TRI-WEEKLY ECONOMIC UPDATE

26 December 2016 – 15 January 2017

Please be advised that today's Weekly Economic Update will be the last for 2016.
We will resume publication on January 13, 2017.
We wish our readers a happy Christmas and a prosperous New Year!

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		FRIDAY (30 December)					
14:00	**PL**	**Flash CPI**	**Dec**	**% y/y**	**0.5**	**0.5**	**0.0**
		MONDAY (2 January)					
9:00	**PL**	**PMI – manufacturing**	Dec	**pts**	**-**	**51.0**	**51.9**
9:55	GE	PMI – manufacturing	Dec	pts	55.5	-	54.3
10:00	EZ	PMI – manufacturing	Dec	pts	54.9	-	53.7
		TUESDAY (3 January)					
16:00	US	ISM – manufacturing	Dec	pts	-	-	54.2
		WEDNESDAY (4 January)					
9:55	GE	PMI – services	Dec	pts	53.8	-	55.1
10:00	EZ	PMI – services	Dec	pts	53.1	-	53.8
11:00	EZ	HICP	Dec	% y/y	0.9	-	0.6
20:00	US	FOMC minutes					
		THURSDAY (5 January)					
	PL	**Bond auction**					
14:15	US	ADP report	Dec	k	170	-	216
		FRIDAY (6 January)					
8:00	GE	Industrial orders	Nov	% m/m	-1.8	-	4.9
9:00	CZ	GDP	Q3	% y/y	-	-	1.9
14:30	US	Non-farm payrolls	Dec	k	175	-	178
14:30	US	Unemployment rate	Dec	%	4.7	-	4.6
16:00	US	Durable goods orders	Nov	% m/m			
		MONDAY (9 January)					
8:00	GE	Industrial output	Nov	% m/m	-	-	0.3
8:00	GE	Exports	Nov	% m/m	-	-	0.5
		WEDNESDAY (11 January)					
	PL	**MPC decision**		**%**	**-**	**1.5**	**1.5**
		FRIDAY (13 January)					
9:00	HU	CPI	Dec	% y/y	-	-	1.1
14:00	**PL**	**Money supply M3**	**Dec**	**% y/y**	**-**	**-**	**9.7**
14:00	**PL**	**Current account**	**Nov**	**€mn**	**-**	**-**	**-393**
14:00	**PL**	**Exports / Imports**	**Nov**	**€mn**	**-**	**-**	**15192**
14:00	**PL**	**CPI**	**Dec**	**€mn**	**-**	**-**	**15162**
14:30	US	Retail sales	Dec	% m/m	-	-	0.1
16:00	US	Michigan index	Jan	pts	-	-	98.0
	PL	**Moody's rating decision**					**A-, stab**
	PL	**Fitch rating decision**					**A2, neg**

Source: BZ WBK, Reuters, Bloomberg

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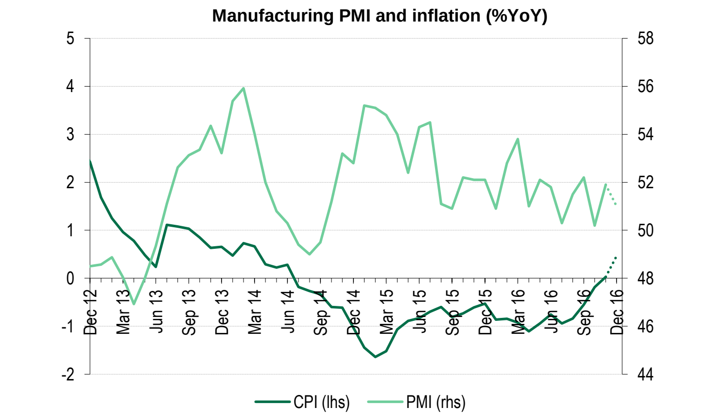
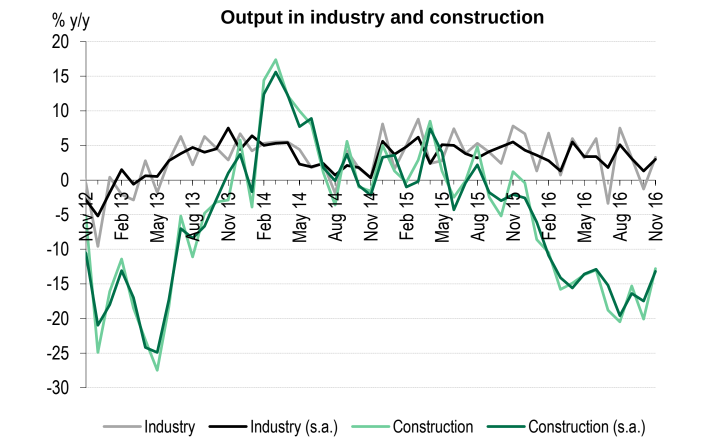
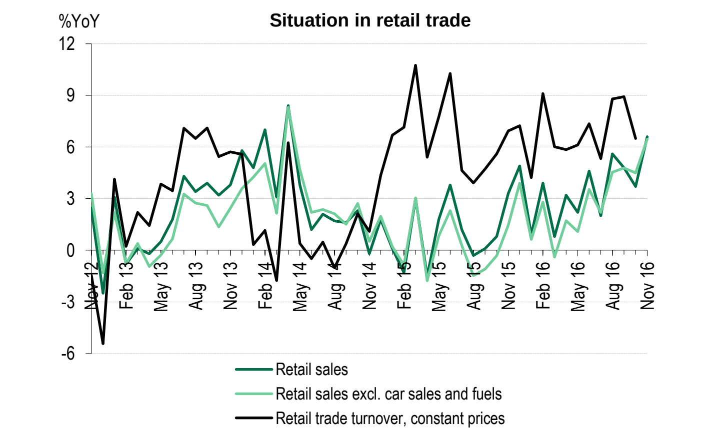
What's hot in the coming weeks – New data and rating reviews



- PMI index will go slightly down in December, in our view, after a surge in November.
- We are expecting the year-end CPI at 0.5% y/y. An upward move of CPI will be mostly driven by fuel prices. CPI is likely to near 1.5% y/y as soon as in January, in our view.
- MPC meeting in January will be a non-event.
- Current account improved in November and is likely to show a surplus, in our view. Both exports and imports are likely to post higher growth rates than in October.
- In our view, it is possible that rating agencies will decide to cut either Poland's outlook or rating with lower retirement age being the main argument. Let us remind that Fitch did not cut neither so far (A-, stable), while Moody's did it in May (A2, negative).

Last week in economy – November data above expectations





- In November, industrial output rose 3.3% y/y, much stronger than expected. Rebound from very weak October figure was driven by the working day effect (neutral in November, negative in October). Interestingly, the rebound was recorded in output for all main categories.
- Construction and assembly output also surprised to the upside, as it contracted by only 12.8% y/y. This sector has also faced an improvement in its three main categories.
- We think that such a broad improvement is not a result of a sudden boost in economic activity but is rather driven by a statistical effect. Interestingly, November's monthly rise in output was the biggest for that month since comparable data are available. It is possible that November holidays have also contributed to this rebound, next to pure number of working days.
- We expect that December will show weaker growth figures than November. Nevertheless, November data seem to show that economic situation is not that poor as one might have thought watching October numbers. After November's readings, we see an upside rise for our 4Q16 GDP forecast. Reading only slightly 2% y/y is possible.
- In November, real retail sales climbed by 7.4% y/y, visibly above forecasts. The upward surprise was mostly driven by car sales and fuels. In our view, similarly as in the case of output, retail sales were supported by the working day effect, while the October's result was undermined by one-off effects.
- PPI inflation jumped to 1.7% y/y in November, way above expectations. In monthly terms, prices climbed by 1.1% m/m, mostly due to strong price hikes in coal mining (24.3% m/m) and metallic ores (18.0% m/m).

Quote of the week – GDP growth to accelerate in 2Q or 3Q17

Mateusz Morawiecki, deputy prime minister, 21 Dec, PAP

GDP growth in 2016 may be slightly lower than expected. This will not weigh on the budget. I hope that the economic growth will accelerate in 2Q or 3Q17, at the latest. Recent data were very optimistic.

Recently we have suggested an incoming wave of downward revisions of GDP growth. The deputy prime minister Mateusz Morawiecki took the cue and does not expect an acceleration of growth until 2Q or even 3Q17. In our view, GDP will pick up already in 1Q17 thanks to, among others, the positive effect of number of working days (the opposite effect in 2Q17), but before it is likely to decelerate further in 4Q16, reaching the bottom slightly below 2% y/y.

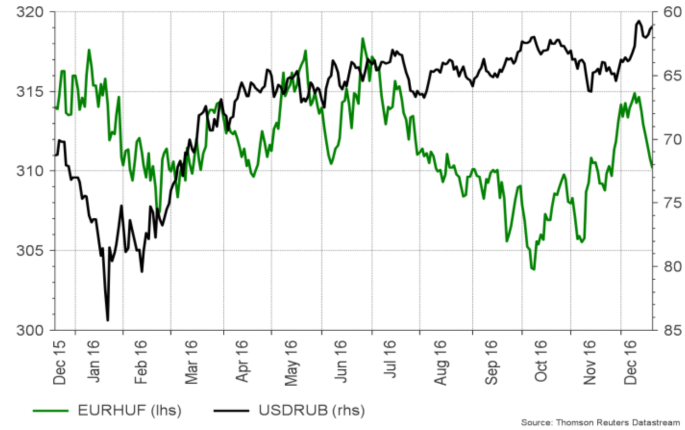
Foreign exchange market – Lower volatility just before Christmas

EURPLN

USDPLN, CHFPLN

EURUSD

EURHUF, USDRUB



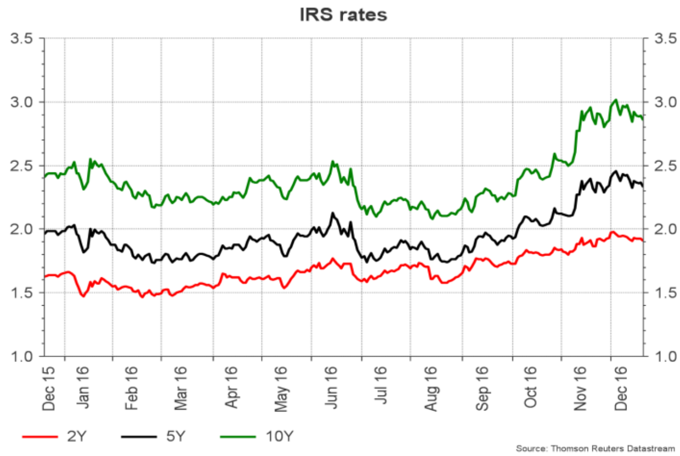
EUR/PLN testing 4.40

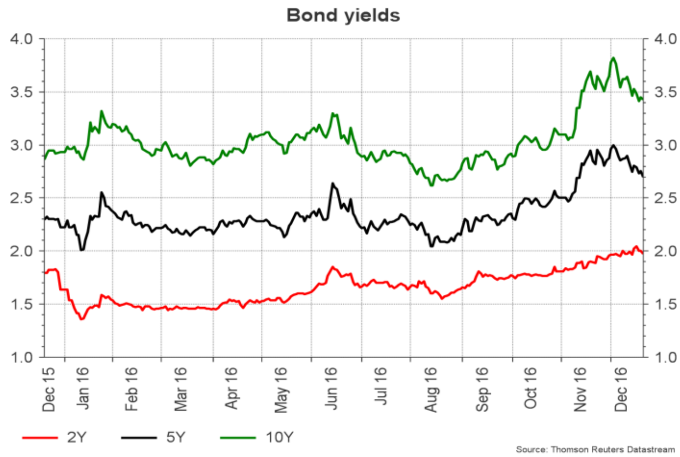
- Just as we suggested last week, the pre-Christmas period was very calm on the Polish FX market with EUR/PLN holding just above 4.40 and USD/PLN stabilizing around 4.24. The zloty gained slightly vs the euro thanks to the positive global market sentiment, better-than-expected domestic macro data and despite the rising conflict on the Polish political scene.
- EUR/PLN was testing the 4.40 level three times last week, but those attempts proved unsuccessful. The lack of strength to break the local low from November suggests, in our view, that a strong impulse is necessary to trigger further strengthening of the zloty versus the euro. So far, we see no such impulse on the horizon. December is usually a positive month for the zloty (EUR/PLN decrease happens much more often than its rise). It is likely that this will be the case also this year, although we do not expect the zloty to extend its gains much further, but rather to stabilise just above 4.40 till year-end.
- FX market fluctuations may increase after the New Year, in our view. First of all, historically January tends to be a more volatile month for the zloty than others. Since 2012, the average high-low EUR/PLN spread for January was PLN0.21, vs. PLN0.13 average for the whole year. January's volatility was higher than in the remaining months in every single year since 2012. Additionally, the new triggers for temporary currency depreciation may appear at the start of 2017 – we expect to see more disappointing macroeconomic data, and the currency may be under the negative pressure of rating agencies' decisions.
- Last year in mid-January, the S&P rating agency surprised the market by downgrading Poland's rating by two notches and changing the outlook to "negative". On January 13, 2017, two rating agencies (Moody's and Fitch) are likely to review their rating assessments for Poland. In our view, it is possible that rating agencies will decide to cut either Poland's outlook (Fitch) or rating (Moody's) with lower retirement age being the main argument. This may cause, at least temporary, negative reaction to the Polish currency.
- As long as the global issues are concerned, important US data are on the agenda in the weeks to come, including manufacturing ISM, monthly non-farm payrolls and release of the FOMC minutes. The December's Fed rate hike was perceived as "hawkish" but this did not have any material negative impact on EUR/PLN.

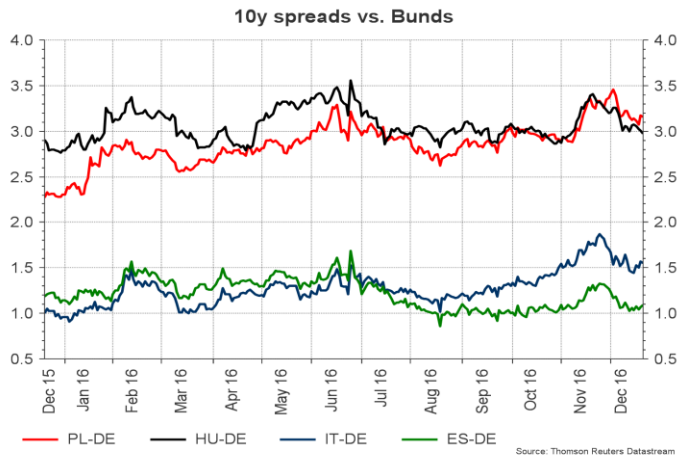
Dollar's appreciation loses momentum

- The dollar's appreciation clearly lost momentum last week and the EUR/USD rebounded slightly after it had hovered around 1,035 for a while.
- We think that the end of 2016 should be quite calm for EUR/USD with the dollar being still well bid but without any acceleration in pace of its appreciation.
- Early 2017 will bring important US macro data releases – manufacturing ISM and monthly non-farm payrolls. December's Fed rate hike boosted the greenback pushing EUR/USD to its multi-year low. The US central bankers became more hawkish and now the market will be looking if the coming macro data will indeed allow for three interest rate hikes in 2017. Investors reaction to the US figures should be straightforward – strong data could support the dollar while below-consensus readings could trigger some profit taking from the recent decline in EUR/USD.

Interest rate market – Waiting for US data







FI market stabilized

- In line with what we suggested last week, the pre-Christmas period on the Polish fixed income market was much calmer when compared to what we have seen in the previous days. The IRS and bond curves remained fairly stable with the intraday volatility clearly lower than observed since the US presidential elections. As a result, the 2Y IRS is still only slightly above 1.90%, the 5Y rate is just below 2.40% and the 10Y IRS holds close to 2.90%.
- In the previous reports, we pointed out that since the US presidential elections the correlation between the Polish and US 10Y benchmarks has been higher than the one between the Polish and German 10Y bonds. However, the Polish 10Y bond proved surprisingly resilient to the December "hawkish" Fed rate hike and since the last week's FOMC decision, the PL-US 10Y spread has fallen to 85bp from c100bp, thus reaching its lowest since January 2016. The correlation has fallen as well – to just below 60% from 95% - since the US presidential elections (still higher than with the Bund).
- In our view, Polish bond outperformance may have been, to some extent, due to the fact that since August Polish long-term debt has been lagging its US peer (in this period, the 10Y spread rose above 140bp from c100bp). On average, the spread in 4Q16 is so far fairly the same as in 3Q16 (122bp vs 126bp).
- 1-12M WIBORs has not changed since last Friday.

Waiting for US numbers

- We think that as long as the end of 2016 should be rather calm on the Polish and global bond market, early 2017 will bring numerous important data releases, including ISM-manufacturing and monthly nonfarm payrolls that could spur volatility.
- In December the FOMC members added one extra dot on their chart, showing the expected number of hikes in 2017 and now the market will analyze if the coming macro data actually allow for three 25bp Fed rate hikes next year. According to Bloomberg, currently the market is not pricing more than two 25bp hikes in 2017 and it appears to us that only a very positive evidence could make the market more hawkish.
- As regards the Polish events, the November's economic activity data surprised to the upside, but this did not have a significant impact on the front end of the curve. The fairly stable 2Y IRS and bond suggests that the market reaction to the December flash CPI could also be muted.
- November's industrial output and retail sales could reinforce the MPC's view that the economic slowdown is temporary and so we do not expect any change in the MPC's rhetoric. This event should be market-neutral.
- As rating agencies might decide to cut Poland's rating (Moody's) or outlook (Fitch) in the middle of January, the bond market might be more volatile ahead of these events (possible weakening of Polish bonds).

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