RATES AND FX OUTLOOK

POLISH FINANCIAL MARKETS

September 2015

Bank Zachodni WBK

Grupa Santander

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Summary

- Even though 2Q GDP growth proved to be slightly lower than expected (slowing to 3.3%YoY from 3.6% in 1Q), we still believe that underlying trends remain robust and Polish economy will accelerate in 2H15E, although probably not as much as we previously anticipated. Private consumption growth should remain robust, supported by falling unemployment and rising labour income, and export growth may even accelerate, fuelled by economic revival in the euro zone. However, investment growth is not likely to re-accelerate significantly. **Poland's GDP growth in 2015E should be probably closer to 3.5% than 4.0%, but our forecast for 2016E at 3.5% is still realistic.**
- Poland has been affected by the worst drought in many years, which is likely to reduce crops and push up food prices. However, we estimate that the overall effect on inflation should be limited. First of all, an increase of food prices should be tamed by higher imports (mind that global food prices are at multi-year lows). Secondly, the impact of more expensive food on CPI should be partly offset by less expensive fuels (prices at the pump fell c2.5% in August, and may drop even 4% in September, according to our estimate) and a cut in gas tariffs in September. **Thus, our CPI forecast for December goes up only slightly to c0.7%YoY, and we still think inflation should head towards 2%YoY in 2016E.**
- Monetary policy in Poland should remain dull in the coming months, in our view, as the Monetary Policy Council is highly likely to keep interest rates unchanged until the end of its term of office (ie, until the start of 2016). Much more interesting is the outlook for 2016**. We drop the assumption of interest rate hike at the end of 2016E**, mainly due to increased uncertainty about global economic outlook (with possible lower GDP growth and inflation worldwide next year). The second reason is the high likelihood that the next MPC could consist of very dovish members. **Nevertheless, we still argue there should be no need for monetary policy easing in 2016E**, given predicted robust economic growth in Poland, inflation rate converging towards the official target, and probably some shift towards less restrictive fiscal policy after elections.
- **We believe that September Fed rate hike (which is still our baseline scenario) could trigger a wave of yield increases throughout global fixed income markets, as it is not currently priced-in.** Also, the scope for more accommodative fiscal and monetary policies in Poland after the elections should support steeper domestic yield curve.
- **The impact of Fed's lift-off on the zloty seems less straightforward, as if the market interprets it as a sign of trust in the economic recovery, the PLN may even gain.** Before that happens, we see several risk factors that may keep risk aversion elevated: the situation in China, upcoming early elections in Greece, and political uncertainty in Poland ahead of general elections in October.

Short- and Medium-Term Strategy: Interest Rate Market

	Change (bp)		Current Level	Expected Trend	
	Last 3M	Last 1M	31 August 2015	1M	3M
Reference rate	0	0	**1.50**	→	→
3M WIBOR	4	0	**1.72**	→	→
2Y bond yield	4	0	**1.79**	→	→
5Y bond yield	2	0	**2.46**	→	↗
10Y bond yield	0	0	**2.93**	↗	↗↗
2/10Y curve slope	-3	0	**114**	↗	↗↗

Note: Single arrow down/up indicates at least a 5bp expected move down/up, double arrow means at least a 15bp move. Source: BZ WBK.

PLN rates: our view and risk factors

Money market: After lower-than-expected domestic data and market turmoil in China, the first rate hike in Poland has been postponed further in the market's view. We also dropped the assumption about possible interest rate hike in 4Q16E, but we believe there should be no reason for monetary easing next year, amid healthy growth and inflation trending up. WIBORs should remain stable in the nearest month, but FRA rates may inch up in case of Fed interest rate hike in September.

Short end: The impact of drought on inflation should be limited, in our view, by higher food imports, as well as declining fuel prices and a cut in gas tariffs. Thus, the short-end of the yield curve may be stabilised by low inflation expectations and some investors' hopes for rate cuts in 2016.

Long end: In our opinion, that September Fed rate hike (which is still our baseline scenario) would trigger a wave of yields increase throughout global fixed income markets, as it is not currently priced-in. A start of policy normalisation should reduce market concerns about world economic outlook, leading to bear steepener in yield curves. A scope for more accommodative fiscal and monetary policies in Poland after the elections should also support steeper domestic yield curve.

Risks to our view: If Fed leaves rates unchanged in September, global fixed income markets should strengthen. It should affect also the Polish market, although we see a risk of Polish bonds underperforming core markets in such scenario, as such decision could spur concerns about the global growth and lead to higher risk aversion.

Short- and Medium-Term Strategy: FX Market

	Change (%)		Current Level	Expected trend	
	Last 3M	Last 1M	31 August 2015	1M	3M
EURPLN	2.5	2.1	**4.23**	→	↘
USDPLN	0.3	-0.4	**3.78**	↘	↘↘
CHFPLN	-1.7	-0.3	**3.92**	→	↘
GBPPLN	1.2	-1.2	**5.83**	↘	↘
EURUSD	2.2	2.5	**1.12**	→	↗

Note: Single arrow down/up indicates at least a 1.5% expected move down/up, double arrow means at least a 5% move. Source: BZ WBK.

PLN FX Market: Our view and risk factors

EUR: We see several risk factors that may keep risk aversion elevated in the nearest weeks, preventing EUR/PLN from falling: the situation in China, upcoming early elections in Greece, political uncertainty in Poland ahead of general elections in October. The proposal of FX loans conversion has been losing importance, as in our view the risk of bill weighing strongly on banks' situation is decreasing. Some PLN strengthening is possible at the end of the month, in our view, if the Fed's rate hike is interpreted as a sign of trust in economic recovery.

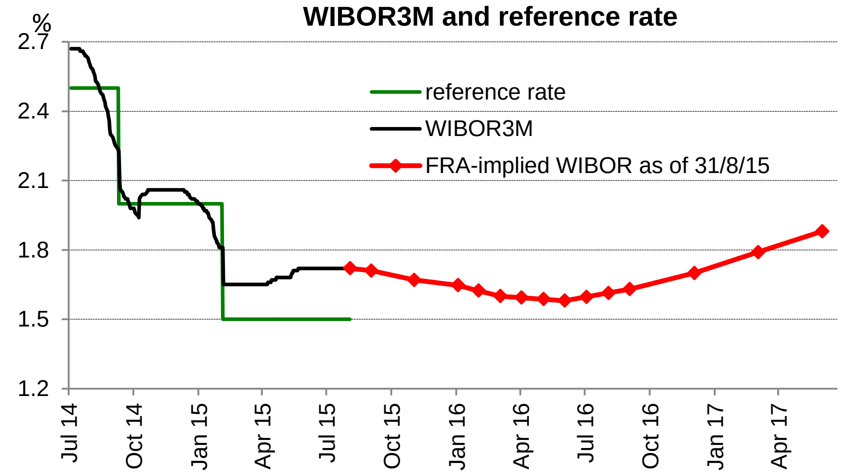
USD: We still expect EUR/USD to go up from current levels, which should justify a stronger zloty against dollar. The Fed rate hike, still possible in 2H15E, should provide USD support, but the prospect of future hikes being only gradual may question the sustainability of any dollar gains. Furthermore, the market is once again "excessively" long the USD, which should imply less of an appetite to bid the USD higher.

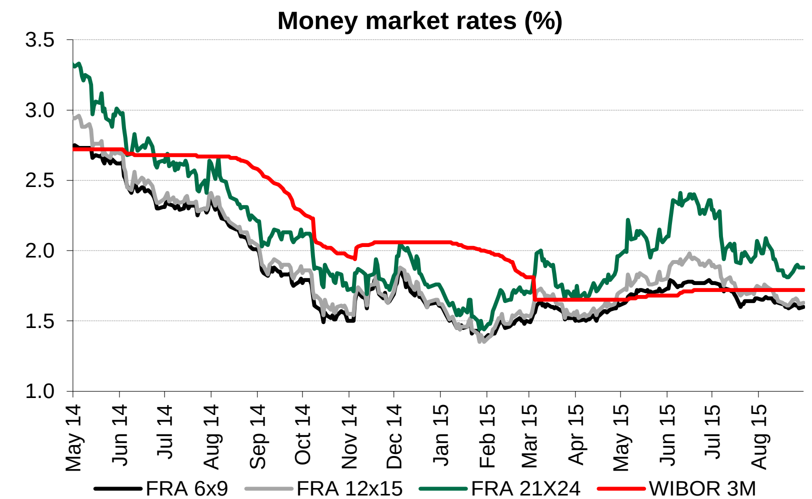
CHF: The recent rise in EUR/CHF could partly reverse in short term amid a possible "safe-haven" bid due to concerns over China. However, we are still negative on CHF vs. EUR, which should allow for zloty strengthening against the Swiss franc in the medium run.

Risks to our view: The turmoil in China, even though stabilised at the end of August, may still deepen, which could fuel risk aversion, hurting the zloty. CEE currencies proved to be more immune to this factor than other EM assets, but some effect is still possible. Paradoxically, if Fed keeps interest rates on hold in September, it could be negative for PLN as investors may treat it as a sign of its deep concern about world economic outlook.

Domestic Money Market: Pricing-in Rate Cuts in Six Months

- Several below-consensus Polish economic activity data and worries about global economic outlook pushed FRA rates further down in August. FRAs fell by 2-20 bp across the curve in monthly basis, with the long matured rates dropping the most. As a result, in the market's view, the first rate hike in Poland has been postponed further. Currently, the market sees c50% odds for a restart of the monetary easing cycle in the next six months. At the same time, it assigns a c65% probability for a rate hike (by 25 bp) in 21 months.
- We decided to postpone further the start of monetary tightening cycle for 2017E, after weaker-than-expected macro data and rising uncertainty about world economic outlook. We expect Poland's economy to continue with healthy growth and inflation rates to trend gradually up in months to come, therefore, there is no reason to restart the monetary easing next year. Thus, we expect WIBORs to remain more or less stable in the coming months, with a gradual increase at the turn of 2015E-16E. FRA rates may inch up in case of Fed interest rate hike in September, following IRS and bond markets.
- Lack of rate hike at the nearest FOMC meeting would strengthen market speculation about possible global economic slowdown and possible monetary easing in Poland. In such scenario, money market rates should decrease at the end of the month.





Source: Reuters, BZ WBK

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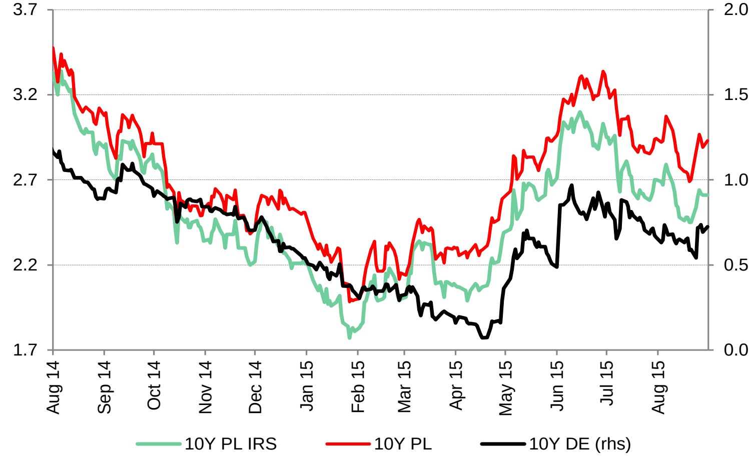
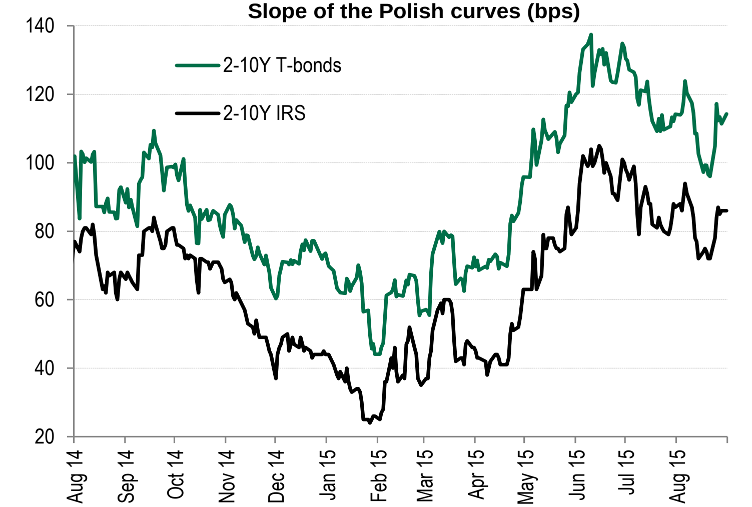
Domestic IRS and the T-Bond Market: Fed Decision Will Be Crucial

- August has been a pretty volatile month in the Polish FI market. First, yields and IRS were falling on the back of the fading odds for the Fed rate hike in September amid worries over the impact that China could have on the global economic growth. Also, the decline was fuelled by the below-consensus Polish economic activity data. However, when the risk aversion rose sharply later in the month, investors' retreat towards safe assets hit the Polish market. Yield of the 10Y benchmark rebounded from the c2.70% support (May's low) and surged back towards 3%. August monthly peak-low spread was 20-25bp for mid- and long-term IRS and bonds.
- We believe that September Fed rate hike (which is still our baseline scenario) could trigger a wave of yields increase throughout global fixed income markets. First of all, because investors started betting for later monetary tightening after recent turmoil in China. Secondly, because the lift-off in September would be a vote of confidence on the strength of US economy and thus may reduce investors' worries about world economic outlook. Still, already in June the Fed's "dot chart" showed lower rates path than in March, and given the recent market turmoil the updated forecasts could go even further down. Should the Fed's statement cool market expectations for the next hikes, the initial market reaction could be muted.
- If Fed leaves rates unchanged in September, global fixed income markets should strengthen. It should affect also the Polish market, although we see a risk of Polish bonds underperforming core markets in such scenario, as such decision could spur concerns about the global growth and an elevated risk aversion could hit Polish assets just like it did in late August.

Yields of Polish and German 10Y Bonds and Polish 10Y IRS (%)



Slope of the Polish curves (bps)

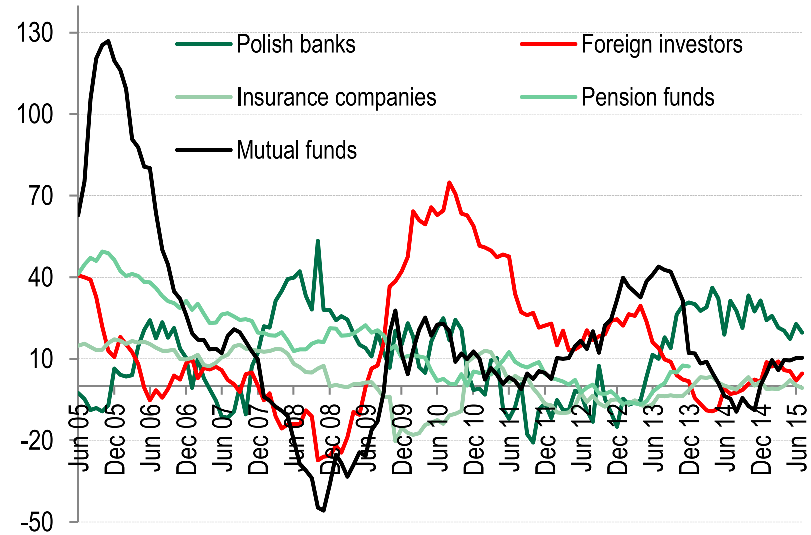


Source: Reuters, Bloomberg, BZ WBK.

Demand Corner: Foreign Investors Still On The Buy Side

- July was the third consecutive month when the foreigners were buying Polish marketable PLN-denominated bonds. At the end of July they held debt worth almost PLN205bn (the highest stock since May 2013), i.e. over PLN1.2bn more than at the end of June.
- Major purchases were made by foreign insurance companies (PLN718m) and pension funds (PLN509m), while foreign banks and investment funds sold Polish debt for PLN642mn and PLN622mn, respectively. As regards geographical breakdown, institutions from Euro zone countries sold Polish bonds worth over PLN1.0bn, and investors from North America purchased similar amount.
- In July the nonresidents accumulated nearly PLN2.5bn of 5Y benchmark PS0420 and held nearly PLN8.8 (38% of the total outstanding) of this bond. They increased holdings also in the 10Y benchmark DS0725 by PLN1.8bn (to PLN17.5bn, 70% of the total outstanding). At the same time, they sold PLN1bn of PS0718.
- Polish banks sold debt worth PLN1.3bn and it was their first reduction since April, and the biggest since June 2014.
- Polish banks purchased PLN1.2bn of PS0417 and they held 35% of this bond outstanding at the end of July.

Annual % change in investors' holdings



Source: Finance Ministry, BZ WBK.

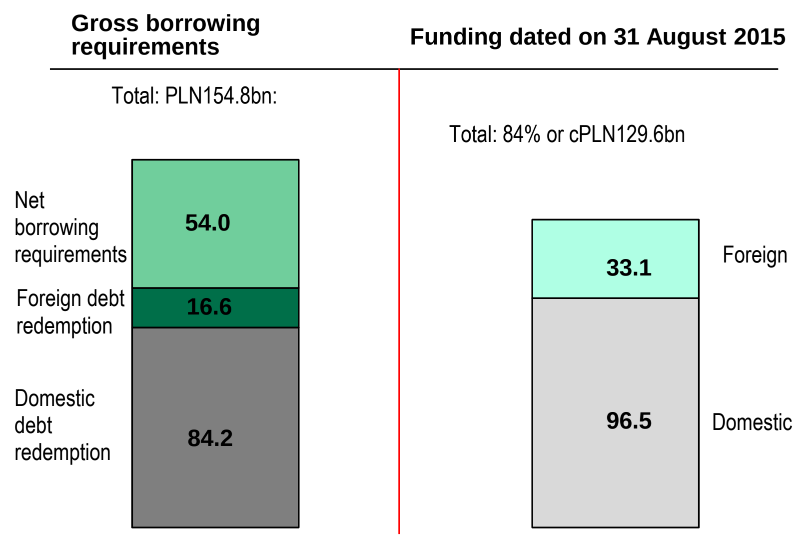
Supply Corner: Increase in Primary Activity After The Summer Lull

- August's auction attracted a healthy demand for T-bonds offered on the primary market. Poland's Ministry of Finance successfully launched long-matured T-bonds at its August auction, selling the 10Y DS0725 benchmark and new WZ0126 floaters worth cPLN4.66bn in total (both at the regular and top-up auctions). The DS0725 yield stood at 3.076%, roughly the same as on the secondary market. The recorded demand amounted to over PLN6.7bn and we believe that domestic investors preferred the WZ0126 (floater), while the non-residents bid for the fixed-rate DS0725. According to our estimates, 84% of this year's gross borrowing needs are now covered at the end of August.

- The Ministry of Finance speeds up its activity on the primary market in September after the summer lull. They will offer T-bonds up to PLN10bn at two regular auctions, including floaters WZ0126 and a new fixed-rate 10Y benchmark DS0726 worth PLN2-4bn at the first auction this month (10 Sep).

- In our view, the supply of Poland's local bonds in September is reasonable and we expect the offered bond to attract a healthy demand from both domestic and foreign investors. In our view, the value of sale should be close to maximum level of the offer, therefore at the end of September this year's gross borrowing needs should be financed in c90% and it is very likely to end funding of the 2015 target at the end of October.

Gross borrowing requirements and financing in 2015



Auction plan for September 2015

Auction date	Settlement date	Series	Planned offer (PLN mn)
10 Sep 2015	14 Sep 2015	DS0726/WZ0126	2,000 – 4,000
24 Sep 2015	28 Sep 2015	To be announced	2,000 – 6,000

Source: Finance Ministry, BZ WBK.

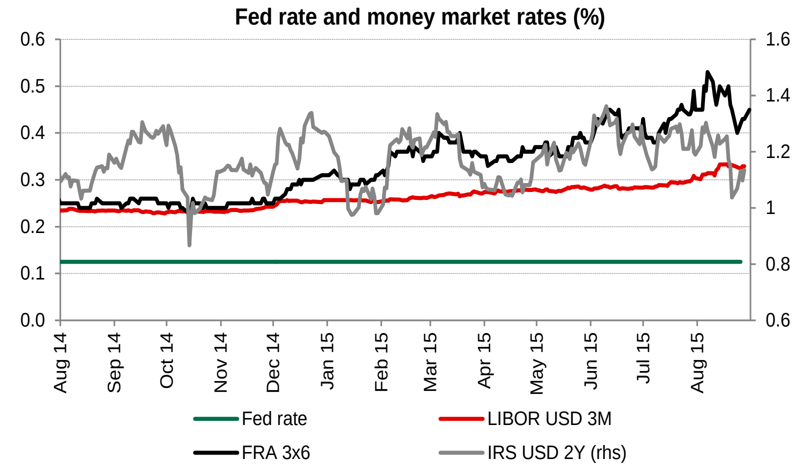
International Money Market and IRS: China, Inflation Outlook and Fed are Crucial in The Short Term

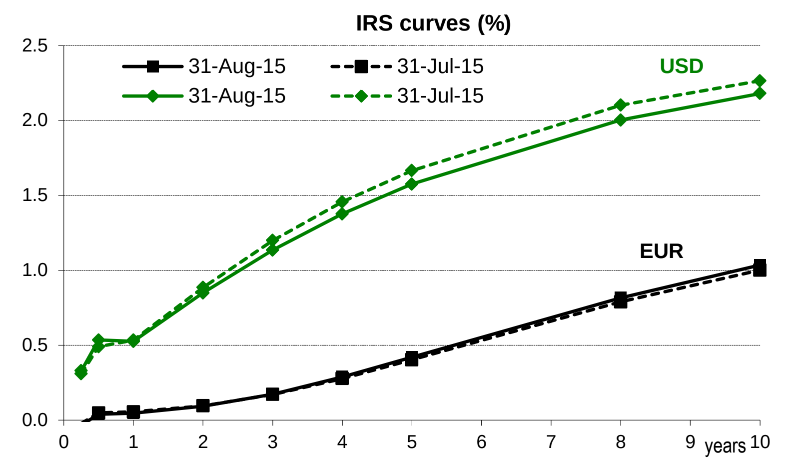
- EURIBOR rates maintained the down trend while the LIBOR USD continued the upside move amid outlook for a divergent monetary policies in the euro zone and the US. What is more, lower crude oil prices renewed expectations that inflation rate would stay far below the central bank's target for a prolonged period. As a consequence the ECB faced a rising pressure to increase the asset purchase programme.

- At the same time, the USD IRS curve moved noticeably down in late August on the back of the concerns over the global growth. The 2Y, 5Y and 10Y IRS fell to its lowest since late April, to 0.77% 1.45% and 2.05%, respectively. EUR IRS rates were more volatile during August – rates increased at the end of the month, while in mid-August rates reached their lowest levels since June.

- In our view, it is still too early for the ECB to change its monetary conditions, including QE programme in upcoming months despite both headline and core inflation staying far away from the ECB's target of 2%. This could likely put more downward pressure on EUR money market rates. On the other hand, USD money market rates could inch up as rate hike by Fed in September is still possible. As a consequence EUR-USD spread could continue to widen.

- Macro developments in both the US and the Euro zone continue to be robust and point to continued recovery. Therefore, we expect EUR and USD IRS rates to increase in the medium to long term. However, signals of the very weak development in China and fears of a hard landing could limit upward pressure of IRS rates increase, in particular if Fed moves the start of monetary tightening till the turn of 2015-16.

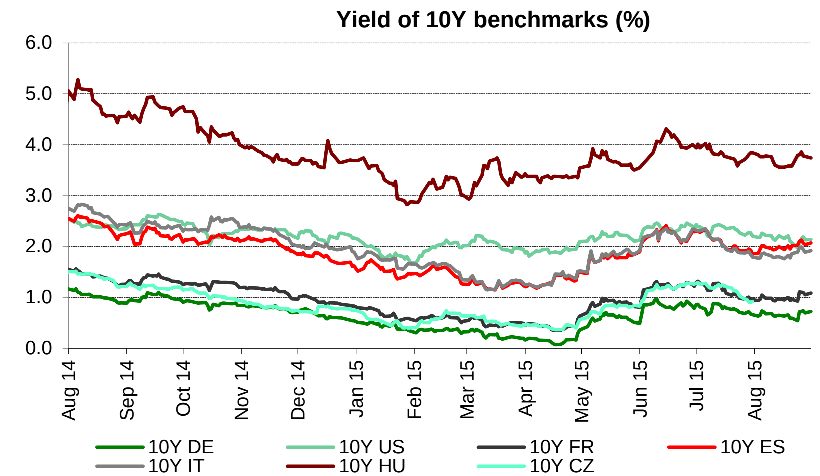


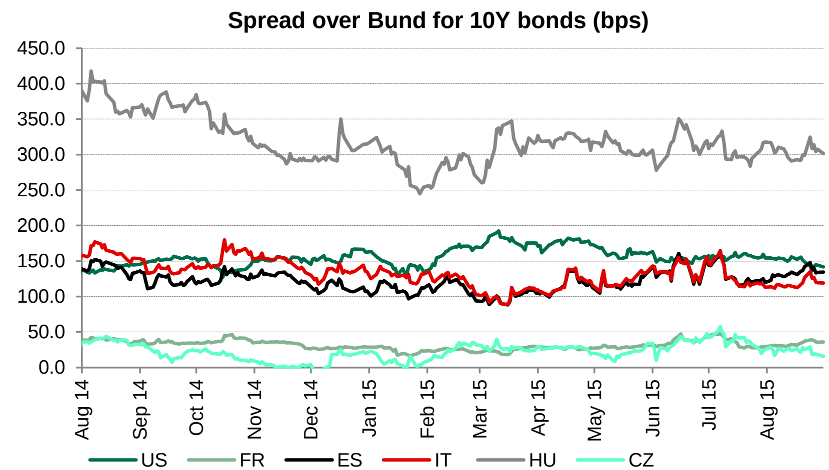


Source: Reuters, ECB, Fed, BZ WBK.

International Bond Market: Central Bank Meetings in the Centre Stage

- August brought high volatility on both the European and US bond markets due to, among others, uncertainty regarding Fed's policy. Yields on core market initially decline (with the 10Y UST temporarily reaching 2.07% and the 2Y Bunds falling to a record low of -0.29%) as the risk of interest rate hikes by the Fed in September lowered due to expected lack of inflation pressure and fears about global growth prospects amid signals of deteriorating economic and market conditions in China. The second half of the month brought some profit taking and yields increased quite visibly, exceeding levels at the end of July, with the 10Y Bund rising again above 0.70%.
- Peripheral Euro zone debt gained visibly as the Greek parliament approved a bailout. Yields of peripheral debt declined towards multi-month lows. However, it was only short-lived rebound as yields moved up due to higher risk aversion. On monthly basis, peripheral countries' yields rose by between 13bp (for Italy) and 23bp (for Portugal) and the spread over Bunds widened gradually, in particular for Portugal (it reached temporarily 215bp, the highest level since mid-July). In contrast, Greek and CEE debt strengthened moderately.
- This month investors are likely to focus on macroeconomic data in Europe and the US and central bank meetings. In the short term, yields on both sides on the Atlantic could decline gradually as inflation rates (both headline and core) in the euro zone and the US are running below targets and news flow from China confirming weak development in economy should shift capital towards lower risky assets. But long-term scenario for core debt remains unchanged. We still see the risk of the curve steepening and higher yields by year end.



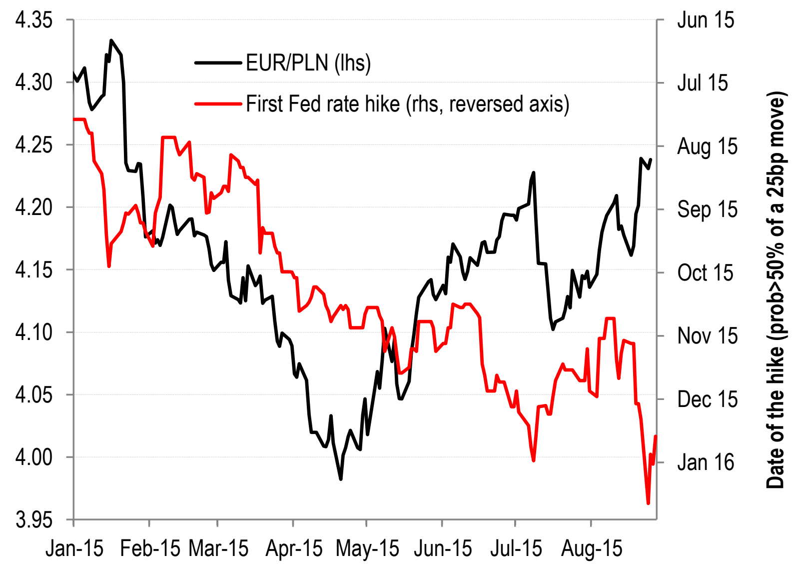


Source: Reuters, BZ WBK.

Foreign Exchange Market: Uncertainty Still High

- The zloty repeated the pattern from the last five years and lost vs euro in August. EUR/PLN rose temporarily above 4.26 on the back of below-consensus Polish economic data, uncertainty about the Polish banking sector, and global risk aversion, fuelled by concern about China. At the same time, the zloty performed quite well vs. the dollar, amid rising EUR/USD.
- In general, the CEE currencies outperformed others in the emerging markets (EM) universe in August – the zloty, forint, koruna and Romanian leu depreciated only slightly vs. the single currency (0-2%) and even gained a little vs. the greenback (0.6-3%).
- In the past, September was often the month when zloty regained ground after weak August, and EUR/PLN was falling just before the date of fixing conversion rate for EU subsidies for farmers. However, we noticed that such regularity has ceased in the last three years and so we do not expect it to be decisive in the coming month.
- We see several risk factors that may keep risk aversion elevated in the nearest weeks, preventing EUR/PLN from falling: the situation in China, early elections in Greece, political uncertainty in Poland ahead of general elections in October. The proposal of FX loans conversion has been losing importance, as in our view the risk of introduction of bill weighing strongly on banks is decreasing. The impact of Fed's rate hike on the zloty may be counterintuitive, in our view, as we noticed that recently the PLN was more vulnerable to worries about global slowdown than to expected timing of Fed rate hike. If the market interprets a September lift-off as a sign of trust in the economic recovery, the PLN may gain at the end of the month.

EUR/PLN and market expectations for the first Fed rate hike



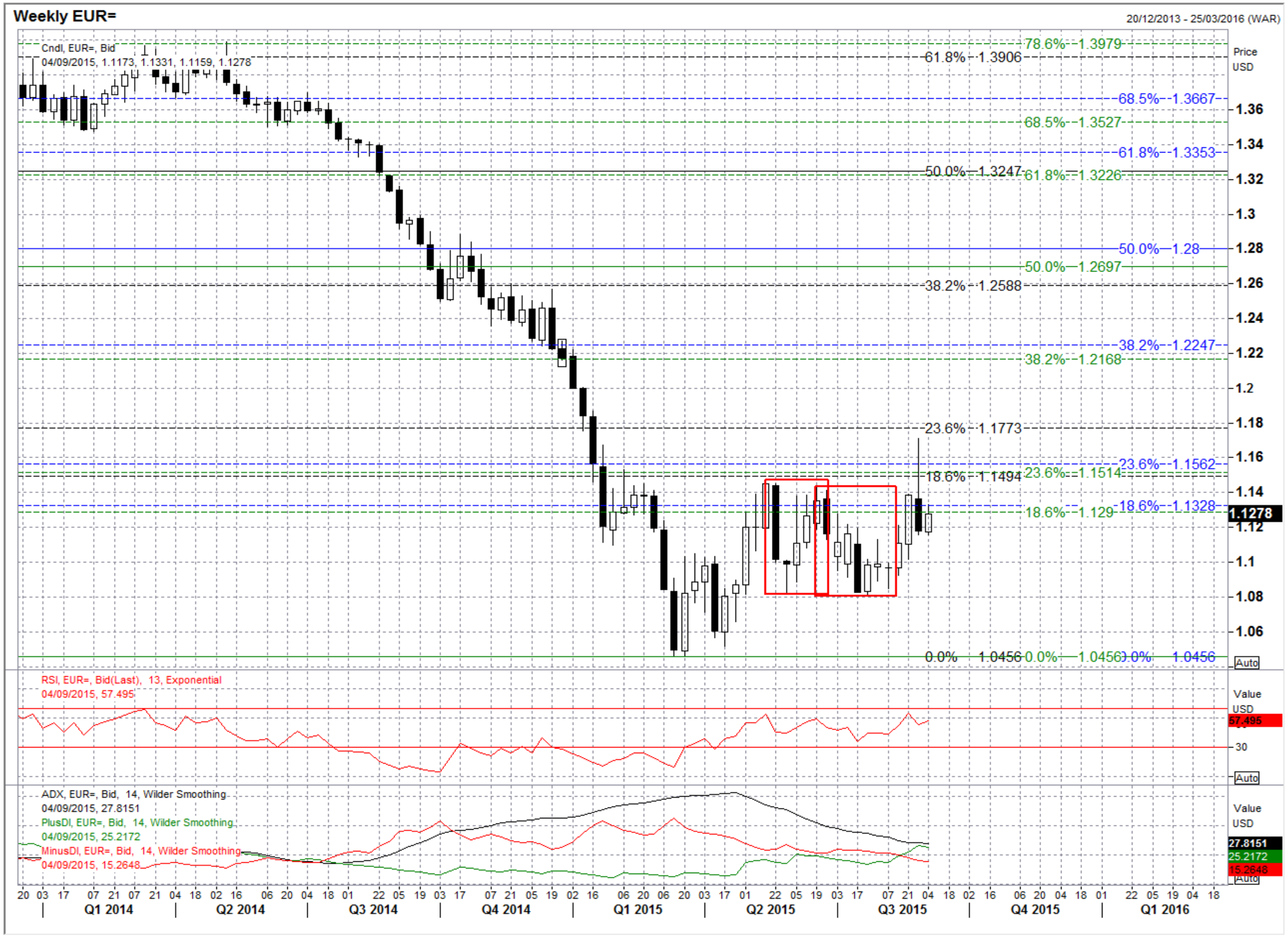
Source: Bloomberg, Santander, BZ WBK

FX Technical Analysis Corner: Second RSI Sell Signal

- Last month, we wrote that RSI gave a sell signal but we highlighted it may not be a clear hint about coming decline.
- Indeed, EUR/PLN rose in August and broke the previous peak.
- In fact, the recent pattern looks similar to what we had seen in the past when the "double sell" RSI signals were recorded.
- RSI gave a second sell signal and we think that EUR/PLN could remain high in the first half of September and start a noticeable decline later on.

Source: Reuters, BZ WBK.

FX Technical Analysis Corner: Still Upside Bias for EUR/USD



- The EUR/USD rebounded from the strong support 1.08 we mentioned last month and broke two resistance levels at 1.12 and 1.146.
- Weekly ADX showed that the trend has changed from downward to upward but it is not very strong so far.
- However, already in April we suggested that the EUR/USD's rise is the biggest in the down trend and since then the exchange rate remains comfortably above the local low. We still think there is an upside bias for EUR/USD.
- First support at 1.10, resistance at 1.171.

Source: Reuters, BZ WBK.

Macroeconomic Forecasts

Poland		2013	2014	2015E	2016E	1Q15	2Q15	3Q15E	4Q15E	1Q16E	2Q16E	3Q16E	4Q16E
GDP	PLNbn	1,662.1	1,728.7	1,796.6	1,898.0	417.8	433.8	443.5	501.5	440.8	459.6	467.9	529.6
GDP	%YoY	1.7	3.4	3.5	3.5	3.6	3.3	3.5	3.6	3.3	3.6	3.6	3.7
Domestic demand	%YoY	0.2	4.9	3.3	3.5	2.6	3.3	3.4	3.9	3.3	3.6	3.5	3.6
Private consumption	%YoY	1.1	3.1	3.2	3.2	3.1	3.0	3.4	3.5	3.3	3.2	3.1	3.1
Fixed investment	%YoY	0.9	9.2	6.9	6.0	11.4	6.4	6.0	6.0	6.0	6.0	6.0	6.0
Unemployment rate [a]	%	13.4	11.5	10.0	9.4	11.7	10.3	9.8	10.0	10.4	9.2	9.0	9.4
Current account balance	EURmn	-5,148	-5,250	736	1,600	1,648	1,505	-1,069	-1,349	2,409	1,544	-1,135	-1,218
Current account balance	% GDP	-1.3	-1.3	0.2	0.3	-0.6	-0.1	0.1	0.2	0.3	0.3	0.3	0.3
General government balance (ESA 2010)	% GDP	-4.0	-3.2	-2.7	-2.3	-	-	-	-	-	-	-	-
CPI	%YoY	0.9	0.0	-0.8	1.7	-1.5	-0.9	-0.8	0.2	1.4	1.7	1.9	2.0
CPI [a]	%YoY	0.7	-1.0	0.7	2.0	-1.5	-0.8	-0.8	0.7	1.5	1.8	2.2	2.0
CPI excluding food and energy prices	%YoY	1.2	0.6	0.6	1.3	0.4	0.3	0.5	1.0	1.2	1.4	1.3	1.3

Source: CSO, NBP, Finance Ministry, BZ WBK estimates. [a] at the end of the period

Interest Rate and FX Forecasts

Poland		2013	2014	2015E	2016E	1Q15	2Q15	3Q15E	4Q15E	1Q16E	2Q16E	3Q16E	4Q16E
Reference rate [a]	%	2.50	2.00	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50
WIBOR 3M	%	3.02	2.52	1.75	1.75	1.87	1.67	1.72	1.73	1.74	1.75	1.75	1.75
Yield on 2-year T-bonds	%	2.98	2.46	1.75	2.05	1.61	1.75	1.80	1.84	1.92	1.98	2.07	2.23
Yield on 5-year T-bonds	%	3.46	2.96	2.31	2.77	1.90	2.35	2.45	2.55	2.66	2.70	2.77	2.93
Yield on 10-year T-bonds	%	4.04	3.49	2.79	3.46	2.24	2.79	2.97	3.15	3.26	3.40	3.52	3.65
2-year IRS	%	3.10	2.51	1.79	2.05	1.65	1.85	1.81	1.84	1.95	2.03	2.05	2.18
5-year IRS	%	3.51	2.92	2.14	2.60	1.80	2.23	2.22	2.30	2.44	2.53	2.62	2.82
10-year IRS	%	3.86	3.34	2.54	3.23	2.06	2.57	2.68	2.85	2.99	3.15	3.30	3.48
EUR/PLN	PLN	4.20	4.18	4.15	4.08	4.20	4.09	4.19	4.12	4.04	4.06	4.09	4.10
USD/PLN	PLN	3.16	3.15	3.69	3.43	3.72	3.70	3.76	3.58	3.44	3.44	3.43	3.42
CHF/PLN	PLN	3.41	3.45	3.90	3.53	3.93	3.93	3.94	3.79	3.65	3.59	3.50	3.39
GBP/PLN	PLN	4.94	5.19	5.70	5.56	5.64	5.67	5.84	5.64	5.50	5.53	5.61	5.62

Source: CSO, NBP, Finance Ministry, BZ WBK estimates. [a] at the end of period

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Economic Calendar and Events

Date		Event:	Note:
2-Sep	**PL**	**MPC meeting – interest rate decision**	**No change in monetary policy conditions**
3-Sep	EZ	ECB meeting – interest rate decision	ECB expected to keep official rates unchanged
4-Sep	US	Non-farm payrolls / Unemployment rate	Key number for Fed's monetary policy outlook; market expects further improvement on the labour market
6-Sep	**PL**	**Referendum in Poland**	
10-Sep	**PL**	**Auction of long-term bonds DS0726 and WZ0126**	**Offer: PLN2-4bn**
14-Sep	**PL**	**CA balance for July**	**We expect CA gap at €0.53bn, close to market consensus**
15-Sep	**PL**	**CPI for August**	**Our forecast is at -0.8%YoY vs market consensus at -0.7%YoY**
16-Sep	**PL**	**Core CPI measures for August**	**We and market see core inflation, excluding food and energy prices, at 0.4%YoY**
	PL	**Wages and employment for August**	**We expect stable employment growth at 0.9%YoY and an increase in wages of 3.6%YoY, in line with market consensus**
17-Sep	**PL**	**Industrial output for August**	**We expect a high increase of 7.1%YoY, well above market expectations (6.1%)**
	PL	**Construction output for August**	**In our view, construction output will increase by 4.0%YoY vs the median forecast of 3%YoY**
	PL	**Retail sales for August**	**We estimate retail sales grew by 1.3%YoY, slightly more than the previous month**
	PL	**Minutes from July MPC meeting**	-
	US	FOMC meeting – interest rate decision	We expect the Fed to keep rates unchanged, but we continue to think that the scenario of lift-off before the end of the year remains.
22-Sep	HU	NMB meeting – interest rate decision	We expect rates to remain unchanged
24-Sep	**PL**	**Auction of T-bonds**	**Offer: PLN2-6bn**
25-Sep	**PL**	**Unemployment rate for august**	**We expect a further slide in unemployment to 10%**
1-Oct	**PL**	**PMI for Poland's manufacturing sector**	**-**

Source: CB, Markit, CSO, Finance Ministry

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Annex

1. Domestic Market Performance
2. Polish Bonds: Supply Recap
3. Polish Bonds: Demand Recap
4. Euro Zone Bonds: Supply Recap
5. Poland vs Other Countries
6. Central Bank Watch

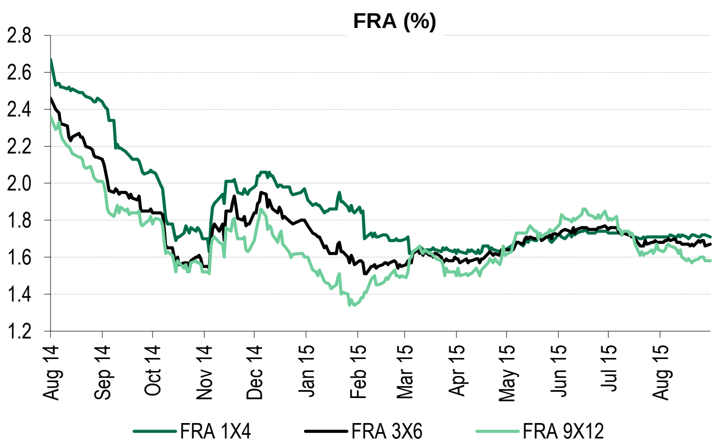
1. Domestic Market Performance

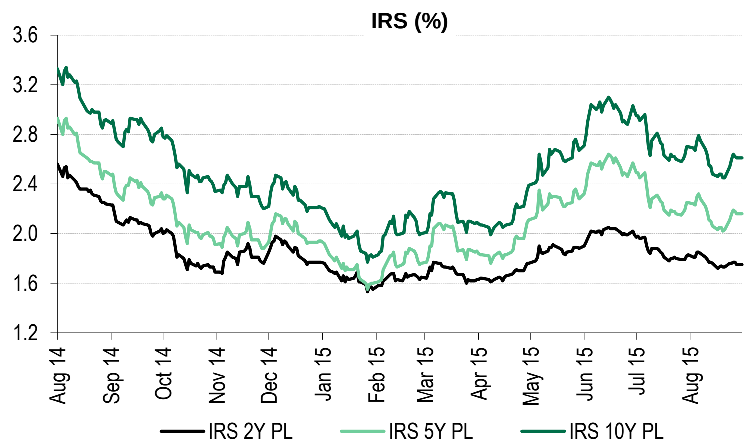
Money market rates (%)

	Reference rate (%)	Poland (%)	WIBOR (%) 1M	WIBOR 3M	WIBOR 6M	WIBOR 12M	OIS (%) 1M	OIS 3M	OIS 6M	OIS 12M	FRA (%) 1x4	FRA 3x6	FRA 6x9	FRA 9x12
End of August	1.50	1.53	1.66	1.72	1.80	1.83	1.45	1.45	1.45	1.46	1.71	1.67	1.60	1.58
Last 1M change (bp)	0	5	0	0	1	0	0	-1	-1	0	0	-1	-6	-6
Last 3M change (bp)	0	16	1	4	4	3	0	-2	-4	-5	2	-6	-11	-16
Last 1Y change (bp)	-100	-104	-93	-87	-80	-79	-96	-78	-59	-52	-75	-47	-41	-43

Bond and IRS market (%)

	BONDS 2Y	BONDS 5Y	BONDS 10Y	IRS 2Y	IRS 5Y	IRS 10Y	Spread BONDS / IRS (bp) 2Y	Spread 5Y	Spread 10Y
End of August	1.79	2.46	2.93	1.75	2.16	2.61	4	30	32
Last 1M change (bp)	0	0	0	-8	-9	-9	8	9	9
Last 3M change (bp)	4	2	0	-13	-12	-6	17	14	6
Last 1Y change (bp)	-39	-7	-18	-49	-34	-31	10	27	13





Source: Reuters, BZ WBK

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2. Polish Bonds: Supply Recap

Total issuance in 2015 by instrument (in PLN mn, nominal terms)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
T-bond auctions	11,204	10,908	4,639	11,442	4,056	4,237	8,283	4,656	9,000	12,000	6,000		86,424
T-bill auctions													0
Retail bonds	97	126	127	129	207	181	150	150	150	150	150	150	1,767
Foreign bonds/credits				4,127	2,278		3,797						10,202
Pre-financing and financial resources at the end of 2014	38,700												38,700
Total	**50,001**	**11,034**	**4,766**	**15,698**	**6,541**	**4,417**	**12,230**	**4,806**	**9,150**	**12,150**	**6,150**	**150**	**137,093**
Redemption	6,071	159	98	14,774	5,858	110	12,597	1,597	446	26,007	213	241	68,172
Net inflows	**43,930**	**10,875**	**4,668**	**924**	**683**	**4,307**	**-367**	**3,209**	**8,704**	**-13,857**	**5,937**	**-91**	**68,921**
Rolled-over T-bonds			6,502			2,082							**8,585**
Buy-back of T-bills/ FX-denominated bonds													**0**
Total	**43,930**	**10,875**	**11,170**	**924**	**683**	**6,389**	**-367**	**3,209**	**8,704**	**-13,857**	**5,937**	**-91**	**77,506**
Coupon payments from domestic debt	*3,491*			*4,382*			*3,306*		*1,295*	*7,720*			*20,194*

Note: Our forecasts = shaded area

Source: MF, BZ WBK

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2. Polish Bonds: Supply Recap (cont.)

Schedule of Treasury security redemptions by instrument (in PLN mn)

	Bonds	Bills	Retail bonds	Total domestic redemption	Foreign bonds/credits	Total redemptions
January	6,023		48	**6,071**	0	**6,071**
February	0		159	**159**	0	**159**
March	0		98	**98**	0	**98**
April	14,679		95	**14,774**	0	**14,774**
May	0		116	**116**	5,742	**5,858**
June	0		110	**110**	0	**110**
July	7,658		136	**7,794**	4,802	**12,597**
August	0		184	**184**	1,412	**1,597**
September	0		162	**162**	284	**446**
October	22,420		146	**22,567**	3,440	**26,007**
November	0		213	**213**	0	**213**
December	0		241	**241**	0	**241**
Total 2015	50,781		1,710	**52,491**	15,681	**68,172**
Total 2016	87,607		2,034	**89,641**	13,886	**103,527**
Total 2017	67,997		1,032	**69,029**	11,759	**80,788**
Total 2018	66,317		1,103	**67,420**	10,844	**78,264**
Total 2019+	63,811		972	**64,783**	22,248	**87,032**
Total 2020+	204,638		2,383	**207,021**	119,836	**326,857**

Source: MF, BZ WBK.

2. Polish Bonds: Supply Recap (cont.)

Scheduled wholesale bond redemptions by holders (data at the end of July 2015, in PLN mn)

	Foreign investors	Domestic banks	Insurance funds	Pension funds	Mutual funds	Individuals	Non-financial sector	Other	Total
Q1 2015	0	0	0	0	0	0	0	0	0
Q2 2015	0	0	0	0	0	0	0	0	0
Q3 2015	0	0	0	0	0	0	0	0	0
Q4 2015	10,107	4,403	4,515	94	932	25	173	2,170	22,420
Total 2015	**10,107**	**4,403**	**4,515**	**94**	**932**	**25**	**173**	**2,170**	**22,420**
	45%	**20%**	**20%**	**0%**	**4%**	**0%**	**1%**	**10%**	**100%**
Total 2016	40,305	25,899	7,968	543	7,198	128	111	6,472	88,624
	45%	29%	9%	1%	8%	0%	0%	7%	100%
Total 2017	26,086	24,293	6,502	516	5,208	93	167	5,132	67,997
	38%	36%	10%	1%	8%	0%	0%	8%	100%
Total 2018	20,565	26,955	3,986	287	8,691	87	172	5,576	66,317
	31%	41%	6%	0%	13%	0%	0%	8%	100%
Total 2019+	20,623	25,667	5,831	482	6,960	77	144	4,026	63,811
	32%	40%	9%	1%	11%	0%	0%	6%	100%
Total 2020+	87,254	57,689	24,256	1,006	20,788	189	263	8,940	200,384
	44%	29%	12%	1%	10%	0%	0%	4%	100%

Source: MF, BZ WBK.

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3. Polish Bonds: Demand Recap

Holders of marketable PLN bonds

	Nominal value (PLN bn)			Nominal value (PLN bn)			% change in July			Share of total in July (%)
	End Jul'15	End Jun'15	End May'15	End 1Q 2015	End 2014	End 2013	MoM	3-mth	YoY	
Domestic investors	313.8	314.3	313.7	309.1	295.9	381.2	-0,2	1,8	11,6	60.5 (-0.2pp)
Commercial banks	164.9	166.3	164.0	163.1	150.8	114.7	-0,8	1,2	19,7	31.8 (-0.3pp)
Insurance companies	53.1	53.3	53.8	52.4	52.8	52.0	-0,4	-0,3	-0,7	10.2 (-0.1pp)
Pension funds	2.9	2.9	2.8	3.1	3.3	125.8	1,8	1,1	-15,6	0.6
Mutual funds	49.8	49.3	50.6	48.5	46.9	46.7	0,9	-1,3	10,4	9.6 (0.1pp)
Others	43.1	42.6	42.6	42.0	42.0	42.0	1.3	3.7	4.1	8.3 (0.1pp)
Foreign investors*	205.0	203.7	199.9	203.8	196.0	193.2	0,6	3,2	4,5	39.5 (0.2pp)
Banks	13.3	14.0	12.7	9.9	9.9	n.a.	-4,6	5,0	5,5	2.6 (-0.1pp)
Central banks	22.9	22.6	23.1	20.3	16.4	n.a.	1,1	-0,9	26,8	4.4
Public institutions	9.5	9.4	9.3	8.8	8.1	n.a.	1,1	2,0	1224,6	1.8
Insurance companies	11.7	11.0	10.6	11.0	10.7	n.a.	6,5	10,5	23,0	2.3 (0.1pp)
Pension funds	12.9	12.4	12.2	13.2	13.0	n.a.	4,1	5,3	4,8	2.5 (0.1pp)
Mutual funds	70.9	71.5	70.8	80.2	78.1	n.a.	-0,9	0,2	-15,0	13.7 (-0.1pp)
Hedge funds	0.0	0.0	0.6	0.1	1.1	n.a.	0,0	-93,2	-55,8	0.0
Non-financial sector	8.1	8.4	8.5	12.6	8.2	n.a.	-3,6	-5,0	-42,9	1.6 (-0.1pp)
Others	18.7	18.6	16.5	17.0	14.3	n.a.	0,8	13,6	13,3	3.6
TOTAL	518.7	518.0	513.6	512.9	491.8	574.3	0,1	0,9	8,7	100

**Total for foreign investors does not match sum of values presented for sub-categories due to omission of a very small group of investors. Detailed data on foreign investors are available only since April 2014 .*

Source: MF, BZ WBK.

4. Euro Zone Bonds: Supply Recap

Euro zone: 2014 issuance completion and 2015 estimated gross borrowing requirements and redemptions (€ bn)

	2014 bond supply	% of completion	2015 total redemption	2015 bond supply	% of completion (YTD*)
Austria	24.7	91.4	13.3	17.0	79
Belgium	31.8	102.2	28.1	32.5	77
Finland	10.0	119.6	7.6	11.4	87
France	173.0	117.4	116.5	187.0	82
Germany	161.0	100.0	155.0	147.0	70
Greece	-	-	-	-	-
Ireland	10.0	117.5	2.3	7.5	84
Italy	235.4	111.8	205.2	252.9	70
Netherlands	50.0	101.7	39.9	48.0	74
Portugal	16.7	101.7	7.2	13.9	77
Spain	129.3	105.4	86.4	130.0	74
Total	**841.9**	**108.1**	661.5	**847.3**	**75**

** YTD is supply since January 1, 2015*

Source: European Commission, Euro zone countries' debt agencies, BZ WBK.

5. Poland vs. Other Countries

Main macroeconomic indicators (European Commission forecasts)

	GDP (%)		Inflation (HICP, %)		C/A balance (% of GDP)		Fiscal balance (% of GDP)		Public debt (% of GDP)	
	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016
Poland	**3.3**	**3.4**	**-0.4**	**1.1**	**-1.8**	**-2.2**	**-2.8**	**-2.6**	**50.9**	**50.8**
Czech Republic	2.5	2.6	0.2	1.4	0.4	0.7	-2.0	-1.5	41.5	41.6
Hungary	2.8	2.2	0.0	2.5	5.5	6.2	-2.5	-2.2	75.0	73.5
EU	1.8	2.1	0.1	1.5	1.9	1.9	-2.5	-2.0	88.0	86.9
Euro zone	1.5	1.9	0.1	1.5	3.5	3.4	-2.0	-1.7	94.0	92.5
Germany	1.9	2.0	0.3	1.8	7.9	7.7	0.6	0.5	71.5	68.2

Main market indicators (%, end of period)

	Reference rate (%)		3M market rate (%)		10Y yields (%)		10Y spread vs Bund (bp)		CDS 5Y	
	2014	end-Aug 2015	2014	end-Aug 2015	2014	end-Aug 2015	2014	end-Aug 2015	2014	end-Aug 2015
Poland	**2.00**	**1.50**	**2.06**	**1.72**	**2.51**	**2.93**	**197**	**221**	**71**	**72**
Czech Republic	0.05	0.05	0.04	0.31	0.75	0.88	2	16	55	50
Hungary	2.10	1.35	2.10	1.36	3.69	3.74	315	302	178	164
Euro zone	0.05	0.05	0.08	-0.033						
Germany					0.54	0.72			17	13

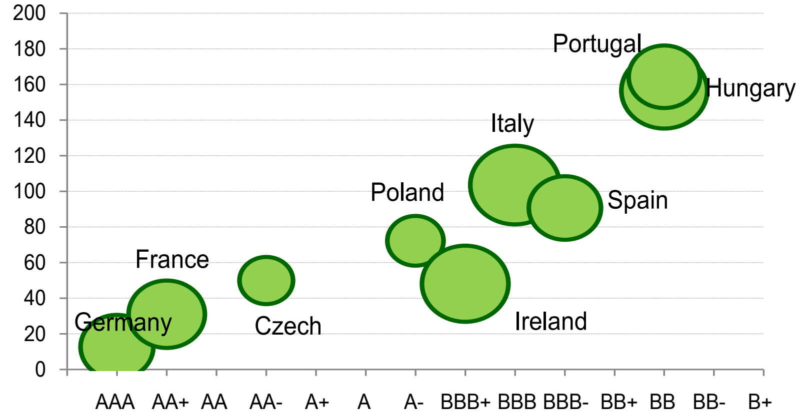
Source: EC – Spring 2015, statistics offices, central banks, Reuters, BZ WBK.

5. Poland vs. Other Countries (cont.)

Sovereign ratings

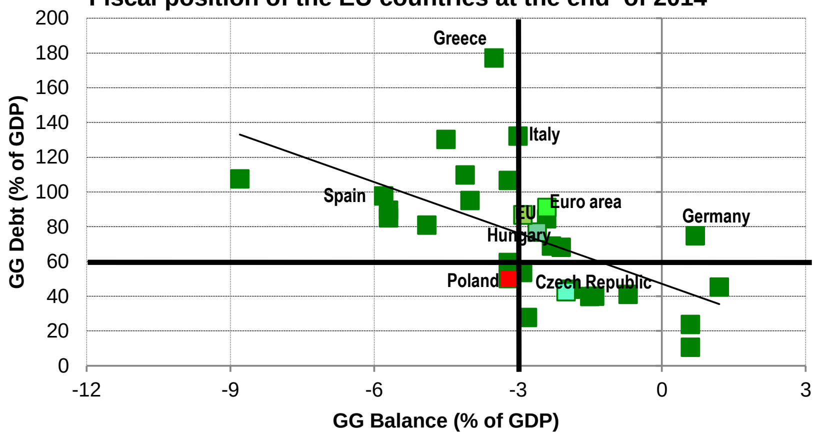
	S&P		Moody's		Fitch	
	rating	outlook	rating	outlook	rating	outlook
Poland	A-	positive	A2	stable	A-	stable
Czech	AA-	stable	A1	stable	A+	stable
Hungary	BB+	stable	Ba1	negative	BB+	stable
Germany	AAA	stable	Aaa	stable	AAA	stable
France	AA	negative	Aa1	negative	AA	stable
UK	AAA	negative	Aa1	negative	AA+	stable
Greece	CCC+	stable	Caa3	negative	CCC	stable
Ireland	A	stable	Baa1	stable	A-	stable
Italy	BBB	stable	Baa2	stable	BBB+	negative
Portugal	BB	stable	Ba1	stable	BB+	negative
Spain	BBB	stable	Baa2	positive	BBB+	stable

5Y CDS rates vs credit ranking according to S&P

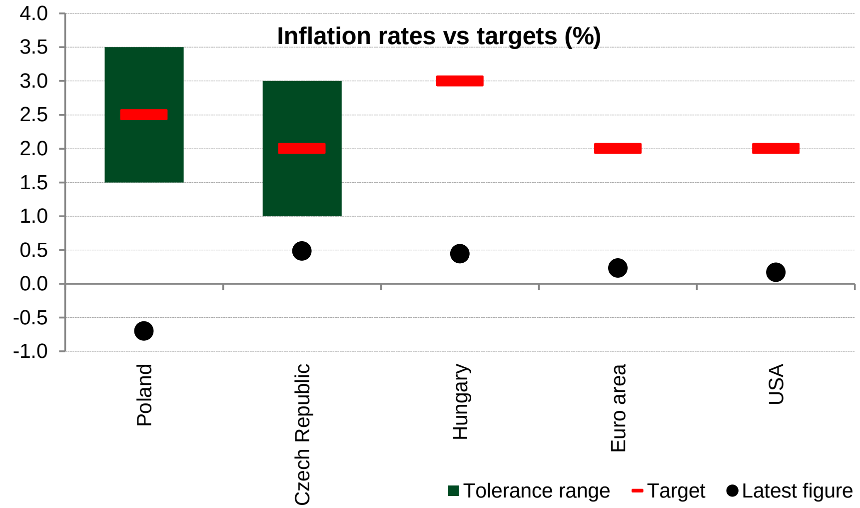


Note: Size of bubbles reflects the debt/GDP ratio

Fiscal position of the EU countries at the end of 2014

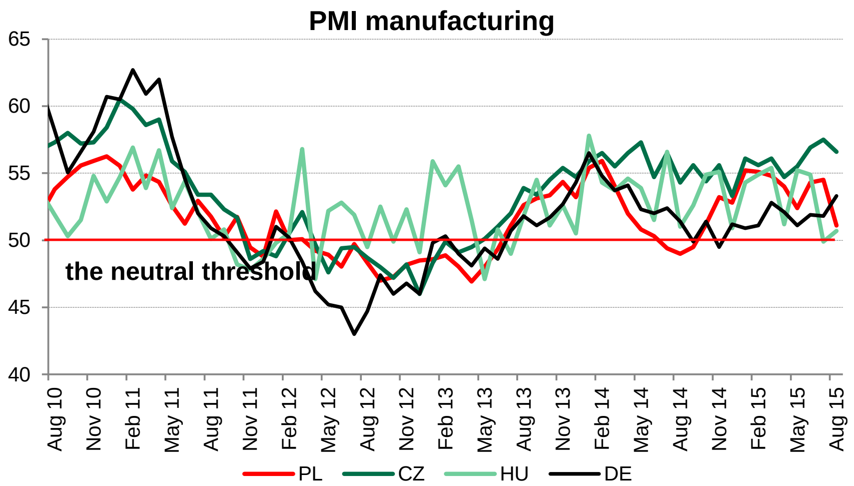


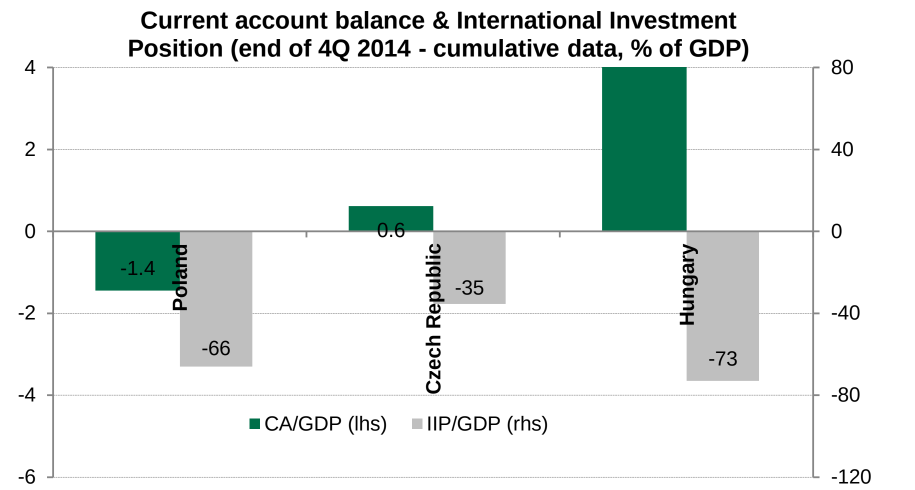
Inflation rates vs targets (%)

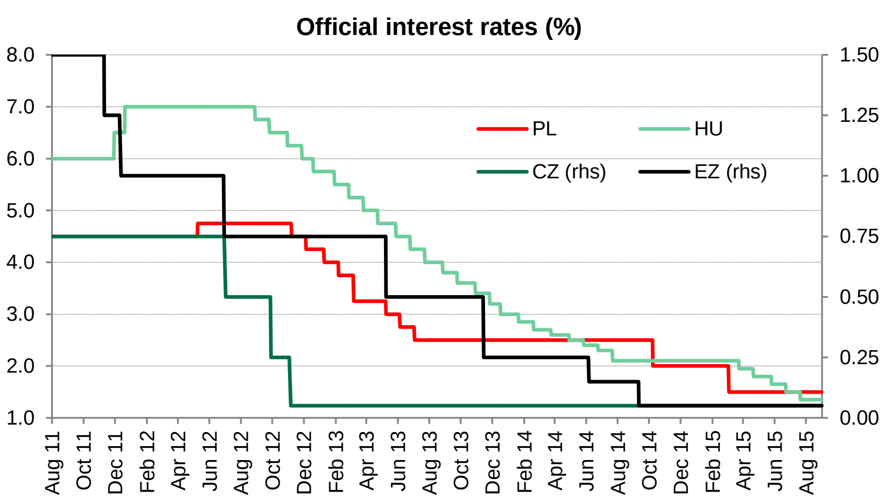


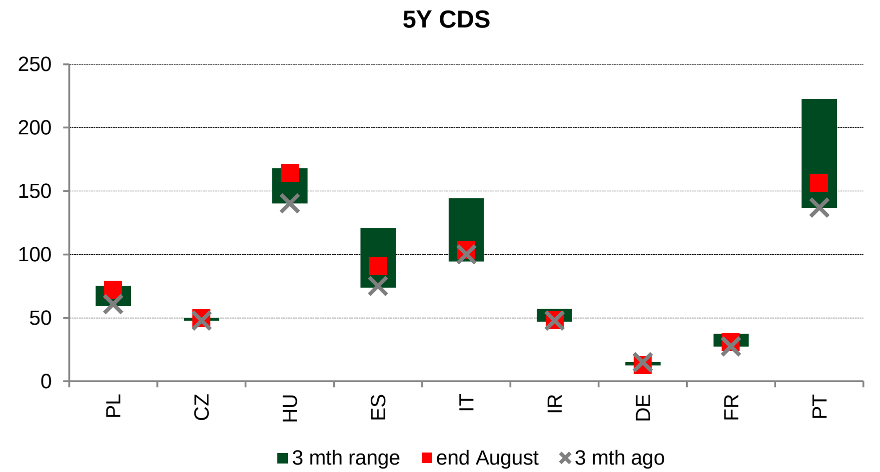
Source: Rating agencies, Reuters, EC, BZ WBK.

5. Poland vs. Other Countries (cont.)



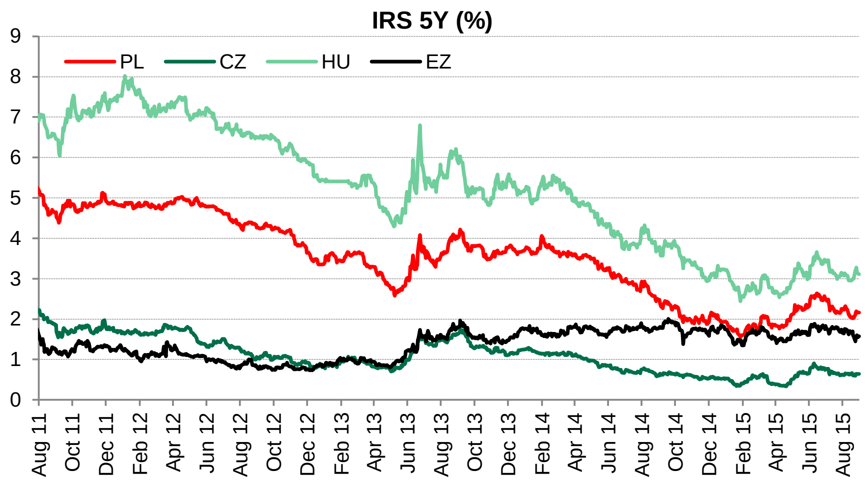


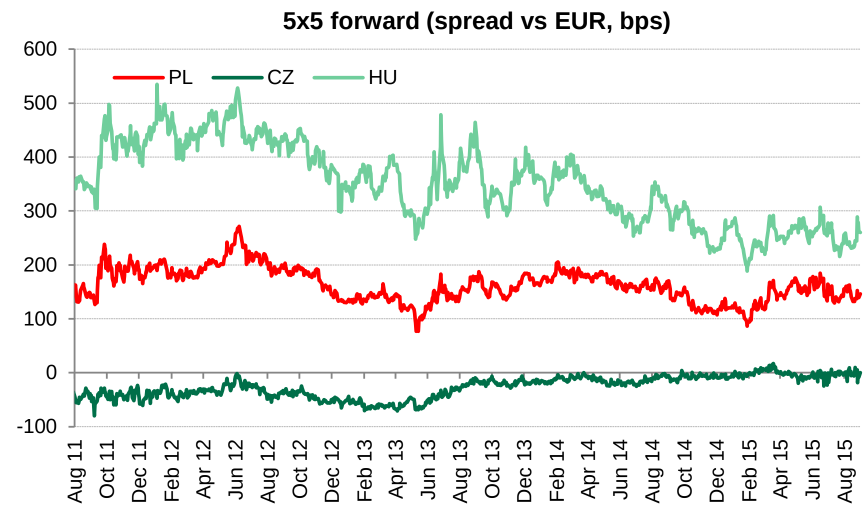


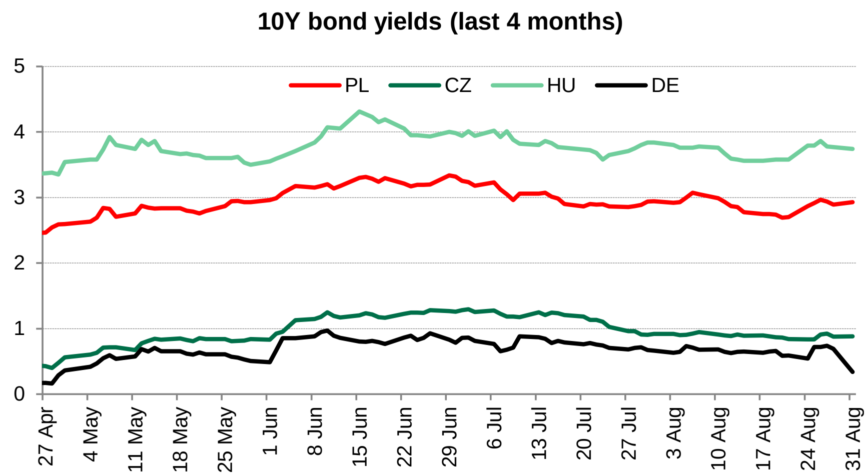


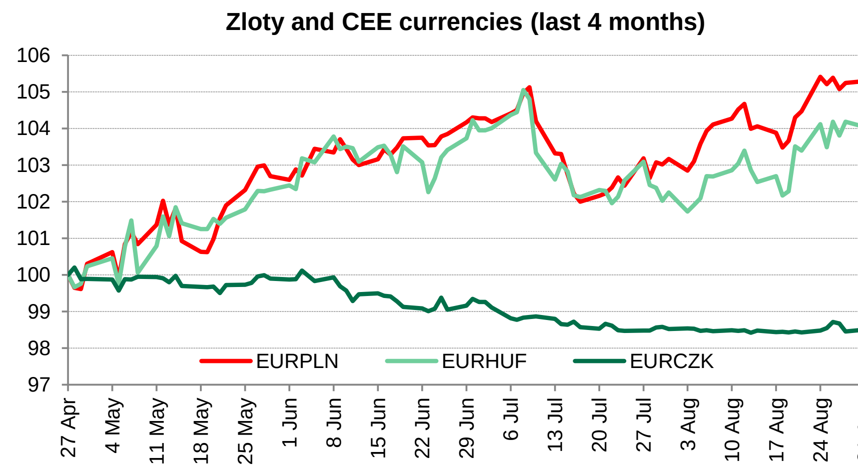
Source: Markit, Eurostat, central banks, Reuters, BZ WBK, EC.

5. Poland vs. Other Countries (cont.)









Source: Reuters, BZ WBK.

6. Central Bank Watch

		Last	2014	2015	Expected changes (bp)			Comments
					1M	3M	6M	
Euro zone	Forecast	0.05	0.05	0.05				We expect the ECB to stay on hold at its September monetary policy meeting. In our view Mr. Draghi should keep a dovish tone in the subsequent press conference, confirming its readiness to expand the policy stimulus if needed. In our view it is too early to expect the ECB to raise or even to extend its QE programme.
	Market implied »				-10	-9	-9	
UK	Forecast	0.50	0.50	0.50				We expect the BoE to keep monetary policy unchanged at its meeting. However, in our view the BoE will start its monetary tightening earlier than current market pricing. We change our base line scenario due to situation in China and we now expect the first 25 bp increase in 1Q 16E.
	Market implied »				2	5	14	
US	Forecast	0-0.25	0-0.25	0.50				Recent events and market volatility have increased the chances of the Fed not adjusting its Fed Funds corridor in September. However, in our view the scenario assuming the start of monetary tightening this month is still very likely taking into account macro developments in the US economy.
	Market implied »				20	33	53	
Poland	Forecast	1.50	2.00	1.50				We expect Poland's MPC to keep interest rates unchanged in September as the macro situation has changed a little since the previous meeting in July. In our view the Council could repeat that its monetary guidance should remain on hold. We uphold our stance that rates will stay unchanged until the end of its term in 1Q 2016.
	Market implied »				-1	-5	-12	
Czech Republic	Forecast	0.05	0.05	0.05				As expected the CNB decided to leave the base rate at 0.05% and confirmed the EURCZK floor close to 27. The Council still takes a fairly relaxed position with regards to potential pressure on the FX cap going forward. Importantly, the CNB published a new forecast, apparently incorporating GDP and inflation at levels which are currently higher than expected.
	Market implied »				-2	-3	-6	
Hungary	Forecast	1.35	2.10	1.35				In line with expectations the MPC kept the interest rate unchanged at 1.35% at its August's meeting. The Council highlighted that the current level of the key rate is in line with their mid-term inflation rate target.
	Market implied »				2	3	6	

Source: Reuters, BZ WBK.

This analysis is based on information available through September 1, 2015 and has been prepared by:

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The views expressed in this report accurately reflect the personal views of the undersigned analyst(s). In addition, the undersigned analyst(s) have not and will not receive any compensation for providing a specific recommendation or view in this report: **Maciej Reluga*, Piotr Bielski*, Agnieszka Decewicz*, Marcin Luziński*, Marcin Sulewski*.**

EXPLANATION OF THE RECOMMENDATION SYSTEM

DIRECTIONAL RECOMMENDATIONS IN BONDS		DIRECTIONAL RECOMMENDATIONS IN SWAPS	
	Definition		**Definition**
Long / Buy	Buy the bond for an expected average return of at least 10bp in 3 months (decline in the yield rate), assuming a directional risk.	**Long / Receive fixed rate**	Enter a swap receiving the fixed rate for an expected average return of at least 10bp in 3 months (decline in the swap rate), assuming a directional risk.
Short / Sell	Sell the bond for an expected average return of at least 10bp in 3 months (increase in the yield rate), assuming a directional risk.	**Short / Pay fixed rate**	Enter a swap paying the fixed rate for an expected average return of at least 10bp in 3 months (increase in the swap rate), assuming a directional risk.

RELATIVE VALUE RECOMMENDATIONS	
	Definition
Long a spread / Play steepeners	Enter a long position in a given instrument vs a short position in another instrument (with a longer maturity for steepeners) for an expected average return of at least 5bp in 3 months (increase in the spread between both rates).
Short a spread / Play flatteners	Enter a long position in given an instrument vs a short position in other instrument (with a shorter maturity for flatteners) for an expected average return of at least 5bp in 3 months (decline in the spread between both rates).

FX RECOMMENDATIONS	
	Definition
Long / Buy	Appreciation of a given currency with an expected return of at least 5% in 3 months.
Short / Sell	Depreciation of a given currency with an expected return of at least 5% in 3 months.

NOTE: Given the recent volatility seen in the financial markets, the recommendation definitions are only indicative until further notice.

Important Disclosures (cont.)

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