Bank Zachodni WBK
Grupa Santander

WEEKLY ECONOMIC UPDATE

11 – 17 November 2013

Central banks surprised investors on several occasions during the past week – the Polish MPC extended the suggested period of stable interest rates until mid-2014, the ECB cut main refinancing rate to 0.25% and the Czech central bank intervened on the FX market. Apparently, the era of ultra-ease monetary conditions lasts and does not seem to end fast. Despite strong plunge of EURUSD and substantial surge of EURCZK, EURPLN stayed in a narrow range trading while Polish debt strengthened.

This week, although shorter due to market holiday on Monday in Poland and in the US, will be full of crucial information. In Poland, next to the release of the new *Inflation Report*, set of key data will be published with October's CPI and flash Q3 GDP in the spotlight. In our opinion, data on current account (acceleration of exports and significant trade surplus) and on GDP (clear rebound) may have moderately positive impact on the domestic currency. Lower than expected data on inflation may neutralise impact of this data on the interest rate market.

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		MONDAY (11 November)					
	PL	**The Independence Day**					
9:00	CZ	CPI	Oct	%YoY	0.9	-	1.0
		TUESDAY (12 November)					
9:00	HU	CPI	Oct	%YoY	1.4	-	1.4
10:00	**PL**	**Publication of Inflation Report**					
14:00	**PL**	**Current account balance**	**Sep**	**€m**	**-762**	**-694**	**-719**
14:00	**PL**	**Exports**	**Sep**	**€m**	**13 648**	**13 800**	**12 451**
14:00	**PL**	**Imports**	**Sep**	**€m**	**13 238**	**13 100**	**12 187**
		WEDNESDAY (13 November)					
11:00	EZ	Industrial output	Aug	%MoM	-0.3	-	1.0
		THURSDAY (14 November)					
8:00	DE	Flash GDP	Q3	%YoY	0.6	-	0.5
9:00	HU	Flash GDP	Q3	%YoY	0.7	-	0.5
9:00	CZ	Flash GDP	Q3	%YoY	-0.4	-	-1.3
10:00	**PL**	**Flash GDP**	**Q3**	**%YoY**	**1.6**	**1.8**	**0.8**
11:00	EZ	Flash GDP	Q3	%YoY	-0.3	-	-0.5
14:00	**PL**	**CPI**	**Oct**	**%YoY**	**1.0**	**0.9**	**1.0**
14:00	**PL**	**M3 money supply**	**Oct**	**%YoY**	**5.8**	**5,8**	**6.1**
14:30	US	Initiaj jobless claims	week	k	330	-	336
		FRIDAY (15 November)					
11:00	EZ	HICP	Oct	%YoY	0.7	-	1.1
14:00	**PL**	**Core inflation**	**Oct**	**%YoY**	**1.3**	**1.3**	**1.3**
15:15	US	Industrial output	Oct	%MoM	0.1	-	0.6

Source: BZ WBK, Reuters, Bloomberg, Parkiet

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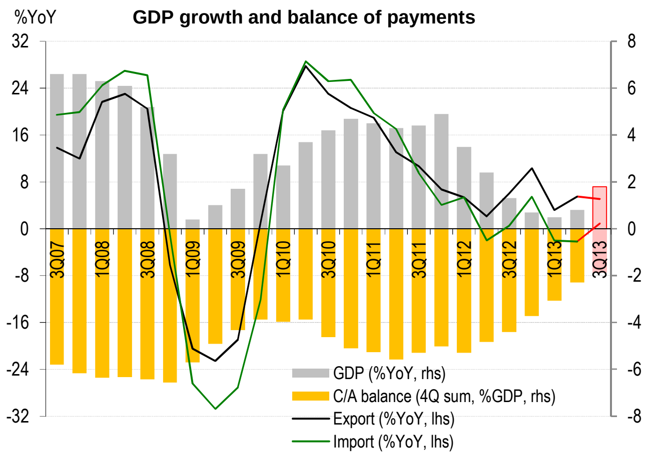
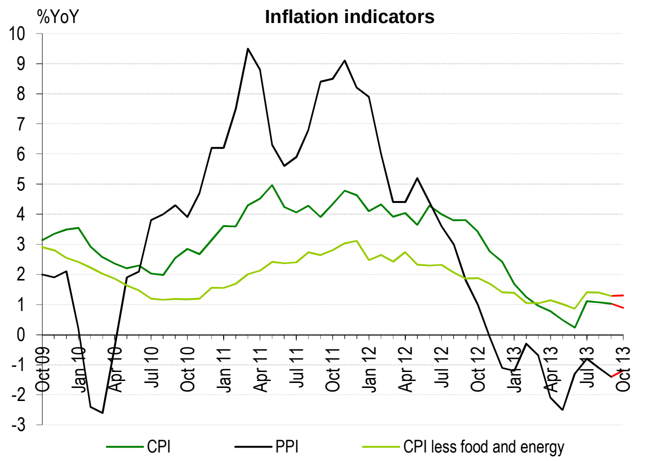
What's hot this week – Short week, yet full of important data



- Shorter week will start with the release of NBP's *Inflation report* and balance of payments data. The Report will show, among others, what assumptions lie behind the NBP's predicted path of inflation, which is quite low, despite anticipated acceleration of economic growth. Please recall that our forecasts assume faster medium-term inflation growth than in the NBP's projection.
- We predict a clear improvement of foreign trade turnover in September (effect of higher external demand, but also number of working days and low statistical base). Despite acceleration of export growth and sizeable surplus in trade in September (Q2 will record the second quarterly surplus in a row!), the current account will be in red (due to, among others, low inflow of transfers from EU). Still, in relation to GDP the current account has been shrinking, which is positive for the zloty.



- Thursday will be the most important day for domestic market, as the CSO will release data about October's inflation and flash GDP estimate for Q3. We predict that economic growth accelerated significantly to 1.8%YoY, from 0.5%YoY in Q1 and 0.8%YoY in Q2. Market consensus is slightly below and we think that such reading may reinforce investors' belief that the Polish economy is reviving, thus strengthening the zloty.
- Inflation rate in October fell according to our estimates to 0.9%YoY, mainly due to low prices of food and falling prices of fuel. Core inflation (due for release on Friday) remained unchanged in our view, at 1.3%YoY. Data about inflation will be important for market expectations concerning the outlook for NBP official interest rates. Median forecast assumes stabilisation of CPI inflation at 1%YoY, thus the lower reading may be the factor that would neutralise the impact of better GDP data on the interest rate market.

Last week in the economy – Central banks in action

NBP projections in subsequent *Inflation reports*

	GDP growth			
	Nov 12	**Mar 13**	**Jul 13**	**Nov 14**
2013	0.5-2.5	0.6-2.0	0.5-1.7	1.0-1.5
2014	1.1-3.5	1.4-3.7	1.2-3.5	2.0-3.9
2015	x	1.9-4.4	1.6-4.2	2.1-4.5
	CPI growth			
	Nov 12	**Mar 13**	**Jul 13**	**Nov 14**
2013	1.8-3.1	1.3-1.9	0.6-1.1	0.9-1.0
2014	0.7-2.4	0.8-2.4	0.4-2.0	1.1-2.2
2015	x	0.7-2.4	0.7-2.4	1.1-2.6

- The Polish MPC kept interest rates on hold in November, as expected. At the same time, the Council surprised, extending the declared period of stable interest rates „at least until the end of the first half of 2014". New projection of the central bank is more optimistic in terms of economic growth (GDP at ca. 3% in 2014 and above 3% in 2015), but the forecast of inflation remained low (below 2%). In our opinion, CPI next year will be higher and the MPC will start hiking rates in the third quarter of 2014.
- The ECB and the Czech central bank delivered even bigger surprises, as the former cut interest rates by 25bps, and the latter intervened in the FX market. Apparently, the era of ultra-loose monetary policy is not over.
- PMI for Polish manufacturing sector increased in October to 53.4, slightly above our forecast and much above market consensus. The record growth of new export orders bodes well for Polish industrial production and exports.

Quote of the week – Government reshuffle to include finance minister?

Donald Tusk, Prime Minister, 8.11, PAP

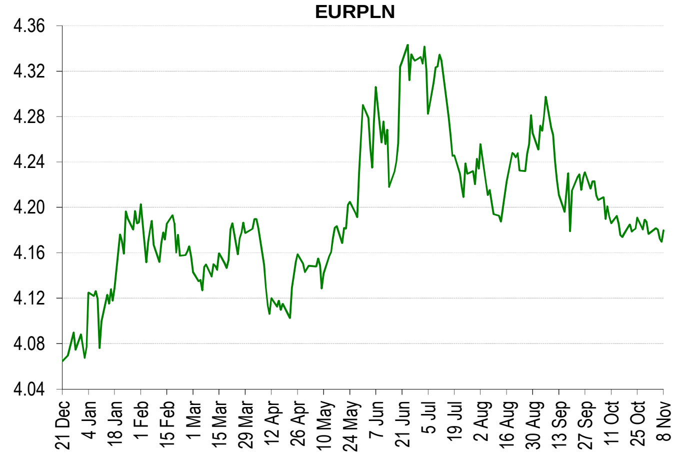
As I said last month, two months ago, half a year ago and year ago - a reshuffling of cabinet will take place in November this year.

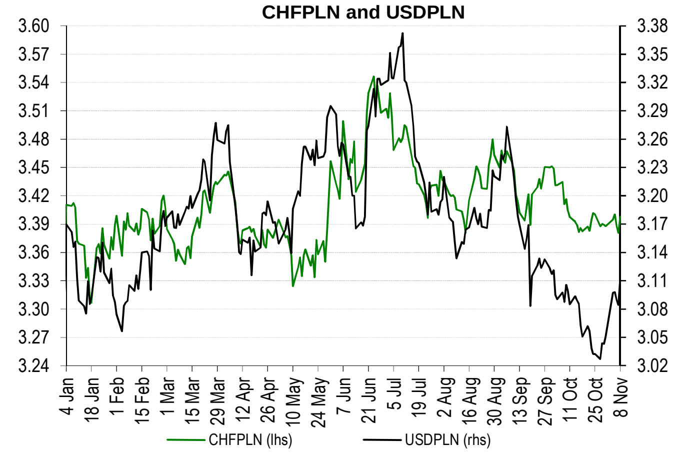
Jacek Rostowski, finance minister, 6.11, Gazeta Wyborcza

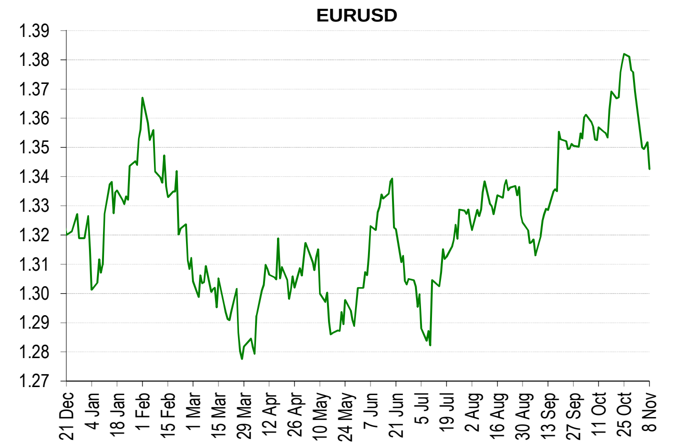
Poland's government should undergo a far-reaching reconstruction. PM Tusk should establish a new team which would lead PO to the parliamentary elections in 2015 and present the program for the coming two years and for the first half of the next term. (...) During the last six years, I was thinking about leaving the government each year. Yet, I'm still there.

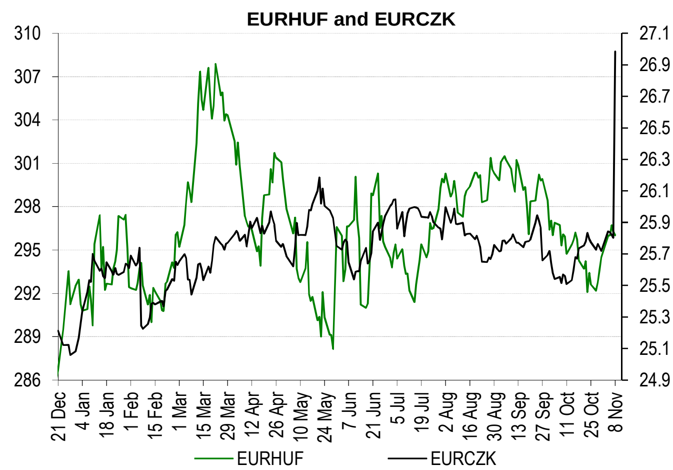
Rumours on a possible dismissal of the Polish finance minister appeared at least two times in recent months. Until now, this scenario did not materialise. Nevertheless, the reconstruction of the government scheduled for November is again a source of speculations whether Rostowski will quit. It is hard to guess to what extent the media information are justified. A possible dismissal of Rostowski crates a risk factor from the point of the Polish market in the short-term. If this happens, a perception by the market of the event would depend on who replace finance minister. If a new candidate is not known for the market, we can see some negative effect on Polish assets.

Foreign exchange market – High volatility, but mainly for the euro and koruna rather than for the zloty









More visible moves, but without breaking changes

- In response to surprising decisions of ECB and CNB, EURPLN tested both upper and lower bands of 4.16-4.20 range last week. Still, though the scale of moves widened when compared to earlier days, no breaking changes were recorded.
- Higher volatility of EURPLN and sudden changes of EURUSD clearly influenced the zloty vs. the dollar – USDPLN surged to 3.14 – highest level since late September.
- We have just had two weeks of crucial global (FOMC meeting, ECB decision, US data) and regional (CNB decision) events. Still, neither substantial plunge of EURUSD nor considerable surge of EURCZK did not manage to push EURPLN from 4.16-4.20 range. This week will be full of vital Polish data. Our forecast of GDP growth in Q3 is slightly above market consensus and confirmation of an economic recovery may have only moderate positive impact on the zloty. Just like data on slightly lower than market expects C/A deficit. Range 4.16-4.20 is still in place, next support and resistance at 4.14 and 4.24, respectively.

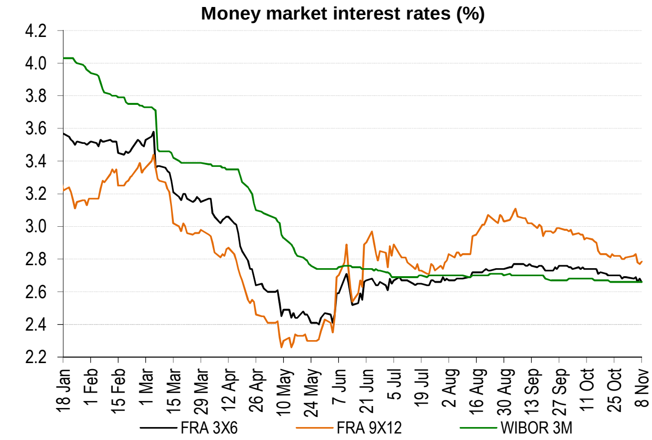
ECB decision hits euro vs. the dollar

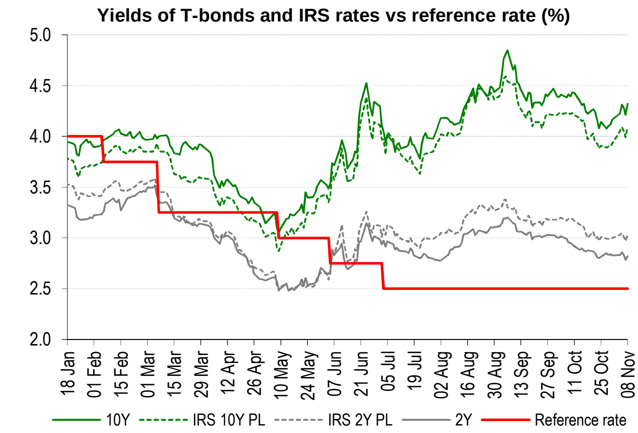
- When considering the low and peak from the past two weeks, EURUSD recorded biggest two-week plunge since November 2011. The euro was under pressure from flash inflation in the euro zone and then after the unexpected ECB rate cut. Consequently, EURUSD plunged from 1.38 to 1.33, retracing a half of an upward move seen since July till October (from 1.275 to 1.382).
- The calendar of macro data releases in the euro zone and the US for coming days is rather poor, only at the end of the next week data on initial jobless claims and industrial output may attract some attention. Many FOMC members will give speeches but neither of them has currently a voting right. Support and resistance for EURSUD is at 1.33 and 1.35.

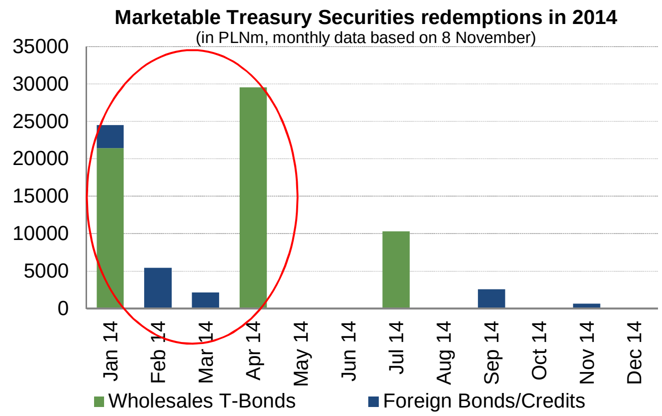
Czech central bank stops talking, starts doing

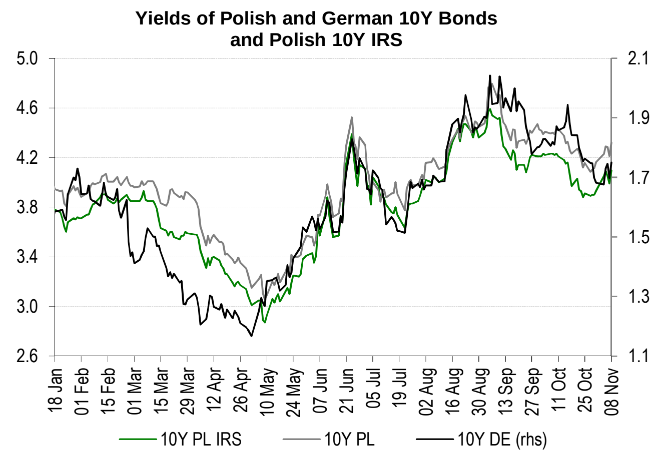
- The CNB has been suggesting for already few months, that after having cut interest rates to 0.05%, it may decide to launch FX interventions as an additional instrument for further monetary policy easing. Only at the November's meeting the majority for motion to weaken the Czech koruna was gathered. CNB informed that its official target for EURCZK is 27.0 and immediately after this decision was announced (and due to prompt actions taken) the exchange rate reached nearly this level. After this substantial surge of EURCZK, the zloty was strongest vs. the Czech koruna since May 2010.
- No major changes occurred on the forint market. The ruling party, Fidesz, proposed expanding the scheme that provides a relief to foreign currency mortgage holders to those who owe more than HUF20m or are behind the instalment payments more than 90 days (currently they are not supported). Recently, Hungarian courts issued some contradicting decisions in lawsuits between borrowers and banks so Hungarian government decided that legal issues concerning foreign exchange loans must be settled before it presents his propositions of further relief for creditors.
- This week flash 3Q GDP data will be released also for Czech Republic and Hungary. After recent decision of the CNB, the importance of the reading for our neighbouring country seems to be limited. Data for Hungary are likely to be more important (also those on CPI), because they may influence market expectations regarding future decisions of Hungarian central bank. If market perceives these figures as dovish, then this may hit forint.

Interest rate market – Profit taking after earlier rally and the US labour market data









Market has just priced-in the first hike in a year's time

- Last week WIBOR rates have remained stable. MPC's decision to extend period of stable official rates till mid-2014 affected mainly FRA market. Only in the day of the MPC meeting FRA rates decreased by 1-5bp, in which rates of longer tenors fell more significantly. However, expectations on future path of the official interest rates remained unchanged. The first hike might take place in one year horizon (FRA12x15 close to 3%).
- This week the most important for market players will be releases of GDP and CPI data (both publications on Thursday). Firstly, GDP data should confirm further acceleration of economic growth, while published early afternoon inflation rate might show, according to our forecast, slight decline. Our forecast is below market consensus (0.9%YoY vs 1%YoY), therefore we do not exclude some decline in money market rates, in particular FRA. In our opinion, current market expectations are too optimistic and hikes might take place earlier (3Q 2014).

Central banks supported domestic debt market

- The beginning of week brought weakening of debt market. It came from global mood deceleration, and also detailed information about Thursday's auction. In the following days investors' mood was under influence of central banks' actions. Market reaction to the MPC's decision was positive, but moderate. More significant fall of yields / IRS rates (in particular on the long end of curves) took place after unexpected ECB decision, trimming official rates by 25bp. However, the end of the week brought some profit taking after earlier significant strengthening and due to better than expected data from the US labour market.
- Last week was very successful for Poland's Ministry of Finance as an issuer. On domestic primary market the Ministry sold 2Y T-bonds OK0116 worth ca PLN3.2bn with auction yield at 2.983% and 5Y benchmark PS0718 worth ca PLN4.79bn with auction yield at 3.589%. Solid demand (PLN14.6bn in total) was generated by mainly domestic non-banking investors, supporting among others by funds from DS1013 redemptions and coupon payments. With great success the Ministry tapped the Japanese market, launching two tranches of Samurai bonds worth JPY60bn. Funds from both issues will finance the 2014 borrowing requirements. We would like to recall that the bulk of next year's redemption in both PLN and foreign currencies is concentrated at the beginning of the year (see chart). What is more, the Ministry of Finance officials say that Poland may hold further bond issues on foreign markets in coming months, in which on the American one. Apart from the public issue of bonds denominated in the US dollar, the Ministry is analysing "the efficiency of other, less standard projects".

Focus on domestic data

- November's MPC decision together with inflation data for October, which will be released this week (CPI, core inflation) should stabilise the front end of curves near current levels, i.e. 2.85% for 2Y benchmark and ca 3% for 2Y IRS. These instruments might stay relatively resistant to changes in investors' mood. One should notice that short term instruments remained very attractive for foreign investors.
- The mid and long ends of curves will vary depending on upcoming domestic and external macro data. After better than expected the US labour market data yield of 10Y T-bonds tested local maximum at 4.30%. We expect both yield and IRS curves to remain steep, with possibility of further 2-5Y spread widening.
- This week a buy-back auction of the US dollar denominated bonds will take place. Nominal value of buy-back is up to $100m. Auction results will be neutral for investors' mood.

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