CPI also rose considerably, from 2.4 to 2.6% y/y - NBP's official release is due on Monday. Also on Monday the NBP will publish monthly balance of payments data. We expect them to show a slightly higher CA surplus in October and a lower trade surplus. On Wednesday monthly labor market data will be published. Employment figures are unlikely to bring any major surprises and we (as most analysts do) expect a flat reading at 2.5% y/y. Wage growth is set to decelerate again, from 5.9 to 5.4% y/y, on the back of unfavorable calendar. The same factor will likely push industrial output growth (publication on Thursday) down into negative territory. Very warm November is also a factor due to its impact on energy output. Finally, next Friday Statistics Poland will release retail sales figures. We expect a weak print, mainly due to the impact of trading day count and high base on sales of food and in nonspecialized stores. The structural shift of Christmas purchases to November is unlikely to negate that.

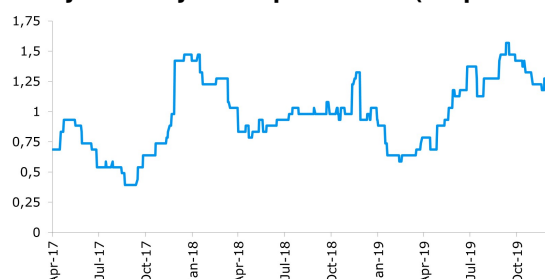
Polish data to watch: December 13th to December 20th

Publication	Date	Period	mBank	Consensus	Prior
CPI final y/y (%)	13.12	Nov	2.7	2.6	2.5
Current account balance (mio EUR)	16.12	Oct	324	250	171
Exports (mio EUR)	16.12	Oct	20900	21591	19279
Imports (mio EUR)	16.12	Oct	20700	21227	18811
Core CPI y/y (%)	16.12	Nov	2.6	2.6	2.4
Employment y/y (%)	18.12	Nov	2.5	2.5	2.5
Average gross wage y/y (%)	18.12	Nov	5.4	5.9	5.9
Consumer confidence	18.12	Dec			
Sold industrial output y/y (%)	19.12	Nov	-1.1	0.9	3.5
PPI y/y (%)	19.12	Nov	0.3	0.3	-0.1
MPC minutes	19.12	Dec			
Real retail sales y/y (%)	20.12	Nov	1.1	4.2	4.6
Business confidence	20.12	Dec			

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

Unchanged (no publications). Next week brings a slew of macro releases and the index is likely to move.

* 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 spending (both consumption and especially investment) and weaker demand outlook are to blame. That being said, consumption will remain very resilient and this makes all the difference compared to 2011-2013 cycle. Our current 2020 forecasts call for 2.8% y/y growth. Downward revision is due to Q3'19 surprise and faster slowdown in investment.
- 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 wage growth.
- 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. Bypassing the expenditure rule via off-balance vehicles changes little in the overall assessment of the fiscal stance. General government deficit will remain low as local governments are set to cut investment considerably.

Financial markets

- In general, PLN remains very stable. Most swings are generated by global growth worries, dollar strength (or weakness) and the occasional local factor bubbling up into the surface (like the CHF loan rulings).
- 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, a slowdown is a 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	4.3	2.8
CPI Inflation y/y (average %)	-0.9	-0.6	2.0	1.6	2.3	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	5.2	5.0
Repo rate (end of period %)	1.5	1.5	1.5	1.5	1.5	1.5

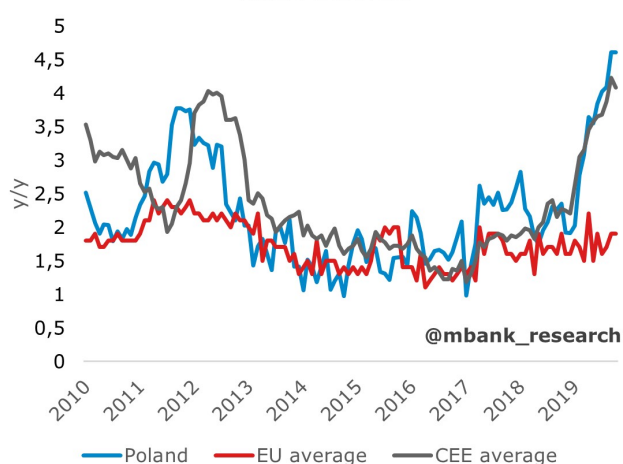
	2019 Q1	2019 Q2	2019 Q3 F	2019 Q4 F	2020 Q1 F	2020 Q2 F	2020 Q3 F	2020 Q4 F
GDP y/y (%)	4.8	4.6	3.9	3.7	3.2	2.7	2.6	2.6
Individual consumption y/y (%)	3.9	4.4	3.9	4.3	4.3	4.0	3.4	2.8
Public Consumption y/y (%)	6.3	3.1	4.7	5.0	3.0	3.0	3.0	3.0
Investment y/y (%)	12.2	9.1	4.7	2.5	-2.0	-3.0	-3.0	-3.0
Inflation rate (% average)	1.2	2.4	2.8	2.7	3.1	2.6	2.1	2.4
Unemployment rate (% eop)	5.9	5.2	5.1	5.2	5.3	4.7	4.8	5.0
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	1.35	1.50	1.53	1.53	1.54
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

Inflation outlook: business as usual

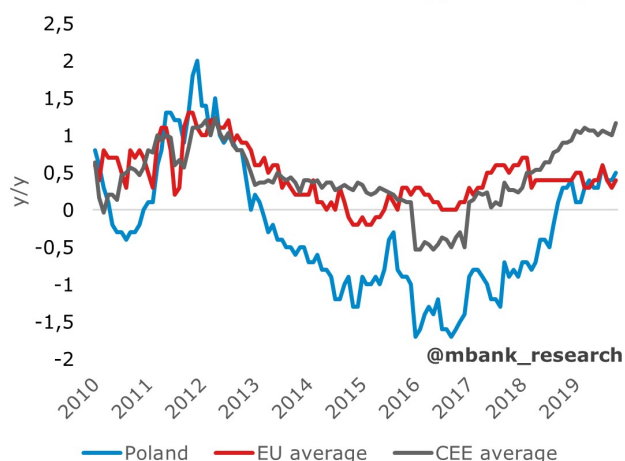
The passing week was devoid of stimuli flowing from fresh data. It is therefore a good time to sum up what we have so far, though. Let's look at inflation in regional breakdowns. Although everything looks as if inflation made a long journey and has embarked on upwards trend, it is unlikely to be the case within the monetary policy horizon. We see a classic hump-shaped inflation path for 2020 with a return below 2.5% becoming more and more likely with every passing month.

HICP: Services



It is fairly easy to see that with regard to inflation in services, Poland stands out in Europe. It stands out to the same extent as the whole CEE region. It is no coincidence given the trends in the labor market and other price increases that were recently penciled in, and given the changes in the market structure in some areas (telecommunication, waste collection, incoming electricity hikes). Some of them went fully independent, some may be somehow connected with the phase of the cycle. And the cycle is turning. Strong, exogenous EU-sponsored investment component has been turning and heading into reverse for a while. Exports performance is in the doldrums as well given the sorry state of the global economy. The conjunction of those negative factors is insufficient to push Polish economy to recession, but sufficient to guarantee further slowdown. We forecast 2.8% GDP growth in 2020. It should coincide with lower labor demand, slower wage growth and in turn, cool inflation in services.

HICP: Non-energy industrial goods



As for inflation in goods, Poland is close to EU average and below CEE levels. Given the state of global manufacturing we are open even to a possibility that those prices return to negative territory. As long as UE inflation is anchored, goods inflation in Poland is unlikely to accelerate. It seems we witness as ceiling in goods inflation.

Fixed income

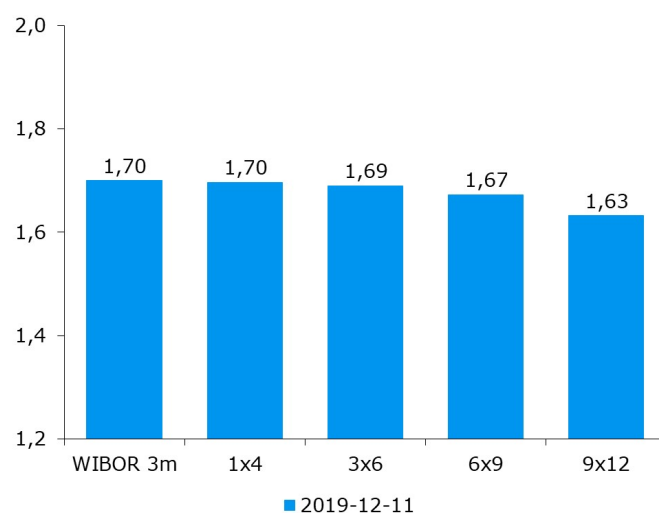
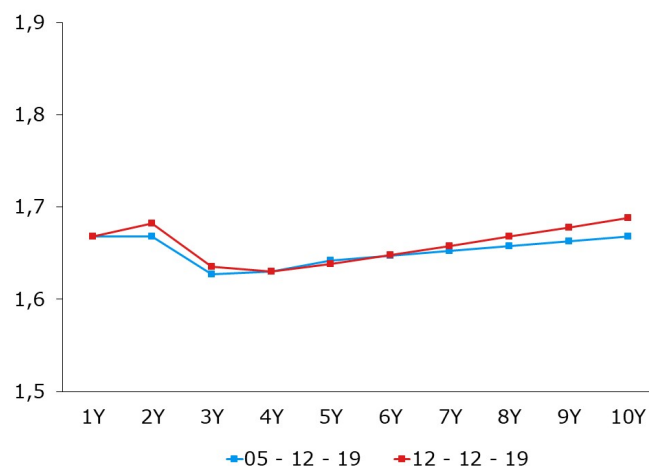
Where have all the flows gone?

Volatility in the local market remains extremely low, there is hardly any turnover with local customers. Most of the offers on bonds come from internationals, who reduce their positions in POLGBs. We don't expect anything to change until next year.

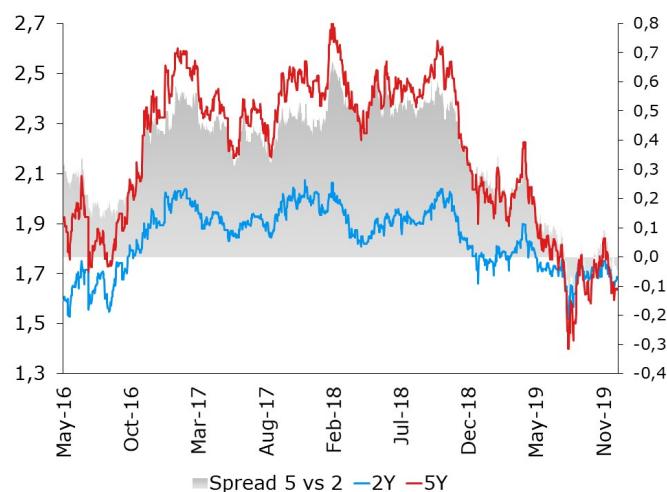
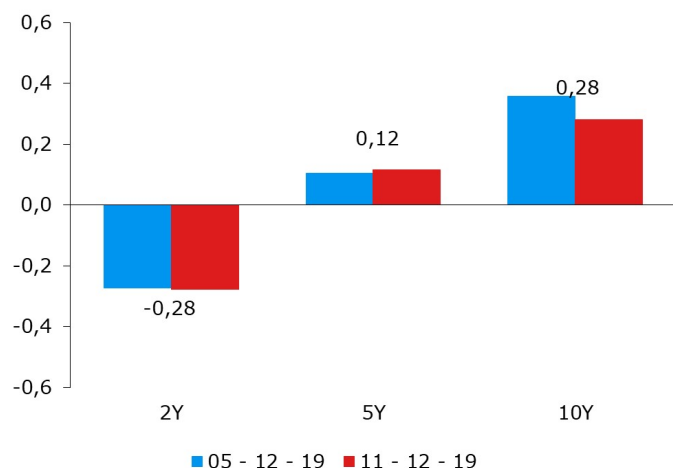
PS1024/5y is 10bps, DS1029/10y is 31bps. PS1024/DS1029 is 25bps DS1029/Bund is 229bps.

DS1021 is trading at 1.38% (1 bps up), PS1024 is trading at 1.75% (no change) and DS1029 is trading at 2.01% (no change).

IRS curve



Asset swaps

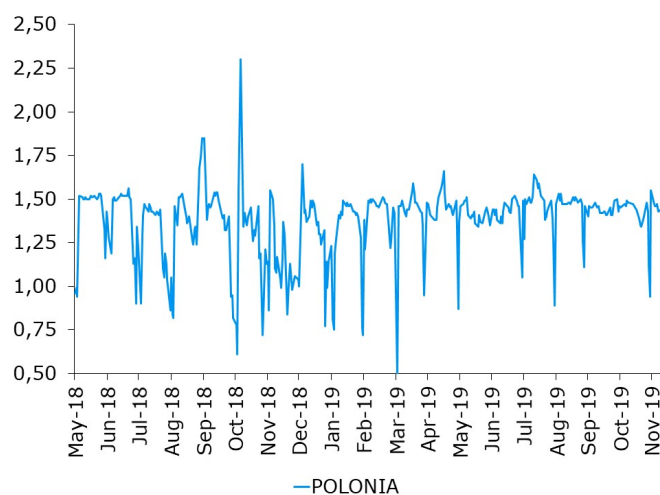
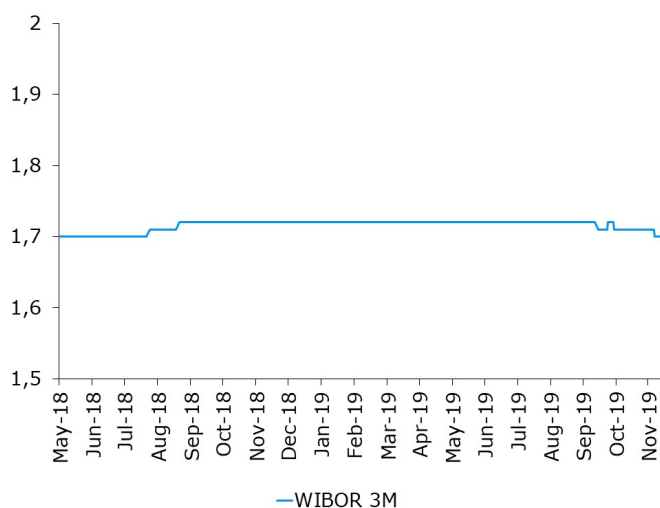
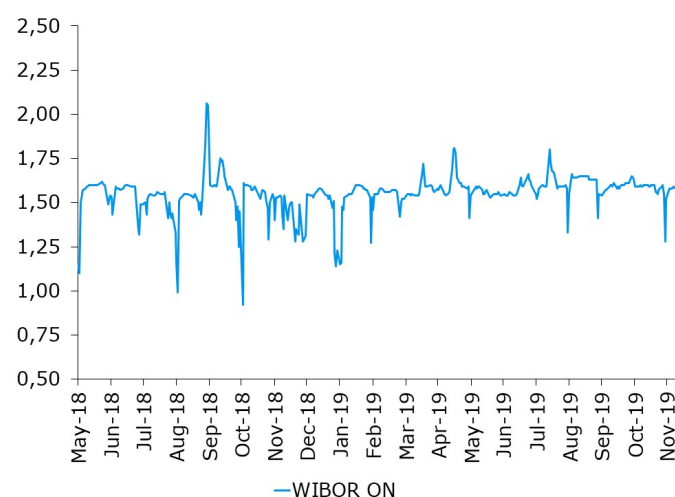
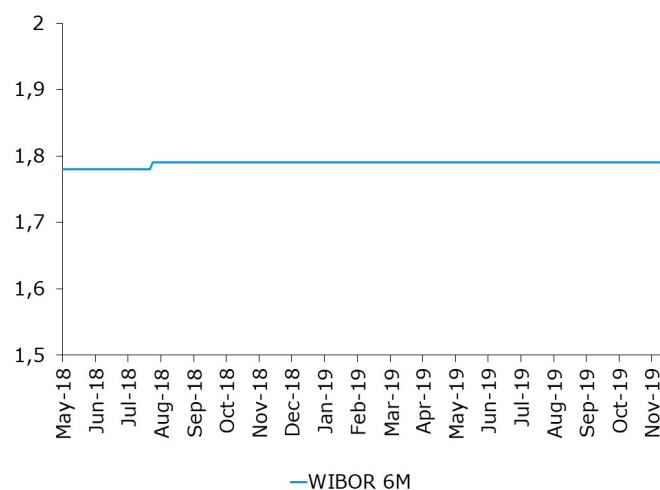


Money market

Very low liquidity

For the past week volatility has been falling drastically. Rates are stuck close to the lower bound of recent range. Looks like trading desks already ended their year. ASW remain wide and this might continue until the end of the year due to funding difficulties. Liquidity is so poor that any significant flow can push the market either way.

Funding for last week was easy, but feels like rates should be lower with such surplus on accounts.



Forex

Spot – Zloty stable, but the tariff deadline on December 15th looms

The trade war continuing to take its toll on market sentiment; investors are still hoping for a delay in tariffs, though. In line with expectations, the Federal Reserve kept interest rates unchanged and signaled no appetite to raise them anytime soon. In recent days, the Zloty was stable and fluctuated in the narrow 4.2715-4.2920 range, despite the increase in global risk factors i.e. uncertainty about tensions between the U.S and China and elections in the United Kingdom. We will see soon if the latter can produce any volatility on FX market.

Opts – EUR/PLN vols – treading water

It was another very calm week on the spot market. Historically, implied volatilities are very cheap, but the realized volatilities are not really encouraging for any purchases. EUR/PLN ATM mid today is 3.35% (0.15% lower), 3 month is 3.7% (0.05% lower) and finally 1 year fixed at 4.1% (unchanged). The skew and currency spread (difference between USD/PLN vol and EUR/PLN) are also lower.

Short-term forecasts

Main supports / resistances:

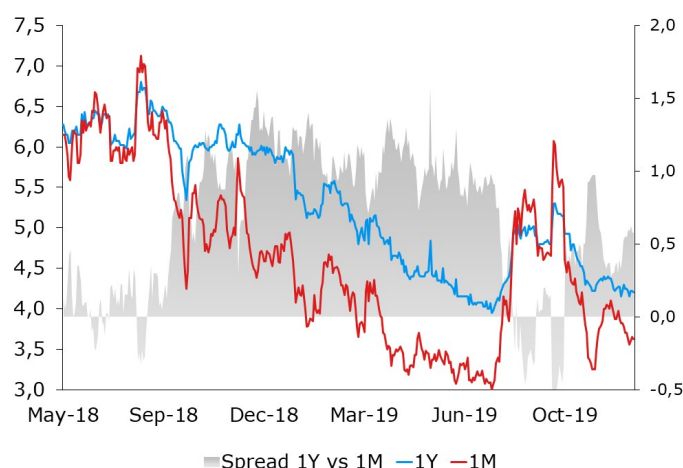
EUR/PLN: 4.2500 / 4.3000

USD/PLN: 3.7500 / 3.9500

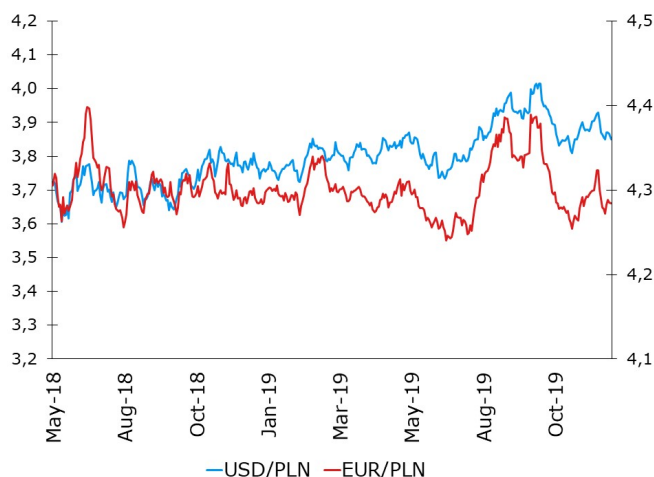
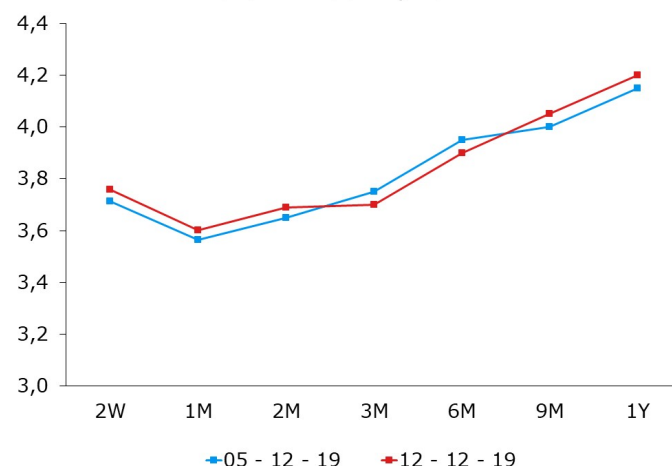
Spot: Current position: None

It was a lucky week for short EUR position. We cashed our position at 4.2730. In our view, EUR / PLN will stay in the 4.26 / 4.31 range in the coming week. We prefer to be on the sidelines now.

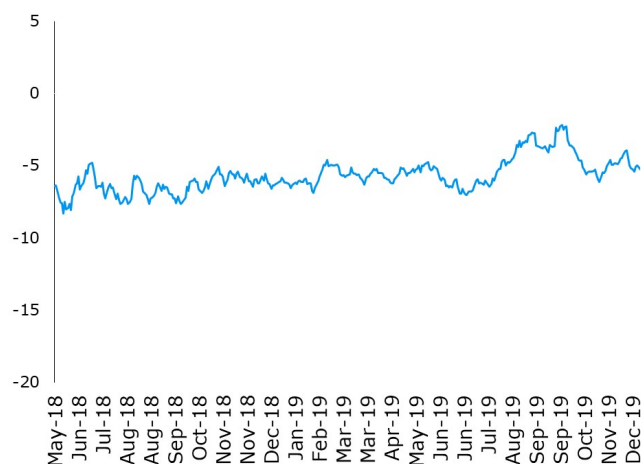
EURPLN volatility



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
12/5/2019	1.91	1.71	1.91	1.69	1.93	1.74	1.71	1.70	1.66	1.62	1.57	1.73
12/8/2019	1.93	1.70	1.92	1.69	1.93	1.74	1.70	1.70	1.67	1.63	1.58	1.74
12/9/2019	1.91	1.70	1.92	1.69	1.93	1.74	1.70	1.69	1.67	1.62	1.57	1.76
12/10/2019	1.84	1.70	1.85	1.69	1.86	1.74	1.69	1.69	1.67	1.63	1.59	1.74
12/11/2019	1.87	1.70	1.91	1.69	1.94	1.74	1.70	1.69	1.67	1.63	1.60	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
12/5/2019	1.740	0.985	1.668	1.395	1.642	1.747	1.669	2.027
12/8/2019	1.740	1.008	1.670	1.398	1.638	1.742	1.688	2.006
12/9/2019	1.740	0.937	1.678	1.394	1.635	1.740	1.656	1.965
12/10/2019	1.740	0.923	1.688	1.402	1.642	1.755	1.695	1.978
12/11/2019	1.740	0.884	1.682	1.405	1.638	1.754	1.688	1.969

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY	
Date	1M	3M	6M	1Y	1M	1Y	1Y	
12/5/2019	3.56	3.75	3.95	4.15	4.15	0.96	0.42	
12/8/2019	3.60	3.85	4.03	4.23	4.23	0.96	0.42	
12/9/2019	3.65	3.75	4.03	4.23	4.23	0.96	0.44	
12/10/2019	3.63	3.80	3.93	4.20	4.20	1.01	0.44	
12/11/2019	3.60	3.70	3.90	4.20	4.20	0.90	0.41	

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
12/5/2019	4.2777	3.8566	3.8989	3.5394	1.2926	0.1676
12/8/2019	4.2721	3.8500	3.8963	3.5446	1.2934	0.1673
12/9/2019	4.2830	3.8704	3.9087	3.5674	1.2911	0.1677
12/10/2019	4.2880	3.8711	3.9251	3.5647	1.2927	0.1680
12/11/2019	4.2851	3.8660	3.9257	3.5570	1.2975	0.1679

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