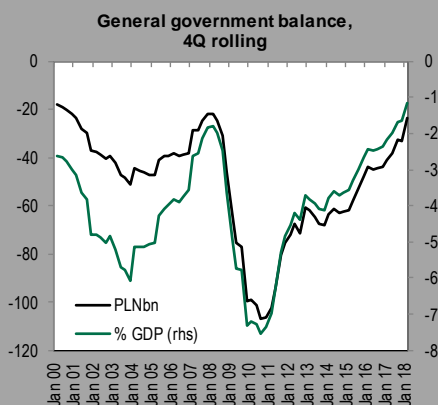
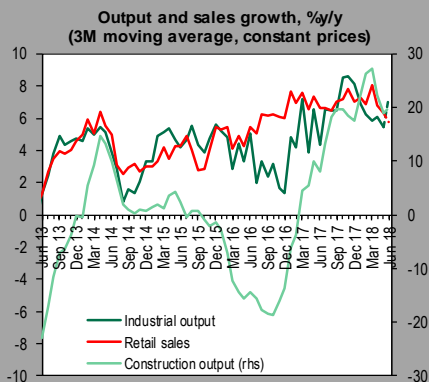


MACROscope

Polish Economy and Financial Markets

July-August 2018

Trade Wars: The Customs Menace



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■ The new episodes of trade wars unfolded, as Donald Trump's administration imposed tariffs on \$34bn worth of Chinese goods and announced plans to add duties on further \$200bn of imports. The menace of disruptions in international trade is rising, but we think it is still too early to say that the dark side clouds the global economic outlook, especially that China signalled it was still ready to negotiate the new trade arrangements with the USA, which gives a new hope for de-escalation of conflict. In fact, **the short-term perspectives look quite optimistic, in our view**. The most recent data from Germany has finally shown some positive surprises after a disappointing start of the year, and data from Poland still confirm that the economic growth remains resilient.

■ It seems more and more likely that **the second quarter of 2018, which has just ended, witnessed a GDP growth near 5% y/y again**, with strong contribution from private consumption and investments and less negative impact of net exports. We still think the peak cycle is behind us, but apparently the economic slowdown in Poland is like the vanishing point on the horizon – it does not come any closer as you march forward.

■ A similar story seems to apply to the inflationary pressure. The CPI growth accelerated slightly in May-June, but the impulse came entirely from higher prices of food and fuels. Meanwhile, core inflation excluding food and energy still shows no signs of life and even decelerated to 0.5% y/y. As we wrote last month, the solid financial results of Polish companies may be delaying the process of pass-through from higher costs to higher prices. However, we still believe that **the upward trend in the underlying inflation will finally materialise in a few quarters' time** as the tensions in the labour market will only get stronger. It should be facilitated by the change in external inflationary environment (higher price growth in Europe), higher prices of commodities, and weaker zloty.

■ The new central bank economic projection is similar to our forecasts. Inflation predicted for 2018 and 2020 has been lowered slightly as compared to the March version, but the return of the CPI above the official 2.5% target is still predicted in 2019-2020. GDP forecast has been increased for 2018 and lowered slightly for 2019-20. The new projection gave the MPC absolutely no new arguments to change view, so the central bank still believes that there are no reasons to mull changes in monetary policy in a foreseeable future. **We still believe that the main interest rates will remain on hold at least until November 2019**. NBP governor Adam Glapiński believes that no policy changes would be needed even until the end of 2020, which would probably make him the last Jedi holding rates stable among the central bankers in the region.

■ Polish currency depreciated sharply at the start of summer holidays, amid concerns about the global economic growth (due to next stage of trade wars), dollar appreciation and political tensions in Italy and Germany. **We see room for moderate recovery of the zloty** due to solid domestic data, but also thanks to stabilisation of global market sentiment and expected euro strengthening vs. dollar.

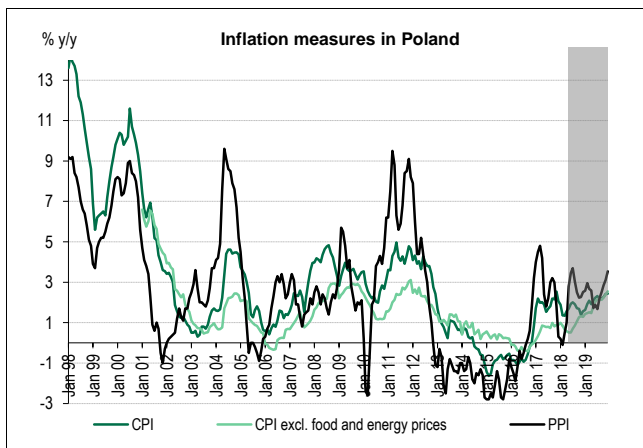
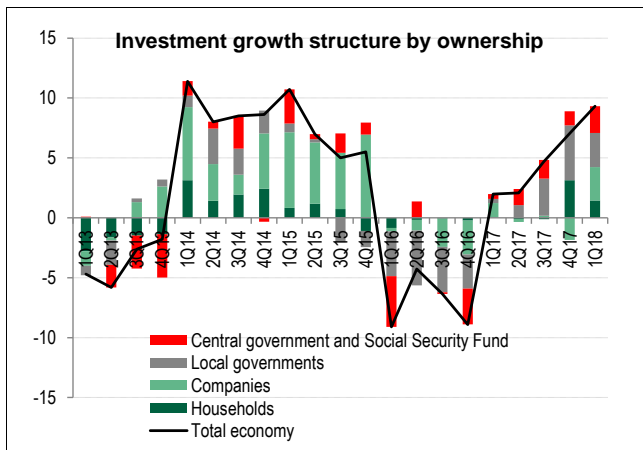
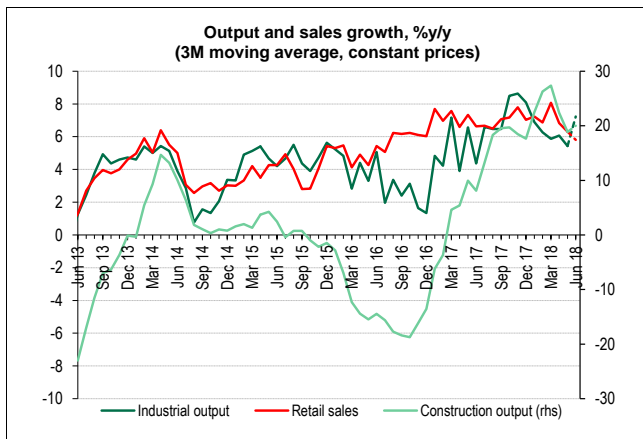
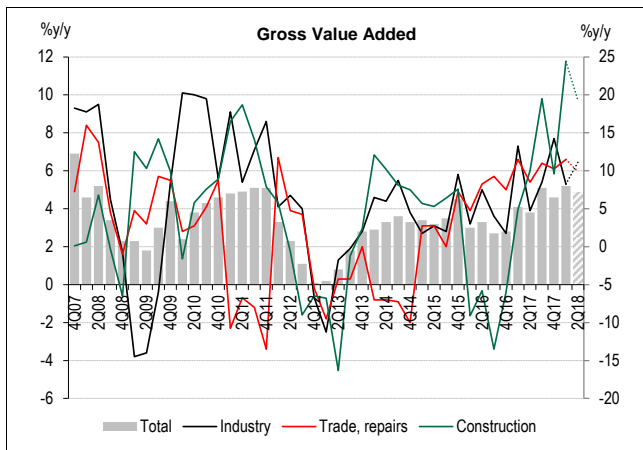
■ Polish bonds remain quite resilient to changing market moods. We think that sizeable bond redemptions and relatively low supply of new debt in July will help **yields to get even lower in the coming weeks**. Market weakening is possible at the end of summer, in our view, when the Ministry of Finance will probably increase bond supply at outright auctions and worries about economic slowdown abroad may cause expectations of additional fiscal stimulus.

Financial market on July 12, 2018:

NBP deposit rate	0.50	WIBOR 3M	1.70	EURPLN	4.3262
NBP reference rate	1.50	Yield on 2-year T-bond	1.61	USDPLN	3.7055
NBP lombard rate	2.50	Yield on 10-year T-bond	3.17	CHFPLN	3.7159

This report is based on information available until 12.07.2018.

Economic update



Source: Stats office, Eurostat, NBP, BZ WBK.

GDP at c5% again?

It is not the first time we need to upgrade our short-term GDP growth forecasts. Performance of manufacturing and construction sector in the course of 2Q suggests such input on the value added side that economic growth might have stayed near 5% also in this quarter. The first 2Q GDP estimate will be released on August 14.

The 3M rolling average growth of output and retail sales headed downwards in April and May, but there should be a rebound of the former in June. Business optimism remains very high and, as we explained in the previous MACROscope, high contribution from inventory changes to GDP growth (something that occurred in 1Q data) were more often a sign of another strong quarter coming than spelled trouble. What is more, the NBP revision to 1Q C/A data suggests that some of the rise of inventories might be converted to stronger exports in next stats office estimates of 1Q growth. The current account was revised up by €260 million, mainly thanks to upward revisions of export and primary income accounts.

This means that the slowdown that was supposed to start as we entered 2018, most likely did not come either in 1Q (which surprised positively with a return to the peak value of GDP growth, 5.2% y/y, instead of a slide from 5.1% to 4.8%) or in 2Q.

The rebound of German industrial output and new orders for May gives hopes that the euro zone is getting out of a soft patch from early 2018 and stays in the expansion phase of the business cycle instead of entering the slowdown phase. This is another reason to keep Polish GDP forecasts close to 5% y/y for 2Q – we have revised our call to 4.9% y/y.

Private investment still out of sync with GDP

Another thing that kept us waiting longer than we expected is the rebound of private investments. Total investments are already accelerating, supported by EU funds and local governments' efforts to secure re-elections this autumn. In case of private investments, a deviation of their pace vs the economic growth held for 8 quarters, as during the global crisis environment of 2009-2010. In 1Q the gap was visibly reduced (in nominal terms, private sector investments rose 5% y/y, GDP 6.3% y/y).

Private consumption to stay strong

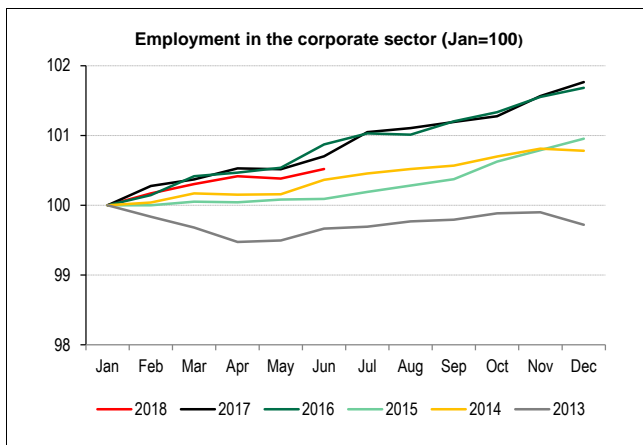
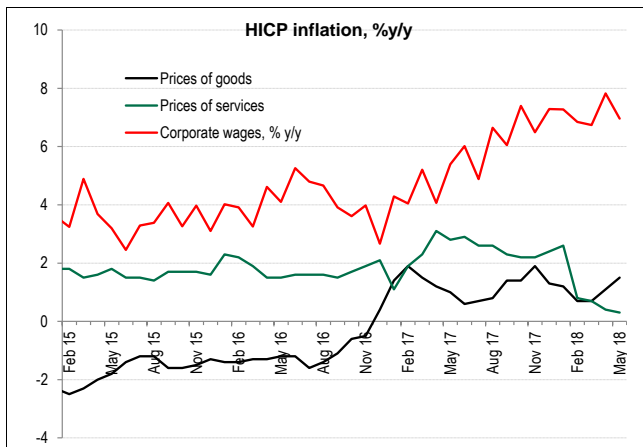
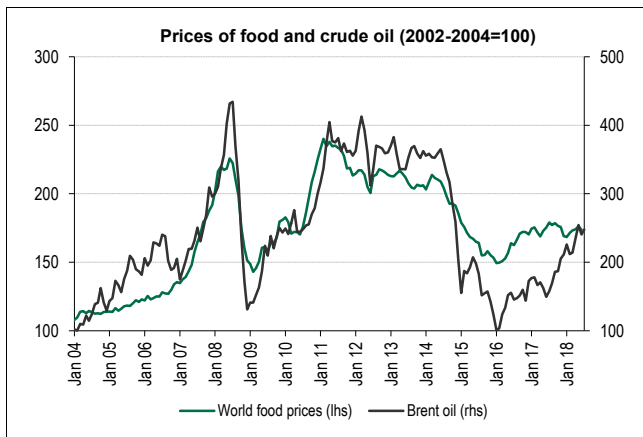
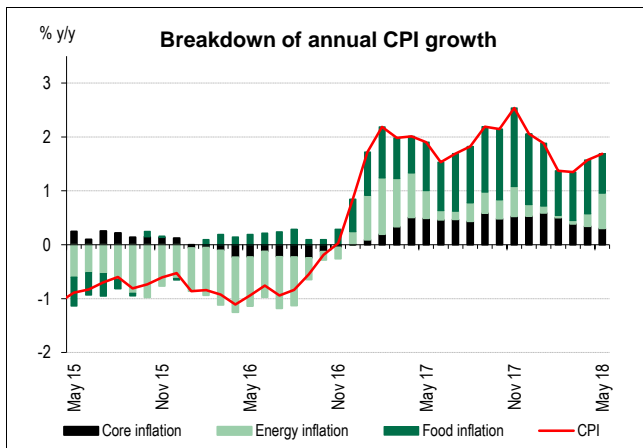
Looking at the high optimism of consumers with exceptional levels of major purchases index, as well as the state of the labour market, a growth rate of consumer expenditures should remain close to 5% y/y in real terms. Retail sales data suggested a slowdown in purchases of durable goods in spring, but in our view, it was a temporary distortion due to the introduction of Sunday trade ban.

PMI disobeyed the slowdown rhetoric too

Manufacturing PMI unexpectedly climbed in June to 54.2pts from 53.3 in May, driven by higher sub-indices for output, new orders and employment, boding well for real activity measures. In terms of spotting the signs of a slowdown, the 2Q18 average PMI was just 0.4 points lower than 4Q17 average. In case of the German counterpart the decrease was by 5.1 points.

The June PMI report mentioned that output costs index was at the highest level since 2011, indicating rising price pressure. PPI rose in May to almost 2.5% and we think 3+% readings are likely in the coming months, mainly due to higher prices of commodities (oil, metals). When mining, metal production and oil refining are excluded, PPI growth is showing an uptick, but, so far, reaching lower than the one in 2017. It seems unlikely that CPI would be resilient to the acceleration of PPI in the longer term, as the two measures are strongly correlated, albeit a reaction may come with a delay. The rise of inflation from 1.7% y/y to 2.5% during 2017 was accompanied by PPI growing by 3.3% on average between January and October (before a slowdown to almost zero in December, with CPI also moving lower at the time). Our [research note](#) on labour costs-inflation link with corporate results suggested there is still some time before the price pressure materializes as higher CPI.

Economic update



Source: Stats office, Eurostat, FAO, Reuters, BZ WBK.

CPI's half-hearted rebound

■ In case of CPI rebound we are not talking about horizon not coming closer but of it moving farther away – as long as we speak about the underlying trend of inflation. At the start of the year, we were already expecting the core inflation to embark on an upward trend. Instead, it kept falling despite the tight labour market situation (which should put pressure on prices of labour-intensive services).

■ According to a flash estimate, CPI climbed in June from 1.7% y/y to 1.9%, less than expected (consensus at 2%, our forecast at 2.1%). The downward surprise was mostly due to a weaker-than-expected increase in fuel prices, which rose 1.1% m/m, while data from gas stations suggested a rise of more than 2% m/m. Food prices also rose less than we expected. Trends in core categories remained subdued. According to our estimates, core inflation excluding food and energy prices remained unchanged at 0.5% y/y.

■ Oil prices rose again recently, and the zloty weakened substantially (4.41 vs. the euro at the start of July, the highest level since January 2017), which could translate into higher prices of imported goods. The FAO food price index also showed some recovery in 1H18, and it usually responded positively to substantial upswings in global oil prices.

■ Local factors could also push food prices higher. We analysed if the dry spell and heat wave in Poland might make inflation settle above 2% y/y this year in our [economic comment](#) on the issue. There was already a week-long period of lower temperatures and showers, but the Institute of Soil Science and Plant Cultivation (IUNG-PIB) has not yet declared the end of agricultural drought (with the broadest geographical coverage recorded since the institute started publishing its reports). Fruit and vegetable prices could respond to this in the months to come, but for now there are no upside surprises with food inflation. In our view, CPI growth was close to this year's peak in June, although a further increase is possible in July. We believe inflation may start moving lower after summer, to end the year around 1.5%, conditional on crop losses due to drought and on further weakness of the transmission channel from higher wages to CPI.

■ Still, we think the risks are skewed towards a higher path, and continue to believe wage pressure will cause services prices inflation to rebound. So far this year services inflation have been decelerating (mostly because of financial services) despite a higher pace of wage growth. On the other hand, goods prices have been rising at an increasing pace.

Labour market signals remain mixed

■ It seems positive labour market trends are losing momentum. In both employment and unemployment statistics recent monthly increases of employment and decreases of unemployment have been smaller than in the same months of previous years. The registered unemployment rate fell by 0.2pp in May while in the post-crisis years the decline between April and May was 0.3-0.5pp. Since March the monthly declines of the number of unemployed have been smaller than the 2010-2017 averages for particular months. Employment is moving away from the high paths for 2016 and 2017.

■ Eurostat's employment expectations index for Polish industry is declining since April. It is now the lowest this year, but still higher than at the peak of activity in 2007, ahead of the crisis. Job offers statistics seem to have peaked, and negative y/y growth appeared already in three months this year. On the other hand, the June manufacturing PMI report stated that employment 'increased at the fastest rate since April 2017, and was among the strongest recorded since the series began in June 1998', amid new work rising at the strongest pace in four months.

■ It does not look like the labour supply constraint became binding just yet, but where the pressure is the highest (construction) there is already high pace of wages (in May the first 10+% y/y reading since 2008).

Monetary policy watch

Excerpts from the MPC's official statement after its July meeting

Despite favourable global economic conditions, inflation abroad remains moderate on the back of **persistently low domestic inflationary pressure across many countries and a decline in some agricultural commodity prices**. At the same time, **significantly higher oil prices than a year ago** are increasing inflation rates.

Notwithstanding relatively high economic growth and wages rising faster than in the previous year, **consumer price growth remains moderate**. The slightly higher annual CPI rate than in the previous months reflects the growth in fuel prices. At the same time, **inflation net of food and energy prices stays low**.

In the Council's assessment, current information and the results of the projection point to a favourable outlook for economic activity growth in Poland, despite the expected slowdown in GDP growth in the coming years. In line with the results of the projection, **inflation will remain close to the target in the monetary policy transmission horizon. As a result, the Council judges that the current level of interest rates is conducive to keeping the Polish economy on a sustainable growth path and maintaining macroeconomic stability**.

Excerpts from the MPC's minutes from its June meeting

The majority of the Council members expressed the opinion that, taking into account current information, **the stabilisation of interest rates would continue to help meet the inflation target**, while supporting the maintenance of balanced economic growth, including a further recovery in investment. Moreover, these Council members pointed out that **the need to take into account the monetary conditions in the immediate environment of the Polish economy**, including the likelihood of the maintenance of negative interest rates in the euro area, **also spoke in favour of keeping the current level of interest rates in the coming quarters**.

In the opinion of some Council members, should incoming data and forecasts suggest a further increase in wage growth and a more marked intensification of inflationary pressure than currently expected, **it might be justified to consider an increase in the NBP interest rates in the coming quarters**. A view was also expressed that **in the event of a significant decline in economic indicators accompanied by a marked deterioration in consumer and corporate sentiment, in the longer run it might be justified to consider a decrease in interest rates**.

NBP's inflation projection, 50% prob. band

	Mar 17	Jul 17	Nov 17	Mar 18	Jul 18
2018	0.9÷2.9	1.1÷2.9	1.6÷2.9	1.6÷2.5	1.5÷2.1
2019	1.2÷3.5	1.3÷3.6	1.7÷3.7	1.7÷3.6	1.9÷3.5
2020	-	-	-	1.9÷4.1	1.7÷3.9

NBP's GDP projection, 50% prob. band

	Mar 17	Jul 17	Nov 17	Mar 18	Jul 18
2018	2.4÷4.5	2.5÷4.5	2.8÷4.5	3.5÷5.0	4.0÷5.2
2019	2.3÷4.4	2.3÷4.3	2.3÷4.3	2.8÷4.8	2.8÷4.7
2020	-	-	-	2.6÷4.6	2.4÷4.3

Timing of the first rate hike by NBP implied from FRAS



Sources: Stats office, NBP, PAP, Reuters, BZ WBK.

MPC unfazed by new projections

▪ The Monetary Policy Council kept interest rates unchanged in July, as expected. It still believes that current level of interest rates warrants continuation of well-balanced economic growth in Poland and that the new economic forecasts of NBP give no reasons to mull changes in monetary policy in a foreseeable future.

▪ The new NBP projection showed a slightly lower path of inflation in 2018 and 2020 as compared to its March version. Yet, CPI is still expected to head above the official 2.5% target in 2019-20 (with mid-point in 2020 at 2.8%, vs. earlier 3.0%). GDP projection has been increased for 2018 and lowered slightly for 2019-20.

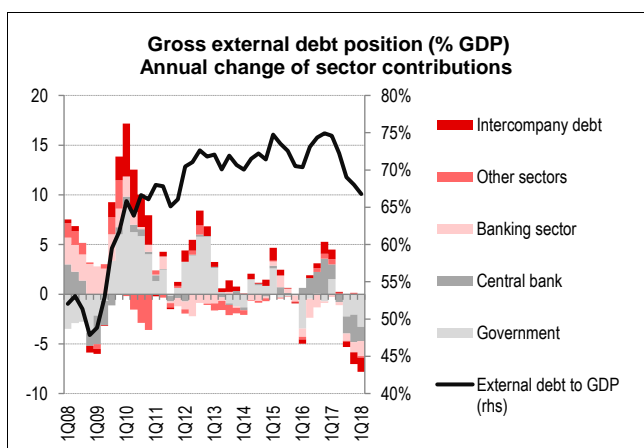
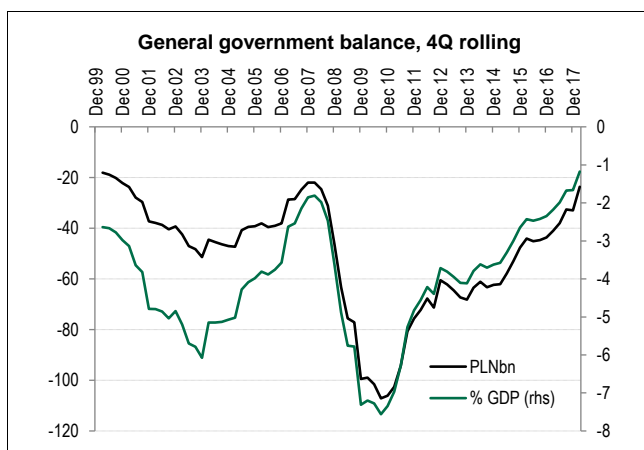
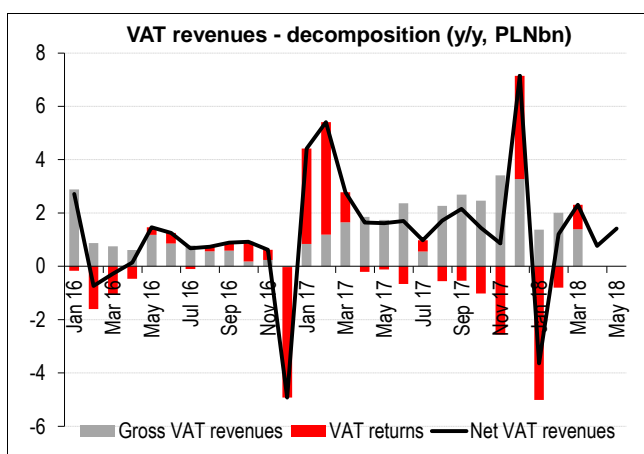
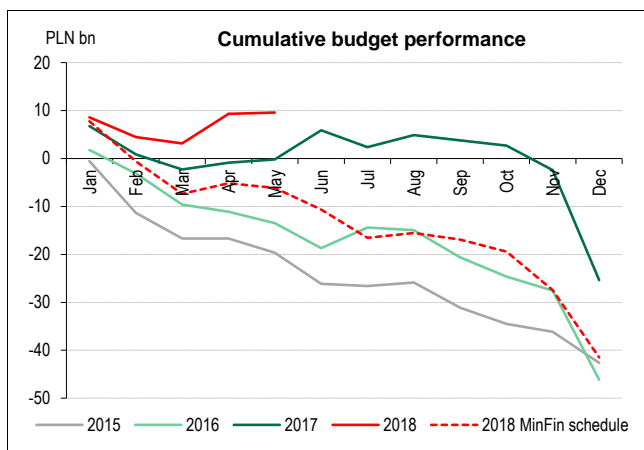
▪ NBP governor Adam Glapiński said during the press conference that in his view the results of the new NBP projection increase the probability of interest rates stabilisation for long. In his view such economic scenario would justify keeping monetary policy on hold even until the end of 2020 (Glapiński made a similar pledge already in May). NBP Governor stressed that it was his private opinion, while other MPC members may have different perspective, which was confirmed immediately by Łukasz Hardt's comment. The latter said that he was not as convinced about no need to change monetary policy next year and that the next decision will be definitely a rate hike, not a cut. But even Hardt, considered one of the most hawkish MPC members, admitted that at this point inflation (and core inflation) remains so low that the central bank does not have to hurry with decisions.

▪ The update of the projections did not provoke important changes in the statement, as if nothing happened. One could say the previous editions of NBP projections were already hinting at consideration of tighter monetary policy, but the unemployment-inflation link evades economic theories (i.e. there is no response of CPI to tight labour market), as Hardt called it. No wonder major central banks are not in a hurry to combat inflation before it is able to reach and stay near/exceed the target, and NBP is not going to outrun them when it comes to monetary policy tightening.

▪ Much attention was paid to the approach and signals from major central banks. In June we learned from the ECB that it plans to deliver the first rate hike in summer 2019 (without being specific if it meant June, July or September). This is an important reference point for the Polish MPC taking into account 'the monetary conditions in the immediate environment of Polish economy'. We do not think a rate hike in the euro zone would be immediately copied by NBP, but with inflation possibly getting up to the target at that time we could see the hawkish camp rise in strength.

▪ Our expectations regarding the monetary policy outlook remain unchanged. We think that the main interest rates will remain unchanged at least until November 2019. The first rate hike is possible at the very end of 2019, in our view, if the economic growth remains decent by then, inflation really exceeds the target with no signs of upward trend coming to an end, and the ECB starts lifting interest rates as well.

Fiscal policy watch



Source: Stats office, Finance Ministry, NBP, BZ WBK.

2018 fiscal position looks great, just do not expect tax cuts

Poland state budget recorded a PLN9.6bn surplus after May vs PLN9.3bn surplus for Jan-Apr period. In May, the positive deviation of the total revenues from the Finance Ministry's plan rose to 5.2%. Although May expenses were slightly above the plan, total spending since the beginning of the year is only 94.7% of the plan. After May, the subsidy for the social security fund was still well below the amount allotted in the same period last year (-33%). Revenues were 7.5% higher than a year ago and expenses stood at a similar level (+0.6% y/y). PIT and CIT revenues rose 16% y/y.

If we assume these trends will continue later in the year, the total 2018 deficit could be well below the PLN41.5bn plan, even below PLN20bn. However, we also assume that some expenses will be accelerated in late 2018 to utilize the fiscal space to spend, the same way as in 2017 (via an amendment that changed spending limits by category, and not the totals), so our full-year estimate of central budget balance sits at cPLN25bn.

Year-to-date inflows from VAT accelerated to c3% in May y/y from 1.1% in April. May alone was quite strong, with about 12% y/y growth of revenues. Year-to-date result is disappointing mostly due to higher VAT returns in January 2018, which amounted to PLN8.9bn versus PLN3.9bn in January 2017. Mind that VAT returns in January 2017 were artificially lowered by the Finance Ministry, which decided to accelerate payments to December 2016. Gross VAT revenues are growing at a healthy rate, 8.1% y/y in March (year-to-date).

Eurostat data on general government net spending showed a surplus of PLN13.0bn in 1Q18 – the best result since comparable data are available (1999) and versus PLN3.7bn in 1Q17. 4Q sum of GG results yields a deficit of 1.2% of GDP – also the lowest level ever. In our view, at the end of the year the deficit will be close to 2017 result (1.7% of GDP) or even lower.

Regardless of the positive fiscal metrics, the Finance Ministry does not plan to lower the base VAT rate back to 22% from 23% in 2019. On the contrary - it introduces next year an extra charge on fuel sales and a 'solidarity tax' (additional PIT rate).

Falling indebtedness

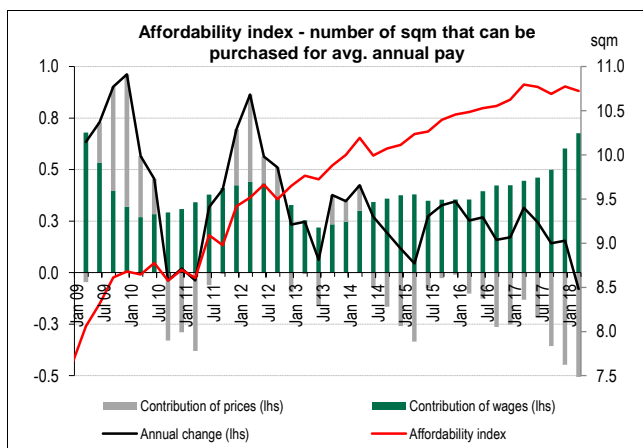
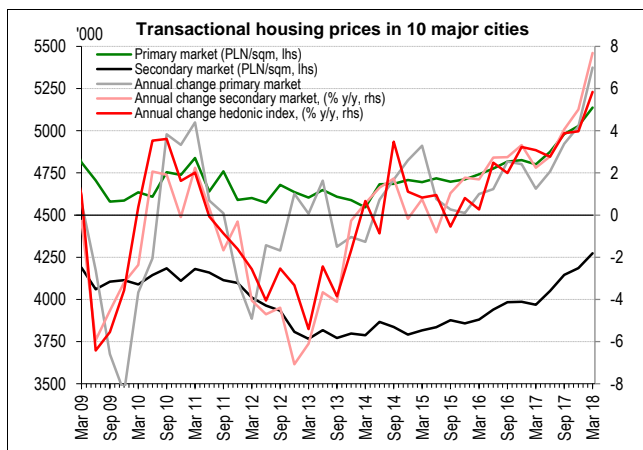
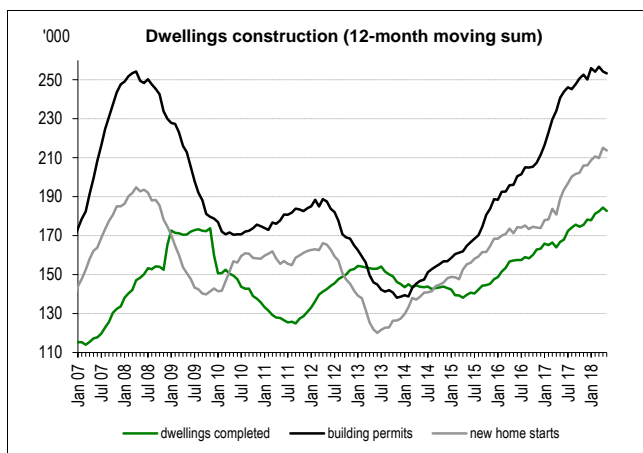
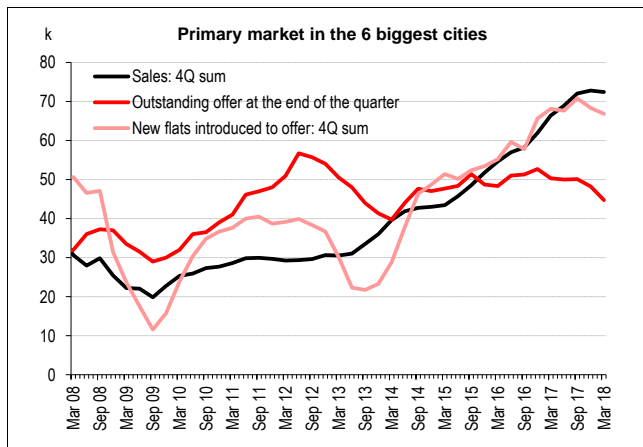
Poland's gross external debt fell to 66.8% of GDP in 1Q18, the lowest since 2011. In annual terms, debt-to-GDP fell by 7.8 percentage points, mostly thanks to strong GDP growth (6.3% y/y in nominal terms) and an almost balanced current account. The government sector contributed most to this decline (-3.3 pp), yet the indebtedness of other sectors, including the central bank, banking sector and debt within capital groups also fell as a percentage of GDP. Net external debt also decreased in 1Q to 29.2% GDP from 31.1% in 1Q17. The relatively high external debt is one of the key obstacles to a sovereign rating upgrade. Fitch said Poland in 2017 was still c18pp above 'A-grade' median with its net external debt-to-GDP. Net international investment position also improved in 1Q18, to -59.2% of GDP from -64.0% of GDP in 1Q17.

New infringement procedure launched against Poland

The European Commission's rule-of-law procedure vs. Poland continues (next hearing of Poland in EU Council likely in September) but it seems a cul-de-sac given the likely veto of Hungary when it comes to sanctions. It looks like the Commission has changed the strategy and now focuses on EU law infringement procedure, with the European Court of Justice, instead of EU politicians, to decide on penalties.

The European Commission informed that it has launched the EU law infringement procedure against Poland, regarding the Polish law on the Supreme Court. The Commission wrote in the statement that given the lack of progress through the Rule of Law dialogue, and the imminent implementation of the new retirement regime for Supreme Court judges, the EC decided to launch the infringement procedure as a matter of urgency and gave Poland one month deadline to

Housing market update



Source: Stats office, Finance Ministry, BZ WBK.

Demand for flats still strong...

According to REAS, rolling 4-quarter sum of primary market sales in 6 biggest cities amounted to 72.4k in 1Q18 and 72.8k in 4Q17 and these were the two best results in history of the survey, i.e. since 2007. On the other hand, 2Q18 pre-sales reported by residential developers fell by 5% y/y. January saw an exhaustion of financial support programme for young people (MdM) and this may have weighed on the demand. At the same time, however, the demand started shifting towards bigger flats (only smaller and cheaper flats were eligible for MdM support). According to the NBP, higher investment demand is the most important factor behind total demand strengthening. In general, demand for housing is supported by positive labour market, low interest rates, high return on rents and inflow of workers from abroad.

...while supply may be starting to stabilise

Supply of flats is historically high, but the last few months seem to point to a slowdown. REAS data on primary market in 6 biggest cities showed that 14.9k new flats were put on the market in 1Q18 as compared to 16.4k new flats in 1Q17. However, the situation is not the same among all cities: Warsaw and Krakow saw total offer going down, while it remained flat or even increased in other cities. Poland stat office's data on total flat supply showed that 12-month rolling sum has stabilised at about 180k for a few months, but this is not enough to state that the trend has changed. The number of building permits, on the other hand has been levelling off for about 6 months. In our view, flat supply will be stagnating or even slowing in the months to come. New construction will be limited by labour constraints in the sector and exhaustion of building space in the biggest cities.

Developers may also face some legislative changes, given ongoing works on two bills: one aimed at making more land available for flat construction (positive for supply) and the other limiting the use of open escrow accounts (negative for liquidity).

Housing prices accelerating markedly

Housing prices accelerated. According to NBP data, in 1Q2018 the primary market transactional prices in 10 biggest cities climbed by 7.0% y/y and secondary market transactional prices in 10 biggest cities rose by 7.7% y/y. Hedonic index (i.e. prices corrected for quality of houses) climbed by 5.8% y/y in 10 biggest cities. Price growths in these three statistics were the highest since 2Q2008. BIS statistics showed the same story: existing flat prices in big and medium cities advanced by 6.6% y/y, the fastest since 1Q08. Momentum of housing prices exceeded wage growth, so the financial availability of flats fell in annual terms for the first time since 2011. Prices are boosted by both strong demand, as well as by rising costs of land, materials and labour.

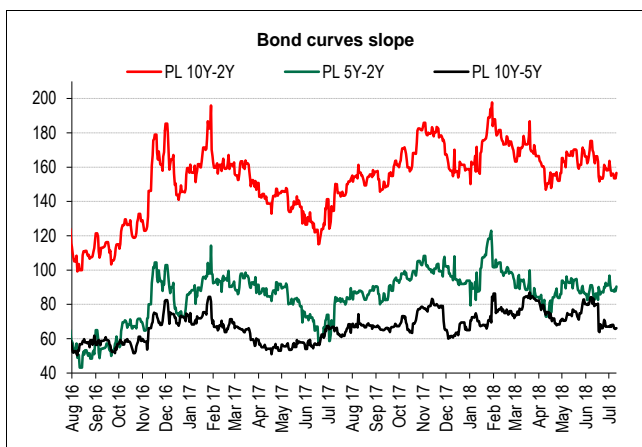
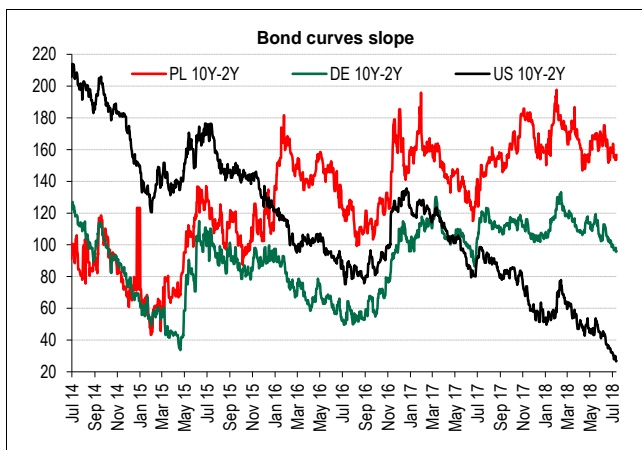
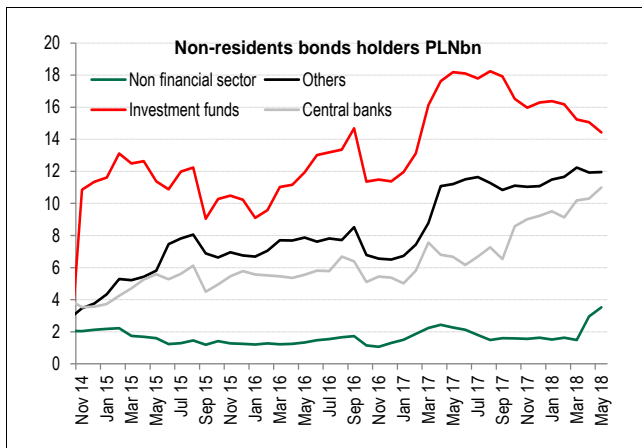
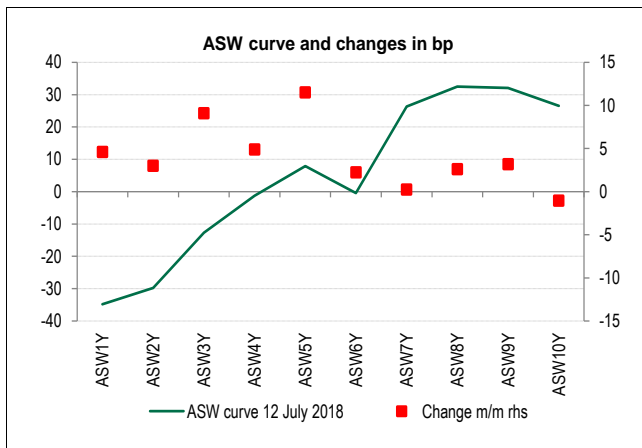
Housing loans grow strongly

Demand for loans remains strong: PLN housing loans origination hit PLN11.9bn in 1Q18, after advancing by 8.9% y/y. In April and May origination rose by 6.0% y/y. Loan margins remain flat at about 260-270bp and banks do not report major changes in their lending policies.

Housing prices to accelerate, but no imbalance seen

To sum up, we are expecting demand for flats to remain strong, driven by positive labour market, amid weakening supply, undermined mostly by high capacity utilisation. This will translate into further acceleration of prices, especially given rising costs of construction works. In the longer run, high investment demand and rising housing prices are likely to drive return on rents down and discourage investors. At the same time, high prices may activate the secondary market sellers, especially these CHF-indebted.

Interest rate market



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

Debt hit by geopolitics

▪ In June, similarly to May, volatility on the market was elevated due to the geopolitical tension related to negotiations on the new global trade deal between the US, China and the EU. Moreover, CEE bonds were affected by crisis in the German governmental coalition as well as changes on the Italian political scene. As a result, yield of domestic debt in the 2Y segment oscillated in a ± 10 bp range and in the 5-10Y segment in a ± 13 bp range. Since the release of June MACROscope, 10Y yield fell by 10bp, while 2-5Y yields went up by 6-7bp. ASW spreads widened by 4bp on the front end of the curve, by 10bp in the middle and narrowed by 2-4bp in the 6-10Y segment. Increase of ASW spreads on the short end was a consequence of short-tenor bonds depreciation amid IRS short rates stabilisation.

Low supply to push yields down

▪ In the next few weeks, we expect yields to decrease as a reaction to the PS0708 bond redemption at the end of the month (cPLN9.5bn principal and cPLN5.2bn coupons) and relatively low supply in July (Ministry of Finance announced a regular auction with PLN4-8bn offer). We believe that the high level of budget liquidity will induce the Ministry to eventually limit its offer to the lower boundary of the announced debt supply. That having said, the results of switch auction conducted on 12 July imply that demand should remain high. It is worth noting that the change of breakdown of non-resident investors base (decreasing share of investment funds, bigger share of central banks) and high demand of Polish banks and other domestic financial investors (insurers and investment funds) should be stabilising for bond prices.

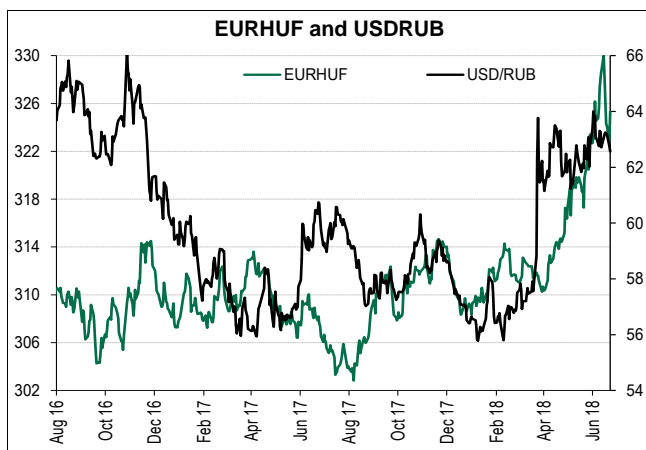
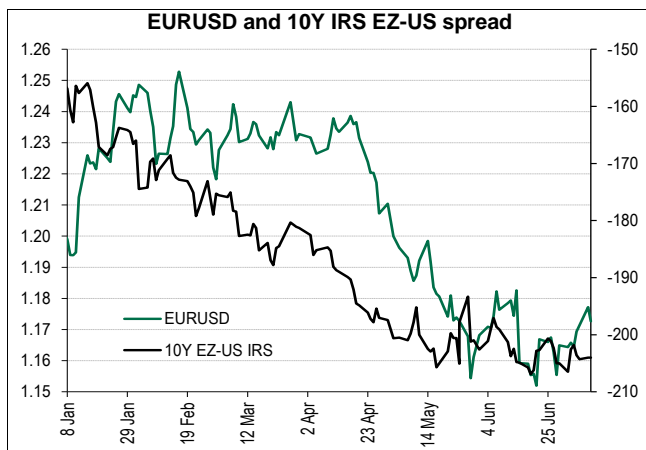
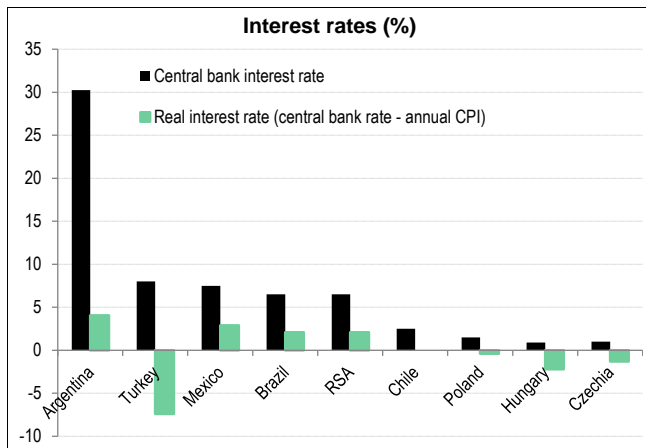
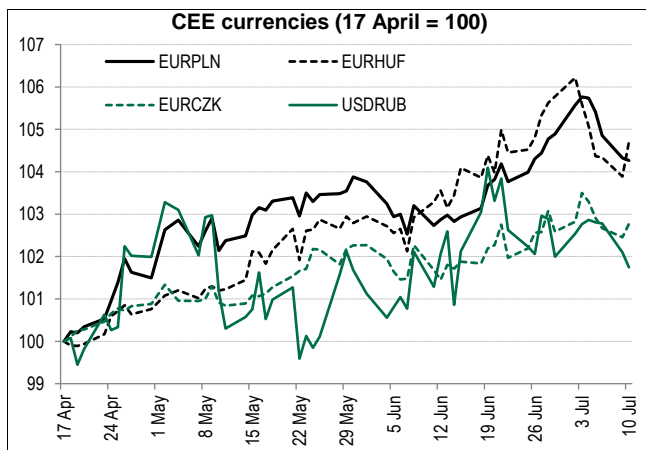
Expected increases of credit risk may elevate yields

▪ At the end of August, we anticipate yields to increase above the current levels. Higher bond supply at the auction in August is likely to push bond prices down. According to the Ministry of Finance, the supply of T-bonds in 3Q18 is expected to amount to PLN10-18 billion. This means that the bulk of 3Q18 supply will be concentrated in August-September. Moreover, we think that at the end of summer markets will start to wager the possibility that European governments will deliver some kind of fiscal stimuli in order to offset the negative impact of escalating trade wars. This will be likely to push bonds up. In our opinion in the extremely low-interest rates environment (no room for further interest rates cut) can translate into increasing of credit risk rather (in the first reaction) than expectations for a deeper monetary stimulation.

Outright auction in July

There is only one regular auction scheduled in July (27th), and the Ministry of Finance is going to offer OK0720, PS0123, WZ0524, WS0428 and WZ0528 worth PLN4-8bn.

Foreign exchange market



Sources: Reuters, Bloomberg, BZ WBK.

Polish zloty – good starting position for recovery

▪ The zloty relief at May/June turn proved only temporary and the next weeks showed Polish currency depreciating sharply amid concerns about the global economic growth (amid next stage of the trade war), dollar appreciation and political tensions in Germany. As a result, EURPLN skyrocketed above 4.40 (its highest since January 2017), USDPLN to 3.80 (last time seen in mid-2017), CHFPLN above 3.80 (highest since July 2017) while GBPPLN stayed below 5.0 seen this year in May.

▪ Since mid-April, when the sell-off on the emerging markets has started, the currencies that underperformed the most (the Argentine peso, South African rand, Brazilian real) were under an additional pressure of their internal issues (political scandals and fears over economic performance). The zloty was the fifth weakest currency and first that has seen some supportive macro data and is not under any serious internal pressure at the moment. Recall that in 2017, the zloty was one of the strongest EM currency and its poor performance so far this year could be partly explained by the fact that it became too expensive versus its EM peers during the previous year. In the mid-April/early July period, half of the main EM currencies lost vs the euro and all of them depreciated vs the dollar.

▪ Obviously, the dollar appreciation observed since mid-April driven largely by mounting expectations for more Fed rate hikes was one of the key factors weighing on the zloty and its EM peers. Looking at the interest rates in main developing countries, we see Poland has one of the lowest interest rates (both in nominal and real terms) that make the zloty more vulnerable during market stress. However, we do not think the dollar appreciation could last in the weeks to come and so we expect the zloty recovery that started in early July to continue in the weeks to come.

▪ Last month we wrote that the PL-DE 10Y bond yield spread at c300bp could attract an inflow of foreign capital on the Polish market. Back then, this provided only temporary support for the zloty. The spread is holding close to 300bp in mid-July and we still view this could be a circumstance that might attract foreign capital leading to stronger currency.

EURUSD could rise slower

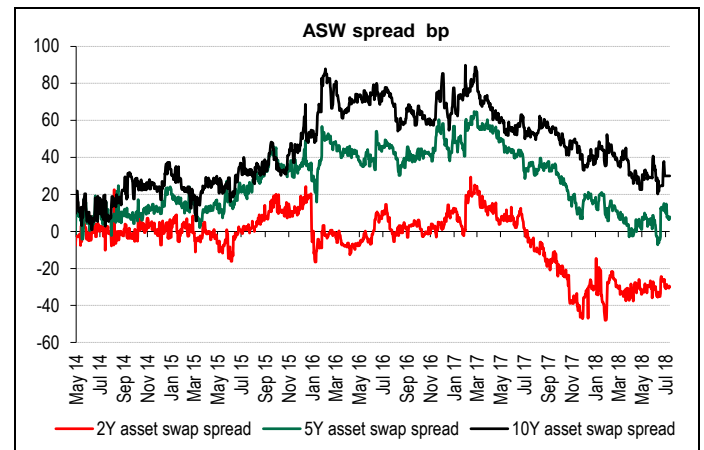
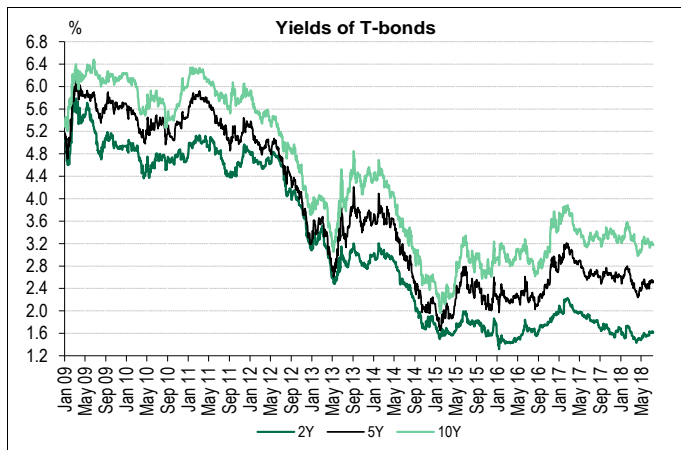
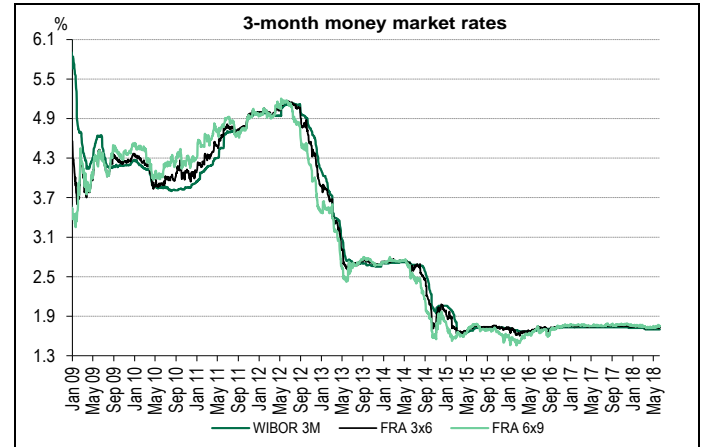
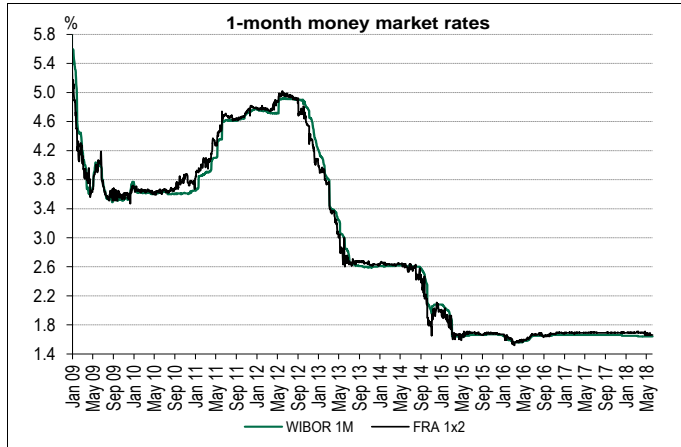
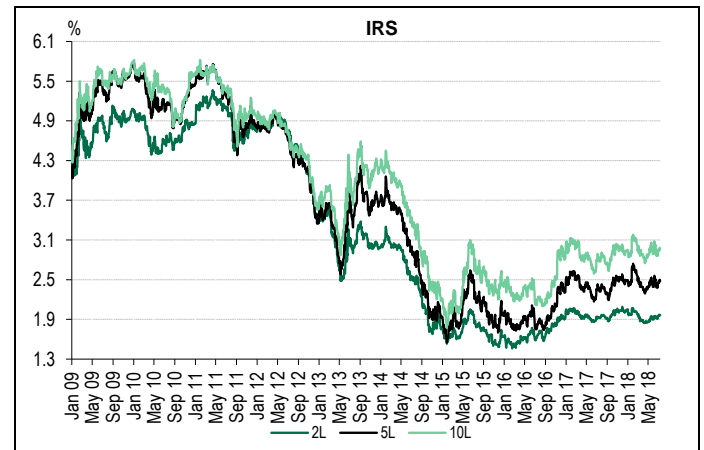
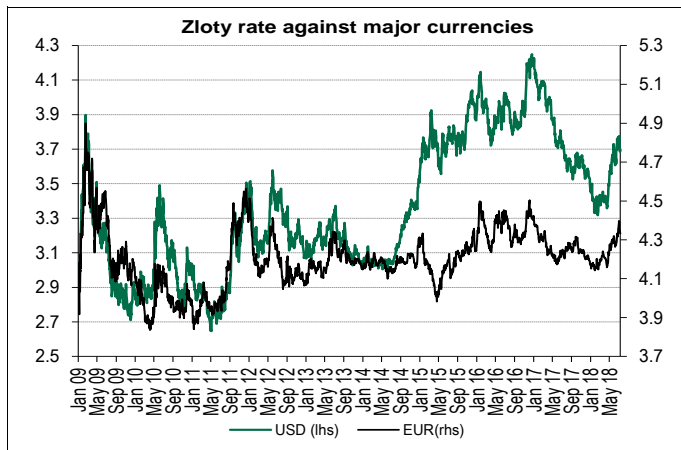
▪ EURUSD stayed low above this year's bottom at 1.15 amid higher demand for safe assets fueled by weaker global economic outlook and thanks to the FOMC adding one more 25bp hike this year (to four in total).

▪ The euro is not recovering at the pace we have expected so far and so now we see slower rise of EURUSD later this year. Story remains the same – the market has largely priced in the coming Fed rate hikes and the ECB confirmed it is on track to normalize the monetary policy in the quarters to come which could provide support for the euro.

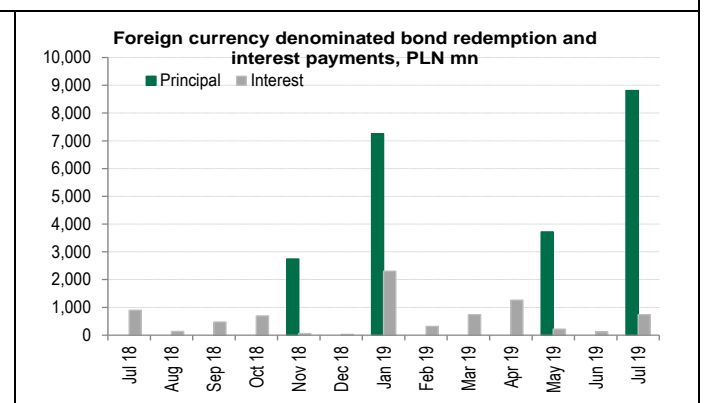
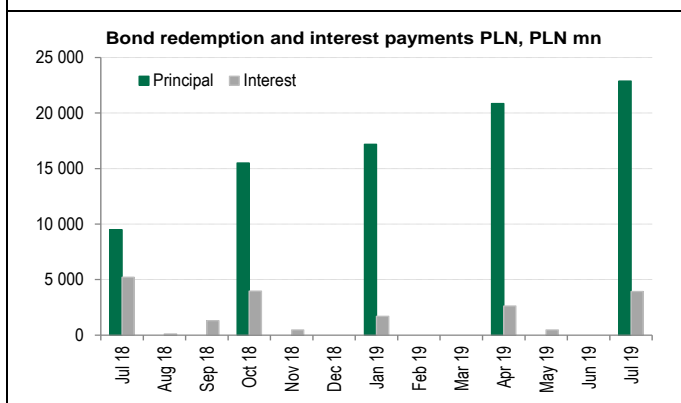
High oil prices support ruble

▪ Last month, the ruble has outperformed its CEE peers thanks to some rebound in oil prices. Koruna depreciated but the hawkish tone of the Czech central bank and the unexpected 25bp rate hike delivered in late June helped to slow EURCZK upside move. The forint was the weakest CEE currency after it reached its weakest level vs the euro ever (EURHUF above 330). The key factor here looks to have been the Hungarian central bank unsuccessful attempt to convince the market that it could shorten the period of its loose monetary policy conditions.

Market monitor



Principal and interest payments



Source: Finance Ministry, Reuters, BZ WBK.

Economic calendar

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
16 July <i>PL: Core inflation (Jun)</i> <i>PL: Balance of payments (May)</i> US: Retail sales (Jun)	17 <i>PL: Wages and employment (Jun)</i> US: Industrial output (Jun)	18 <i>PL: Industrial output (Jun)</i> <i>PL: PPI (Jun)</i> EZ: CPI (Jun) US: House starts (May) US: Fed Beige Book	19 US: Philly Fed index (Jul)	20 <i>PL: Retail sales (Jun)</i>
23 <i>PL: Money supply (Jun)</i> US: Home sales (Jun)	24 <i>PL: Unemployment rate (Jun)</i> DE: Flash PMI – services (Jul) DE: Flash PMI – manufacturing (Jul) EZ: Flash PMI – manufacturing (Jul) EZ: Flash PMI – services (Jul) HU: Central bank decision	25 DE: Ifo index (Jul) US: New home sales (Jun)	26 EZ: ECB decision US: Durable goods orders (Jun)	27 US: Michigan index (Jul) US: Advance GDP (Q2)
30 US: Pending home sales (Jun)	31 <i>PL: Flash CPI (Jul)</i> EZ: Flash CPI (Jul) US: Consumer incomes (Jun) US: Consumer spending (Jun) US: Consumer confidence index (Jul)	1 August <i>PL: PMI – manufacturing (Jul)</i> EZ: PMI – manufacturing (Jul) DE: PMI – manufacturing (Jul) US: ISM – manufacturing (Jul) US: ADP report (Jul) US: FOMC decision	2 CZ: Central bank decision US: Industrial orders (Jun)	3 DE: PMI – services (Jul) EZ: PMI – services (Jul) US: ISM – services (Jul) US: Non-farm payrolls (Jul) US: Unemployment rate (Jul)
6 DE: Industrial orders (Jun) CZ: Industrial output (Jun)	7 DE: Exports (Jun) DE: Industrial output (Jun) HU: Industrial output (Jun)	8 HU: CPI (Jul)	9 CZ: CPI (Jul)	10 US: CPI (Jul)
13 <i>PL: Balance of payments (Jun)</i>	14 <i>PL: CPI (Jul)</i> <i>PL: CZ, HU, EZ: Flash GDP (Q2)</i> EZ: Industrial output (Jun) DE: ZEW index (Aug)	15 US: Retail sales (Jul) US: Industrial output (Jul)	16 <i>PL: Core inflation (Jul)</i> US: House starts (Jun) US: Philly Fed index (Aug)	17 <i>PL: Wages and employment (Jul)</i> EZ: CPI (Jul) US: Flash Michigan (Aug)
20 <i>PL: Industrial output (Jul)</i> <i>PL: PPI (Jul)</i>	21 HU: Central bank decision	22 <i>PL: Retail sales (Jul)</i> US: Home sales (Jul)	23 <i>PL: Money supply (Jul)</i> DE: Flash PMI – services (Aug) DE: Flash PMI – manufacturing (Aug) EZ: Flash PMI – manufacturing (Aug) EZ: Flash PMI – services (Aug) US: New home sales (Jul)	24 <i>PL: Unemployment rate (Jul)</i> US: Durable goods orders (Jul)
27 DE: Ifo index (Aug)	28 US: Consumer confidence index (Aug)	29 US: Preliminary GDP (Q2) US: Pending home sales (Jun)	30 US: Consumer incomes (Jul) US: Consumer spending (Jul)	31 <i>PL: GDP (Q2)</i> <i>PL: CPI (Jul)</i> US: Michigan index (Aug)
3 September <i>PL: PMI – manufacturing (Aug)</i> EZ: PMI – manufacturing (Aug) DE: PMI – manufacturing (Aug)	4 US: ISM – manufacturing (Aug)	5 <i>PL: MPC decision</i> HU: GDP (Q2) DE: PMI – services (Aug) EZ: PMI – services (Aug)	6 DE: Industrial orders (Jul) CZ: Industrial output (Jul) HU: Industrial output (Jul) US: ADP report (Aug) US: ISM – services (Aug)	7 DE: Exports (Jun) DE: Industrial output (Jul) US: Non-farm payrolls (Aug) US: Unemployment rate (Aug)
10 CZ: CPI (Aug)	11 DE: ZEW index (Sep) HU: CPI (Jul)	12 EZ: Industrial output (Jul)	13 <i>PL: CPI (Aug)</i> US: CPI (Jun) EZ: ECB decision	14 <i>PL: Rating review by Moody's</i> <i>PL: Core inflation (Aug)</i> US: Retail sales (Aug) US: Industrial output (Aug) US: Flash Michigan (Sep)

Source: GUS, NBP, Bloomberg.

Economic data and forecasts for Poland

Monthly economic indicators

		Jun 17	Jul 17	Aug 17	Sep 17	Oct 17	Nov 17	Dec 17	Jan 18	Feb 18	Mar 18	Apr 18	May 18	Jun 18E	Jul 18E
PMI	pts	53.1	52.3	52.5	53.7	53.4	54.2	55.0	54.6	53.7	53.7	53.9	53.3	54.2	54.0
Industrial production	% y/y	4.4	6.2	8.8	4.4	12.3	9.2	2.8	8.7	7.3	1.6	9.3	5.4	7.0	13.4
Construction production	% y/y	11.6	19.8	23.6	15.3	20.2	19.9	12.8	34.7	31.3	16.1	19.7	20.8	19.5	15.4
Retail sales ^a	% y/y	6.0	7.1	7.6	8.6	8.0	10.2	6.0	8.2	7.9	9.2	4.6	7.6	9.1	11.1
Unemployment rate	%	7.0	7.0	7.0	6.8	6.6	6.5	6.6	6.9	6.8	6.6	6.3	6.1	5.9	5.9
Gross wages in corporate sector	% y/y	6.0	4.9	6.6	6.0	7.4	6.5	7.3	7.3	6.8	6.7	7.8	7.0	7.7	8.6
Employment in corporate sector	% y/y	4.3	4.5	4.6	4.5	4.4	4.5	4.6	3.8	3.7	3.7	3.7	3.7	3.6	3.3
Exports (€)	% y/y	7.2	15.0	13.4	11.5	15.8	15.5	2.6	12.1	5.9	-1.6	8.6	2.1	7.4	13.5
Imports (€)	% y/y	14.3	14.6	8.7	8.9	15.4	15.9	10.9	16.7	8.1	1.4	9.9	3.3	9.4	19.4
Trade balance	EUR mn	-202	-136	288	479	284	208	-1,175	-164	-520	-205	314	-272	-554	-1,075
Current account balance	EUR mn	-902	-296	311	218	206	54	-847	1,955	-782	-785	-21	-563	-1,472	-1,325
Current account balance	% GDP	-0.4	-0.2	0.0	0.3	0.3	0.3	0.2	0.0	-0.1	-0.2	-0.2	-0.3	-0.4	-0.7
Budget balance (cumulative)	PLN bn	5.9	2.4	4.9	3.8	2.7	-2.4	-25.4	8.6	4.5	3.1	9.3	9.6	5.2	1.5
Budget balance (cumulative)	% of FY plan	-9.9	-4.0	-8.2	-6.4	-4.5	4.1	42.7	-20.6	-10.8	-7.5	-22.5	-23.1	-12.4	-3.7
CPI	% y/y	1.5	1.7	1.8	2.2	2.1	2.5	2.1	1.9	1.4	1.3	1.6	1.7	1.9	2.0
CPI excluding food and energy	% y/y	0.8	0.8	0.7	1.0	0.8	0.9	0.9	1.0	0.8	0.7	0.6	0.5	0.5	0.7
PPI	% y/y	1.8	2.2	3.0	3.2	3.0	1.8	0.3	0.2	-0.1	0.5	1.0	2.8	3.5	3.7
Broad money (M3)	% y/y	5.0	5.0	5.4	5.4	5.7	4.5	4.6	4.8	4.9	5.8	5.7	6.6	7.3	7.7
Deposits	% y/y	4.5	4.6	5.0	5.0	5.3	4.2	4.1	4.5	4.6	5.1	5.1	6.0	6.4	6.4
Loans	% y/y	4.5	4.5	5.0	5.1	4.7	3.7	3.6	4.0	4.2	4.3	3.9	5.5	5.9	6.2
EUR/PLN	PLN	4.21	4.24	4.26	4.27	4.26	4.23	4.20	4.16	4.16	4.21	4.19	4.28	4.30	4.35
USD/PLN	PLN	3.75	3.68	3.61	3.59	3.63	3.60	3.55	3.41	3.37	3.41	3.42	3.63	3.69	3.72
CHF/PLN	PLN	3.87	3.83	3.74	3.73	3.69	3.63	3.60	3.55	3.61	3.60	3.53	3.64	3.73	3.75
Reference rate ^b	%	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50
3M WIBOR	%	1.73	1.73	1.73	1.73	1.73	1.73	1.72	1.72	1.72	1.71	1.70	1.70	1.70	1.70
Yield on 2-year T-bonds	%	1.94	1.89	1.80	1.73	1.71	1.60	1.69	1.62	1.73	1.56	1.52	1.57	1.60	1.62
Yield on 5-year T-bonds	%	2.62	2.67	2.67	2.61	2.69	2.62	2.64	2.63	2.73	2.46	2.33	2.49	2.48	2.53
Yield on 10-year T-bonds	%	3.21	3.32	3.35	3.27	3.39	3.40	3.29	3.34	3.51	3.27	3.08	3.23	3.23	3.17

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

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

Quarterly and annual economic indicators

		2016	2017	2018E	2019E	1Q18	2Q18E	3Q18E	4Q18E	1Q19E	2Q19E	3Q19E	4Q19E
GDP	PLN bn	1,858.5	1,982.1	2,097.1	2,213.9	485.4	508.3	516.5	586.9	510.7	536.5	545.3	621.3
GDP	% y/y	3.0	4.6	4.6	3.7	5.2	4.9	4.5	4.0	3.8	3.8	3.6	3.5
Domestic demand	% y/y	2.2	4.7	5.5	4.0	6.8	5.4	5.1	4.8	3.9	4.1	3.9	4.1
Private consumption	% y/y	3.9	4.8	4.9	4.5	4.8	5.0	5.0	5.0	4.8	4.6	4.4	4.2
Fixed investments	% y/y	-8.2	3.4	6.4	4.0	8.1	7.9	6.4	4.9	4.0	4.0	4.0	4.0
Industrial production	% y/y	2.9	6.5	6.6	5.0	5.6	7.2	8.5	5.3	5.6	5.8	5.0	3.9
Construction production	% y/y	-14.5	13.7	15.3	1.4	25.6	20.0	14.1	8.5	0.8	2.2	0.4	2.0
Retail sales ^a	% y/y	3.9	8.2	7.9	6.2	8.4	7.0	9.8	6.7	4.3	7.1	6.0	7.2
Unemployment rate ^b	%	8.2	6.6	5.9	5.5	6.6	5.9	5.8	5.9	5.9	5.4	5.3	5.5
Gross wages in the national economy ^a	% y/y	3.8	5.7	7.6	8.2	6.2	7.0	7.4	8.9	9.0	8.4	8.0	8.3
Employment in the national economy	% y/y	2.3	3.7	2.8	1.0	2.8	2.7	2.4	2.3	1.3	1.0	0.9	0.6
Exports (€)	% y/y	3.1	12.0	5.6	3.3	5.1	6.0	7.0	4.4	4.7	4.4	3.5	0.6
Imports (€)	% y/y	2.7	13.4	8.3	4.8	8.3	7.5	10.3	7.3	6.2	5.8	5.1	2.2
Trade balance	EUR mn	2,935	821	-4,554	-7,930	-888	-512	-929	-2,226	-1,725	-1,287	-1,780	-3,138
Current account balance	EUR mn	-1,254	896	-4,017	-6,999	378	-2,057	-1,594	-744	-306	-2,750	-2,396	-1,547
Current account balance	% GDP	-0.3	0.2	-0.8	-1.4	-0.2	-0.4	-0.8	-0.8	-0.9	-1.1	-1.2	-1.4
General government balance	% GDP	-2.3	-1.7	-1.7	-2.0	-	-	-	-	-	-	-	-
CPI	% y/y	-0.6	2.0	1.7	2.2	1.5	1.7	1.9	1.5	1.9	2.2	2.3	2.5
CPI ^b	% y/y	0.8	2.1	1.6	2.5	1.3	1.9	1.7	1.6	2.2	2.3	2.3	2.5
CPI excluding food and energy	% y/y	-0.2	0.7	0.9	2.1	0.8	0.5	0.9	1.3	1.5	1.9	2.3	2.5
PPI	% y/y	-0.2	2.9	2.0	2.5	0.2	2.4	3.1	2.3	2.7	2.1	2.2	3.2
Broad money (M3) ^b	% y/y	9.6	4.6	7.3	7.4	5.3	6.0	6.6	7.3	7.3	7.3	7.3	7.4
Deposits ^b	% y/y	9.1	4.1	7.1	7.4	4.9	5.6	6.4	7.1	7.2	7.3	7.3	7.4
Loans ^b	% y/y	4.7	3.6	7.9	6.5	4.7	5.8	6.9	7.9	7.6	7.2	6.8	6.5
EUR/PLN	PLN	4.36	4.26	4.25	4.29	4.18	4.26	4.31	4.26	4.27	4.29	4.30	4.31
USD/PLN	PLN	3.95	3.78	3.55	3.46	3.40	3.58	3.66	3.55	3.50	3.47	3.45	3.44
CHF/PLN	PLN	4.00	3.84	3.62	3.48	3.59	3.63	3.69	3.58	3.50	3.49	3.47	3.45
Reference rate ^b	%	1.50	1.50	1.50	1.75	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.75
3M WIBOR	%	1.70	1.73	1.70	1.76	1.72	1.70	1.70	1.70	1.70	1.70	1.72	1.91
Yield on 2-year T-bonds	%	1.66	1.89	1.60	1.71	1.64	1.57	1.62	1.58	1.56	1.61	1.79	1.89
Yield on 5-year T-bonds	%	2.37	2.78	2.52	2.44	2.61	2.43	2.51	2.53	2.59	2.60	2.50	2.52
Yield on 10-year T-bonds	%	3.05	3.44	3.26	3.41	3.37	3.18	3.21	3.26	3.33	3.41	3.43	3.46

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

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