

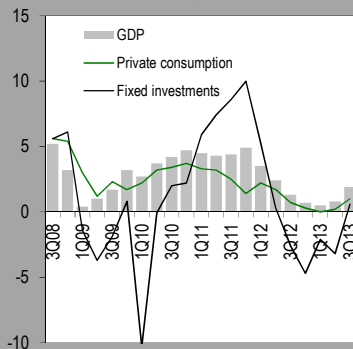
MACROscope

Polish Economy and Financial Markets

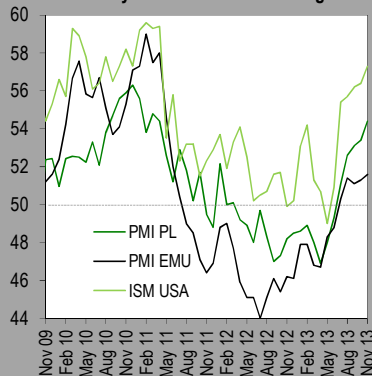
December 2013

Another breath of optimism

Economic growth (%YoY)



Activity indices in manufacturing



■ **Information from the Polish economy released recently are gradually raising optimism regarding the economic growth this and next year.** Data on Q3 GDP were not only better than forecasts but the acceleration was also to more extent based on recovering domestic demand. More and more clear improvement in the labour market is favouring acceleration of consumer demand growth. Rebound in investment proved to be surprisingly quick, as total investment growth turned positive already in 3Q, despite probably still shrinking investment spending of the public sector. The most recent data are suggesting that positive trends are being continued in 4Q, and the scale and pace of economic recovery is even higher than we earlier anticipated.

■ **Positive data convinced us to increase GDP growth forecasts for Poland – to 1.5% this year and 3.1% in 2014.** It is possible that other institutions will soon start improving forecasts for Poland too, given positive data confirming that recovery is persistent. This may also be the case for the NBP projection (although in this case the next updates will take place only in February and then in July). Still, we do not expect such changes in the economy that could convince the MPC to withdraw from its pledge that interest rates will remain on hold at least until the end of first half of 2014.

■ **We still expect the first interest rate hike in 3Q 2014, but more likely in September than in July.** The decision should be triggered by strengthening economic recovery, increasingly driven by domestic demand, and a gradual rise of inflation towards the inflation target. However, the risk for the interest rates scenario is in our opinion asymmetric towards a later start of monetary tightening. This results from two factors. First of all, inflation path could be in fact lower than we currently anticipate. Secondly, there are possible changes in the MPC, which may shift the balance of votes towards more dovish. In the nearest days the President Bronisław Komorowski will appoint the new member to replace Zyta Gilowska. Jerzy Osiatyński, mentioned as the most likely candidate, would surely join the group of MPC members favouring extension of period of interest rates stability into 2H 2014. Furthermore, the number of MPC members may be increased by three more members in 2014 if the parliament approves the NBP Act amendment prepared by the Ministry of Finance.

■ **In November the situation in financial markets was mainly under the influence of global factors.** Worries that Fed may start QE3 tapering already this year (result of publication of FOMC minutes) were not only contributing to zloty depreciation but also to the weakening of bonds in the middle and at the long end of the yield curve; meanwhile, the short end remained relatively immune to changes of moods in core markets. Start of December saw slight rebound; the zloty and bonds slightly strengthened. However, risk factors for investors' behaviour remain unchanged. December's FOMC meeting (we expect delaying the start of QE3 tapering until 1Q 2014) may add some volatility in the financial markets. Nevertheless, we stick to the forecast that average EURPLN rate will reach ca. 4.18 in December.

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ECONOMIC ANALYSIS DEPARTMENT:

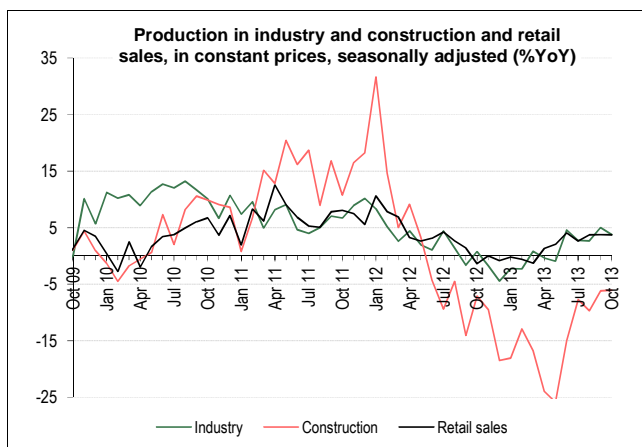
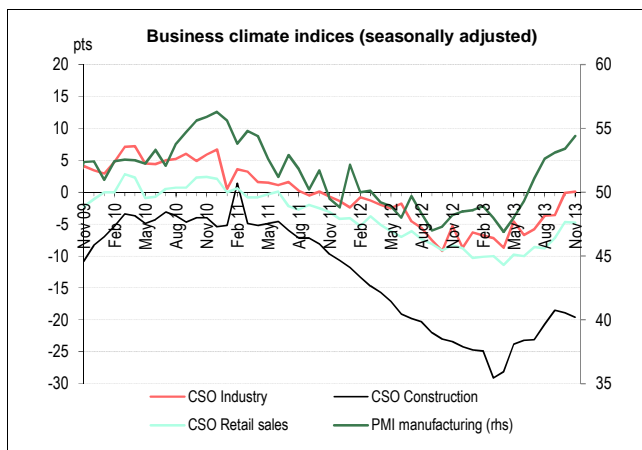
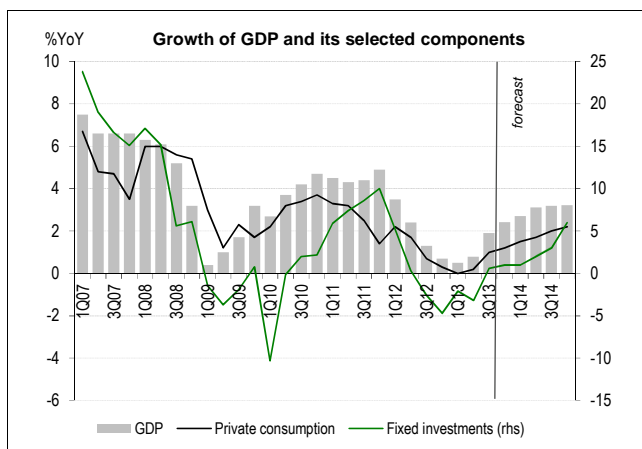
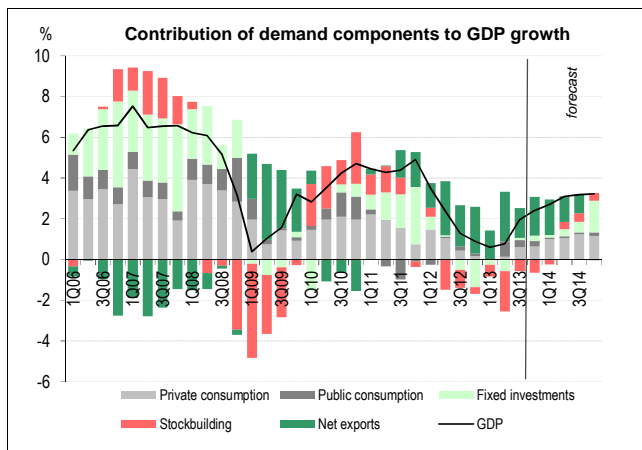
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Financial market on 11 December 2013:

NBP deposit rate	1.00	WIBOR 3M	2.65	EURPLN	4.1803
NBP reference rate	2.50	Yield on 2-year T-bond	2.87	USDPLN	3.0386
NBP lombard rate	4.00	Yield on 5-year T-bond	3.63	CHFPLN	3.4221

This report is based on information available until 11.12.2013

Economic update



Source: CSO, NBP, Markit, BZ WBK

Domestic demand bottoming-out

▪ GDP growth in Poland reached 1.9%YoY in Q3 2013 as compared to 0.8%YoY in Q2 and 0.5%YoY in Q1. The data confirmed the economy is gradually gaining steam and that this process – in line with our expectations – is not entirely based on rapid exports' expansion, but more and more reliant on domestic demand.

▪ Domestic demand growth in Q3 was positive for the first time since Q1 2012 and reached 0.5%YoY. This was driven by a revival in consumer demand (individual consumption increased by 1%YoY, after three quarters of stagnation) and – what seems particularly important – some pickup in investment activity (fixed investment rose by 0.6%YoY, following four consecutive quarters of clear declines). While consumption growth was roughly consistent with our expectations, pickup in investments was a positive surprise. Most likely, it was driven by higher investment activity in the private sector, however we did not expect this rebound to be strong enough to compensate for weakness in public investments already in Q3. In our view, this gives a reason to be slightly more optimistic about the pace of domestic demand growth in the following quarters.

▪ At the same time, external demand is still a significant engine driving the rebound of the Polish economy – pace of growth of exports accelerated in Q3 to 6.4%YoY (the highest number in 2.5 years) and taking under account forecasts showing further improvement of economic conditions abroad (particularly in Germany), we expect even higher growth rates of external trade in coming quarters. However, given our assumptions of gradual acceleration of domestic demand, imports will also gain steam. Still, we expect that both in 2013 and 2014 net exports' contribution will remain positive (though it will diminish gradually).

The economy is speeding up in Q4

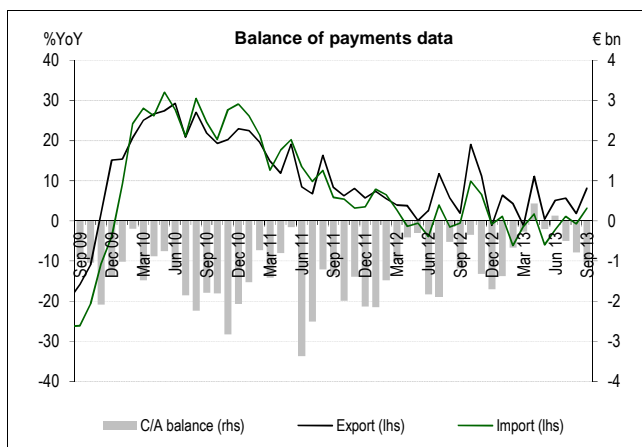
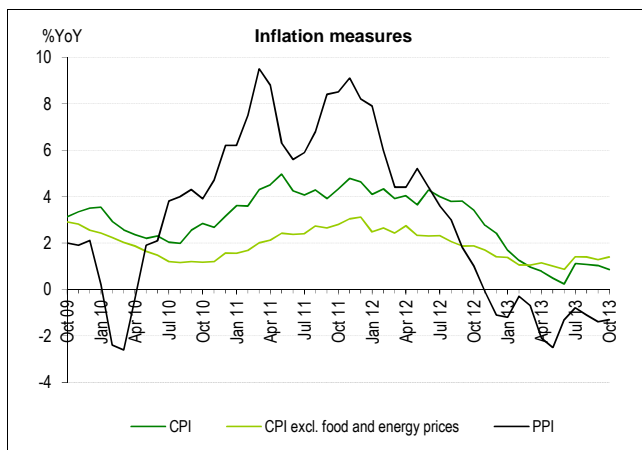
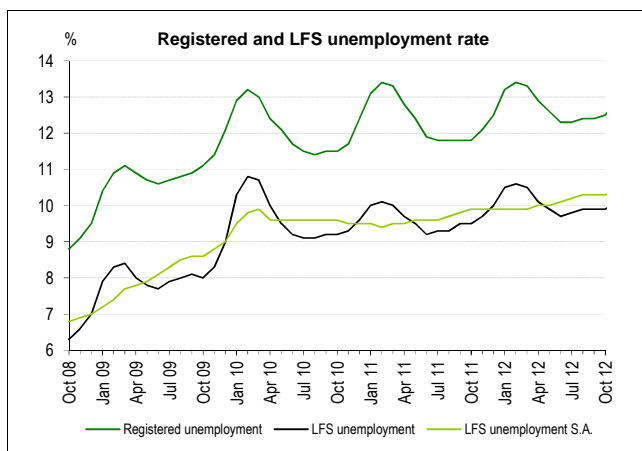
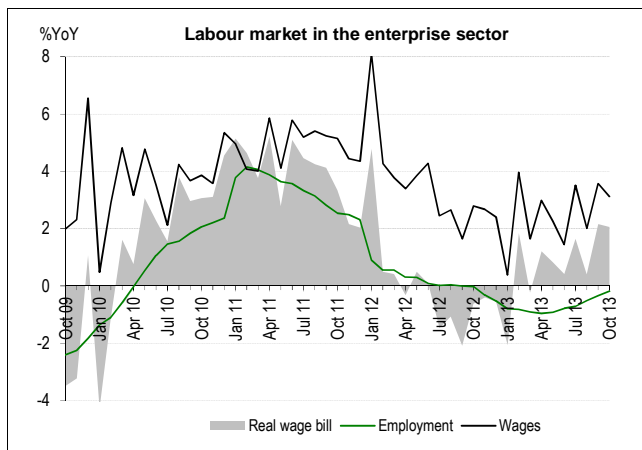
▪ PMI index climbed in November to 54.4pts (the highest level since April 2011). Subindices for output and new orders reached the highest levels in many months, while companies were reporting strengthening demand from Poland but also from Europe and the USA. The CSO business climate index rose in November to 0.1pts and was positive for the first time since October 2011. Leading consumer confidence indicator (WWUK) climbed to -28.6pts, which is also the highest level since October 2011. Thus, leading indicators are suggesting that the economy was accelerating further in Q4. However, this trend can be less visible in "hard" data, as there is a negative working day effect in Q4 (while this effect was positive in Q3), which will weigh on some statistics, especially on industrial output.

▪ Industrial output increased in October 4.4%YoY, as compared with 6.3%YoY in September. According to the CSO, the output after seasonal adjustment increased by 3.8%YoY. Just like in previous months, the best performance was recorded in sectors traditionally focused on foreign markets. This indicates that export is still a very important engine driving the ongoing recovery.

▪ Construction and assembly output surprised to the upside – annual pace of growth improved to -3.2% (-6.1% after seasonal adjustment). This result was partly due to convenient weather conditions seen this year. Nevertheless, this was yet another month of recovery of this sector after a deep contraction seen in H1 and it seems to confirm a gradual rebound in investments.

▪ Annual pace of retail sales growth decelerated to 3.2%YoY from 3.9%YoY in September. Volumes in retail trade turnover also showed some deceleration in October, to 5.1%YoY from 7.1%YoY a month earlier. October's retail sales data are in line with our baseline scenario, assuming a gradual revival in private consumption. In coming months we expect retail sales growth to accelerate.

Economic update



Source: CSO, NBP, BZ WBK

Employment already higher than one year ago?

- The annual change of employment in the corporate sector inched up in October to -0.2% from -0.3%YoY in September after a monthly increase of employed by 5k. Initially we thought that such a good result was partially due to favourable weather conditions in October, supporting some seasonal jobs (like in construction). However, the detailed data from corporate sector showed that employment in the construction sector declined slightly and a substantial improvement was recorded in the manufacturing and trade. Moreover, since April 23k jobs were added in the corporate sector, while analogous period of 2012 saw a decline by 20k. These data confirmed a strengthening of positive tendencies developing in the labour market. In our view we may see a positive growth rate of employment already in the data for November. What is interesting, according to the LFS survey, in Q3 number of employed people was already higher than one year ago (+0.1%), and number of jobseekers was lower (-0.2%), which translated into declining unemployment rate (9.8% vs. 9.9% in 3Q2012). This is suggesting that the economic situation may be improving faster than it is shown by monthly data from the corporate sector.

- Average wages in the corporate sector increased by 3.1%YoY. Real growth of wages stays at moderate level (2.3%YoY), which is supporting private consumption growth, while not generating excessive increase of labour costs for companies. The wage bill in corporate sector increased in October by 2.9%YoY in nominal terms and by 2.1%YoY in real terms. This is slightly weaker growth than in September, but still, a substantial improvement has been recorded in this area since the beginning of the year.

- According to estimates of the Labour Ministry and our forecasts, the registered unemployment rate climbed in November to 13.2% from 13.0% in October, in line with a seasonal pattern.

Inflation will rise slowly

- October's headline inflation declined to 0.8%YoY from 1.0%YoY in September. Food prices were the main culprit behind this fall, as they declined by 0.1%MoM while usually we have a seasonal rebound in this category. The prices of most other categories were rising, so core inflation excluding food and energy prices advanced to 1.4%YoY from 1.3%YoY. 12M PPI inflation is still running below zero (-1.3%YoY).

- We maintain our forecast of gradual increase of inflation in coming months (but probably not in November yet). Scale of this move should not endanger MPC's declaration of stable interest rates until mid-2014. However, in Q3 2014 interest rates may go up if CPI remains on the upside (and above path presented in the recent NBP projection) and pace of GDP growth is close to 3% (amid rising domestic demand).

Deficit in current account despite trade surplus

- Current account balance recorded a deficit of €1.02bn in September. This was the deepest deficit since January 2013.

- Trade balance reached a surplus of €673m, which was the highest foreign trade surplus since comparable data are available (January 2000).

- The current account deficit widened despite strong trade surplus due to deterioration of services (€259m), current transfers (-€151m) and income accounts (-€1.8bn). In the two former cases, this was probably a transitory deterioration, due to seasonal issues and pattern of EU transfers' inflow. However, trend of deteriorating income account is more persistent, and this implies that even with trade balance turning persistently into surplus it will be difficult to remove the current account deficit in Poland.

Monetary policy watch

Fragments of MPC communiqué after December's meeting

Growth in global economic activity remains moderate. (...) Moderate growth in global economic activity and decline in energy prices were conducive to inflation decrease in many countries.

The monetary policy of major central banks remains highly expansionary. In November, the European Central Bank lowered its main policy rate, whereas other major central banks maintained the current scale of their monetary expansion.

In Poland, GDP data for 2013 Q3 confirmed the continuation of a gradual economic recovery. (...) October saw a minor slowdown in the annual growth of industrial output and retail sales. Construction and assembly output continued to fall, albeit at a slower pace. Yet, business climate indicators suggest a further gradual recovery in the coming quarters.

Demand and cost pressures in the economy remain low. CPI inflation in October fell to 0.8% y/y (from 1.0% y/y in September), continuing well below the inflation target of 2.5%. This was accompanied by persistently low core inflation and a fall in producer prices in industry. At the same time, inflation expectations remained low.

In the opinion of the Council, gradual economic recovery is likely to continue in the coming quarters, however, inflationary pressures will remain subdued. Therefore, the Council decided to keep the NBP interest rates unchanged. **The Council maintains its assessment that NBP interest rates should be kept unchanged at least until the end of the first half of 2014.**

President's Chancellery on appointing new MPC member

9.10 (PAP) Surely the President will not delay the nomination the new MPC member, replacing professor Zyta Gilowska. But firstly, the legal doubts must be reconciled whether the new member will finish current term of office or will be appointed for the full 6-year term. This hasn't been settled yet.

17.10 (PAP) According to the Bureau of Law of the President's Chancellery both the grammatical interpretation and functional interpretation of cited legislation lead to the conclusion that the legislator has adopted the concept of individual tenure of individual MPC members and not the Council as a whole and, that the appointment of each member shall be for a period of six years.

15.11 (PAP) Decision (on nominating new MPC member) will be announced at the end of November or the beginning of December.

4.12 (PAP) Mr President informed today that he already has a candidate for the new MPC member and he will nominate him after the return from visit in the Persian Gulf, i.e. after 13 December.

At least two quarters of predictable monetary policy ahead

As expected, the Monetary Policy Council left interest rates unchanged in December, and the Council maintained the declaration to keep them stable at least until the end of the first half of 2014. We do not expect to see any circumstances that would make the MPC to abandon this pledge.

We still think that the closer we get to the middle of 2014, the more justified will be the question when to start monetary policy tightening. Not so long ago, some MPC members have seen no signs of economic recovery at all, while at the last press conference Marek Belka said the recovery is "gradual, yet inevitable". We think that next economic data will reinforce the Council's belief in further situation improvement. Especially that the recovery will be fuelled increasingly by domestic demand amid improvement of labour market conditions. In our opinion, core CPI may get closer to – or even rise above – 2% in the first half of the next year. Consequently, the recent correction of the inflation path presented in the November's *Inflation report* may appear to be insufficient and we may see a next revision in early 2014. Thus, the first interesting MPC meeting may be in February when updated CPI and GDP projections will be released. The following revision will take place in July 2014, which is already after the declared period of stable interest rates.

In the second half of 2014 the Council will have to answer the question whether in a different macroeconomic environment (faster economic growth, higher inflation) the main interest rate should be maintained at a record low level (which – please recall – has been established when both real GDP growth and inflation rate were close to zero).

We expect two interest rate hikes (by 25bp each) in the second half of 2014, the first one in the autumn.

Two main risk factors for this scenario (implying possible delay of stable rates' period) are as follows: (1) realisation of lower inflation path than we currently predict (for example due to lower prices of food and commodities abroad); (2) possible changes in the MPC composition towards more dovish Council (details below).

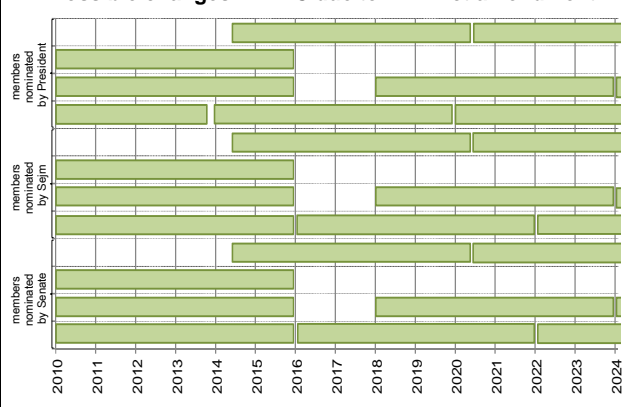
New members may join the MPC

The first change in the MPC should take place in the nearest days – the President is running out of statutory time (3 months) to nominate the successor of Zyta Gilowska. According to unofficial information the most likely candidate is Jerzy Osiatyński, current economic advisor to the President. His views on monetary policy are undoubtedly much more dovish than those of Ms. Gilowska (see next page).

More changes may take place next year. The Ministry of Finance has prepared new version of amendment to the NBP Act, assuming that in 2014 the Sejm, the Senate and the President would each add one member to the MPC and thus it would temporarily constitute of 12 members (+NBP Governor). In 2016, when the term of current MPC members ends, only three new members would be chosen (by one from Sejm, Senate and President) and thus temporarily there would be only 6 MPC members (+NBP Governor). After next two years, three more MPC members would be added to the MPC and this way the Council would reach the target size of 9 members plus the NBP Governor. This way, the rotation of MPC members in following years would be gradual (three members replaced each two years). We think this is a reasonable solution, that should increase the monetary policy stability and consistency.

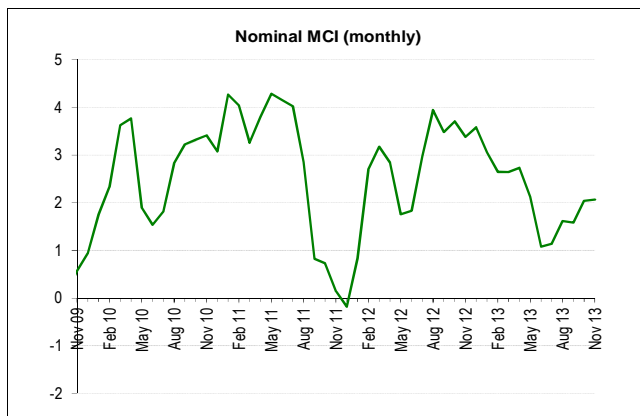
At the same time, a possible introduction of three new members of the MPC in 2014 could significantly shift the balance of votes towards a more dovish monetary policy. Gathering majority for interest rate hike would then require 7 votes, as opposed to 5 (including NBP President) currently, which may imply that it will take more time until monetary tightening starts.

Possible changes in MPC due to NBP Act amendment



Sources: NBP, BZ WBK

Restrictiveness of the Monetary Policy (Council)



MCI stable and relatively low

- MCI monetary restrictiveness index was stable in November, as both FX and money markets did not post major changes last month.
- MCI climbed slightly over the last months, but is still running at relatively low level. This is suggesting that monetary conditions are not a hindrance for economic growth.
- Recent NBP studies suggest that impact of exchange rate on inflation (so-called pass-through) can be weaker than estimated earlier, while interest rate effect is stronger. If this is the case, then a considerable easing of monetary conditions in 2012 and 2013 (by 225 basis points) can strongly affect inflation next year.



Rzońca (1.44)

Winiński (1.45)

Gilowska (1.54)

Kaźmierczak (1.41)

Glapiński (1.38)

Hausner (1.03)

Belka (0.96)

Zielińska-Głębocka (0.81)

Chojna-Duch (0.73)

Bratkowski (0.58)



Some MPC members think that rates' stabilisation may be prolonged

At the press conference after the last MPC meeting the NBP Governor Marek Belka said the MPC members were unanimously backing the statement that interest rates should remain on hold at least until the middle of 2014. This was confirmed by members' comments in recent weeks. Moreover, some MPC members apparently think that the stabilisation of interest rates may last longer than officially declared – Anna Zielińska-Głębocka said that rates may remain on hold until the end of third quarter, Adam Glapiński, Andrzej Bratkowski and Elżbieta Chojna-Duch think it may be even until the end of 2014. Although the latter MPC member still does not exclude a rate cut “if growth is slow (...), especially when other central banks will go towards monetary policy easing”, it seems to be an isolated opinion and the vast majority of Council members think that the next change in monetary policy in Poland will be a rate hike.

This group is likely to grow after appointment of new MPC member

If Jerzy Osiatyński becomes the next MPC member, as recently suggested by Thomson Reuters, the group of central bankers supporting a longer period stabilisation of interest rates will undoubtedly grow in number. In the recent interview for PAP the current economic advisor to the President said it is hard to expect that monetary policy may significantly boost investments and economic growth, but still, one has to make sure that it does not hamper economic growth. Therefore, in his opinion, “maintaining current level of interest rates as long as possible is highly desirable”. So in total, we may have soon at least as five people in the MPC who argue for lengthening the period of interest rates stabilisation. Without the support of the NBP Governor this may be still not enough though.

... but improvement of economic situation should be argument against

We are not convinced that current balance of votes in the MPC will persist if next data will be consistent with our expectations, confirming a scenario of accelerating economic growth, increasingly fuelled by domestic demand. Marek Belka underscored recently that the structure of economic growth is even more important for the MPC that the pace of growth. Other MPC members also mentioned in their comments that they are not afraid of inflationary pressure until the economic rebound is based mainly on net exports. However, this is changing right now. We predict that information that will appear in the following months will trigger a revision of NBP projections concerning economic growth and inflation (stronger recovery of domestic demand, more significant rebound of the labour market, consequently higher CPI and core inflation), which will have impact on the MPC members' assessment of monetary policy outlook. Already in the minutes of the November's MPC meeting there was a mention that according to some MPC members inflation growth may be higher than predicted in the NBP projection, if wage pressure is stronger than assumed or in case of negative supply-side shocks in commodity markets. The same MPC members noticed that possible inflation rise may cause a drop in real interest rates. Meanwhile, Andrzej Rzońca reminded at the last MPC's press conference (speaking in the name of the entire Council) that the MPC wants to conduct a conventional monetary policy, which is characterised by positive real interest rates.

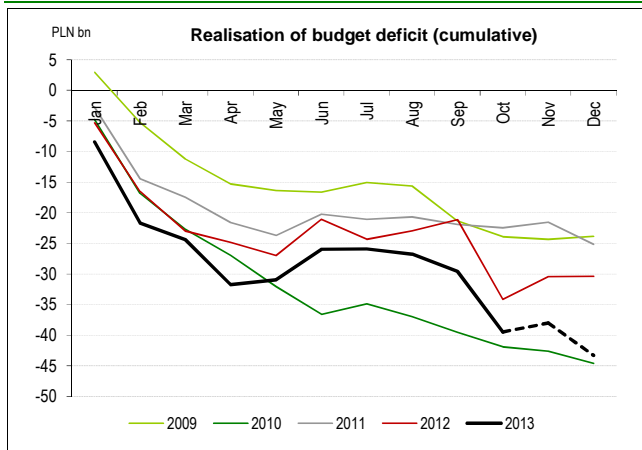
Index is between 0 and 2. A vote for the majority view is given a score of 1. A vote for a more hawkish (less dovish) decision than the majority view has a score of 2 and a vote for a less hawkish (more dovish) decision than the majority view has a score of 0. Value of the index for a given MPC member is a weighted average of points for all votes. Recent votes have higher weights, more distant – lower.

Numbers directly by the name are values of the index for period since the beginning of current term of office of the current MPC and NBP governor.

Direction of the restrictiveness axis reflects our expectations regarding direction of interest rate changes in the nearest 12 months.

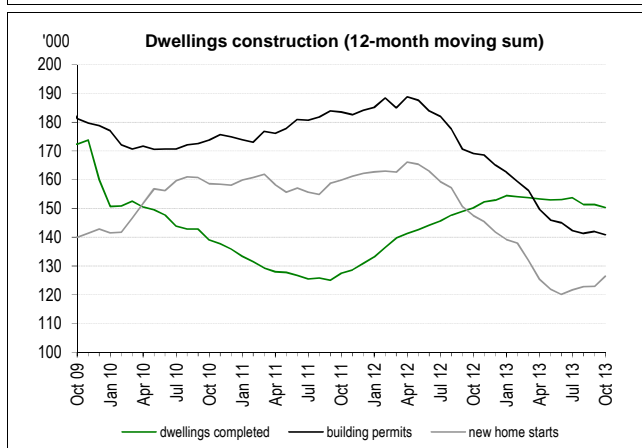
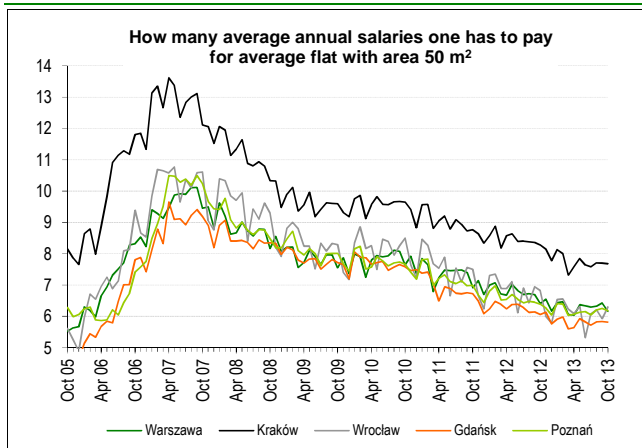
Source: NBP, Reuters, BZ WBK

Fiscal policy watch



	Spread vs Bunds (10Y) in bps			CDS (5Y USD)		
	11.12	change since 12.11.13	change since 31.12.12	11.12	change since 12.11.13	change since 31.12.12
Poland	259	-4	19	83	-2	4
Czech	41	-14	-13	60	1	-3
Hungary	406	-33	-86	281	13	11
Greece	696	-6	-357	26	17	26
Spain	221	-15	-179	164	-5	-123
Ireland	165	-13	-154	123	-1	-93
Portugal	418	2	-150	343	-13	-94
Italy	223	-14	-98	185	-13	-89
France	48	-8	-20	52	2	-37
Germany	-	-	-	24	1	-15

Housing market



Source: MoF, Reuters, GUS, szybko.pl, BZ WBK

The 2013 budget deficit will be lower than assumed

At the end of October the budget deficit amounted to ca. PLN39.5bn, which represented 76.5% of annual plan. On the revenues side, improvement in tax income, in particular from VAT (revenues reached nearly PLN12bn, up from ca. PLN9bn on average in January-September period) was observed. At the same time, the realisation of expenditure after 10 months was more or less at the same level as in the same period of 2012.

According to comments from the Ministry of Finance, in November there was a budget surplus of PLN1bn. It means that the end of the year, like in previous years, brings some savings on the spending side and a better realisation of tax incomes thanks to economic rebound. All in all, we uphold our stance that this year deficit will be lower than planned (after amendment) by ca. PLN8bn.

Central banks' actions influence trends on markets

The unexpected ECB's decision to cut official interest rates at its November's meeting supported the German bond market. However, Bunds strengthening was only short-lived. More hawkish rhetoric of minutes from FOMC meeting in October brought an upward impulse for core markets yields. We observed a correction at the beginning of December.

In November peripheral debt slightly strengthened due to improving growth prospects in those countries. Consequently, spread vs Bund narrows, while CDS prices decline.

Central banks' activity has still remained crucial for investors, who mainly concentrate on Fed's meeting this month. This meeting is very interesting, in particular taking into account that FOMC will release its newest economic forecasts, which might determine the timing of tapering. If FOMC decides to postpone decision in December, we expect core yields to decline. However, higher yields still remain our baseline scenario in mid-term.

Housing affordability improving, prices started rising

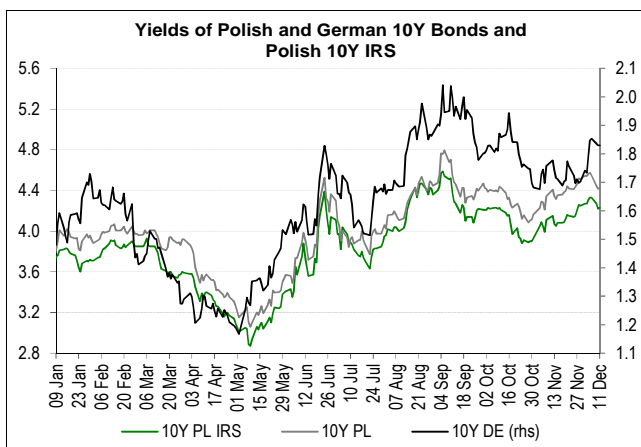
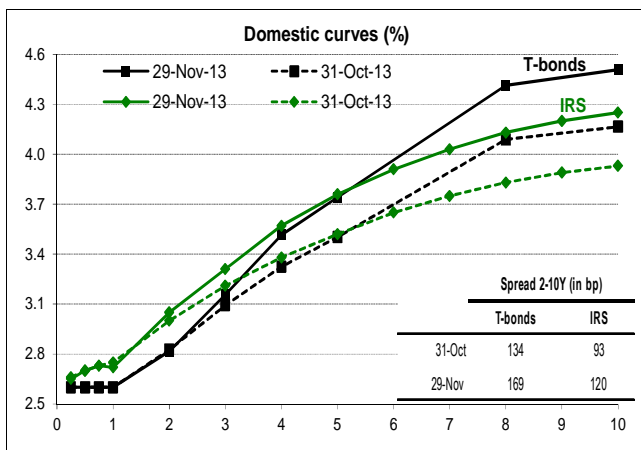
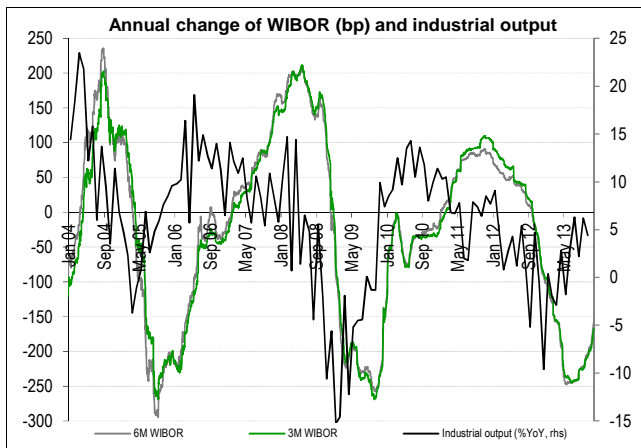
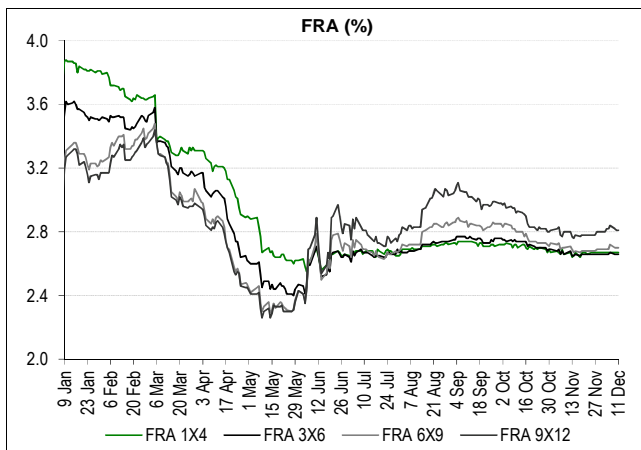
October was the third month in a row of gradual increase in weighted average offered home prices on the secondary market in the largest Polish cities. Currently, the pace of change is relatively limited (by 1-3% during 3M, depending on location), however, it is likely that finally we are dealing with the beginning of the more persistent tendency. What is more, according to the real estate agents a slight increase in offered prices is accompanied by significant growth in number of people who are interested in purchasing home and in the number of transactions on the market. What is interesting, average transaction prices in many cities dropped in the recent month as customers' demand is still concentrating on the cheapest apartments.

Rebound on the real estate market is supported by gradual improvement in housing affordability – currently the relation between average wages and average house prices has returned to the level from 2005, i.e. from the early stage of the housing boom in Poland. Meanwhile, indices of loan-financed housing availability, calculated by us, improved even more considerably (relation of theoretical instalment of loan for a 50-meter flat to average wage declined by ca. 20% over the last year).

Until now these changes had limited impact on the situation on the credit market – in recent months mortgage loans for households have been growing by a modest 3.6%YoY (after FX correction). It clearly means that activated demand, as we mentioned two months ago, concerns mostly „cash” investors.

The supply of the new housing on the market is still growing at the fairly good pace, but investors are limiting investment plans, which might result in the smaller offer of housing in coming quarters.

Interest rate market



Source: Reuters, BZ WBK

CPI outlook limits rates increase

▪ In November situation on money market did not change significantly. The extension of period of stable official rates (at least) till mid-2014 by the MPC at its November's meeting kept WIBOR rates more or less unchanged since the end of September. November's MPC decision together with the Council's comments convinced investors that the first rate hike might take place in 12 months horizon (4Q 2014). The beginning of December brought gradual increase in FRA9x12 rate, suggesting that investors do not exclude that the start of monetary tightening might be a bit earlier.

▪ The chart beside shows a relationship between annual changes of WIBOR rates (3M, 6M) and the Polish industrial output. However, historical data indicate that WIBOR reacts to changes in the real economy with a lag and this situation should also take place in coming months. We think the market may be clashed between comments from the MPC members (Bratkowski, Chojna-Duch), suggesting that period of stable rates might be longer than assumed in November's statement and upcoming macro data confirming an economic rebound. The market surely remembers that the MPC is sensitive to current macro data and thus if next data surprise to the upside – just like they did recently – they may influence the market expectations.

▪ We expect WIBOR rates to remain more or less stable in coming months as long as inflation outlook is fairly benign and economic growth is moderate. However, FRA rates might be more volatile. Stronger signals of economic revival might quickly translate into higher rates.

Curves become steeper

▪ In November yields of bonds and IRS rates, mainly on the mid and long-end of curves, increased quite considerably. This development was mainly due to deterioration of investors' moods on the global market (increase of yields of Bunds and of the US Treasuries due to hawkish FOMC's minutes). The cabinet reshuffle, including the change of the finance minister, did not affect yields of Polish bonds.

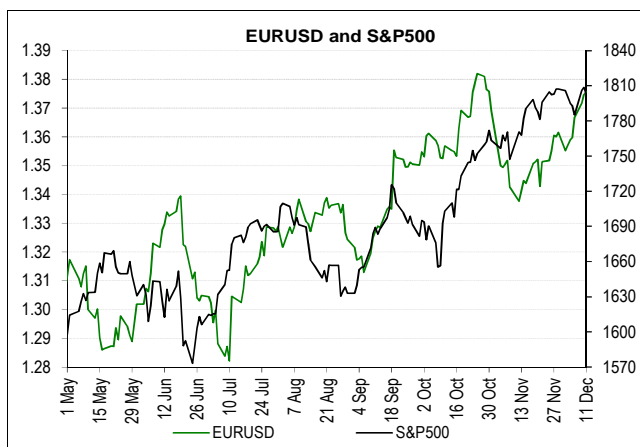
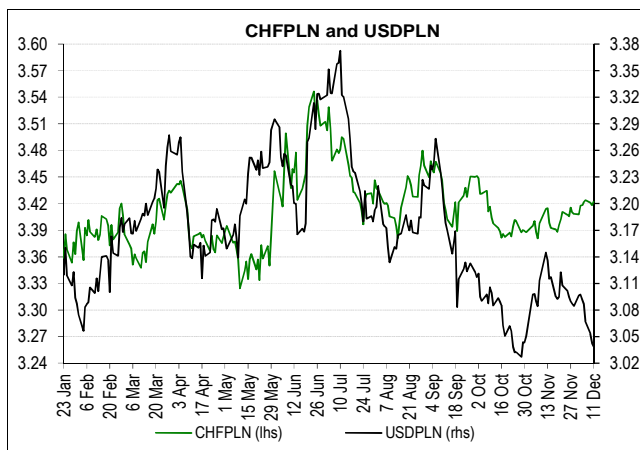
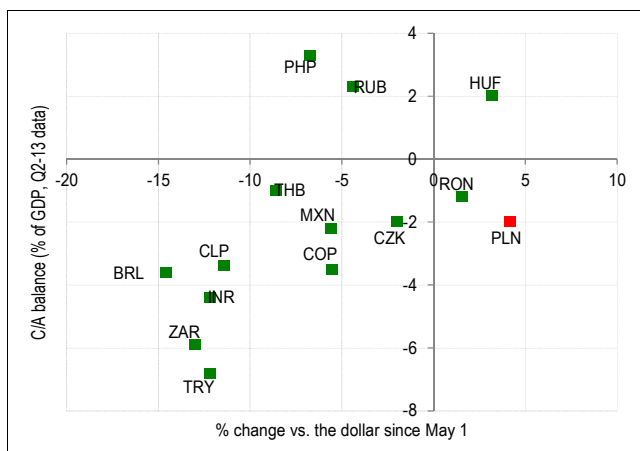
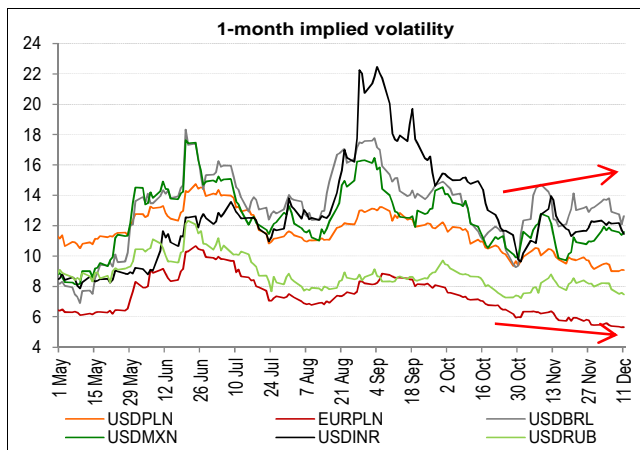
▪ Bearish steepener was developing on the interest rate market last month. 2-10Y spread for IRS surged quite significantly to nearly 120bp (from 93bp), while for bonds this indicator increased sharply to ca 170bp from 134bp. What is more, domestic bonds clearly underperformed peripheral debt (Italian, Spanish or even Portuguese). One should notice that yield spread between Polish 10Y Bond and its German counterpart is close to the upper band of range trading observed since June/July 2013. The beginning of December brought both IRS and bond yields increase due to investors' mood deterioration on core markets. But it is worth to highlight that the pace of domestic yields increase was moderate in comparison with growth of global benchmarks. Yield on 10Y benchmark temporarily reached 4.61% and then shifted to the south again, towards 4.40%.

Global environment still crucial for market mood

▪ We still believe that front ends of curves are well anchored near current levels, supported by subdued CPI outlook (lower than earlier expected inflation path) and the MPC's comments.

▪ At the same time mid and long end of curves are still strongly dependent on global environment, in particular on future Fed's decision about QE3 tapering as early as in December. Lack of such decision should bring some rebound after significant weakening. We uphold our scenario that T-bond yields will increase in medium term.

Foreign exchange market



Sources: CSO, Reuters, BZ WBK

Zloty still awaiting an impulse

▪ No breaking changes occurred in case of EURPLN during the last few weeks, the range trading continued and even narrowed further. Thus, November and the first half of December was a rather boring period on the Polish foreign exchange market.

▪ This is clearly reflected in 1M implied volatility for EURPLN exchange rate. In the second week of December it declined to the lowest level since the data are available (in Bloomberg). This is quite striking observation given the fact that currently the market is under impact of changing expectations on the timing of FOMC first step towards reducing the bond buying program. A few months ago we showed that other emerging currencies – like Brazilian real, Mexican and Chilean peso – depreciated versus the dollar more than the zloty amid period of elevated worries over prompt QE3 tapering. Greater volatility of these currencies and their bigger vulnerability to sudden changes of market sentiment is reflected in changes in 1M implied volatility – some divergence between changes for EURPLN (or even USDPLN) and USDBRL, USDMXN or USDINR occurred. It seems that zloty's better performance may be to some extent explained by stronger external position of the Polish economy. The second chart shows that C/A deficit as a percentage of GDP is lower than in case of many emerging countries.

▪ It is also worth to notice that very positive US labour market data trigger lower and lower volatility of EURUSD and do not prevent US stock indexes on their way to fresh record high. The zloty does not benefit from periods of higher demand for risky assets, but at least does not depreciate due to worries over QE3 tapering.

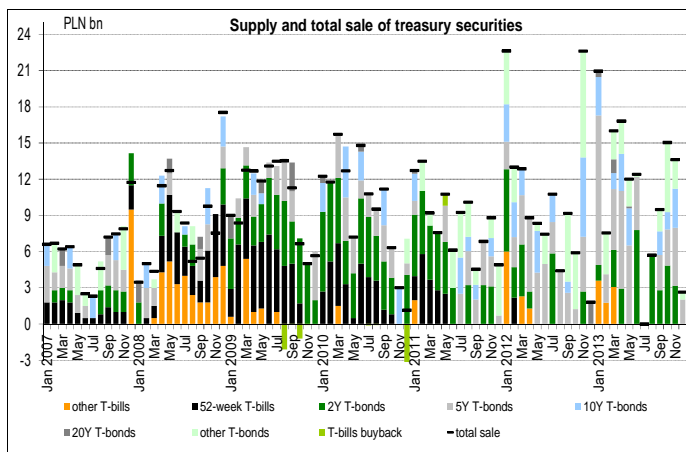
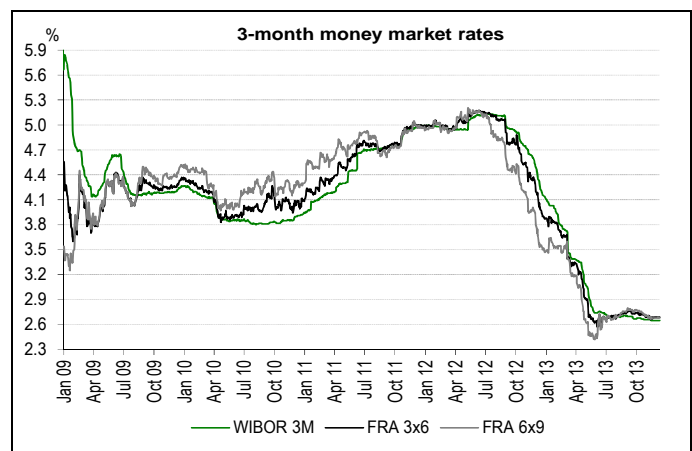
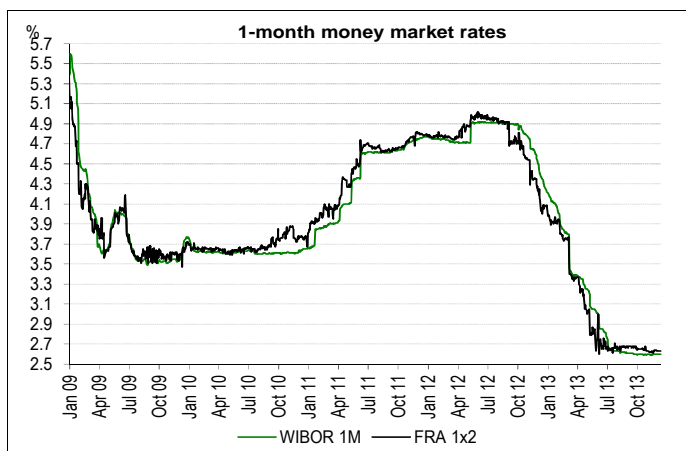
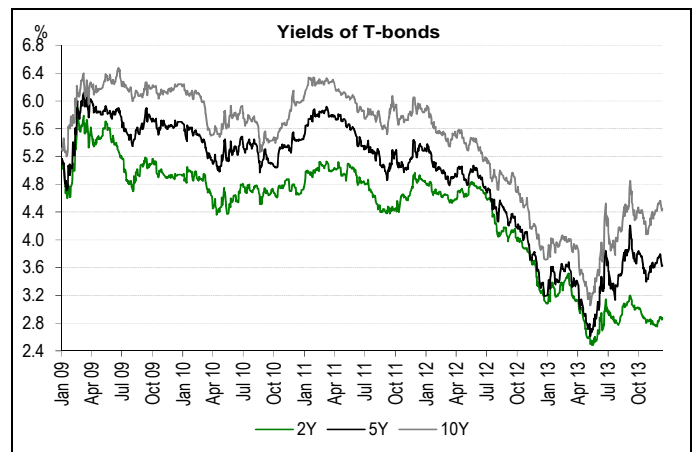
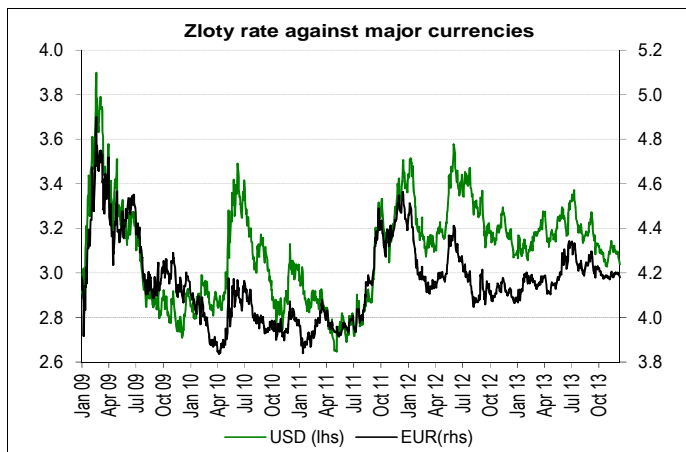
▪ Considering the Polish FX market, it seems, that currently expectations for further economic rebound neutralise an uncertainty regarding the timing and pace of reducing the scale of QE3. We do not expect scaling back the size of monetary policy stimulus already in December, but even if this takes place, it does not have to hit the zloty considerably. Additionally, December is a month when the NBP and the Polish state bank BGK are present on the market quite often and a perspective of their return this year may constrain the volatility. We expect average EURPLN at 4.18 in the final month of the year, though technical analysis suggests a risk of short term depreciation to ca. 4.24.

EURUSD up due to ECB rhetoric and despite strong US data

▪ In line with what we had expected, after a substantial plunge at the turn of October and November (triggered by ECB decision and strong US data), EURUSD resumed the upward trend. The single currency was supported by dovish remarks of Jannet Yellen, data showing a rebound of inflation in the euro zone and less dovish than expected tone of the ECB after the December's meeting. Mario Draghi suggested that after the surprising November's rate cut, the bank does not feel any pressure to take immediate nonstandard measures. Lower worries over, for example, cutting the deposit rate below zero, helped the euro to pare nearly all losses suffered at the turn of October and November. EURUSD is close to 1.38 in mid-December.

▪ Data from the US labour market for October and November showed an increase of payrolls by at least 200k. Despite this fact, the dollar did not gain versus the euro. The correlation between EURUSD and S&P500 since November 8 and mid-December is nearly 0%. This clearly shows that hopes for continuation of an economic rebound (and improvement of companies' earnings) proved stronger than worries over trimming the monetary stimulus. The euro also benefited from this fact. We do not expect QE3 tapering to be announced in December. We suppose that the FOMC may hit that first step to reduce scale of bond buying program is looming, but it may hold on until Jannet Yellen takes over the governing of the Fed (in late February).

Market monitor



Treasury bill auctions in 2012/2013 (PLNm)

Auction date	OFFER	DEMAND/SALE
09.01.2012	49-week: 1000-2000	5402/2223
30.01.2012	30-week: 1000-2000	3249/1997
30.01.2012	51-week: 1000-2000	4225/1592
27.02.2012	52-week: 1000-2000	6711/2190
26.03.2012	52-week: 1000-3000	5402/2223
23.04.2012	31-week	3117/1332
07.01.2013	20-week: 2000-3000	10967/3602
04.02.2013	20-week: 1000-2000	7728/1747
04.03.2013	25-week: 2000-3000	7324/3084

* based on data of the Ministry of Finance

Treasury bond auctions in 2012/2013 (PLNm)

month	date	First auction			Second auction			Switch auction			
		T-bonds	offer		date	T-bonds	offer	date	T-bonds	offer	
December											
January '13	3.01	DS1023/WS0429	3000-5000	3664.3	23.01	OK0715/PS0418	6000-9000	13693.8	6.12	OK0113/PS0413	WS
February	7.02	PS0418/WZ0117	4000-6000	5806.5	13.02	OK0715/WZ0124	3000-5000	4584.7			
March	20.03	OK/PS/WZ	2000-6000	8080.6					7.03	PS0413/OK0713/DS1013	DS/WS/WZ
April	11.04	DS1023/WZ0124	3000-5000	5029.1	23.04	OK/WZ/PS	5000-10000	11788.6			
May	9.05	PS0718	3500-5500	6498.0	16.05	DS/WZ/WS	2000-6000	5505.4			
June	6.06	PS0718/WZ0119	3000-5000	4606.5					19.06	OK0713/DS1013	
July	-										
August	7.08	OK0116	3000-5000	5695.0							
September	5.09	OK0112/PS0718	5000-7000	5706.8					25.09	DS1013/OK0114	WZ0119/DS1023
October	3.10	PS0718	2500-4500	3008.0	22.10	OK0116/IZ0823/DS1023	6000-12000	12019.9	16.10	EUR20140203**	445.0
November	7.11	OK0116/PS0718	4000-7000	7964.2	13.11	USD20140115**	100	132.2	20.11	OK0114/PS0414	DS1023/WS/WZ/IZ
December									5.12	OK0114/PS0414	PS0416/WZ0119

* with supplementary auction, ** buy-back auction, *** demand/sale,

Source: MoF, Reuters, BZ WBK

Economic calendar

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
9 December DE: Exports (Oct) DE: Industrial output (Sep) CZ: Industrial output (Oct)	10	11 HU: CPI (Nov)	12 EZ: Industrial output (Oct) US: Retail sales (Nov)	13 <i>PL: Money supply (Nov)</i> <i>PL: Balance of payments (Oct)</i> <i>PL: CPI (Nov)</i>
16 <i>PL: Core inflation (Nov)</i> CN: Flash PMI – manufacturing (Dec) DE: Flash PMI – manufacturing (Dec) EZ: Flash PMI – manufacturing (Dec) US: Industrial output (Nov)	17 <i>PL: Wages and employment (Nov)</i> DE: ZEW index (Dec) EZ: HICP (Nov) CZ: Central bank decision HU: Central bank decision US: CPI (Nov)	18 <i>PL: Industrial output (Nov)</i> <i>PL: PPI (Nov)</i> DE: Ifo index (Dec) US: House starts (Nov) US: Building permits (Nov) US: Fed decision	19 <i>PL: MPC minutes</i> US: Philly Fed index (Dec) US: Home sales (Nov)	20 US: Final GDP (Q3)
23 <i>PL: Retail sales and unemployment rate (Nov)</i> US: Personal income (Nov) US: Consumer spending (Nov) US: Michigan index (Dec)	24 US: Durable goods orders (Nov) US: New home sales (Nov)	25 Christmas	26 Second day of Christmas	27
30 US: Pending home sales (Nov)	31 <i>PL: Inflation expectations (Dec)</i> US: S&P/Case-Shiller (Oct) US: Consumer confidence index (Dec)	1 January	2 <i>PL: Balance of payments (Q3)</i> <i>PL: PMI – manufacturing (Dec)</i> CN: PMI – manufacturing (Dec) DE: PMI – manufacturing (Dec) EZ: PMI – manufacturing (Dec) US: ISM – manufacturing (Dec)	3
6 DE: PMI – services (Dec) EZ: PMI – services (Dec) US: ISM-services (Dec) US: Industrial orders (Nov)	7 EZ: Flash HICP (Dec)	8 <i>PL: MPC decision</i> DE: Exports (Nov) DE: Industrial orders (Nov) US: ADP report (Dec) US: Minutes Fed	9 EZ: ECB decision GB: BoE decision CZ: Industrial output (Dec) CZ: CPI (Dec) CZ: Final GDP (Q3) DE: Industrial output (Nov)	10 US: Non-farm payrolls (Dec) US: Unemployment rate (Dec)
13	14 <i>PL: Money supply (Dec)</i> DE: Finalny GDP (Q3) EZ: Industrial output (Nov) US: Retail sales (Dec)	15 HU: CPI (Oct) US: Fed Beige Book	16 EZ: HICP (Dec) US: CPI (Dec) US: Philly Fed index (Jan)	17 <i>PL: Balance of payments (Nov)</i> US: House starts (Dec) US: Building permits (Dec) US: Industrial output (Dec) US: Flash Michigan (Jan)

MPC meetings and data release calendar for 2013

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
ECB meeting	10	7	7	4	2	6	4	1	5	2	7	5
MPC meeting	8-9	5-6	5-6	9-10	7-8	4-5	2-3	20	3-4	1-2	5-6	3-4
MPC minutes	24	21	21	25	23	20	-	22	19	17	21	19
GDP*	-	-	1	-	29	-	-	30	-	-	29	-
CPI	15	15 ^a	14 ^b	15	15	13	15	14	13	15	14	13
Core inflation	16	-	15	16	16	14	16	16	16	16	15	16
PPI	18	19	19	18	21	19	17	20	18	17	21	18
Industrial output	18	19	19	18	21	19	17	20	18	17	21	18
Retail sales	24	25	22	23	24	25	23	26	24	22	26	-
Gross wages. employment	18	18	18	17	20	18	16	19	17	16	19	17
Foreign trade	about 50 working days after reported period											
Balance of payments*	2	-	28	-	-	28	-	-	30	-	-	-
Balance of payments	18	12	14	15	15	17	12	12	11	11	12	13
Money supply	14	14	14	12	14	14	12	14	13	14	14	13
Business climate indices	22	21	22	22	22	21	22	23	20	22	22	20

* quarterly data. ^a preliminary data for January. ^b January and February

Source: CSO, NBP, Ministry of Finance, Reuters, Bloomberg

Economic data and forecasts

Monthly economic indicators

		Nov 12	Dec 12	Jan 13	Feb 13	Mar 13	Apr 13	May 13	Jun 13	Jul 13	Aug 13	Sep 13	Oct 13	Nov 13	Dec 13
PMI	pts	48.2	48.5	48.6	48.9	48.0	46.9	48.0	49.3	51.1	52.6	53.1	53.4	54.4	55.0
Industrial production	%YoY	-0.5	-9.6	0.4	-2.1	-2.9	2.8	-1.8	2.8	6.3	2.2	6.3	4.4	0.4	11.6
Construction production	%YoY	-5.4	-24.9	-16.1	-11.4	-18.5	-23.1	-27.5	-18.3	-5.2	-11.1	-4.8	-3.2	-11.6	7.0
Retail sales ^a	%YoY	2.4	-2.5	3.1	-0.8	0.1	-0.2	0.5	1.8	4.3	3.4	3.9	3.2	3.7	5.0
Unemployment rate	%	12.9	13.4	14.2	14.4	14.3	14.0	13.5	13.2	13.1	13.0	13.0	13.0	13.2	13.5
Gross wages in enterprises sector ^a	%YoY	2.7	2.4	0.4	4.0	1.6	3.0	2.3	1.4	3.5	2.0	3.6	3.1	2.7	2.0
Employment in enterprises sector	%YoY	-0.3	-0.5	-0.8	-0.8	-0.9	-1.0	-0.9	-0.8	-0.7	-0.5	-0.3	-0.2	0.1	0.3
Export (€)	%YoY	11.2	-1.1	6.4	4.3	-1.2	11.1	0.4	5.1	5.6	1.9	8.1	3.6	4.4	22.6
Import (€)	%YoY	6.6	-0.9	1.1	-6.2	-1.3	1.7	-6.0	-2.2	1.1	-0.7	3.2	1.8	0.3	11.1
Trade balance	EURm	-259	-1 156	-64	426	-502	621	2	569	175	246	673	623	279	-65
Current account balance	EURm	-1 315	-1 705	-1 375	-668	-272	436	-204	133	-497	-785	-1 024	-194	-810	-715
Current account balance	% GDP	-3.8	-3.7	-3.5	-3.4	-3.2	-3.0	-2.9	-2.4	-2.0	-2.1	-2.0	-2.0	-1.8	-1.6
Budget deficit (cumulative)	PLNbn	-30.4	-30.4	-8.4	-21.7	-24.4	-31.7	-30.9	-26.0	-25.9	-26.8	-29.6	-39.5	-38.0	-43.3
Budget deficit (cumulative)	% of FY plan	86.9	86.9	16.4	42.0	47.3	61.6	60.0	50.4	50.3	51.9	57.4	76.6	73.7	84.0
CPI	%YoY	2.8	2.4	1.7	1.3	1.0	0.8	0.5	0.2	1.1	1.1	1.0	0.8	0.8	1.0
CPI excluding prices of food and energy	%YoY	1.7	1.4	1.4	1.1	1.0	1.1	1.0	0.9	1.4	1.4	1.3	1.4	1.5	1.8
PPI	%YoY	-0.1	-1.1	-1.2	-0.3	-0.7	-2.1	-2.5	-1.3	-0.8	-1.1	-1.4	-1.3	-1.3	-1.0
Broad money (M3)	%YoY	5.7	4.5	4.4	5.5	6.6	7.4	6.5	7.0	6.6	6.1	6.1	5.9	6.0	6.1
Deposits	%YoY	5.8	4.7	5.0	5.2	6.6	7.1	6.0	6.5	5.6	5.8	6.0	5.9	5.5	5.0
Loans	%YoY	2.3	2.3	3.6	3.7	3.5	2.3	1.4	3.5	3.7	3.3	3.7	2.9	3.2	3.7
EUR/PLN	PLN	4.13	4.10	4.14	4.17	4.16	4.14	4.18	4.28	4.28	4.23	4.24	4.19	4.19	4.18
USD/PLN	PLN	3.22	3.12	3.11	3.12	3.21	3.18	3.22	3.25	3.27	3.18	3.17	3.07	3.10	3.07
CHF/PLN	PLN	3.43	3.39	3.37	3.39	3.39	3.39	3.36	3.47	3.46	3.43	3.43	3.40	3.40	3.38
Reference rate ^b	%	4.50	4.25	4.00	3.75	3.25	3.25	3.00	2.75	2.50	2.50	2.50	2.50	2.50	2.50
WIBOR 3M	%	4.62	4.26	4.03	3.80	3.48	3.29	2.86	2.74	2.70	2.70	2.69	2.67	2.65	2.65
Yield on 2-year T-bonds	%	3.66	3.23	3.25	3.36	3.26	2.89	2.55	2.86	2.87	2.98	3.07	2.90	2.80	2.85
Yield on 5-year T-bonds	%	3.78	3.35	3.46	3.56	3.46	3.03	2.80	3.43	3.36	3.67	3.86	3.62	3.64	3.70
Yield on 10-year T-bonds	%	4.21	3.87	3.91	4.00	3.93	3.50	3.28	3.95	3.97	4.31	4.50	4.28	4.38	4.50

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates; ^a in nominal terms, ^b at the end of period

Quarterly and annual economic indicators

		2011	2012	2013	2014	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14
GDP	PLNbn	1 523.2	1 595.2	1 632.7	1 708.3	377.9	395.7	404.3	454.8	393.4	414.3	423.3	477.3
GDP	%YoY	4.5	1.9	1.5	3.1	0.5	0.8	1.9	2.4	2.7	3.1	3.2	3.2
Domestic demand	%YoY	3.6	-0.2	-0.3	2.2	-0.9	-1.7	0.5	0.5	1.0	1.9	2.3	3.4
Private consumption	%YoY	2.6	0.8	0.6	1.8	0.0	0.2	1.0	1.2	1.5	1.7	2.0	2.2
Fixed investments	%YoY	8.5	-0.8	-0.5	3.7	-2.1	-3.2	0.6	1.0	1.0	2.0	3.0	6.0
Industrial production	%YoY	7.7	1.0	2.5	5.6	-2.0	1.2	4.9	5.2	6.0	5.2	5.1	5.8
Construction production	%YoY	12.3	-1.0	-11.0	9.5	-15.6	-22.9	-7.0	-2.3	4.7	14.4	11.5	6.9
Retail sales ^a	%YoY	11.2	6.0	2.5	4.9	0.9	0.8	4.0	4.1	4.8	6.0	3.2	5.6
Unemployment rate ^b	%	12.5	13.4	13.5	12.7	14.3	13.2	13.0	13.5	13.8	13.0	12.6	12.7
Gross wages in national economy ^a	%YoY	5.2	3.7	3.2	4.4	2.6	3.3	4.0	2.8	3.6	4.3	4.8	5.0
Employment in national economy	%YoY	0.6	0.0	-0.8	0.5	-0.7	-1.1	-1.3	-0.1	0.3	0.5	0.5	0.4
Export (€)	%YoY	12.1	5.9	5.8	11.0	3.2	5.5	5.3	9.0	11.0	11.0	11.0	11.0
Import (€)	%YoY	12.2	2.3	0.3	8.9	-2.0	-2.2	1.2	4.0	7.0	8.0	9.5	11.0
Trade balance	EURm	-10 059	-5 175	2 986	6 502	-139	1 194	1 094	837	1 345	2 439	1 788	929
Current account balance	EURm	-18 519	-14 191	-5 662	-1 795	-2 313	362	-2 306	-1 405	-203	956	-1 116	-1 432
Current account balance	% GDP	-5.0	-3.7	-1.5	-0.4	-3.1	-2.3	-2.0	-1.5	-0.9	-0.7	-0.4	-0.4
General government balance	% GDP	-5.0	-3.9	-4.8	-3.5	-	-	-	-	-	-	-	-
CPI	%YoY	4.3	3.7	0.9	1.8	1.3	0.5	1.1	0.9	1.5	1.8	1.6	2.2
CPI ^b	%YoY	4.6	2.4	1.0	2.2	1.0	0.2	1.0	1.0	1.6	2.1	1.9	2.2
CPI excluding food and energy prices	%YoY	2.4	2.2	1.3	2.1	1.2	1.0	1.4	1.6	2.1	2.2	2.1	2.1
PPI	%YoY	7.6	3.4	-1.2	0.7	-0.7	-2.0	-1.1	-1.2	-0.5	0.7	0.7	1.9
Broad money (M3) ^b	%YoY	12.5	4.5	6.1	5.7	6.6	7.0	6.1	6.1	5.4	4.8	6.2	5.7
Deposits ^b	%YoY	11.7	4.7	5.0	6.9	6.6	6.5	6.0	5.0	4.8	4.8	6.0	6.9
Loans ^b	%YoY	14.4	1.2	3.7	4.4	3.5	3.5	3.7	3.7	4.0	2.9	3.0	4.4
EUR/PLN	PLN	4.12	4.19	4.20	4.06	4.16	4.20	4.25	4.19	4.14	4.08	4.04	3.99
USD/PLN	PLN	2.96	3.26	3.16	2.96	3.15	3.22	3.21	3.08	3.04	3.00	2.94	2.86
CHF/PLN	PLN	3.34	3.47	3.41	3.23	3.38	3.41	3.44	3.40	3.32	3.26	3.21	3.11
Reference rate ^b	%	4.50	4.25	2.50	3.00	3.25	2.75	2.50	2.50	2.50	2.50	2.75	3.00
WIBOR 3M	%	4.54	4.91	3.02	2.86	3.77	2.96	2.70	2.66	2.65	2.72	2.92	3.17
Yield on 2-year T-bonds	%	4.81	4.30	2.97	3.22	3.29	2.77	2.98	2.85	2.88	3.07	3.35	3.58
Yield on 5-year T-bonds	%	5.44	4.53	3.47	3.88	3.49	3.09	3.63	3.65	3.73	3.82	3.95	4.03
Yield on 10-year T-bonds	%	5.98	5.02	4.04	4.67	3.95	3.58	4.26	4.39	4.57	4.60	4.70	4.82

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates;

^a in nominal terms, ^b at the end of period

This analysis is based on information available until 11.12.2013 has been prepared by:

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