

# WEEKLY ECONOMIC UPDATE

## 15 – 21 December 2014

The global market was quite volatile last week even without any important data releases. This week is filled with publications of crucial macro figures – both Polish and foreign – and important events with the FOMC meeting in the spotlight. In our view, Polish CPI and industrial output data will keep hopes for more NBP rate cuts alive and this may support domestic bonds and drag the IRS slightly down. What should be positive for the FI market could, however, hit the zloty. Additional pressure on the Polish currency may come from a much wider-than-expected C/A deficit – our forecast is well below the consensus. We still expect the zloty to appreciate vs. the euro in the coming months, but the pace of this trend may be sluggish given the recent adverse events.

### Economic calendar

CZAS W-WA	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
<b>MONDAY (15 December)</b>							
14:00	PL	CPI	Nov	%YoY	-0.5	-0.5	-0.6
14:00	PL	Current account	Oct	€m	-320	-783	-235
14:00	PL	Exports	Oct	€m	14 701	14 500	14 251
14:00	PL	Imports	Oct	€m	14 416	14 300	13 647
15:15	US	Industrial output	Nov	%MoM	0.7	-	-0.1
<b>TUESDAY (16 December)</b>							
2:45	CN	Flash PMI – manufacturing	Dec	Pts	49.8	-	50.0
9:30	DE	Flash PMI – manufacturing	Dec	Pts	50.2	-	49.5
10:00	EZ	Flash PMI – manufacturing	Dec	Pts	50.6	-	50.1
11:00	DE	ZEW index	Dec	Pts	6.5	-	3.3
14:00	PL	Core inflation	Nov	%YoY	0.5	0.5	0.2
14:00	PL	Employment in corporate sector	Nov	%YoY	0.8	0.9	0.8
14:00	PL	Wages in corporate sector	Nov	%YoY	3.6	3.5	3.8
14:00	HU	Central bank decision		%	2.1	-	2.1
14:30	US	House starts	Nov	k	1035	-	1009
14:30	US	Building permits	Nov	k	1060	-	1092
<b>WEDNESDAY (17 December)</b>							
11:00	EZ	HICP	Nov	%YoY	0.3	-	0.3
13:00	CZ	Central bank decision		%	0.05	-	0.05
14:00	PL	Industrial output	Nov	%YoY	1.0	-1.4	1.6
14:00	PL	Construction and assembly output	Nov	%YoY	-3.5	-11.5	-1.0
14:00	PL	PPI	Nov	%YoY	-1.2	-1.3	-1.2
14:30	US	CPI	Nov	%MoM	-0.1	-	0.0
20:00	US	FOMC decision					
<b>THURSDAY (18 December)</b>							
10:00	DE	Ifo index	Dec	pts	105.5	-	104.7
14:00	PL	MPC minutes					
14:30	US	Initial jobless claims	week	k	-	-	294
16:00	US	Philly Fed index	Dec	pts	26.0	-	40.8
<b>FRIDAY (19 December)</b>							
No important data releases							

Source: BZ WBK, Reuters, Bloomberg

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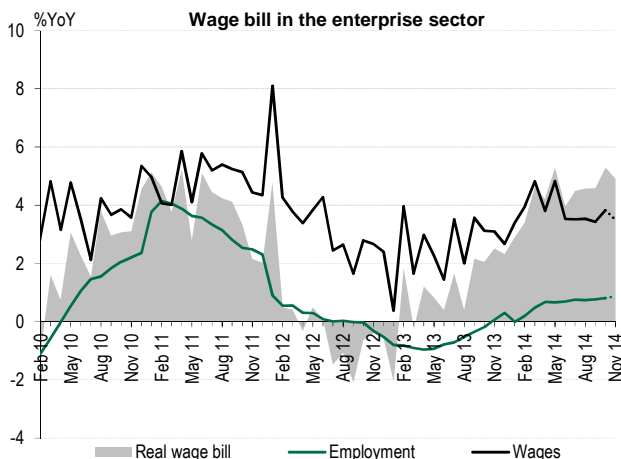
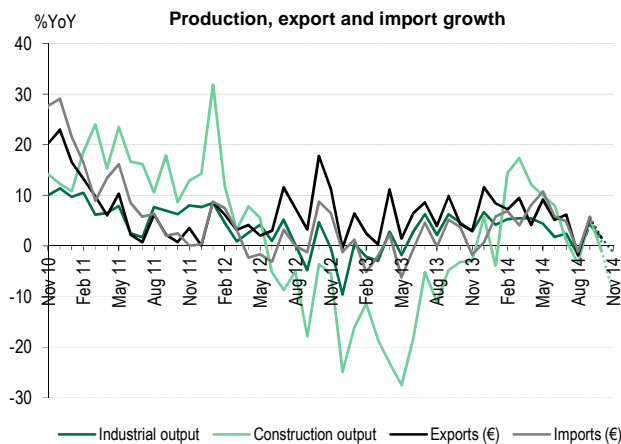
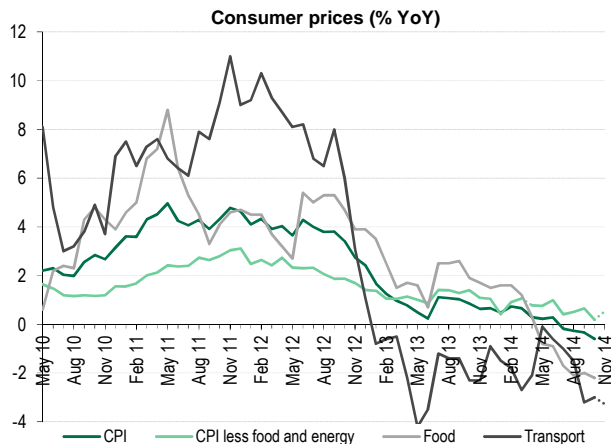
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## Last week in the economy – Heavy macro calendar to confirm slowdown amid no inflation



▪ This week's domestic macro calendar is truly heavy, starting with CPI for November. We expect CPI to inch up to -0.5%YoY from -0.6%YoY in October, though the slight rise will be caused by a base effect in communication prices. The deflationary pressure is not waning, however. On the contrary, it is strengthening. We recently revised our short-term CPI forecasts due to the considerable decline of oil prices, which will lead to lower fuel prices for consumers in Poland. Our current forecast shows that negative CPI growth may continue even until 3Q2015. We expect CPI to reach 1.0%YoY at the end of 2015.

▪ Other inflation measures, such as PPI and core inflation, are also due for release this coming week. These are also likely to confirm the picture outlined by CPI: absence of an upward pressure in prices on the horizon.

▪ We expect a deceleration of both export and import growth in October, mainly on the back of a neutral working- days' effect (which was positive in September). Statistics office data on foreign trade in the first ten months of the year suggested that both exports and imports may have been slightly higher in October than we forecast. Moreover, the data showed some revival of export growth to some euro zone countries, like Germany and France, which bodes well for Polish exports. However, our estimates are based on the assumption that data for the previous months are not revised, which is rarely the case, so it is difficult to draw strong conclusions before more details are released. The current account deficit is likely to widen compared with the September reading, due to lower inflows of EU funds and a lower trade surplus.

▪ Labour market trends most likely stayed positive in November and we expect to see a slight acceleration in employment growth and slightly lower wage growth. Still, demand for jobs remains robust, which means that the moderate wage growth, coupled with the negative inflation, is boosting households' disposable income.

▪ Poland's industrial and construction sectors are probably not faring too well and we expect output in both to contract (YoY). The euro zone's weak economic activity is likely to weigh on the Polish industry in the months to come. However, the recent PMI survey pointed to improving foreign demand from Central and Eastern Europe. If export data will additionally confirm a revival of demand from Germany and France, the outlook could improve markedly.

▪ Generally, we think that data released this week will be dovish, confirming that the Polish economy is slowing down in Q4. We expect this slowdown to be modest and temporary, but let us note that confirmation of the slowdown is one of the conditions indicated by the MPC that could force its policymakers to consider further adjustment of rates.

## Quote of the week – Impossible to see the future is

**Andrzej Bratkowski, MPC member, 8 Dec, forward-looking.pl**

Currently a cut by 100bp seems most justified.

**Jerzy Osiatyński, MPC member, 8 Dec, Reuters**

There is room to cut rates by 50bp at least. I feel I do not meet the basic objective of the MPC, as inflation will not return to target for two years.

**Elżbieta Chojna-Duch, MPC member, 8 Dec, Reuters, PAP**

Price declines in Poland are caused by global factors, mostly by the falling fuel prices. We cannot exert influence over this with our interest rates. (...) There is chance for cautious rate cut in the coming months, although the room for monetary policy easing has narrowed noticeably.

**Anna Zielińska-Giębocka, MPC member, 8 Dec, Bloomberg**

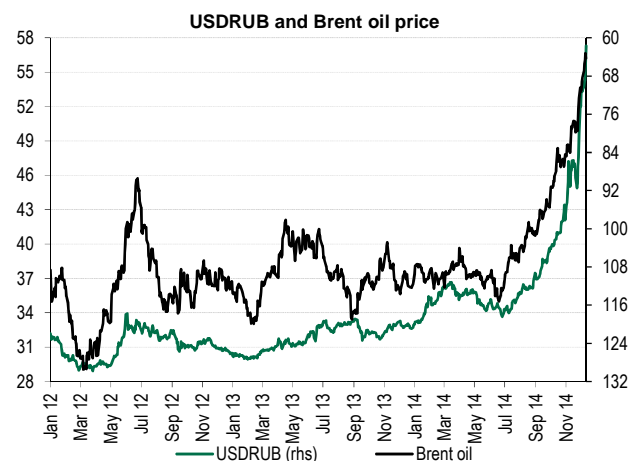
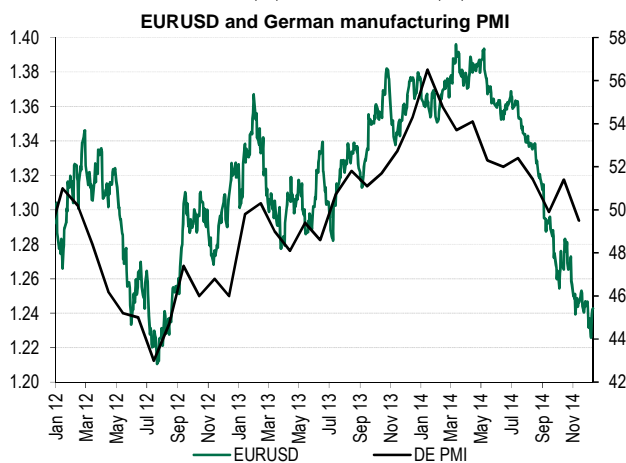
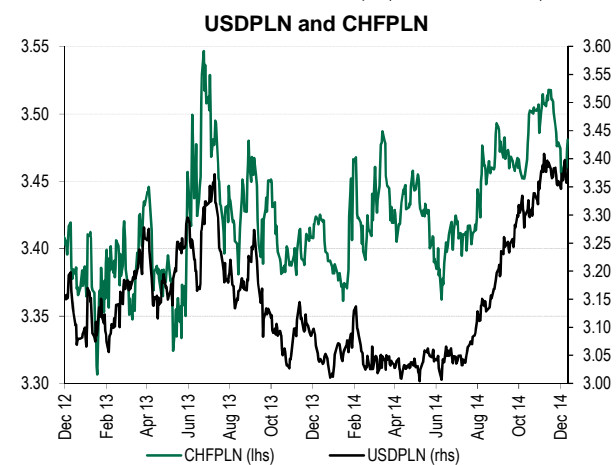
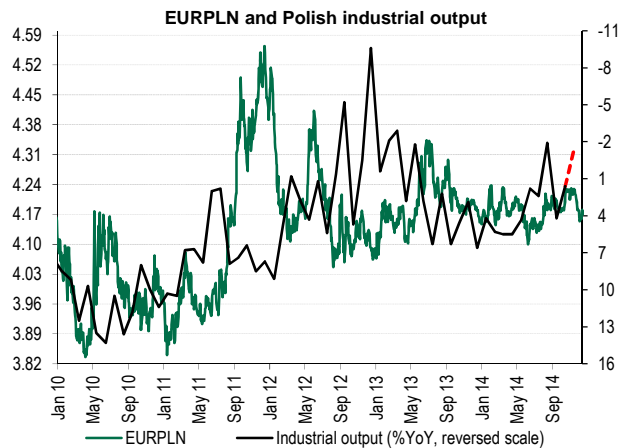
It's impossible to predict what our next moves will be.

**Andrzej Rzońca, MPC member, 10 Dec, PAP**

Interest rates should not be lower than they currently are. Further stimulation of internal demand can cause imbalances in the Polish economy.

Recent comments of the MPC members clearly show that there is conflict and much confusion within the monetary policy authority. A. Bratkowski was clearly the star last week when he refused to take part in editing of the MPC's minutes as he felt "censored". He chose to publish his views on monetary policy on his personal blog instead. Bratkowski and Osiatyński are determined to cut interest rates since inflation is far from the target and the economy is growing below its potential. On the opposite side, there are Rzońca, Winięcki and Kaźmierczak who see no need for policy easing. E. Chojna-Duch, who may be crucial for MPC decision, said that currently there is no need to cut rates, but at the same time admitted that there are chances for cautious rate cut in the coming months. A. Zielińska-Giębocka best summarised this flow of news by saying that it was simply impossible to forecast the MPC's decisions as the Council itself does not know what will happen. Apparently, "the dark side clouds everything" for the Council. We still expect that data showing slower GDP growth and deepening deflation will trigger one more interest rate cut by 25bp in 1Q15.

## Foreign exchange market – Polish data may weigh on the zloty



### EUR/PLN rebounds to 4.18

▪ The zloty depreciated vs. the main currencies – EUR/PLN touched 4.18, while USD/PLN broke 3.37. Deterioration of the global market sentiment and depreciation of other CEE currencies were the main drivers of the domestic currency's weakening.

▪ It is highly likely that the Polish FX market will be volatile in the coming week. Several important global events (economic activity data in Europe, outcome of the FOMC meeting) could trigger noticeable moves in EUR/PLN (also due to the drying liquidity towards the end of the year).

▪ At the same time, we think that Polish macro data – CPI and industrial output in particular – may renew expectations for rate cuts in Poland and this could weigh on the zloty, at least this week. Also, our C/A deficit forecast is well below market consensus.

▪ Breaking of the 4.16-4.17 support area last week opened the door to further EUR/PLN decline towards 4.12 and we do not think that its rise last week denies this scenario. However, given the recent deterioration of the market sentiment (pressure on the EM currencies, non-zero odds for rate cuts in Poland), the pace of the zloty's appreciation may be sluggish.

### Euro recovers vs. dollar, high volatility ahead

▪ The euro recovered slightly vs. the dollar last week thanks to cautious comments of the FOMC members. Dennis Lockhart said he did not want to rush in removing the sentence from the Committee's statement that interest rates will remain low for a considerable time and John Williams said this remark was still valid. EUR/USD reached its weekly top at c.1.25, but corrected to 1.24 on strong US data and the low take-up at the second ECB TLTRO auction.

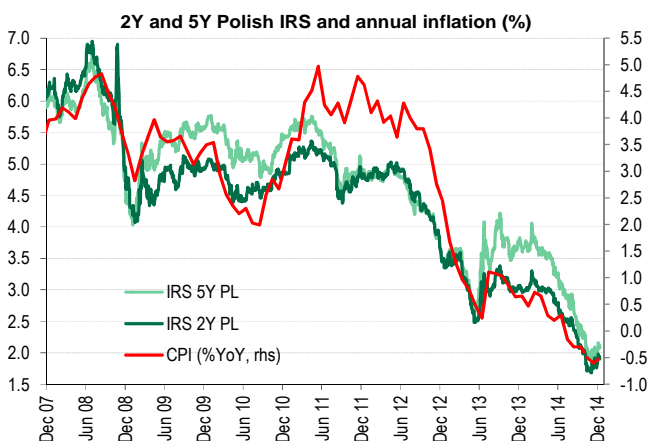
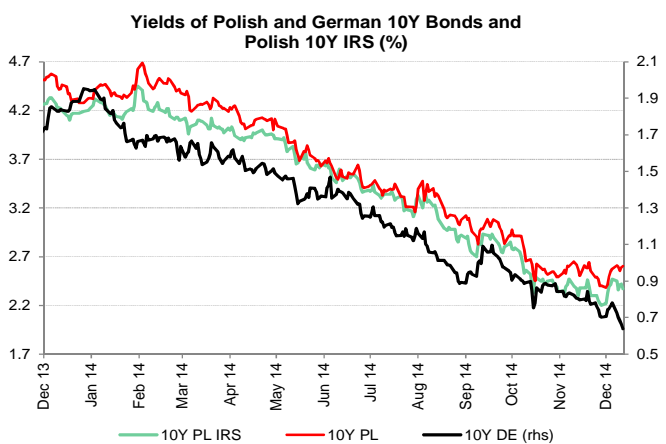
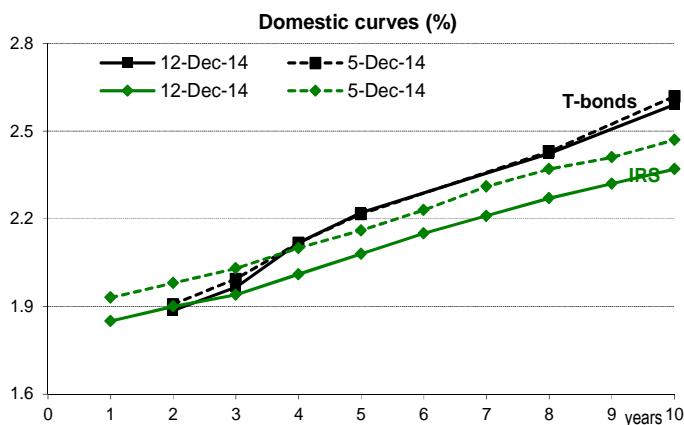
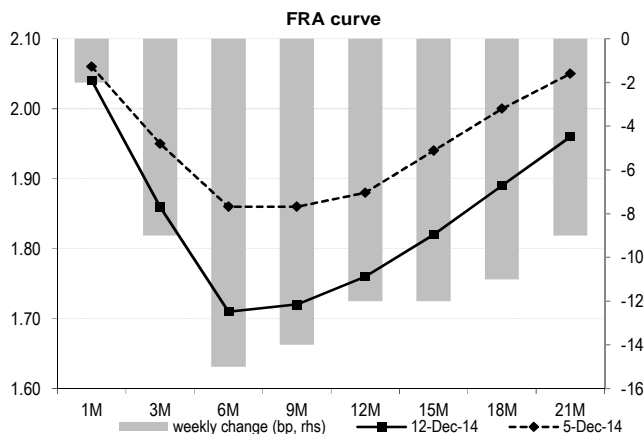
▪ EUR/USD stayed within the previous week's trading range (1.227-1.25) for most of last week. We do not, however, expect this to continue in the coming days as there is plenty of crucial events on the agenda. European economic activity numbers and the FOMC statement (including fresh economic forecasts), as well as Janet Yellen's press conference, are very likely to trigger noticeable moves in EUR/USD. The lower year-end liquidity may fuel volatility, too.

### Ruble can't stop falling

▪ Last week the ruble reached its fresh record low vs. the dollar. USD/RUB increase above 57 was not stopped even by the 100-bp rate hike (to 10.50%) by the Russian Central Bank announced on Thursday. The Bank's statement says that more hikes are likely should inflation continue running above the target. However, we do not think that higher interest rates could halt the ruble's depreciation. Monetary policy tightening is very likely to put even more pressure on the already fragile Russian economy and this should rather not encourage the capital inflow. We think that the ruble's weakness is closely related to plummeting oil prices and the lack of confidence in the Russian economy, plus the risk of imposing capital controls and/or a possible outbreak of more serious military conflict with Ukraine. Thus, the ruble may remain under pressure from a medium-term perspective.

▪ The forint was the weakest since mid-November vs. the euro after the Hungarian stat office released data showing CPI falling more than expected in November (to an all-time low at -0.7% YoY). Renewed expectations that the Hungarian Central Bank may restart the easing cycle pushed EUR/HUF to 309 on Thursday (vs. 303 in late November). This week the Hungarian Central Bank meets and investors will be sensitive to any change in statement's tone towards more dovish.

## Interest rate market – Domestic and global factors could support domestic debt



### Market still anticipates rate cuts

- WIBOR rates were stable last week, while FRAs were more volatile, tracking changes in the IRS rates. The FRA curve shifted down by 4-14bp in weekly terms, with the 6x9 and 9x12 rates dropping the most. Consequently, both now point to a WIBOR 3M decline of 34-35bp in a 6-9 months' horizon. The fall in rates was chiefly caused by dovish comments of some MPC members (Bratkowski, Osiatyński), who signalled quite significant rate cuts.

- The domestic T-bond and IRS markets showed high intra-day volatility over the past week. The beginning of the week brought some rebound in T-bond yields and the IRS rates after their significant increase at the end of the previous week. However, in the following days, both yields and the IRS rates rose across the board due to a slightly higher risk aversion sentiment on the market caused by news from Greece. The risk of political destabilisation in Athens pushed capital towards safe haven assets, the German Bunds in particular (yield of the 10Y German benchmark reached a fresh record low of 0.623%). Consequently, it caused some sell-off among the emerging market peers, including the Polish assets.

- Despite the slightly negative sentiment on the global market and the persistent pressure on the risky assets, domestic T-bond yields and IRS rates stayed below levels that were reached at the end of the previous week. On a weekly basis both curves shifted down gradually (by 2-5bp). What is more, the 2-10Y spreads remained more or less stable (at 70bp for T-bonds and 49bp for IRS). At the same time, the spread over Bunds for all the sectors slightly widened, in line with the global trends.

### Domestic macro data and the FOMC meeting centre stage

- The pre-holiday week on the financial market will be very interesting, filled with macro data releases and central bank meetings (with the FOMC meeting as the key event). Domestic macro data should show further slowdown in economic activity (our forecast for industrial output is well below the market consensus) and deflation in both consumer and producer prices (our forecasts here are similar to the market's). If our forecasts materialise, expectations for further rate cuts will be kept alive at the beginning of next year (in line with our baseline scenario), supporting valuation of the domestic assets, especially on the front end and belly of the curves.

- The long end of the curves will remain more vulnerable to the global market sentiment. The disappointing results of the second TLTRO strengthened expectations for QE in the euro zone at the beginning of 2015 and these expectations could get a further boost if incoming euro zone macro data will again be weaker than expected. However, the FOMC meeting will be the key event of the coming week. New macro and interest rate forecasts will be presented at the meeting. Lack of changes in the Fed's rhetoric, as compared to the previous tone, together with signals that rates may stay unchanged in the longer run (with signals from Europe) should support the domestic curves. However, the risk factor remains unchanged, i.e. the unstable political situation in Greece.

- The upcoming year-end is usually characterised by lower liquidity and lower investors' activity. Therefore, we expect to see a horizontal trend on both the T-bond yields and IRS rates.

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