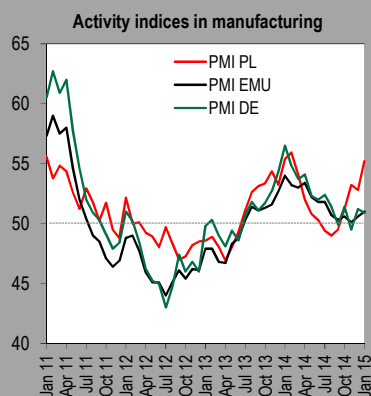
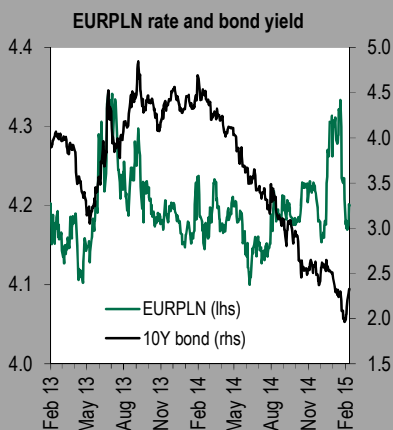


MACROscope

Polish Economy and Financial Markets

February 2015

Take it easy



In this issue:

Economic update	2
Monetary policy watch	4
Fiscal policy watch	6
Interest rate market	7
Foreign exchange market	8
Market monitor	9
Economic calendar	10
Economic data & forecasts	11

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■ **Central banks around the world are on a monetary easing spree:** At least 17 have eased policy so far in 2015. The most significant move was probably that of the European Central Bank, which decided to expand its QE programme from March on a bigger scale than anticipated. Other banks followed, taking steps aimed mainly at driving down the value of their currencies. One striking exception was the Swiss National Bank (SNB), which abandoned the 1.20 floor for EURCHF, triggering a sharp currency appreciation. The decision sent ripples of volatility through the financial markets and raised concern about countries with sizeable CHF debt exposures, like Poland. While several proposals of how to ease the situation of CHF-indebted households are still under discussion, **we argue that the economic impact of the Swiss franc appreciation on Polish households is unlikely to be large and the outlook for private consumption in 2015 remains optimistic.**

■ **Poland's Monetary Policy Council (MPC) kept interest rates on hold in February, but it also made it clear that a rate decision is getting closer and that a cut, or cuts, could exceed 25bp.** The change in the MPC's rhetoric, larger-than-expected QE in the Euro zone and the recent policy easing by other central banks around the world have convinced us that Polish interest rates could come down 50bp this year. A rate cut in March is very likely, in our view. While a 50bp rate cut in one move cannot be ruled out completely, we think that two cuts of 25bp each are more probable, unless uncertainty over Greece and Ukraine fades significantly and economic data surprise to the downside.

■ **There are many signs that the Polish economy is faring better than expected.** GDP growth in 2014 was 3.3% (probably one of the highest in Europe), fuelled by robust private consumption and booming investment. The labour market is in full swing. Indicators of consumer and business climate are still heading north. S&P recently upgraded Poland's sovereign rating outlook to positive, highlighting its sound growth prospects, while, according to a PwC report, the 'World in 2050', Poland will be the fastest-growing economy in the EU in the next few decades. We still expect a slowdown in Poland's economic growth at the start of 2015, but it should be relatively mild and short-lived. Recent data suggest that the economic outlook in the Euro zone is improving, helped by lower oil prices, the weaker euro and the ECB's QE.

■ **Recent central bank decisions and geopolitical tensions caused high volatility in the financial markets.** The zloty depreciated and fixed income markets experienced a correction after a long rally. **We expect Poland's currency and bonds to stabilise in the near term and rebound in the coming months, as global risk aversion fades.**

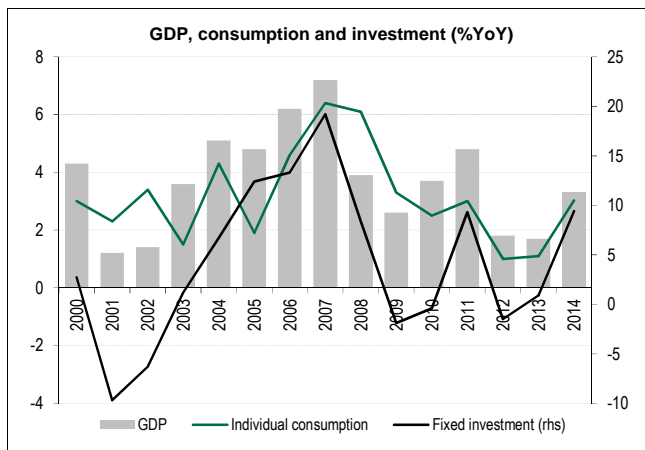
Financial market on 11 February 2015:

NBP deposit rate	1.00	WIBOR 3M	1.96	EURPLN	4.1999
NBP reference rate	2.00	Yield on 2-year T-bond	1.67	USDPLN	3.7094
NBP lombard rate	3.00	Yield on 5-year T-bond	1.93	CHFPLN	4.0068

This report is based on information available until 11.02.2015.

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Economic update



GDP growth slowing, but still near 3%

Poland's GDP expanded by 3.3% in 2014. Domestic demand proved to be the main engine of growth, with private consumption rising 3.0% and fixed investment up 9.4%. Net exports made a negative contribution to GDP growth for the first time since 2010, mainly due to a significant acceleration in imports.

We expect the detailed 4Q report, due at the end of February, to show the economy slowed to 3.1% from 3.3%YoY in 3Q. Private consumption probably decelerated to 3.0% vs. 3.2%YoY in 3Q and investment growth is likely to have eased to 8.8%YoY from 9.9%YoY. We expect net exports' contribution to be similar to 3Q (-1.5pp).

Signs of recovery ahead?

While we assume that the GDP slowdown may continue into 1Q15, it should be quite gentle and short-lived since optimism among the domestic consumers and entrepreneurs is improving. The labour market is still positive and households' real disposable income is expanding at a solid pace, supporting private consumption (see details on the next page). Meanwhile, recent business climate surveys show that activity at Polish companies has been improving, despite the challenging external environment.

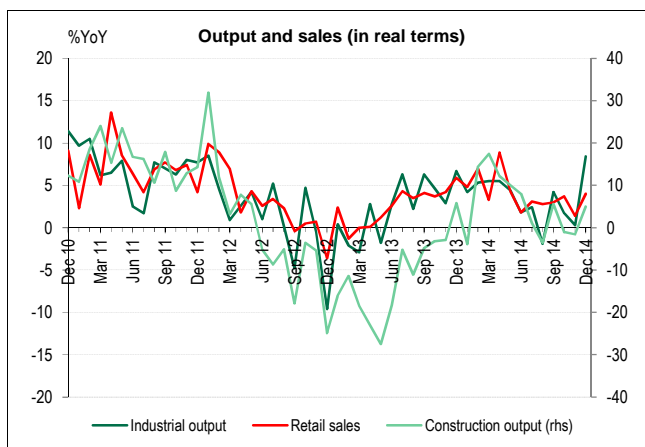
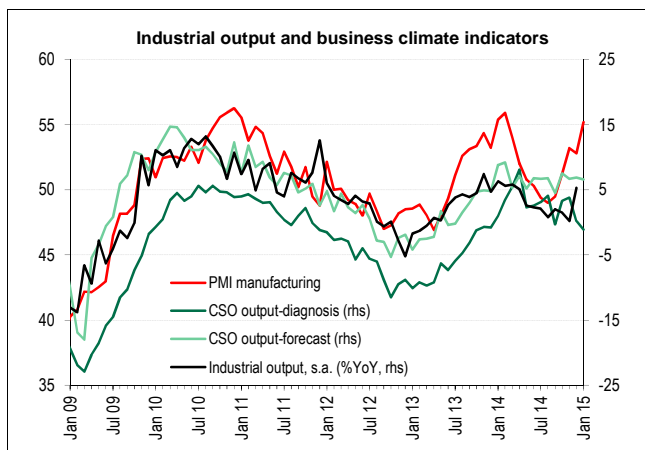
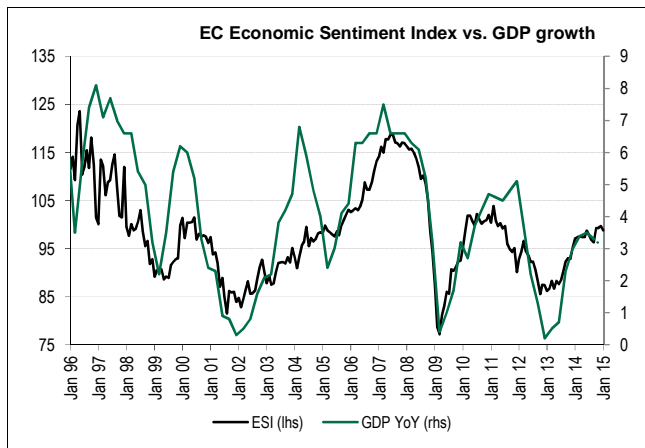
The Polish manufacturing PMI index jumped to 55.2 in January from 52.8, well above expectations. This was the fourth positive surprise in the last five months and the number was the highest since February 2014. The rise was driven by an improvement in all the main constituents. Rising orders (mainly domestic, with export orders improving less) led companies to increase production and hire more people. Higher demand was also reflected by the jump in the backlogs of work sub-index, which reached its highest level in four years. At the same time, prices of finished goods fell for the 26th month in a row despite rising demand. This was due to more intense competition, among other things.

While we would be cautious about drawing firm conclusions from the PMI index, as it has clearly diverged from industrial production growth in last two years (see chart) and most of the other business climate surveys also suggest that the outlook for the Polish economy is quite positive. The economic climate index published by the Central Statistical Office confirms the improvement in manufacturing and construction and the still fairly buoyant sentiment in retail trade. The European Commission's Economic Sentiment Index fell slightly in January from December's 3.5-year high, but remained consistent with GDP growth well above 3%.

In the Euro zone, the growth outlook is improving, helped by the lower oil prices, a weaker euro and the ECB's QE. This should boost Poland's export growth in the coming months. In fact, we have seen some early signs of external demand improvement in the last few months. Polish exports to some EU countries started picking up in October (see last month's report). We think these trends will continue.

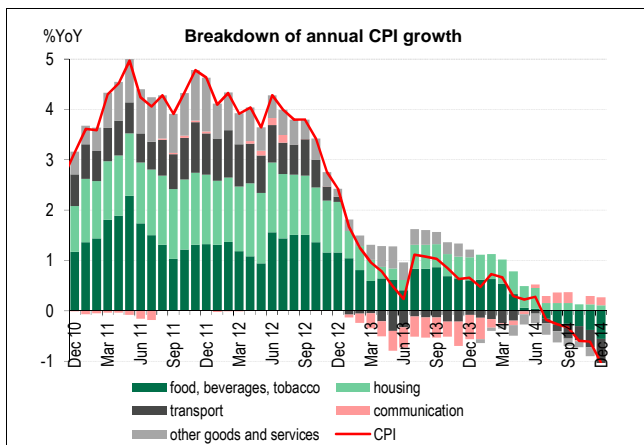
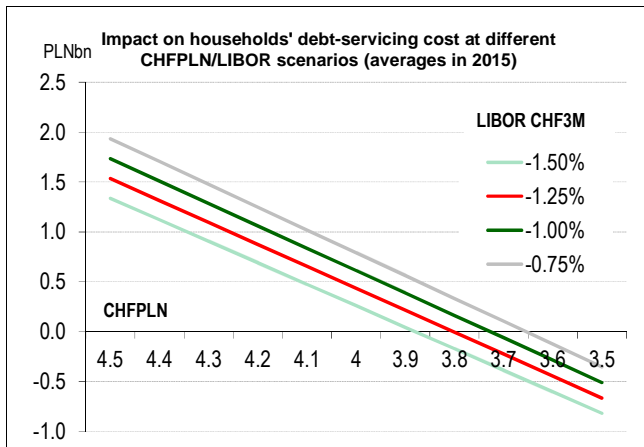
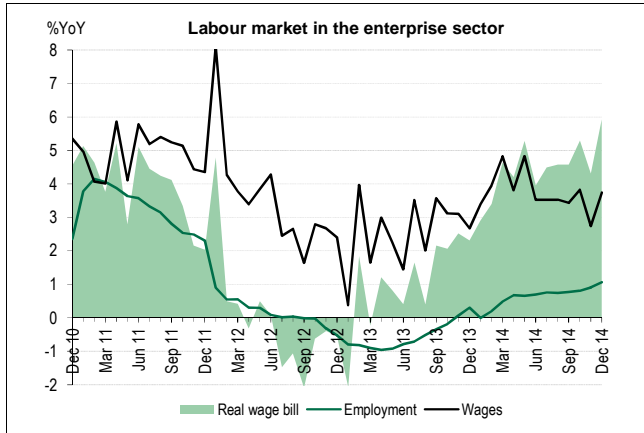
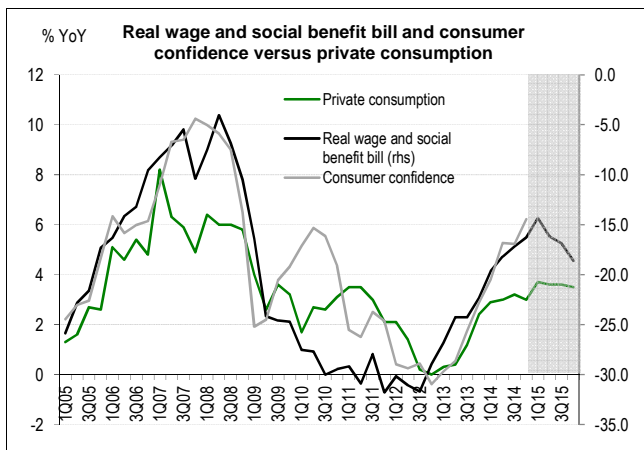
January production and sales may bring positive surprises

Industrial output and retail sales growth for December were better than expected and we think readings for January may also bring positive surprises, as suggested by car market data, among other things. January saw a small rise in the number of new car registrations, both in MoM and YoY terms, which is striking, given the seasonality (January is usually weaker than December) and the fact that last year's car sales were artificially boosted by temporary tax allowances. Poland's car production was also surprisingly strong in January, which bodes well for industrial output at the start of the year (vehicles account for c.10% of total industrial output).



Source: CSO, Markit, European Commission, BZ WBK.

Economic update



Source: CSO, NBP, BZ WBK.

Consumption outlook is still positive . . .

▪ The outlook for private consumption for 2015 is still positive, supported by the strength of the labour market situation, declining prices and lower interest rates. Thus, private consumption will probably remain an important engine of GDP growth and should help stabilize economic growth at close to 3%.

. . . as the labour market is strong . . .

▪ December's labour market data proved better than expected. Growth in employment in the corporate sector accelerated to 1.1%YoY from 0.9%YoY in November, while wage growth climbed to 3.7%YoY from 2.7%YoY in November.

▪ In monthly terms, employment in the corporate sector declined by 1.7k people, the best December result since 2007. The rebound in wage growth proves that November's slowdown was only a one-off effect due to a shift in bonus payments in mining. We expect wage growth to remain at 3%-4%YoY in the coming months. In 4Q14 as a whole wages were up 3.4%YoY compared with 3.5%YoY in 3Q.

▪ The real wage bill in the corporate sector expanded by 5.9%YoY in December, the most since late 2008 and well above the 4.3% average increase in January-November last year.

. . . households will pay lower interest on debt . . .

▪ The SNB's decision to abandon the 1.20 floor for EURCHF caused much concern about the possible impact of a stronger Swiss franc on CHF-indebted households. However, according to our estimates, the net effect on Polish household budgets should be relatively small, as lower LIBOR rates will offset a considerable part of the CHF appreciation. We estimate a 110bp fall in rates offsets a 10% CHF appreciation. Since the SNB decision, 3M CHF LIBOR has fallen by c75bp to -0.9%, while the CHFPLN has risen c11.5% to 4.03. Even in a scenario where CHFPLN averages 4.50 in 2015 and 3M LIBOR remains stable at -0.75%, the annual cost of servicing CHF loans for households should rise only by cPLN2bn. In what we think is the most likely scenario (CHFPLN in the 3.90-4.00 range, LIBOR nearing -1%), instalment payments on CHF loans could increase by PLN500mn per year.

▪ Meanwhile, households should benefit much more from the lower cost of servicing PLN-denominated debt. Even if there are no more interest rate cuts in Poland, total interest on household PLN debt should be cPLN3.5bn lower than in 2014, according to our estimates. If the MPC decides to cut rates by 50bp in March-April (which is our baseline scenario), consumers would save cPLN5.5bn this year in interest payments on PLN-denominated loans.

▪ To sum up, we estimate that changes in debt servicing costs should be consumption-positive, as costs should drop by cPLN5.0bn this year, the equivalent of 0.5% of annual consumption. Even in an extreme scenario of a considerable PLN depreciation and no further MPC rate cuts the effect would be net positive (by cPLN1.5bn).

. . . and consumer prices are declining

▪ The CPI fell 1.0%YoY in December, largely due to a sharp drop in fuel prices (-4.8%MoM). Core inflation, excluding food and energy, rose 0.5%YoY.

▪ In January fuel prices at the pump declined further (-7%MoM) and in February they could shed an additional 4%, even though the trend in global crude oil prices reversed. We expect CPI deflation to deepen in 1Q15E, perhaps to below -1.5%YoY, and think YoY CPI growth could remain negative until 3Q15E or even 4Q15E.

Monetary policy watch

Excerpts from the MPC's communiqué after its February meeting

In the past month, oil prices have fallen again, accompanied by a decline in the prices of some other commodities. Along with moderate global economic growth, this has been pulling down inflation in many countries. In Poland's immediate environment - including the euro area and most of the Central and Eastern European countries - annual price growth has declined below zero. The fall of commodity prices may support economic growth in countries which are net commodity importers.

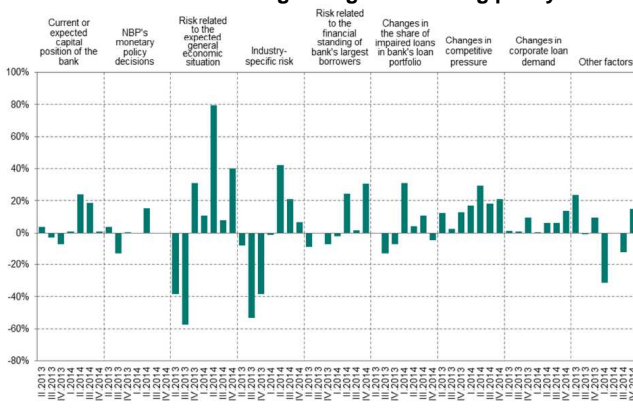
Major central banks are keeping their interest rates at historically low levels. At the same time, the European Central Bank has expanded its asset purchase programme significantly, adding sovereign bonds to the range of instruments targeted. The Swiss National Bank, in turn, unexpectedly abolished the Swiss franc's asymmetric peg to the euro, which resulted in its sharp appreciation vis-a-vis other currencies, including the zloty. The SNB also decreased its policy interest rates.

Bank lending both to households and enterprises continues to rise at a steady rate. At the same time, the sharp appreciation of the Swiss franc has increased the indebtedness of households with liabilities in this currency, which may limit their consumption.

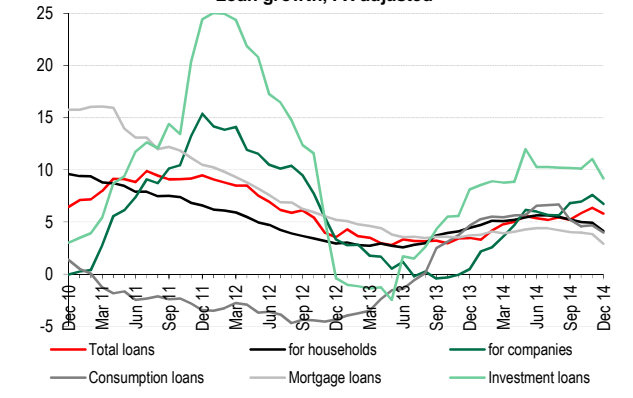
Labour market data point to a further decline of unemployment (in seasonally adjusted terms) resulting to a large extent from rising corporate employment. Yet, wage pressure in the corporate sector remains limited, as indicated by continued moderate wage growth.

Taking into account the recently heightened volatility in the financial markets, the Council has decided to leave the NBP interest rates unchanged. However, the Council does not rule out a monetary policy adjustment in the nearest future, should the expected period of deflation be extended, which would increase the risk of inflation remaining below the target in the medium term. A more comprehensive assessment of the outlook for inflation returning to the target will be possible after the Council gets acquainted with the incoming information, including the March NBP projection.

Factors influencing changes in lending policy



Loan growth, FX adjusted



Sources: NBP, Reuters, BZ WBK

The MPC signalled a rate cut in March

▪ The Monetary Policy Council (MPC) kept interest rates unchanged in February. The decision came as no surprise. Recent data from the Polish economy were quite positive (with solid growth in industrial output, a recovery in the labour market and a strong rise in the January PMI), so the MPC members that were waiting for convincing signals of economic slowdown failed to find any new arguments. Additionally, financial market turmoil after the SNB decision and uncertainty about Greece and Ukraine did not support a cut in February. In January the NBP president clearly suggested that periods of high FX volatility were not ideal for adjusting interest rates and he reiterated that this month. The MPC's February statement said it kept interest rates unchanged "taking into account the recently heightened volatility in the financial markets".

▪ However, the MPC's statement and press conference both clearly pointed to a high probability of an interest rate cut in March. The key sentence in the final paragraph of the statement was changed: Currently, the MPC does not exclude adjustment in the monetary policy "should the expected period of deflation be extended, which would increase the risk of inflation remaining below the target in the medium term". The MPC removed the second condition it had set for a rate cut: macro data confirming the economic slowdown. In our view, this is a clear signal that the moment for a rate cut has come closer. In fact, the NBP governor said clearly at the post-meeting press conference that the odds of a rate cut have increased and he did not rule out an adjustment of more than 25bp.

▪ The change in the Monetary Policy Council's rhetoric, larger-than-expected QE in the Euro zone and a recent wave of policy easing by other central banks around the world, have convinced us that the total scale of interest rate cuts in Poland could be 50bp this year. A rate cut in March is very likely, in our view. While a 50bp rate cut in one move cannot be ruled out completely, we think that two cuts of 25bp each are more probable, unless uncertainty over Greece and Ukraine fades significantly and economic data surprise to the downside.

Banks ease lending standards

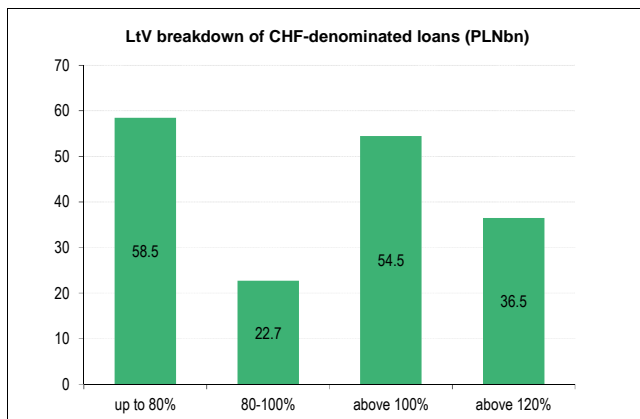
▪ According to the National Bank of Poland's (NBP) senior loan officer opinion survey, banks eased lending policies for companies and households at the start of this year. This was mainly the result of more optimistic economic expectations and, to a lesser extent, of competitive pressure in the banking industry.

▪ As regards demand for loans, banks reported no major changes in corporate credit and mortgage loan demand, but saw a rise in households seeking consumer loans, mainly for durable goods.

▪ Meanwhile, central bank money supply data showed total loan growth accelerating to 6.9%YoY in December, the highest since June 2012. However, some of this effect was due to a sharp zloty depreciation at the end of the year - CHFPLN was up 2%MoM and 5%YoY, while EURPLN rose 2%MoM and 3%YoY, which boosted the value of FX-denominated loans.

▪ After eliminating the effect of exchange rate fluctuations, there was a slight deterioration of total loan growth in the banking system. According to our estimates, growth in consumer loans decelerated to 4%YoY, while FX-adjusted growth of mortgage loans slowed to 2.9%YoY (the lowest since comparable data have been available, ie 1997). Growth in loans to companies also slowed but remained quite robust, with FX-adjusted investment loans expanding over 9%YoY and current loans up 5%YoY.

Restrictiveness of the Monetary Policy (Council)



Rise of CHFPLN may affect the housing market

- On the previous page we argued that we expect the impact of rising CHFPLN on households' finances to be rather low, as FX effect will be partly offset by lower interest rates and by banks' initiative to lower commissions on FX operations. In fact, in current market conditions some debtors already should have lower instalments than one year ago (especially those with longer maturities of loans). Thus, we expect no major rise of NPL in the banking system.

- On the other hand, FX is affecting the nominal value of loans, thus recent developments are likely to increase the number of CHF loans with an LTV above 100%. We estimate that their share may jump from c40% to c50%, diminishing the liquidity of the housing markets, especially in big cities (selling property with an LTV of more than 100% can be problematic).



Rzońca (1.16)

Winiński (1.15)

Kaźmierczak (1.14)

Glapiński (1.12)

Hausner (1.09)

Chojna-Duch (0.78)

Belka (0.77)

Zielińska-Głębocka (0.70)

Osiatyński (0.55)

Bratkowski (0.34)



The index runs from 0 to 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.

The MPC is keeping a close eye on the financial markets

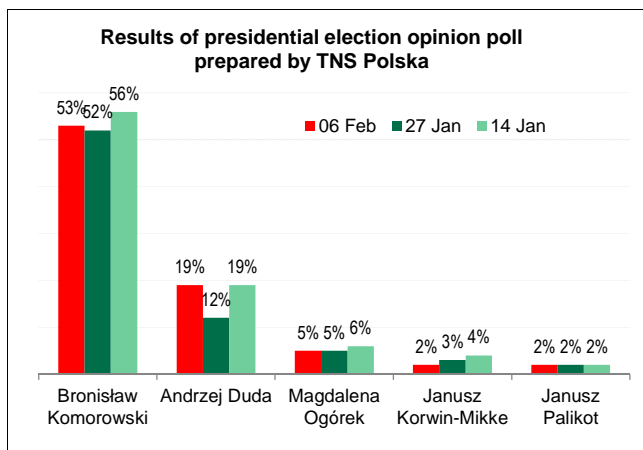
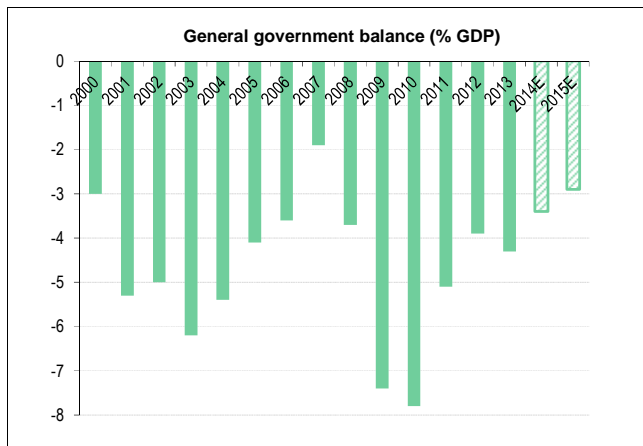
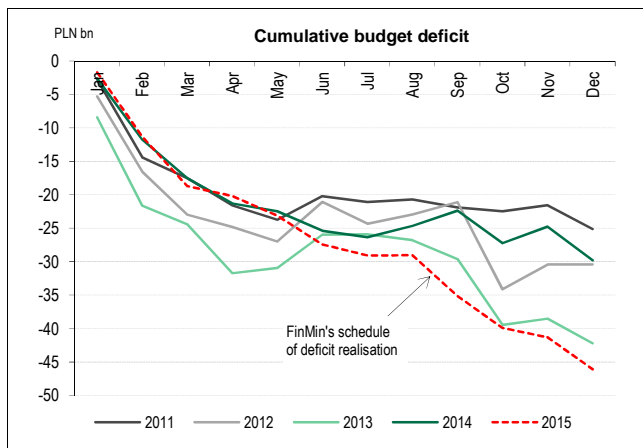
The last MPC conference in February clearly showed that an interest rate cut in March is highly probable. However, it has also become clear in recent weeks that the MPC is watching the financial market's situation with the utmost attention. Recent turmoil in the FX market, due to Swiss National Bank's decision to abandon the EURCHF floor, discouraged Andrzej Bratkowski (the only MPC member who voted for a 100bp rate cut in December) from making more considerable cuts and currently he supports smaller moves of 25bp. During the last MPC post-meeting conference even Jerzy Osiatyński, another dovish member, stressed that he is concerned about Greece's impact on the markets. Thus, a rapid increase in financial market volatility would most likely make the MPC postpone or even drop its decision to cut rates further.

NBP sceptical about conversion of CHF-loans into PLN

Andrzej Jakubiak, the head of Polish Financial Supervision Authority (KNF), recently put forward an idea to convert CHF-denominated loans into PLN. The draft proposal assumes a voluntary conversion of loans at the current CHFPLN rate, with the resulting FX loss shared 50:50 between the borrower and the lender. Borrowers would also compensate banks for the difference in PLN and CHF interest rates since the origination of the loan.

In our view, if such an operation were done by commercial banks without close assistance from the central bank, it would introduce a lot of stress to market, as banks would be forced to close their CHF contracts and buy a lot of Swiss francs. This view was supported by deputy NBP President Andrzej Raczko, who warned of possible PLN depreciation and investors' retreat from Polish assets. We think that a massive loan conversion is impossible without considerable input from the NBP, which could supply Polish banks with francs in non-market operation, and would help them to reverse CHF financing transactions. However, Marek Belka, the NBP president, said the discussion about CHF loans is a destabilising factor that is complicating monetary policy. Government officials also seem to be quite sceptical about the KNF proposal. Finance minister Mateusz Szczurek said that the KNF solution needs to be worked out if it is to be implemented on a mass scale. Meanwhile, Prime Minister Ewa Kopacz said she was not an advocate of Hungarian-style, enforced loan conversion from CHF to PLN. Still, in her view, the solutions for currency loans have to be discussed further. We think all these comments suggest that the Polish regulator's proposals are not very likely to be implemented at this point. However, the issue will be subject to further analysis.

Fiscal policy watch



	Spread vs. Bunds (10Y) in bp			CDS (5Y USD)		
	11.02	change since 12.01.15	change since 31.12.14	11.02	change since 12.01.15	change since 31.12.14
Poland	198	20	1	65.7	-3	-5
Czech	21	11	0	49.3	-4	-5
Hungary	296	-16	-19	139.6	-40	-38
Greece	1052	146	146	197	17	18
Spain	126	10	19	92.6	5	6
Ireland	89	0	18	46.5	0	-5
Portugal	222	9	7	169.5	-14	-31
Italy	132	132	-2	109.9	-16	-29
France	0.27	0	0	41.8	-1.5	-4
Germany	-	-	-	16.1	0	-2

Source: Finance Ministry, Reuters, TNS Polska, BZ WBK.

Fiscal budget is consolidating

- There are still no official data on the 2014 budget execution but the Finance Ministry predicts that the deficit was slightly below PLN30bn at the end of the year, ie PLN18bn less than planned. Budget revenues were more than PLN5bn higher, while spending was more than PLN12bn lower than expected.

- The ministry published the schedule for its 2015 budget, which assumes that the deficit will rise sharply in 1Q15 (to over 40% of the annual plan) and will then increase more slowly towards the planned level of PLN46.08bn.

- In our view, in 2015 it will be difficult to achieve such spectacular results as in 2014. GDP growth and its structure (with quite healthy domestic demand) should be supportive for tax revenues, but this effect will be largely neutralised by persistent deflation. Furthermore, in an election year, the government may be unwilling to adjust public spending to below the level planned.

- The general government deficit was PLN30.9bn (ESA2010), or 2.5% of GDP, in the first nine months of 2014. Despite a favourable situation in the first three quarters, in our opinion the deficit will have widened quite significantly in the last quarter of the year, due to high investment and social spending and some slowdown in tax income, among other things. The finance minister admitted recently that the general government gap for 2014 as a whole was probably over 3.3% of GDP.

- Standard & Poor's decided to revise Poland's rating outlook to positive from stable and affirmed its sovereign credit ratings for foreign and local currency. Fitch left Poland's rating at A- with a stable outlook. S&P highlighted that sound GDP growth prospects should translate into higher income levels and improved creditworthiness over the forecast period. Moreover, the agency could consider raising its ratings if Poland's institutional and governance effectiveness continued to improve or if external debt metrics improved faster than anticipated by S&P. In our view, an outlook upgrade would be possible if the fiscal deficit dropped below 3% of GDP and Poland exited the Excessive Deficit Procedure.

Incumbent Bronisław Komorowski tops presidential poll

- Poland will hold a presidential election on May, 10. Currently, there are 12 candidates, however, the formal registration has not begun yet.

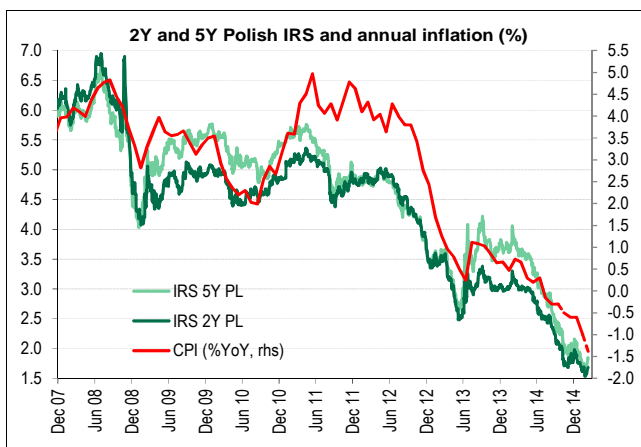
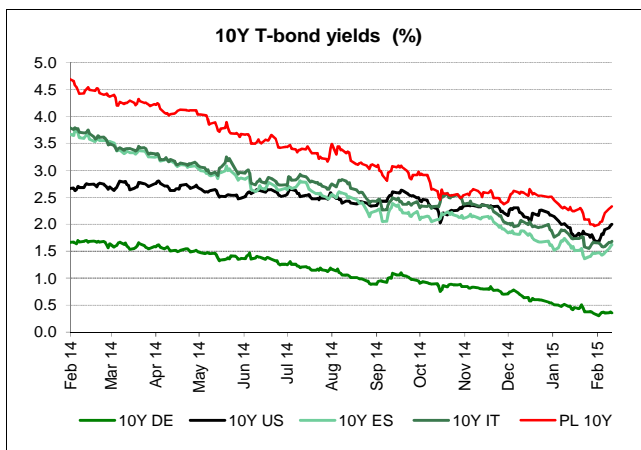
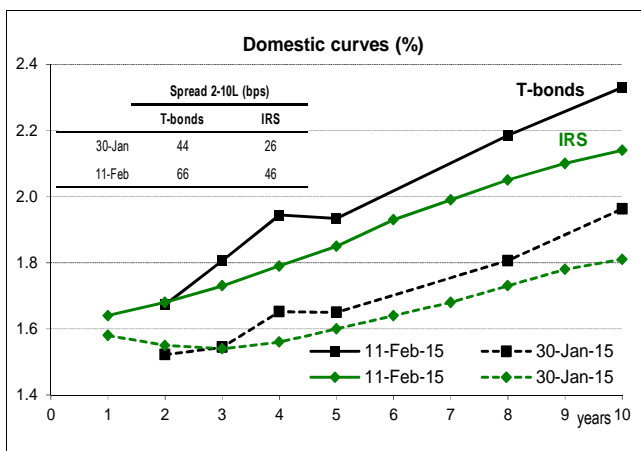
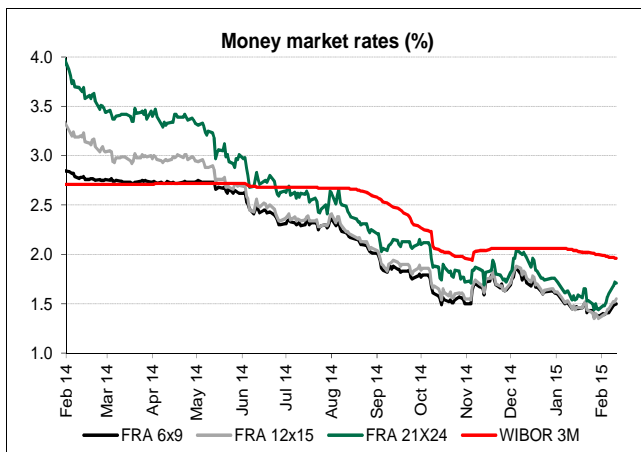
- President Bronisław Komorowski is strong favourite to win. A new survey released by TNS Polska shows that if elections were to take place in February, the incumbent president would take 53% of the votes. The poll places Andrzej Duda (PiS) in the second place, with 19%, and Magdalena Ogórek (SLD) third with 5%.

Core market should benefit from QE in the medium term

- In January, core and peripheral debt markets benefited from the ECB's decision to launch a significant QE programme and from deflation in the Euro zone and a further drop in oil prices. European yields hit fresh record lows and the 10Y UST yield dropped slightly. However, the Greek election result sent peripheral yields back up at the end of January. Much stronger-than-expected US labour market data caused another correction in the first week of February by renewing expectations of early Fed rate hikes.

- In our view, the QE programme will remain a game changer and is likely to impact the market significantly due to the decline in net government bond supply in the Euro zone. Therefore, we expect core markets to remain strong, particularly as uncertainty about Greece is likely to exert more downward pressure on yields of German bunds. As regards peripheral countries, their debt should remain attractive for investors seeking yields or relative value.

Interest rate market



Source: Finance Ministry, Reuters, Bloomberg, BZ WBK.

WIBORs show that rate cut hopes strengthen

- Money market rates continued to ease in January. While the decline in WIBORs was subdued (6-7bp over the month), FRA rates fell significantly (by 24-32bp), supported by a visible strengthening in the IRS market. Even without a rate cut in February, WIBORs dropped another 1-4bp in the first ten days of the month, while longer tenor FRAs (starting from six months) were 12-28bp higher than at the end of January, largely because of the upward move on the IRS market.

- After the recent correction in FRA rates, the market is now pricing in a 50bp fall in interest rates (25bp in one month's time and another 25bp in the next three months), down from the 75bp seen at the end of January.

- We decided to revise down our path of the WIBORs as we believe that the MPC will cut rates by 50bp in total in the coming months. We expect a more pronounced decline in WIBOR rates once the rate cut is delivered.

Yield correction after significant strengthening in January

- The Polish fixed income market gained sharply in January. The surprisingly large expansion of the ECB asset purchase programme had a very positive impact on Polish bonds and IRS by encouraging investors to accumulate assets rather than take profits. Yields and IRS rates dropped significantly (following a rally on core and peripheral Euro zone debt markets) to set new record lows across the curves, with the 10Y benchmark yield falling temporarily below 2%, ie below the NBP reference rate.

- In the first week of February, the rally in both bonds and IRS lost some steam. This was mainly due to the gradual rise in yields on core markets. Moreover, the MPC's decision to keep rates unchanged in February brought some profit-taking as some investors felt disappointed. The fresh supply of T-bonds at the auction (see below) also added to the higher yields. All these factors, together with much stronger-than-expected US labour market data and a renewed risk of Greece exiting the euro, resulted in the 10Y benchmark yield rising temporarily to 2.30%, its highest level since mid-January.

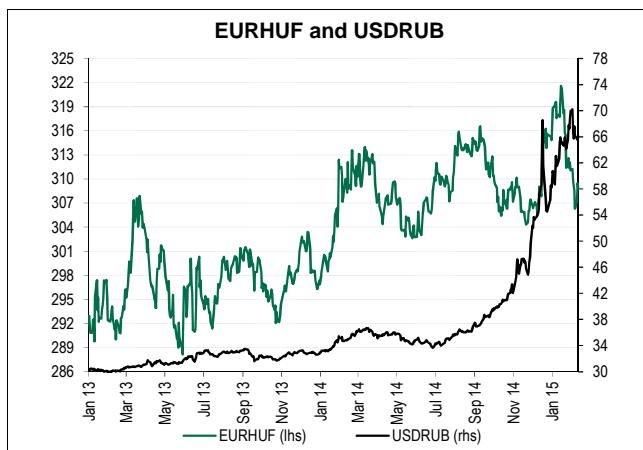
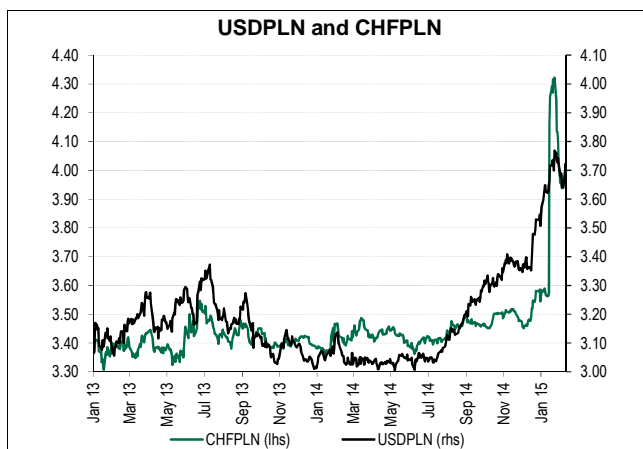
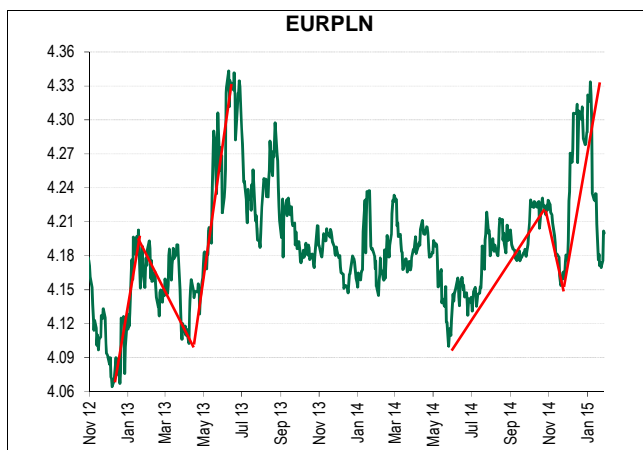
- Poland's Finance Ministry successfully sold T-bonds worth PLN11.2bn on the primary market in January, or c40% of the maximum supply planned for 1Q15 (PLN30bn). At the first auction in February, it tapped the market for more than it had originally planned – cPLN5.9bn vs the PLN3.0-5.0bn on offer. We estimate that the ministry has now covered c44% of its 2015 borrowing needs.

Further strengthening likely

- The interest rate market clearly shows that domestic Polish assets are treated as emerging market ones when investors are in risk aversion mode. Moreover, the positive correlation between the 10Y Polish T-bond and the 10Y German bund lost momentum. Therefore, Polish assets did not benefit from the rebound in core markets.

- We perceive the recent curve steepening as a temporary phenomenon and expect it to flatten should worries about the situation in Greece subside and global markets stabilise. We expect the 5Y and 10Y tenors to recover, thanks to the expected cash inflows from the ECB. Meanwhile, January data due for release (low CPI, some slowdown in real activity) should provide further support by fuelling hopes of further rate cuts ahead. Therefore, we think that the short end should perform worse than the belly and long end of curves.

Foreign exchange market



Sources: Reuters, Bloomberg, BZ WBK.

The EUR/PLN slide . . .

▪ In January we said the zloty's sharp depreciation in late December was exaggerated, as the liquidity was very thin in the final days of the past year. As we expected, EUR/PLN followed the pattern seen in 1H13 and the zloty has recovered all the losses it suffered vs the euro in late 2014. The downward move of EUR/PLN was quite volatile as, first, the SNB abandoned the EUR/CHF 1.20 and then, a week later, the ECB extended its asset purchase programme by much more than had been expected. At the same time, USD/PLN continued the upward move that started in June 2014 as EUR/USD stayed low. This pushed USD/PLN to nearly 3.80, its highest level since June 2009.

. . . may stabilize for now

▪ We expect EUR/PLN to stay close to 4.20 in the coming weeks, due to adverse domestic and international factors. The MPC's rhetoric after the January meeting was very dovish and it seems an interest rate reduction should happen in the coming months (we anticipate two rate cuts of 25bp in March-April). Trimming the refi rate to 1.5% may diminish the positive impact of monetary policy easing in the Euro zone announced last month by the ECB. More easing by the MPC is likely to make the zloty much less attractive and slow the EUR/PLN's downward trend.

▪ Another issue that may prompt investor concern is the potential conversion of CHF mortgage loans into zlotys, proposed recently by the head of the financial regulator. The key question is whether the Polish central bank would provide Swiss francs to commercial banks that need to close FX swap positions when Poles decide to take up the option to convert their mortgages, or whether banks would have to buy CHF in the market. The latter would potentially have a significant negative impact on the zloty. However, we think this scenario is not very likely, so the risk to the currency is not substantial.

▪ As regards external factors, the situations in Greece and Ukraine are, in our view, the most serious issues that could hit the zloty. Investors are worried about whether Greece can come to an agreement with its creditors and the impact on the unity of the Euro zone. Meanwhile, the conflict in Eastern Europe continues and the EU decided to widen the sanctions that can be imposed on Russia.

▪ We expect EUR/PLN to stay close to 4.20 in February and March and resume its downward trend in 2Q, as signs of an economic recovery become more apparent and the ECB continues its asset purchase programme that supports risky assets, including the zloty.

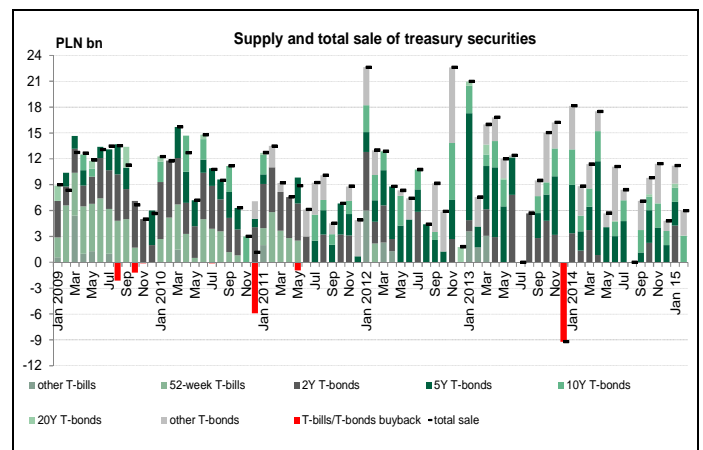
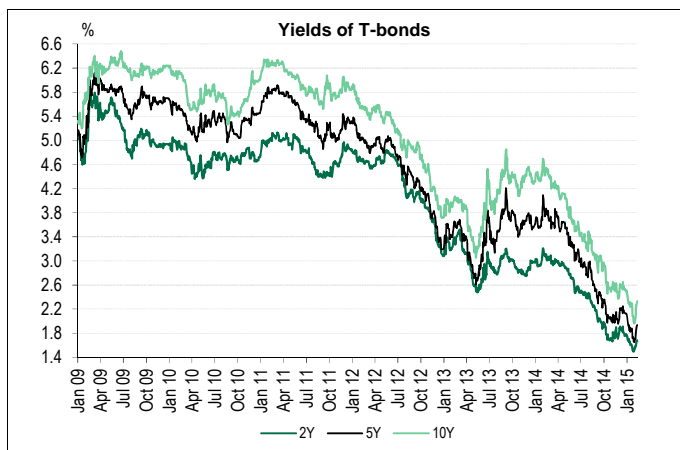
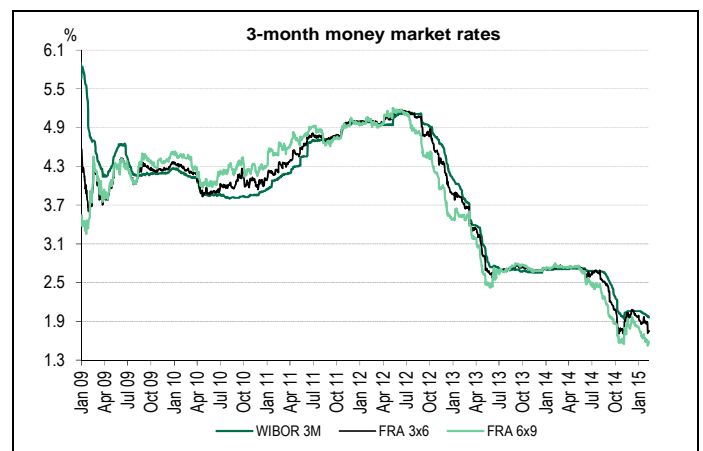
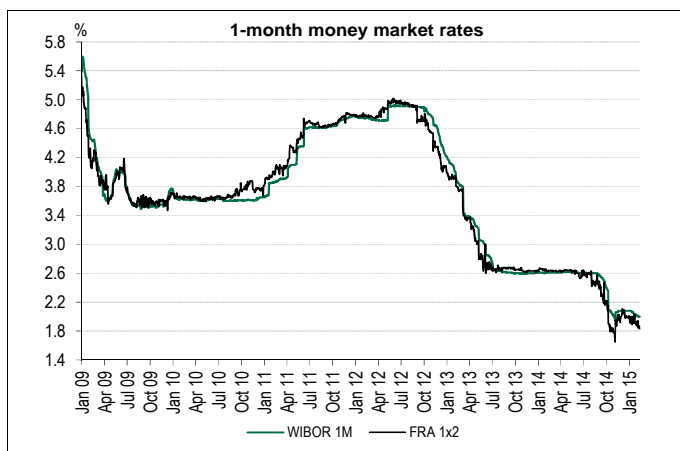
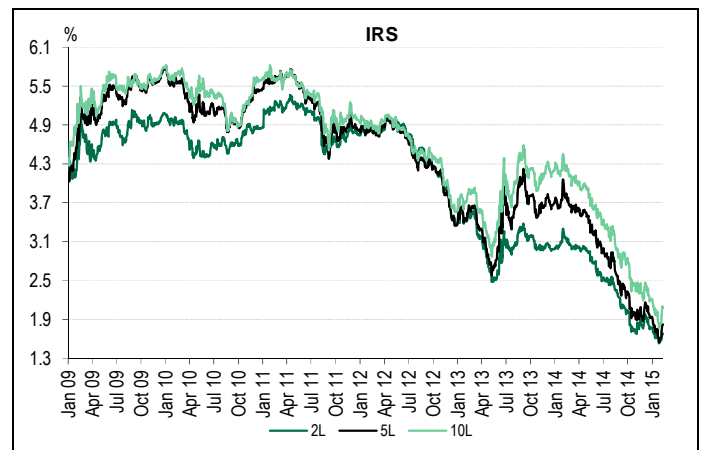
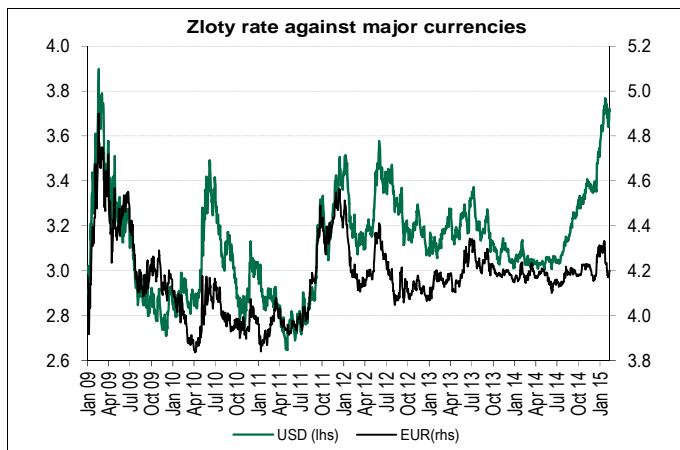
ECB and Greece pressure the euro

▪ In late January EUR/USD reached c1.11, its lowest level since September 2003, in reaction to the ECB decision. Tensions related to Greece also weighed on the single currency.

▪ We have decided to revise our EUR/USD forecasts and now see the 2015 low point at 1.12 in 1Q, with the exchange rate close to 1.18 at year-end (vs 1.23 anticipated previously).

▪ The euro has depreciated sharply after the ECB's January 22 decision to extend the asset purchase programme, but we think easing in the Euro zone has already been priced-in to a large extent. Also, a strong dollar is not good for the US economy and, thus, the Fed may try to play down expectations of rate hikes and limit the potential for the dollar to appreciate. However, Greek bailout negotiations may keep the exchange rate low in the coming weeks and this seems to be main risk to our scenario of a rise in EUR/USD later in 2015.

Market monitor



Treasury bond auctions in 2014/2015 (PLN mn)

month	First auction				Second auction				Switch auction		
	date	T-bonds	offer		date	T-bonds	offer		date	T-bonds	offer
February '14	6.02	OK0716/WZ0119	2000-4000	4810.0	13.02	PS0718/DS1013	3000-5000	4011.0	20.03	PS0414/OK0714	PS0718/DS1023
March	6.03	OK0716/WZ0119	2500-5500	6573.0							
April	3.04	DS1023/WZ0119	3000-5000	5781.0	23.04	OK0716/PS1016/PS0718	5000-	11722.3			
May	8.05	PS0719/WZ0119	3000-5000	5694.2	22.05	IDS1024	1000-2000	1270.0			
June	5.06	DS/WS/WZ	3000-5000	4989.7					18.06	OK0714/WZ0115	WZ0119/PS0719
July	3.07	DS0725/WS0428	1000-3000	2419.0	23.07	WZ0119/PS0719	2000-6000	5999.0			
August	-	-	-	-							
September	4.09	DS0725/WS0124	2000-3000	3595.0	25.09	USD20150716**	Up to 400	354.4	18.09	WZ0115/PS0415	WZ0119/PS0719
October	23.10	OK0716/PS0719	2000-6000	6062.1					2.10	WZ0115/PS0415	WZ0124/DS0725/WS0428
November	6.11	WZ/DS/WS	2000-4000	4495.7					20.11	WZ0115/PS0415/OK0715	WZ0119/PS0719
December									18.12	WZ0115/PS0415/OK0715	PS0719/WZ0124/DS0725
January '15	15.01	WZ/DS/WS	3000-5000	4198.5	22.01	OK0717/PS0420	5000-7000	7005.2			
February	5.02	WZ/DS/WS	3000-5000	5980.0	12.02	OK0717/PS0420	3000-5000				

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

Economic calendar

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
9 February DE: Exports (Dec) CZ: CPI (Jan)	10	11	12 EZ: Industrial output (Dec) US: Retail sales (Jan)	13 <i>PL: CPI (Jan)</i> <i>PL: Money supply (Jan)</i> <i>PL: Balance of payments (Dec)</i> US: Flash Michigan (Feb)
16	17 <i>PL: Wages and employment (Jan)</i> DE: ZEW index (Feb)	18 <i>PL: Industrial output (Jan)</i> <i>PL: PPI (Jan)</i> US: House starts (Jan) US: Building permits (Jan) US: Industrial output (Jan) US: FOMC minutes	19 <i>PL: MPC minutes</i> US: Philly Fed index (Feb)	20 <i>PL: Retail sales (Jan)</i> <i>PL: Unemployment rate (Jan)</i> CN: Flash PMI – manufacturing (Feb) DE: Flash PMI – manufacturing (Feb) EZ: Flash PMI – manufacturing (Feb)
23 DE: Ifo index (Feb) US: Home sales (Jan)	24 DE: GDP (Q4) EZ: HICP (Jan) HU: Central bank decision US: Consumer confidence index (Feb)	25 US: New home sales (Jan)	26 US: CPI (Jan) US: Durable goods orders (Jan)	27 <i>PL: GDP (Q4)</i> <i>PL: Inflation expectations (Feb)</i> CZ: GDP (Q4) US: Preliminary GDP (Q4) US: Pending home sales (Jan) US: Michigan index (Feb)
2 March <i>PL: PMI – manufacturing (Feb)</i> CN: PMI – manufacturing (Feb) DE: PMI – manufacturing (Feb) EZ: PMI – manufacturing (Feb) EZ: Flash HICP (Feb) US: ISM – manufacturing (Feb) US: Personal income (Jan) US: Consumer spending (Jan)	3	4 <i>PL: MPC decision</i> DE: PMI – services (Feb) EZ: PMI – services (Feb) US: ADP report (Feb) US: ISM – services (Feb) US: Fed Beige Book	5 EZ: ECB decision DE: Industrial orders (Jan) US: Industrial orders (Jan)	6 DE: Industrial output (Jan) EZ: GDP (Q4) HU: GDP (Q4) US: Non-farm payrolls (Feb) US: Unemployment rate (Feb)
9 DE: Exports (Jan) CZ: CPI (Feb)	10 HU: CPI (Feb)	11	12 EZ: Industrial output (Jan) US: Retail sales (Feb)	13 <i>PL: CPI (Feb)</i> <i>PL: Money supply (Feb)</i> CZ: Industrial output (Jan) US: Flash Michigan (Mar)
16 <i>PL: Balance of payments (Jan)</i> <i>PL: Core inflation (Jan)</i> US: Industrial output (Feb)	17 <i>PL: Wages and employment (Feb)</i> DE: ZEW index (Mar) EZ: HICP (Feb) US: House starts (Feb) US: Building permits (Feb)	18 <i>PL: Industrial output (Feb)</i> <i>PL: PPI (Feb)</i> US: FOMC decision	19 <i>PL: MPC minutes</i> US: Philly Fed index (Mar)	20

Calendar of MPC meetings and data releases for 2015

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
ECB meeting	22	-	5	15	-	3	16	-	3	22	-	3
MPC meeting	13-14	3-4	3-4	14-15	5-6	2-3	7-8	-	1-2	5-6	3-4	1-2
MPC minutes	22	19	19	23	21	18	-	20	17	22	19	17
Flash GDP*		13			15			14			13	
GDP*	-	27	-	-	29	-	-	28	-	-	30	-
CPI	15	13 ^a	13 ^b	15	14	15	15	13	15	15	13	15
Core inflation	16	-	16	16	15	16	16	14	16	16	16	16
PPI	21	18	18	20	20	18	17	19	17	19	19	17
Industrial output	21	18	18	20	20	18	17	19	17	19	19	17
Retail sales	27	-	-	-	-	-	-	-	-	-	-	-
Gross wages, employment	20	17	17	17	19	17	16	18	16	16	19	16
Foreign trade	about 50 working days after reported period											
Balance of payments*			31									
Balance of payments	13	13	16	13	15							
Money supply	14	13	13	14	14							

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

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

Economic data and forecasts for Poland

Monthly economic indicators

		Jan 14	Feb 14	Mar 14	Apr 14	May 14	Jun 14	Jul 14	Aug 14	Sep14	Oct14	Nov 14	Dec 14	Jan 15E	Feb 15E
PMI	pts	55.4	55.9	54.0	52.0	50.8	50.3	49.4	49.0	49.5	51.2	53.2	52.8	55.2	54.5
Industrial production	% YoY	4.2	5.3	5.5	5.5	4.4	1.8	2.4	-1.9	4.2	1.7	0.3	8.4	-0.5	4.4
Construction production	% YoY	-3.9	14.4	17.4	12.2	10.0	8.0	1.1	-3.6	5.6	-1.0	-1.6	5.0	1.1	0.5
Retail sales ^a	% YoY	4.8	7.0	3.1	8.4	3.8	1.2	2.1	1.7	1.6	2.3	-0.2	1.8	1.3	1.9
Unemployment rate	%	13.9	13.9	13.5	13.0	12.5	12.0	11.8	11.7	11.5	11.3	11.4	11.5	12.1	12.0
Gross wages in corporate sector	% YoY	3.4	4.0	4.8	3.8	4.8	3.5	3.5	3.5	3.4	3.8	2.7	3.7	3.3	3.2
Employment in corporate sector	% YoY	0.0	0.2	0.5	0.7	0.7	0.7	0.8	0.7	0.8	0.8	0.9	1.1	1.4	1.3
Exports (€)	% YoY	8.4	7.3	9.5	5.1	10.4	5.7	6.7	-0.9	6.1	4.1	2.3	11.7	1.4	3.2
Imports (€)	% YoY	5.8	6.9	4.1	8.9	11.8	7.5	7.2	0.1	6.1	4.7	4.7	12.6	4.3	3.6
Trade balance	EUR mn	105	-79	132	39	-160	86	-167	-102	648	-8	-96	-261	-269	-134
Current account balance	EUR mn	-1,100	-651	345	269	-161	-927	-811	-987	18	-470	-268	-539	-1,322	-693
Current account balance	% GDP	-1.3	-1.2	-1.1	-1.1	-1.1	-1.2	-1.3	-1.4	-1.3	-1.4	-1.3	-1.3	-1.3	-1.3
Budget deficit (cumulative)	PLN bn	-2.6	-11.7	-17.5	-21.3	-22.5	-25.4	-26.4	-24.6	-22.4	-27.2	-24.8	-29.8	-1.7	-11.3
Budget deficit (cumulative)	% of FY plan	5.6	24.7	36.8	44.8	47.3	53.4	55.5	51.9	47.1	57.4	52.1	62.7	3.7	24.5
CPI	% YoY	0.5	0.7	0.7	0.3	0.2	0.3	-0.2	-0.3	-0.3	-0.6	-0.6	-1.0	-1.4	-1.6
CPI excluding food and energy	% YoY	0.4	0.9	1.1	0.8	0.8	1.0	0.4	0.5	0.7	0.2	0.4	0.5	0.6	0.4
PPI	% YoY	-1.0	-1.4	-1.3	-0.7	-1.0	-1.8	-2.0	-1.5	-1.6	-1.3	-1.6	-2.5	-3.4	-3.7
Broad money (M3)	% YoY	5.4	5.2	5.2	5.4	5.2	5.2	6.0	7.4	7.9	7.7	8.4	8.4	8.8	8.7
Deposits	%YoY	4.9	4.7	4.7	5.4	5.5	5.5	6.7	7.8	7.5	7.8	8.5	8.1	8.5	8.3
Loans	%YoY	4.2	4.7	5.3	6.1	5.4	4.9	5.4	6.3	6.2	7.2	7.4	7.3	7.7	7.7
EUR/PLN	PLN	4.18	4.18	4.20	4.18	4.18	4.14	4.14	4.19	4.19	4.21	4.21	4.21	4.28	4.18
USD/PLN	PLN	3.07	3.06	3.04	3.03	3.04	3.04	3.06	3.15	3.25	3.32	3.38	3.42	3.68	3.70
CHF/PLN	PLN	3.39	3.42	3.45	3.43	3.42	3.39	3.41	3.46	3.47	3.48	3.50	3.50	3.96	3.99
Reference rate ^b	%	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.00	2.00	2.00	2.00	2.00
3M WIBOR	%	2.70	2.71	2.71	2.72	2.72	2.69	2.68	2.65	2.45	2.07	2.03	2.06	2.03	1.94
Yield on 2-year T-bonds	%	2.99	3.06	2.99	2.94	2.79	2.54	2.45	2.30	2.02	1.77	1.78	1.84	1.60	1.60
Yield on 5-year T-bonds	%	3.67	3.79	3.68	3.60	3.36	3.10	2.89	2.73	2.40	2.12	2.04	2.16	1.82	1.80
Yield on 10-year T-bonds	%	4.42	4.47	4.26	4.10	3.80	3.54	3.34	3.23	2.98	2.63	2.54	2.55	2.21	2.18

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

Source: CSO, NBP, Finance Ministry, BZ WBK estimates.

Quarterly and annual economic indicators

		2012	2013	2014	2015E	1Q14	2Q14	3Q14E	4Q14	1Q15E	2Q15E	3Q15E	4Q15E
GDP	PLN bn	1,615.9	1,662.1	1,725.4	1,779.2	403.1	418.4	426.8	477.1	412.4	430.6	439.3	496.9
GDP	% YoY	1.8	1.7	3.3	3.2	3.4	3.5	3.3	3.1	2.8	3.1	3.2	3.5
Domestic demand	% YoY	-0.4	0.2	4.6	4.6	3.4	5.6	4.9	4.6	4.5	4.7	4.4	4.8
Private consumption	% YoY	1.0	1.1	3.0	3.6	2.9	3.0	3.2	3.0	3.7	3.6	3.6	3.5
Fixed investments	% YoY	-1.5	0.9	9.4	8.4	11.2	8.7	9.9	8.8	9.0	9.0	8.0	8.0
Industrial production	% YoY	1.0	2.3	3.4	5.4	4.9	3.7	1.8	3.1	4.3	5.6	6.0	5.4
Construction production	% YoY	-1.0	-10.3	4.3	6.3	9.8	9.9	1.1	1.0	2.6	6.9	7.4	6.7
Retail sales ^a	% YoY	6.0	2.6	3.1	4.3	5.1	4.6	1.9	1.4	1.6	2.4	5.4	7.6
Unemployment rate ^b	%	13.4	13.4	11.5	10.9	13.5	12.0	11.5	11.5	11.7	10.4	10.3	10.9
Gross wages in the national economy ^a	% YoY	3.7	3.4	3.6	4.0	4.2	3.5	3.5	3.1	3.5	3.6	4.2	4.6
Employment in the national economy	% YoY	0.0	-1.1	0.1	0.8	-0.3	0.1	0.3	0.5	0.8	0.8	0.7	0.6
Exports (€)	% YoY	6.5	5.7	6.3	5.8	8.4	7.0	4.1	5.7	3.0	4.8	6.8	8.5
Imports (€)	% YoY	2.2	0.2	6.6	7.4	5.6	9.4	4.6	7.0	4.6	6.5	8.5	10.0
Trade balance	EUR mn	-7,146	635	140	-2,428	159	-35	381	-365	-452	-703	-257	-1,016
Current account balance	EUR mn	-13,697	-5,245	-5,265	-8,236	-1,403	-808	-1,777	-1,277	-2,380	-1,302	-2,810	-1,744
Current account balance	% GDP	-3.5	-1.3	-1.3	-1.9	-1.1	-1.2	-1.3	-1.3	-1.5	-1.6	-1.8	-1.9
General government balance	% GDP	-3.9	-4.3	-3.4	-2.9	-	-	-	-	-	-	-	-
CPI	% YoY	3.7	0.9	0.0	-0.7	0.6	0.3	-0.3	-0.7	-1.4	-0.9	-0.6	0.3
CPI ^b	% YoY	2.4	0.7	-1.0	0.8	0.7	0.3	-0.3	-1.0	-1.4	-0.8	-0.4	0.8
CPI excluding food and energy	% YoY	2.2	1.2	0.6	0.7	0.8	0.8	0.5	0.4	0.5	0.6	0.7	1.2
PPI	% YoY	3.4	-1.3	-1.5	-2.6	-1.2	-1.2	-1.7	-1.8	-3.5	-2.9	-2.7	-1.4
Broad money (M3) ^b	% oY	4.5	6.2	8.2	5.8	5.2	5.2	7.9	8.4	7.8	7.1	6.5	5.8
Deposits ^b	%YoY	4.7	6.0	8.1	6.0	4.7	5.5	7.5	8.1	7.6	7.1	6.5	6.0
Loans ^b	%YoY	1.2	3.6	6.9	6.4	5.3	4.9	6.2	7.3	7.1	6.9	6.6	6.4
EUR/PLN	PLN	4.19	4.20	4.18	4.13	4.19	4.17	4.18	4.21	4.21	4.15	4.11	4.06
USD/PLN	PLN	3.26	3.16	3.15	3.60	3.06	3.04	3.15	3.37	3.70	3.67	3.57	3.47
CHF/PLN	PLN	3.47	3.41	3.45	3.89	3.42	3.42	3.45	3.50	3.97	3.93	3.86	3.78
Reference rate ^b	%	4.25	2.50	2.00	1.50	2.50	2.50	2.50	2.00	1.75	1.50	1.50	1.50
3M WIBOR	%	4.91	3.02	2.52	1.69	2.71	2.71	2.59	2.06	1.92	1.61	1.60	1.63
Yield on 2-year T-bonds	%	4.30	2.98	2.46	1.48	3.01	2.76	2.26	1.80	1.57	1.44	1.44	1.48
Yield on 5-year T-bonds	%	4.53	3.46	2.96	1.66	3.71	3.35	2.67	2.11	1.75	1.53	1.58	1.78
Yield on 10-year T-bonds	%	5.02	4.04	3.49	2.00	4.38	3.82	3.18	2.58	2.15	1.85	1.88	2.08

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

This analysis is based on information available until 11.02.2015 has been prepared by:

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