



# RATES AND FX OUTLOOK

## POLISH FINANCIAL MARKETS

May 2016



Bank Zachodni WBK

 Grupa Santander

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# Summary

- Recent signals from the Polish economy have been mixed. On one hand, GDP growth in 4Q15 was revised up to 4.3% y/y and employment growth in 1Q16 was surprisingly strong, suggesting that firms are still expanding. On the other hand, production and sales data for March were clearly disappointing and April's business climate surveys showed new signs of weakness in manufacturing. We remain moderately optimistic about Poland's GDP growth and we still expect it to be close to 3.5% this year, driven by both relatively healthy external demand and strong private consumption (receiving an extra boost from the child allowances programme starting in 3Q16E).
- Deflation deepened again in April (-1.1% y/y according to the flash estimate), probably mainly due to the cut in gas tariffs, but we think the trend should reverse soon. It seems that the Monetary Policy Council (MPC) is well aware of the fact that deflation may not disappear before 4Q16 and we think that, in the nearest months, data about real activity may be much more important for the monetary policy outlook than data about inflation. In April, the majority of MPC members agreed that monetary easing cannot be ruled out "in case of an economic slowdown in Poland and deepening deflation" and, in such circumstances, a more significant adjustment could take place rather than a series of small rate cuts. However, recent comments by some Council members (Chrzanowski, Gatnar, Zubelewicz) rejected the possibility of rate cuts and even signalled that monetary tightening could be more likely than easing. We think such comments reflect their strong belief that economic growth will remain strong in the coming quarters.
- This means real activity data releases (flash 1Q16 GDP, monthly data for April) may be quite important for market sentiment in the coming weeks. Other key factors to watch are Moody's rating decision (May 13) and possible new proposals about how to deal with CHF loans (which may be revealed at the end of May or beginning of June).
- April saw an increase in yields on global markets, partly due to signs of reviving economic activity in emerging economies, and we think that, after a short-term respite in recent days, this trend may continue in May, additionally supported by speculation that the Fed may lift interest rates in June/July. On top of that, the risk premium for Polish assets will probably remain high due to domestic risks (particularly uncertainty about CHF loan conversion). We expect Moody's to leave Poland's rating unchanged and lower the outlook to negative, which may be a trigger for a temporary strengthening of the bond market. However, in general we see limited room for yields to decline in the coming weeks. Any major disappointment in macro data (which we do not expect) would be a reason for bullish curve steepening (because it increases the probability of rate cuts).
- We do not expect the zloty to strengthen in the coming weeks, mainly due to the internal risks already mentioned. Another factor that could negatively affect the Polish currency is uncertainty ahead of the EU referendum in the United Kingdom.

# Short- and Medium-Term Strategy: Interest rate market

	Change (bp)		Current Level	Expected Trend	
	Last 3M	Last 1M	4 May 2016	1M	3M
Reference rate	0	0	1.50	→	→
3M WIBOR	-2	0	1.67	→	→
2Y bond yield	6	9	1.52	→	→
5Y bond yield	-1	9	2.27	→	→
10Y bond yield	-3	26	3.10	→	→
2/10Y curve slope	-9	17	158	→	→

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:** We expect WIBORs to remain stable and FRA rates to stay in a horizontal trend in the coming weeks/months. The Monetary Policy Council (MPC) is unlikely to change its policy or the statement, repeating that interest rate cuts are not necessary as long as economic growth remains decent.

**Short end:** Banks' demand for short-term bonds should keep yields at the short end of the curve relatively stable.

**Long end:** We think that yields on global markets may continue the upward trend seen in April, amid hopes for better economic activity and speculation that the Fed may lift interest rates in June/July. The risk premium for Polish assets will probably stay high, due to domestic risk factors (uncertainty about CHF loan conversion chief among them). If Moody's keeps Poland's rating unchanged, it could be a temporary support for the bond market. However, in general we see limited room for yields to decline in the coming weeks.

**Risks to our view:** If Moody's downgrades Poland's rating, and not just the outlook, then the bond market would weaken, in our view, at least temporarily. Any major disappointment from macro data (which we do not expect) would be a reason for a bullish curve steepening (as it raises the probability of rate cuts).

# Short- and Medium-Term Strategy: FX market

	Change (%)		Current Level	Expected Trend	
	Last 3M	Last 1M	4 May 2016	1M	3M
EUR/PLN	-0.2	3.9	4.40	→	→
USD/PLN	-3.0	2.8	3.83	→	↗
CHF/PLN	1.6	3.4	4.01	↘	↘↘
GBP/PLN	-4.1	4.9	5.55	↗	↗↗
EUR/USD	2.9	1.0	1.15	↘	↘

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:** In the last ten years, the zloty has only gained vs the euro twice in May (in 2008 and in 2014). We do not expect it to strengthen in the coming weeks, given the looming Moody's rating decision and worries about new proposals on how to deal with FX loans. Another factor that could negatively affect the Polish currency is uncertainty ahead of the EU referendum in the United Kingdom.

**USD:** The USD/PLN rebounded in April from its six-month low, as we expected, and we see further upward potential for this exchange rate in the nearest weeks. Our positive outlook for the euro through to the end of 2016 remains, but we still suspect that the recent rise in EUR/USD may have been overdone, implying downside risks may dominate over the coming weeks or months.

**CHF:** The SNB views the CHF as 'heavily overvalued' and remains willing to intervene to weaken it (we think a cut in the deposit rate, driving it further into negative territory, and/or more FX intervention is possible). We still expect EUR/CHF to rise and thus CHF/PLN to decline by the end of the year.

**Risks to our view:** Significant negative surprises from economic data (including 1Q16 GDP), Moody's, or a costly new proposal for CHF loan conversion could trigger zloty depreciation. But on the other hand, all those factors could also surprise positively, in which case the zloty would gain strength, trimming recent losses.

# Fiscal Plans: Higher tax collection curbs deficit

- According to the 2016 Convergence Programme (CP) approved by the government, real GDP growth should accelerate from 3.8% this year to 4.1% in 2019 (forecasts up to 2018 are the same as assumed by the previous government in its 2015 CP). In our view, these forecasts are quite optimistic but not impossible.
- The General Government (GG) deficit is expected to fall to 1.3% of GDP in 2019 (last year this target was assumed for 2018). Public debt to GDP will also be higher than the path expected in 2015 – above 50% on the forecast horizon. The delay in achieving the 1.3% target is the result of higher expenses that will be only partly covered by higher tax collection.
- The programme assumes a VAT cut in 2017 and improved tax collection, but no hike in tax-free allowances or a lower retirement age (although the document showed cost estimates for these measures).
- We see no major risk to the budget in 2016, as higher than planned revenues from NBP profits (PLN4.7bn higher) are likely to offset lower revenues from the bank tax, retail tax and, possibly, indirect taxes.
- Assumptions for 2017 seem a bit more risky, as the programme implies a very ambitious rise in revenues: according to our estimates, after excluding one-offs and discretionary changes (a VAT cut and higher tax collection), planned revenue growth in 2017 amounts to 8.1% (vs a 5.6% rise in nominal GDP). However, this may be partly due to higher expected inflows of EU funds in 2017 (as assumed by the European Commission in its Spring Economic Forecasts).
- The CP assumes a reduction of VAT rates in 2017, even though the finance minister declared that he would like to cancel this move. We view decision to withdraw a tax cut as highly probable.

Finance Ministry estimates of new budget proposals  
(effect on GG balance in PLNbn, cum. change vs 2016)

		2017	2018	2019	
Included in baseline CP scenario	VAT cut	-7.2	-7.6	-8.1	
	Better tax collection	Min	6.5	11.9	21.7
		Assumed*	10.0	18.0	26.0
	Max	16.7	27.0	33.4	
Not in baseline CP scenario	Higher tax-free allowance	-4.0	-8.0	-12.0	
	Lower retirement age	-8.6	-10.2	-11.9	

\* BZ WBK estimate of inflows assumed in the CP based on available partial information

Main assumptions of the Convergence Programme (%YoY)

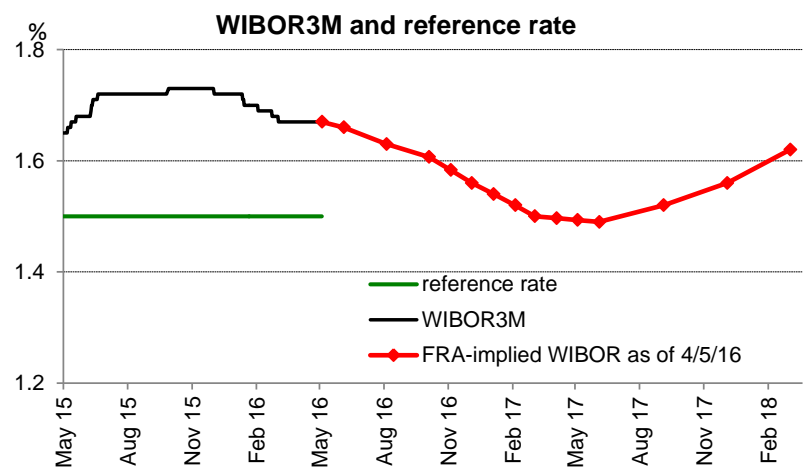
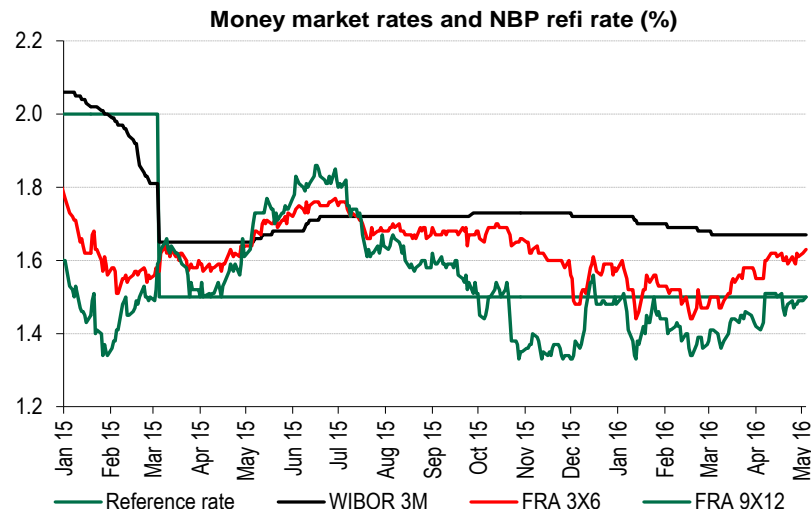
	2016	2017	2018	2019
Nominal GDP	4.1	5.6	6.0	6.5
Spending	4.4	6.4	4.7	4.7
Revenues	4.4	5.6	7.1	6.5
Revenues ex one-offs in 2016**	1.9	8.1	7.1	6.5
Revenues ex one-offs in 2016, ex VAT cut and ex better tax collection**	1.6	8.1	6.1	5.7

\*\* BZ WBK estimate; One-offs include: NBP profit (PLN7.9bn) and inflows from LTE auction (PLN9.2bn).

Source: NBP, MF, EC, BZ WBK

# Domestic Money Market: Rates likely to move sideways

- In April, WIBOR rates were quite stable (the 1M rate increased by just 1bp on a monthly basis), while FRAs continued their gradual upward trend. Both the MPC's official statement and comments from members confirmed that the Council sees no need for monetary policy easing in Poland in the nearest months, which put some upward pressure on FRAs, as we expected. All in all, on monthly basis, the FRA curve shifted up by another 2-10bp across the board, with the long-term rates increasing most.
- The FRA market is still pricing in some monetary easing in the coming months. However, investors scaled back their expectations of rate cuts, seeing a c50% chance rates will fall by 25bp in the next six months (down from 80% in early April).
- In our view, the MPC will pay more attention to economic growth than to CPI inflation in the nearest months. Therefore, investors will focus on economic activity data (labour market, industrial output, retail sales for April, the 1Q16 GDP flash release in mid-May and further details at the end of month). The market seems to be pricing in a moderate slowdown of GDP in 1H16 though, and we think that only a major surprise could significantly affect investors' expectations about the monetary policy outlook.
- Overall, we expect WIBORs to remain stable and FRA rates to fluctuate in a horizontal range in the coming weeks/months.



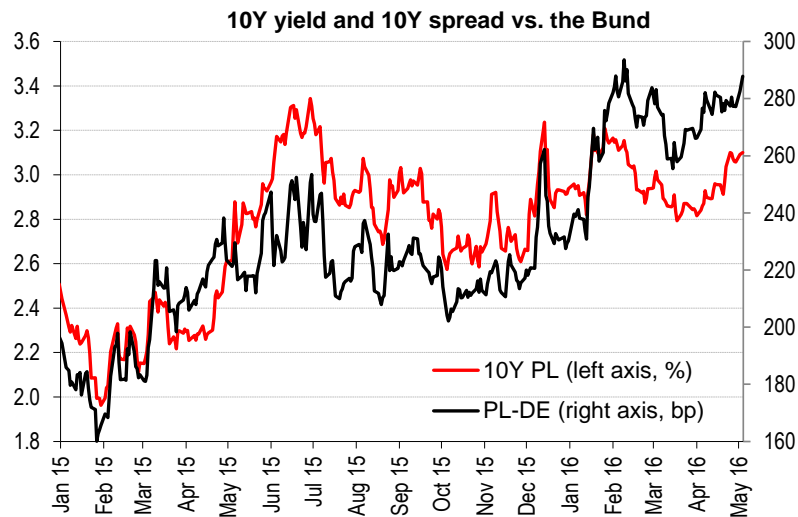
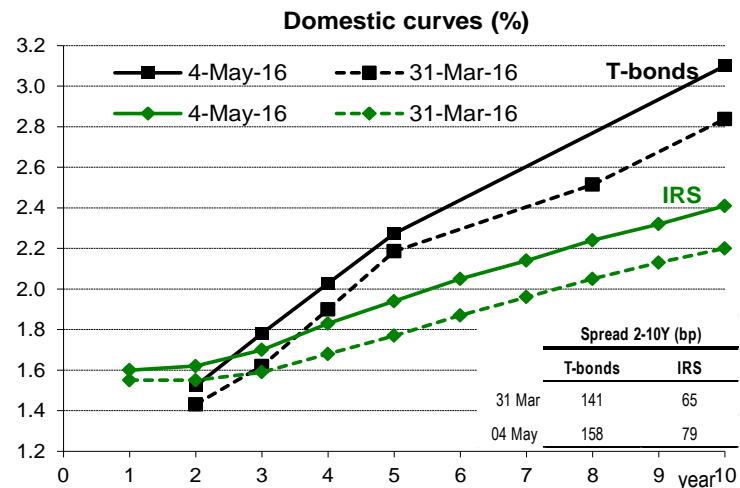
Source: Reuters, BZ WBK

# Domestic IRS and the T-Bond Market: Local factors still point to a higher risk premium

In April, both the bond and IRS markets suffered from the deterioration in the global mood after a favourable 1Q16. Yields increased after the FOMC left the door open for a rate hike in June and still from domestic political uncertainty. Tracking trends on the core markets, the Polish yields and IRS rates increased visibly, with the 10Y benchmark yield rising to 3.10%, the highest level since mid-February. What is more both T-bond and IRS curves steepened somewhat as the long ends underperformed the front ends. At the same time, the risk premium widened moderately as the Polish 10Y benchmark spread over the Bund increased to c280bp at the end of the month.

We think that yields on global markets may continue the upward trend seen in April, despite a short-term respite in recent days, amid hopes of improved economic activity and speculation that the Fed may lift interest rates in June/July. Domestic risks will probably keep the risk premium for Polish assets high. If Moody's keeps Poland's rating unchanged on May 13, it could provide temporary support for the bond market (in a recent Reuters' survey, 11 out of 24 analysts expected a downgrade). However, in general, we see limited room for yields to decline in the coming weeks.

Fiscal risk may recede into the background for some time, in our view, after the government confirmed its pledge to cut the fiscal deficit in the medium term under its new Convergence Programme, unless new economic data show a major disappointment and imply revenue growth falling short of target.



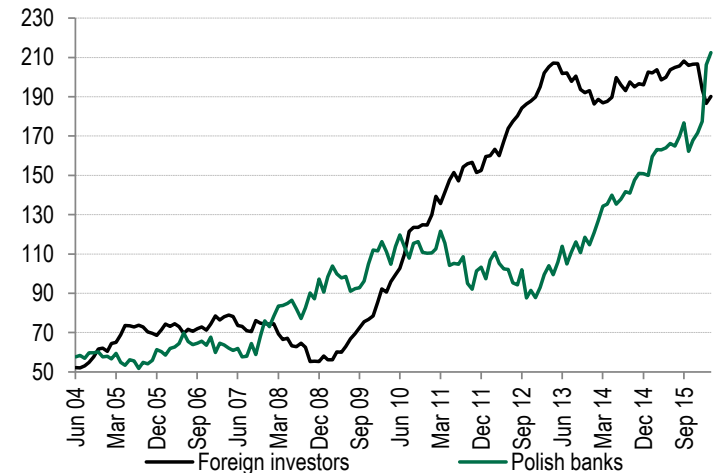
Source: Reuters, BZ WBK.



# Demand Corner: Foreign mutual funds accumulate 10Y benchmark bonds

- ❶ In March foreign investors bought Polish, PLN-denominated marketable bonds worth PLN3.6bn, after an outflow of more than PLN20bn in January-February. At the end of 1Q, the nominal value of their portfolio stood at cPLN190bn. Non-residents remained focused on the mid- and long-term benchmarks and the biggest monthly purchase was recorded for DS0726 (+PLN4.7bn to over PLN10bn, 59% of the outstanding issue). Nearly PLN1.5bn of this was mutual fund buying.
- ❷ Within the group of non-residents, the most active buyers were the commercial banks (+PLN4.5bn, the biggest monthly rise since comparable data are available). In contrast, central banks cut their exposure by PLN1.4bn (the third month in a row of selling and the biggest monthly reduction since August), led by Middle Eastern central banks. Mutual funds stopped disposing of Polish bonds and in March purchased debt with a PLN650mn nominal value. However, 1Q as a whole saw their biggest quarterly sales since the comparable data are available.
- ❸ As regards other investor groups, Polish banks continued to accumulate Polish bonds and bought PLN6.2bn of debt. The nominal value of their portfolio rose to a fresh all-time high of PLN212bn.

Polish PLN, marketable bonds held by foreign investors and Polish banks (PLNbn)



Source: Finance Ministry. BZ WBK.

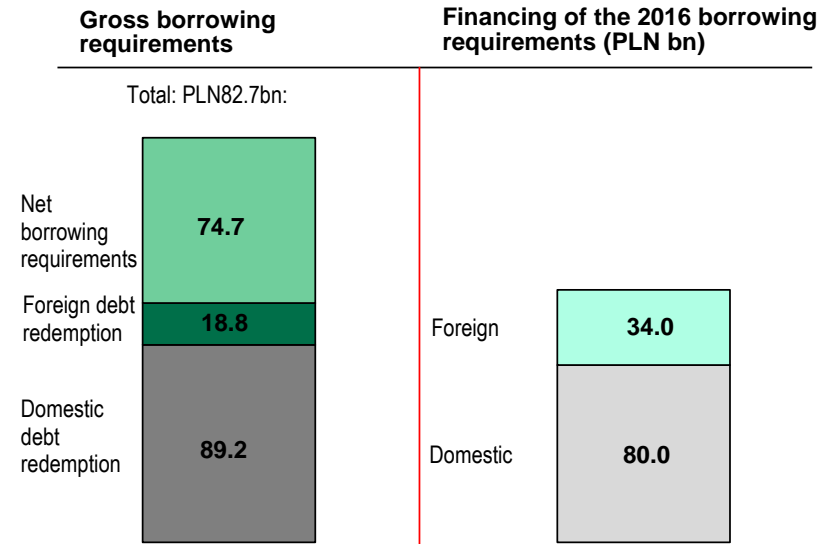
# Supply Corner: Poland T-bond issuance already exceeds 60% of the full-year target

In April, as in previous months, Poland successfully launched T-bonds on both domestic and international markets. Recorded demand was decent, with the bid-cover ratio higher than in March. Up to the end of April Poland has covered c62% of the total gross borrowing needs for 2016, selling nearly PLN61bn via regular, top-up and switch auctions on the domestic market. The Ministry of Finance was also very active on international markets, tapping them for EUR-denominated bonds worth €2.5bn in total and USD-denominated bonds worth US\$1.75bn.

The ministry has just released its issuance plan for May. It assumes two regular auctions, worth PLN4-11bn in total. At the first auction (May 5) the ministry sold 2Y OK1018 and 10Y DS0726 benchmarks worth PLN4.7bn, slightly more than originally planned (PLN4.5bn). Supply at the second auction (May 25) should be PLN2-6bn but will depend on market conditions, but the ministry will not offer the same bonds it is selling earlier in May.

May's offer of Treasury securities is moderate and we see no problem in selling that amount, in particular taking into account strong demand from Poland's banks. We estimate that after May (assuming total sales are at the maximum level) this year's gross borrowing needs could be c68% covered.

## Background of borrowing requirements' financing

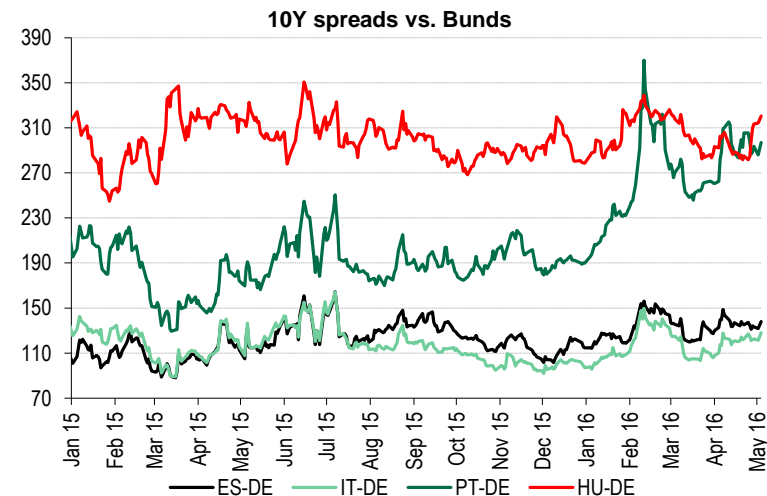
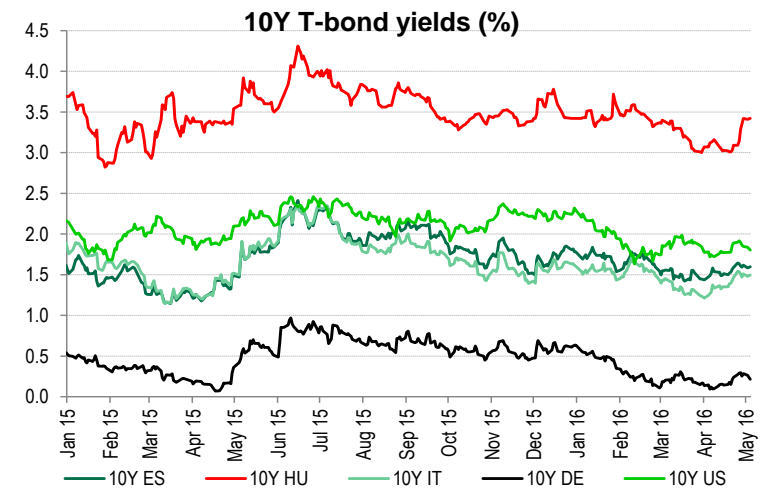


## Auction plan for May 2016

Auction Date	Settlement Date	T-bond/T-bills to Be Offered	Offer (PLN mn)	Sale (PLN mn)
5 May 2016	9 May 2016	OK1018/DS0726	2,500-4,500	4,703.9
25 May 2016	30 May 2016	To be announced; choice will depend on the market conditions	2,000-6,000	

# International Interest Rate Market: Strong US macro data lead to higher yields

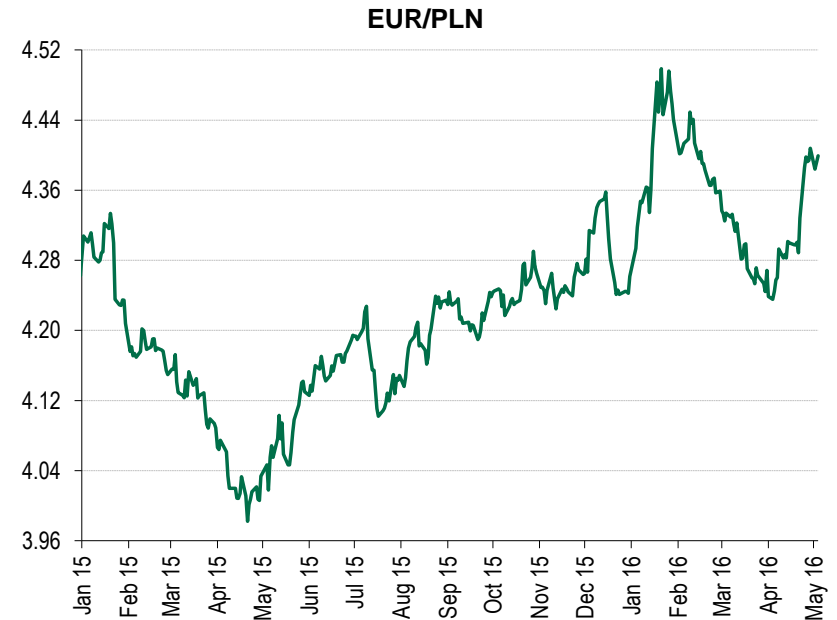
- In April, global yields increased markedly. This stemmed from the sharp rise in the oil price, the pick-up in global economic activity and perceptions of a reduced risk that the UK referendum will produce a vote to leave the EU. As a result, the credit risk for both peripheral and CEE debt markets increased visibly, with the spread over Bunds widening, in particular for Portugal (by over 30bp on a monthly basis).
- In mid-April Hungary's junk-rated yields fell below Poland's for the first time since 2002. We think this was caused by the interest rate differential, among other things. As expected, the Hungarian central bank (MNB) cut interest rates by 15bp at its April meeting, trimming the reference rate to 1.05%. The central bank said 'the sustainable achievement of the inflation target points to a further slight reduction in the policy rate'. However, more hawkish-than-expected comments from the MNB caused a significant increase in yields at the end of April.
- Macroeconomic data releases in Europe and the US will continue to be key, as further monetary policy adjustments by both the FOMC and ECB are strongly data dependent. We continue to see the US economy as strong enough to allow the FOMC to proceed with very gradual rate hikes. We maintain our call of another 25bp hike in June/July if the US macro data remain solid. This is clearly more hawkish than the market is currently pricing-in and it could generate upward pressure on yields.
- In our view the ECB's QE programme and attractive carry trade should support peripheral debt markets. However, the spread over Bunds should remain range bound, thanks, in part, to less favourable fiscal and political news flows.



Source: Reuters, ECB, Fed, BZ WBK.

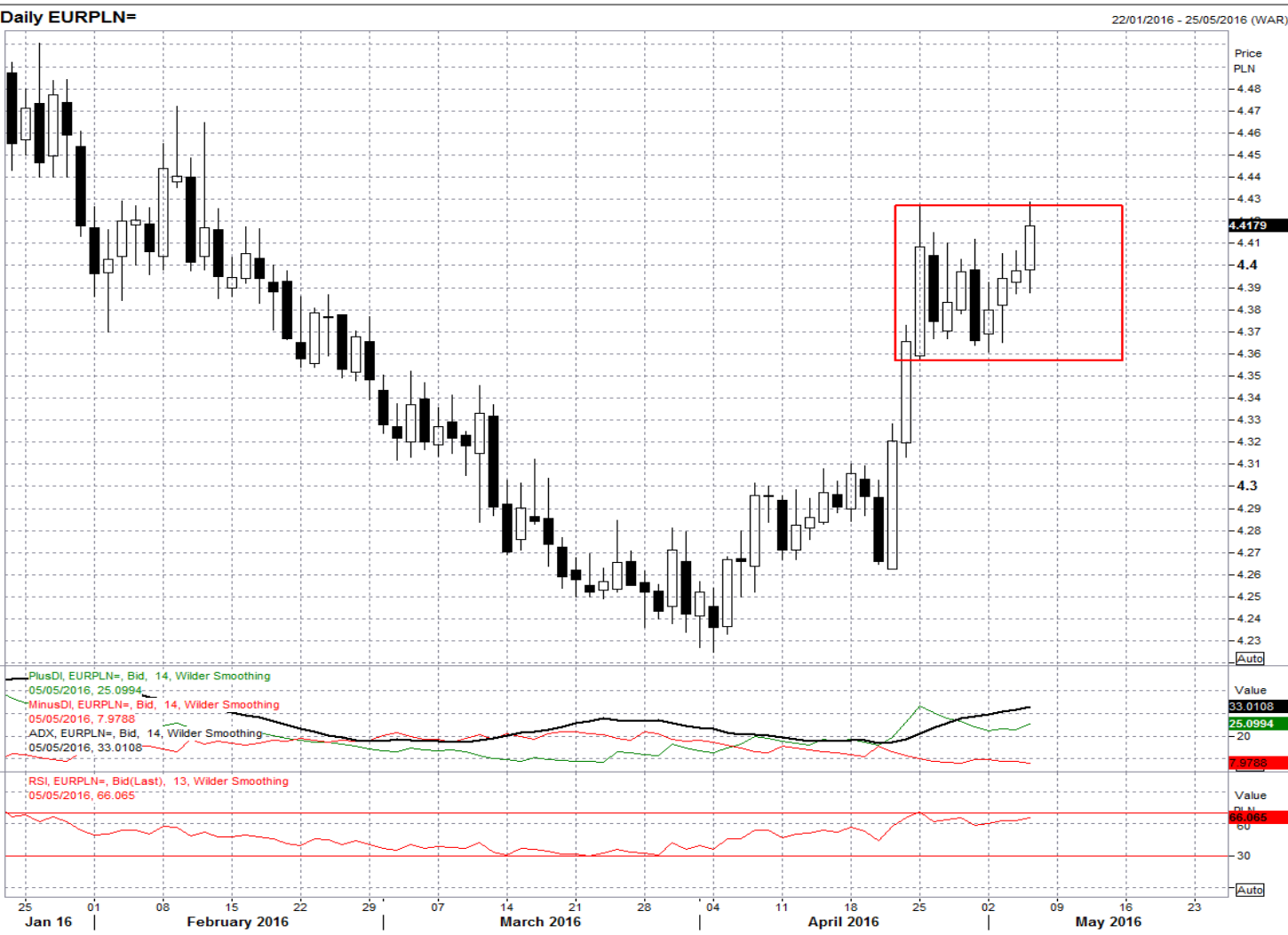
# Foreign Exchange Market: Sell in May?

- Our last month call saying that we did not expect the zloty to continue its appreciation proved correct and timely, as April's edition of our report was published just a day after EUR/PLN reached its new 2016 low. Since then the exchange rate has surged to 4.40 from 4.24, amid renewed concern about Poland's sovereign rating and the impact of the new FX bill on the banking system.
- Moody's may review its "A2" rating for Poland on May 13. We think the outlook could be revised to negative from stable and we do not expect the agency to cut the actual rating, but this may provide only temporary support for the Polish currency. Internal risk factors are still alive and another event that could negatively affect the zloty in the coming weeks is uncertainty ahead of the EU referendum in the United Kingdom.
- Although the zloty lost substantial ground in April, we are rather pessimistic as regards the room for a lasting recovery. We note the zloty has firmed against the euro in May only twice in the last ten years: in 2008 (when risky assets were rallying worldwide a few months before the US financial crisis) and in 2014 (on expected monetary policy easing in the Euro zone). We do not think the sentiment in the equity market is strong enough to provide much support for the zloty and the ECB is likely to refrain from taking more action in the short term. This is why we think there is limited room for the zloty to gain in the immediate future.



Source: Reuters, BZ WBK

# FX Technical Analysis Corner: EUR/PLN on the rise



- EUR/PLN jumped sharply in April even without the buy signal from the RSI (the oscillator did not finally manage to fall below 30pts).
- In early May the exchange rate is testing the upper boundary of the consolidation zone. There seems to be more upside potential as the ADX is climbing, suggesting the trend is strengthening. However, we do not expect EUR/PLN to rise above 4.50.

Source: Reuters, BZ WBK.

# FX Technical Analysis Corner: EUR/USD may stay high



- ▶ EUR/USD has been testing the 1.15-1.17 resistance area quite aggressively.
- ▶ The downward corrections in the upside trend became deeper and deeper, but the exchange rate managed to break out of the pattern.
- ▶ ADX is rising on both daily and weekly charts, indicating that the upside trend may still strengthen in the near future.

Source: Reuters, BZ WBK.

# Macroeconomic Forecasts

Poland		2013	2014	2015	2016E	1Q15	2Q15	3Q15	4Q15	1Q16E	2Q16E	3Q16E	4Q16E
GDP	PLNbn	1,656.3	1,719.1	1,790.1	1,845.9	413.1	431.0	437.1	508.4	423.8	442.3	449.2	530.6
GDP	%YoY	1.3	3.3	3.6	3.5	3.6	3.1	3.4	4.3	3.6	3.5	3.5	3.3
Domestic demand	%YoY	-0.7	4.9	3.3	3.1	2.9	3.0	3.0	4.5	3.5	1.7	2.8	4.2
Private consumption	%YoY	0.2	2.6	3.1	4.1	3.1	3.1	3.1	3.0	3.1	3.8	4.6	4.8
Fixed investment	%YoY	-1.1	9.8	6.1	3.5	11.8	5.8	4.4	4.4	4.5	4.0	3.0	3.0
Unemployment rate <sup>a</sup>	%	13.4	11.4	9.8	8.7	11.5	10.2	9.7	9.8	10.0	8.9	8.5	8.7
Current account balance	EURmn	-5,031	-8,303	-1,011	1,896	900	864	-2,348	-427	563	2,408	-1,672	596
Current account balance	% GDP	-1.3	-2.0	-0.2	0.4	-1.3	-0.4	-0.4	-0.2	-0.3	0.0	0.2	0.4
General government balance (ESA 2010)	% GDP	-4.0	-3.3	-2.6	-3.0	-	-	-	-	-	-	-	-
CPI	%YoY	0.9	0.0	-0.9	-0.5	-1.5	-0.9	-0.7	-0.6	-0.9	-0.8	-0.6	0.2
CPI <sup>a</sup>	%YoY	0.7	-1.0	-0.5	0.5	-1.5	-0.8	-0.8	-0.5	-1.1	-0.6	-0.3	0.5
CPI excluding food and energy prices	%YoY	1.2	0.6	0.3	0.0	0.4	0.3	0.3	0.2	-0.1	-0.1	0.0	0.5

Source: CSO, NBP, Finance Ministry, BZ WBK estimates. <sup>a</sup> at the end of the period

# Interest Rate and FX Forecasts

Poland		2013	2014	2015	2016E	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16E	3Q16E	4Q16E
Reference rate <sup>a</sup>	%	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	1.68	1.87	1.67	1.72	1.73	1.69	1.67	1.67	1.69
Yield on 2-year T-bonds	%	2.98	2.46	1.70	1.49	1.61	1.75	1.80	1.65	1.45	1.48	1.50	1.53
Yield on 5-year T-bonds	%	3.46	2.96	2.21	2.27	1.90	2.35	2.43	2.19	2.23	2.26	2.25	2.35
Yield on 10-year T-bonds	%	4.04	3.49	2.69	3.11	2.24	2.79	2.93	2.77	2.98	3.03	3.10	3.33
2-year IRS	%	3.10	2.51	1.72	1.54	1.65	1.85	1.78	1.58	1.54	1.57	1.52	1.52
5-year IRS	%	3.51	2.92	2.02	1.91	1.80	2.23	2.17	1.89	1.85	1.87	1.89	2.03
10-year IRS	%	3.86	3.34	2.41	2.47	2.06	2.57	2.62	2.38	2.32	2.36	2.48	2.73
EUR/PLN	PLN	4.20	4.18	4.18	4.37	4.20	4.09	4.19	4.26	4.37	4.36	4.41	4.33
USD/PLN	PLN	3.16	3.15	3.77	3.87	3.72	3.70	3.77	3.90	3.96	3.85	3.90	3.77
CHF/PLN	PLN	3.41	3.45	3.92	3.83	3.93	3.93	3.90	3.93	3.98	3.93	3.77	3.63
GBP/PLN	PLN	4.94	5.19	5.77	5.78	5.64	5.67	5.84	5.91	5.67	5.63	5.92	5.90

Source: CSO, NBP, Finance Ministry, BZ WBK estimates. <sup>a</sup> at the end of period



# Economic Calendar and Events

Date		Event:	Note:
6-May	PL	MPC meeting – interest rate decision	We expect the MPC to keep NBP rates on hold
12-May	PL	CPI for April	We expect the final CPI reading to be unchanged from the flash number of -1.1%y/y
	PL	M3 money supply for April	We expect double-digit growth of M3, higher than consensus (10.6% vs 9.9%)
13-May	PL	Flash GDP for 1Q16E	Our forecast is 3.6% y/y vs market expectations of 3.4% y/y
	PL	Core CPI for April	Our and the market's forecast is -0.3% y/y
	PL	C/A Balance of payments for March	We expect a surplus of €141mn, well below the consensus (€410mn)
	PL	Moody's will announce its decision on Poland's rating	
18-May	PL	Wages and employment for April	We expect employment growth of 2.8% y/y and wage growth of 3.7% y/y, close to consensus
19-May	PL	Industrial output for April	We expect 3.8% y/y, in line with the consensus
	PL	Construction output for April	We expect -14.1% y/y, below the consensus (-13.2% y/y)
	PL	Real retail sales for March	We expect 5.8% y/y, slightly above the consensus (5.1% y/y)
	PL	PPI inflation for March	We expect -1.3%YoY, in line with consensus
24-May	HU	MNB meeting – interest rate decision	We expect the MNB to leave rates unchanged
25-May	PL	T-bond auction	Offer: PLN2-6bn
27-May	PL	Minutes from May MPC meeting	
TBA	PL	Registered unemployment rate for April	We expect further decline to 9.6%, in line with consensus
31-May	PL	GDP growth for 1Q16	Our forecast is 3.6% y/y
	PL	Investment for 1Q16	Our forecast is 4.5% y/y, well above market consensus of 3.0% y/y
	PL	Private consumption for 1Q16	Our forecast is 3.1% y/y. close to market consensus at 3.2% y/y

Source: CB, Markit, CSO, Finance Ministry

# Annex

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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

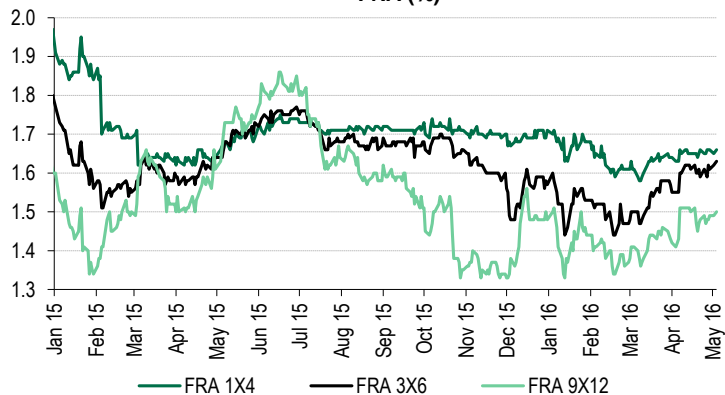
## Money market rates (%)

	Reference	Poland	WIBOR (%)				OIS (%)				FRA (%)			
	rate (%)	(%)	1M	3M	6M	12M	1M	3M	6M	12M	1x4	3x6	6x9	9x12
End of April	1.50	1.11	1.57	1.67	1.74	1.76	1.42	1.37	1.29	1.24	1.66	1.61	1.54	1.49
Last 1M change (bp)	0	-38	1	0	0	0	18	9	7	5	1	3	5	4
Last 3M change (bp)	0	-17	-3	-3	-1	-1	3	4	8	9	-2	8	8	5
Last 1Y change (bp)	0	-41	-6	2	8	8	-3	-7	-14	-19	2	-2	-9	-17

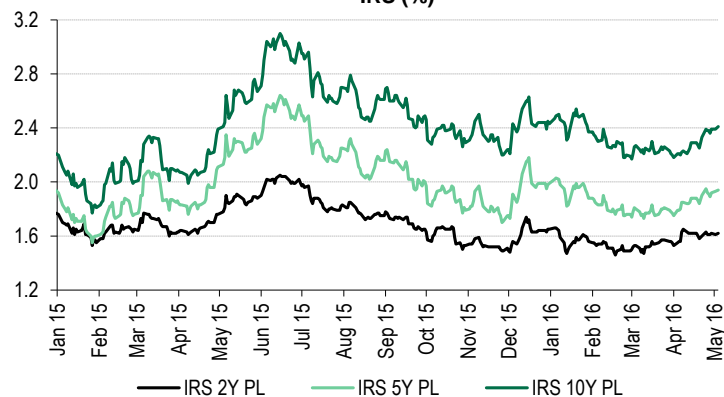
## Bond and IRS market (%)

	BONDS			IRS			Spread BONDS / IRS (bp)		
	2Y	5Y	10Y	2Y	5Y	10Y	2Y	5Y	10Y
End of April	1.49	2.25	3.06	1.62	1.92	2.39	-13	33	67
Last 1M change (bp)	6	8	21	6	13	16	0	-5	5
Last 3M change (bp)	-3	-12	-9	6	4	2	-9	-16	-11
Last 1Y change (bp)	-16	5	47	-14	-17	4	-2	22	43

FRA (%)



IRS (%)



Source: Reuters, BZ WBK

## 2. Polish Bonds: Supply Recap

### Total issuance in 2016 by instrument (in PLN mn, nominal terms)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
<b>T-bond auctions</b>	12,629	16,221	8,387	14,891	10,000	8,500	7,500	3,600	4,000	10,000	3,000		98,729
<b>T-bill auctions</b>	2,400	2,390	1,000			700	500		700				7,690
<b>Retail bonds</b>	200	600	175	167	160	192	200	215	200	250	1100	250	3,709
<b>Foreign bonds/credits</b>	7,700			9,883						3,206			20,788
<b>Pre-financing and financial resources at the end of 2015</b>	36,500												36,500
<b>Total</b>	<b>59,429</b>	<b>19,211</b>	<b>9,562</b>	<b>24,941</b>	<b>10,160</b>	<b>9,392</b>	<b>8,200</b>	<b>3,815</b>	<b>4,900</b>	<b>13,456</b>	<b>4,100</b>	<b>250</b>	<b>167,416</b>
<b>Redemption</b>	13,680	11,645	153	18,494	146	124	8,795	8,688	2,590	23,573	4,884	910	93,683
<b>Net inflows</b>	<b>45,749</b>	<b>7,566</b>	<b>9,409</b>	<b>6,447</b>	<b>10,014</b>	<b>9,268</b>	<b>-595</b>	<b>-4,873</b>	<b>2,310</b>	<b>-10,118</b>	<b>-784</b>	<b>-660</b>	<b>73,734</b>
<b>Rolled-over T-bonds</b>			8,590										8,590
<b>Buy-back of T-bills/ FX-denominated bonds</b>													0
<b>Total</b>	<b>45,749</b>	<b>7,566</b>	<b>17,999</b>	<b>6,447</b>	<b>10,014</b>	<b>9,268</b>	<b>-595</b>	<b>-4,873</b>	<b>2,310</b>	<b>-10,118</b>	<b>-784</b>	<b>-660</b>	<b>82,324</b>
<b>Coupon payments from domestic debt</b>	1,084			3,767			3,306		1,295	5,487			14,940

Note: Our forecasts = shaded area

Source: MF, BZ WBK

## 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	13,451		229	13,680	0	13,680
February	0		647	647	10,999	11,645
March	0		153	153	0	153
April	12,637		136	12,773	915	13,688
May	0		146	146	0	146
June	0		124	124	0	124
July	9,931		226	10,156	911	11,067
August	3,689	2,400	199	6,288	0	6,288
September	0	2,390	200	2,590	0	2,590
October	22,420		242	22,661	911	23,572
November	0		1,056	1,056	1,628	2,684
December	0		210	210	0	210
<b>Total 2016</b>	<b>62,127</b>	<b>4,790</b>	<b>3,567</b>	<b>70,485</b>	<b>15,364</b>	<b>85,848</b>
<b>Total 2017</b>	<b>72,603</b>		<b>2,485</b>	<b>75,087</b>	<b>11,728</b>	<b>86,815</b>
<b>Total 2018</b>	<b>78,877</b>		<b>1,313</b>	<b>80,190</b>	<b>12,977</b>	<b>93,167</b>
<b>Total 2019</b>	<b>63,811</b>		<b>1,237</b>	<b>65,048</b>	<b>23,512</b>	<b>88,559</b>
<b>Total 2020</b>	<b>65,481</b>		<b>634</b>	<b>66,115</b>	<b>21,805</b>	<b>87,920</b>
<b>Total 2021+</b>	<b>221,698</b>		<b>1,749</b>	<b>223,447</b>	<b>134,266</b>	<b>357,713</b>

Source: MF, BZ WBK.

## 2. Polish Bonds: Supply Recap (cont.)

Scheduled wholesale bond redemptions by holders (data at the end of March 2016, in PLN mn)

	Foreign investors	Domestic banks	Insurance funds	Pension funds	Mutual funds	Individuals	Non-financial sector	Other	Total
<b>Q1 2016</b>	8,007	2,151	2,027	54	579	26	42	459	13,346
<b>Q2 2016</b>	4,631	4,876	1,710	180	361	15	45	820	12,637
<b>Q3 2016</b>	4,113	5,717	1,923	75	1,963	26	44	710	14,571
<b>Q4 2016</b>	5,736	12,221	1,825	62	1,037	7	29	1,502	22,420
<b>Total 2016</b>	<b>22,486</b>	<b>24,966</b>	<b>7,485</b>	<b>371</b>	<b>3,940</b>	<b>74</b>	<b>160</b>	<b>3,491</b>	<b>62,973</b>
	36%	40%	12%	1%	6%	0%	0%	6%	100%
<b>Total 2017</b>	24,119	30,005	7,158	597	5,068	108	96	5,453	72,603
	33%	41%	10%	1%	7%	0%	0%	8%	100%
<b>Total 2018</b>	17,804	39,367	4,203	432	8,303	77	163	6,752	77,101
	23%	51%	5%	1%	11%	0%	0%	9%	100%
<b>Total 2019</b>	17,977	30,597	5,803	176	4,436	82	148	4,593	63,811
	28%	48%	9%	0%	7%	0%	0%	7%	100%
<b>Total 2020</b>	23,479	25,074	4,200	135	6,917	64	64	3,861	63,794
	37%	39%	7%	0%	11%	0%	0%	6%	100%
<b>Total 2021+</b>	92,290	64,600	24,239	280	20,622	362	285	7,941	210,618
	44%	31%	12%	0%	10%	0%	0%	4%	100%

Source: MF, BZ WBK.

## 3. Polish Bonds: Demand Recap

### Holders of marketable PLN bonds

	Nominal value (PLN bn)			Nominal value (PLN bn)			% change in March			Share of total in March (%)
	End Mar'16	End Feb'16	End Jan'16	End 3Q 2015	End 2014	End 2013	MoM	3-mth	YoY	
<b>Domestic investors</b>	358.0	352.6	321.2	325.5	295.9	381.2	1.5	4.7	15.8	65.3 (-0.1)
<b>Commercial banks</b>	212.5	206.2	177.4	176.7	150.8	114.7	3.0	23.9	30.3	38.8 (0.5pp)
<b>Insurance companies</b>	51.1	52.0	51.6	52.5	52.8	52.0	-1.8	-2.1	-2.5	9.3 (-0.3pp)
<b>Pension funds</b>	1.9	1.9	2.0	3.0	3.3	125.8	0.0	-22.8	-38.4	0.4
<b>Mutual funds</b>	48.7	48.6	46.6	49.7	46.9	46.7	0.3	3.5	0.4	8.9 (-0.1pp)
<b>Others</b>	43.8	43.9	43.6	43.7	42.0	42.0	-0.2	0.2	4.3	8.0 (-0.2pp)
<b>Foreign investors*</b>	190.2	186.5	193.7	208.2	196.0	193.2	1.9	-8.0	-6.7	34.7 (0.1pp)
<b>Banks</b>	19.3	14.8	16.5	13.5	9.9	n.a.	30.6	51.9	94.9	3.5 (0.8pp)
<b>Central banks</b>	27.7	29.2	29.3	28.3	16.4	n.a.	-4.9	-7.9	36.4	5.1 (-0.4pp)
<b>Public institutions</b>	9.5	9.4	9.4	9.7	8.1	n.a.	0.4	1.1	7.5	1.7
<b>Insurance companies</b>	11.9	11.4	12.2	11.6	10.7	n.a.	4.1	-4.6	7.7	2.2
<b>Pension funds</b>	13.8	13.4	13.2	13.0	13.0	n.a.	2.9	-2.1	4.5	2.5
<b>Mutual funds</b>	41.7	41.1	47.4	64.7	78.1	n.a.	1.6	-24.0	-47.9	7.6
<b>Hedge funds</b>	0.04	0.04	0.04	0.1	1.1	n.a.	6.5	6.5	-96.0	0.0
<b>Non-financial sector</b>	6.7	6.6	6.4	12.2	8.2	n.a.	2.0	-26.2	-18.3	1.2
<b>Others</b>	17.2	17.7	17.8	19.5	14.3	n.a.	-2.8	-9.3	1.4	3.1 (-0.1)
<b>TOTAL</b>	548.1	539.2	514.9	533.7	491.8	574.3	1.7	12.9	6.9	100

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

Source: MF, BZ WBK.

## 4. Euro Zone Bonds: Supply Recap

Euro zone: 2016 net and gross supply by country vs 2015 (€ bn)

	2016 gross issuance	% change (vs 2015)	2016 net issuance	% change (vs 2015)	YTD bond issuance completion
Austria	19.4	14	5.6	50	54%
Belgium	33.6	3	8.0	84	62%
Finland	15.8	58	5.9	169	59%
France	187.0	0	60.5	-14	46%
Germany	168.6	16	0.0	-100	34%
Greece	-	-	-	-	-
Ireland	10.8	-20	2.7	-76	61%
Italy	221.9	-10	38.6	-9	44%
Netherlands	36.8	-23	8.5	5	29%
Portugal	11.9	-34	5.1	-55	42%
Spain	138.8	0	45.5	6	38%
<b>Total</b>	<b>844.5</b>	<b>-1</b>	<b>180.3</b>	<b>-1</b>	<b>43%</b>

\* YTD is supply since January 1, 2016

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)	
	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017
<b>Poland</b>	3.7	3.6	0.0	1.6	-0.3	-0.9	-2.6	-3.1	52.0	52.7
<b>Czech Republic</b>	2.1	2.6	0.5	1.4	-1.5	-1.3	-0.7	-0.6	41.3	40.9
<b>Hungary</b>	2.5	2.8	0.4	2.3	5.0	4.5	-2.0	-2.0	74.3	73.0
<b>EU</b>	1.8	1.9	0.3	1.5	2.2	2.1	-2.1	-1.8	86.4	85.5
<b>Euro zone</b>	1.6	1.8	0.2	1.4	3.7	3.6	-1.9	-1.6	92.2	91.1
<b>Germany</b>	1.6	1.6	0.3	1.5	8.5	8.3	0.2	0.1	68.6	66.3

### Main market indicators (% , end of period)

	Reference rate (%)		3M market rate (%)		10Y yields (%)		10Y spread vs Bund (bp)		CDS 5Y	
	2015	End-Apr 2016	2015	End-Apr 2016	2015	End-Apr 2016	2015	End-Apr 2016	2015	End-Apr 2016
<b>Poland</b>	1.50	1.50	1.72	1.67	2.94	3.06	230	277	75	85
<b>Czech Republic</b>	0.05	0.05	0.29	0.29	0.60	0.50	-4	21	50	41
<b>Hungary</b>	1.35	1.05	1.35	1.05	3.42	3.42	279	313	164	144
<b>Euro zone</b>	0.05	0.00	-0.13	-0.251						
<b>Germany</b>					0.63	0.29			12	17

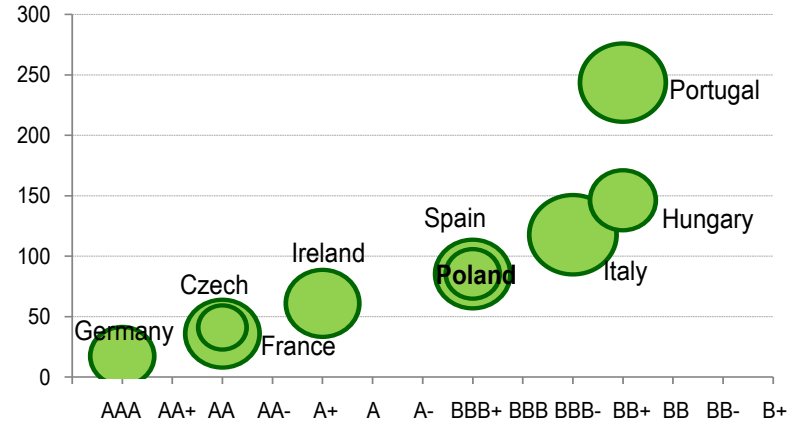
Source: EC – Spring 2016, statistics offices, central banks, Reuters, BZ WBK.

# 5. Poland vs. Other Countries (cont.)

**Sovereign ratings**

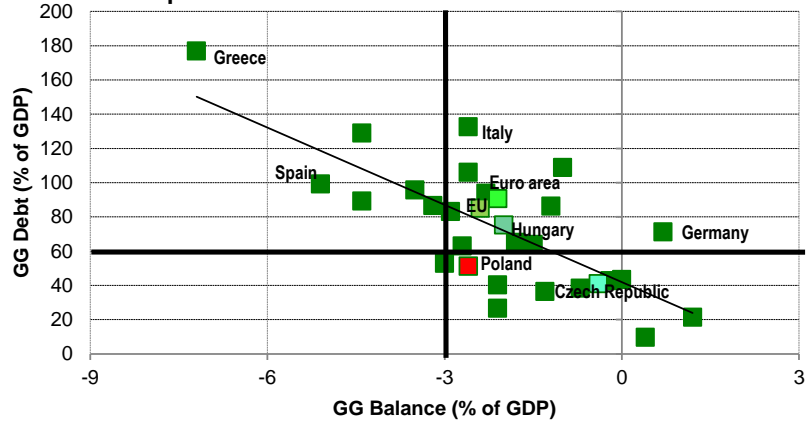
	S&P		Moody's		Fitch	
	rating	outlook	rating	outlook	rating	outlook
Poland	BBB+	negative	A2	stable	A-	stable
Czech	AA-	stable	A1	stable	A+	stable
Hungary	BB+	stable	Ba1	positive	BB+	positive
Germany	AAA	stable	Aaa	stable	AAA	stable
France	AA	negative	Aa2	stable	AA	stable
UK	AAA	negative	Aa1	stable	AA+	stable
Greece	B-	stable	Caa3	stable	CCC	stable
Ireland	A+	stable	Baa1	positive	A	stable
Italy	BBB-	stable	Baa2	stable	BBB+	stable
Portugal	BB+	stable	Ba1	stable	BB+	stable
Spain	BBB+	stable	Baa2	stable	BBB+	stable

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



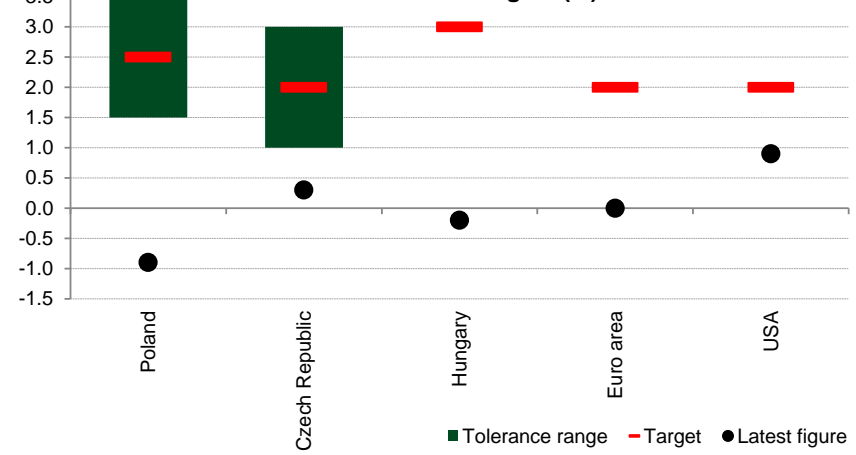
Note: Size of bubbles reflects the debt/GDP ratio

**Fiscal position of the EU countries at the end of 2015**

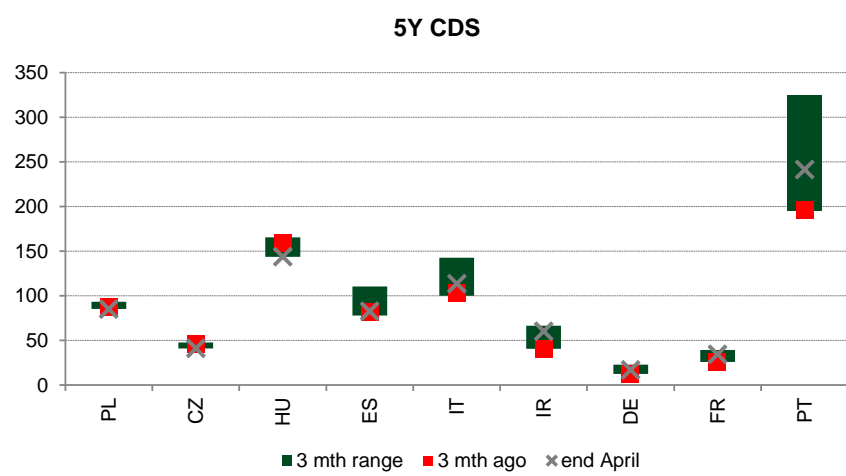
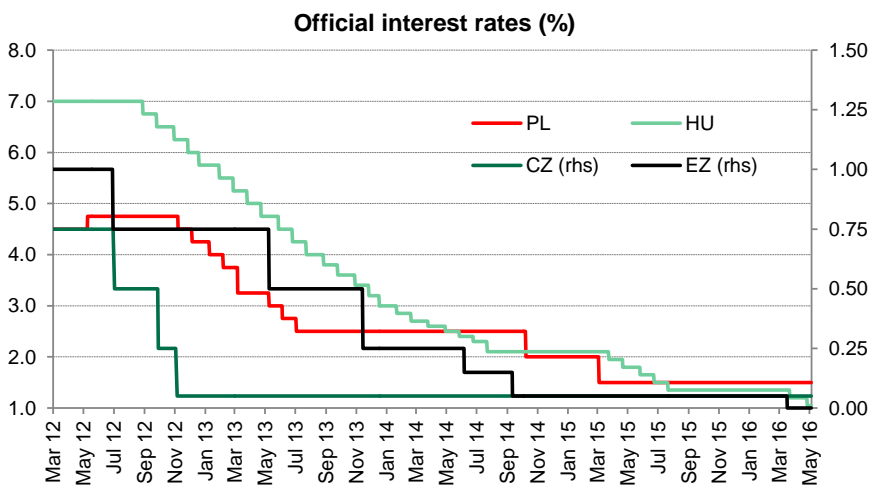
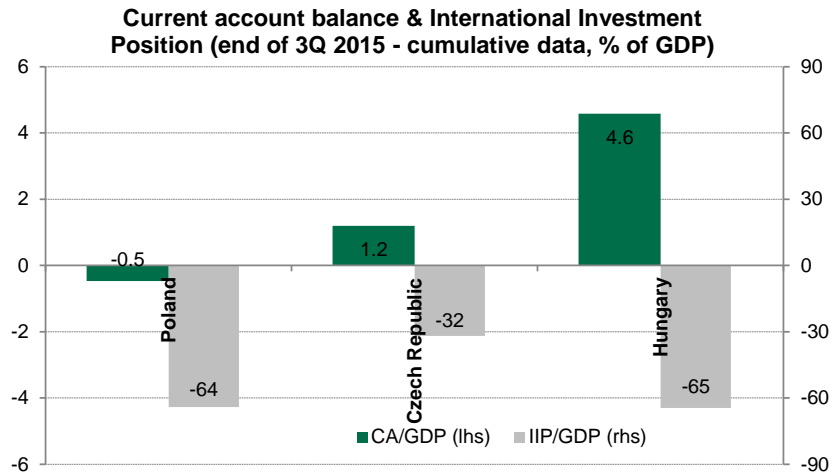
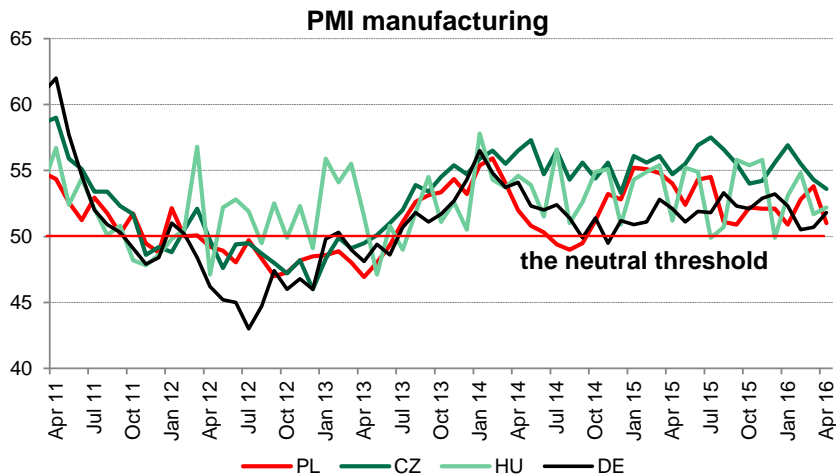


Source: Rating agencies, Reuters, EC, BZ WBK.

**Inflation rates vs targets (%)**

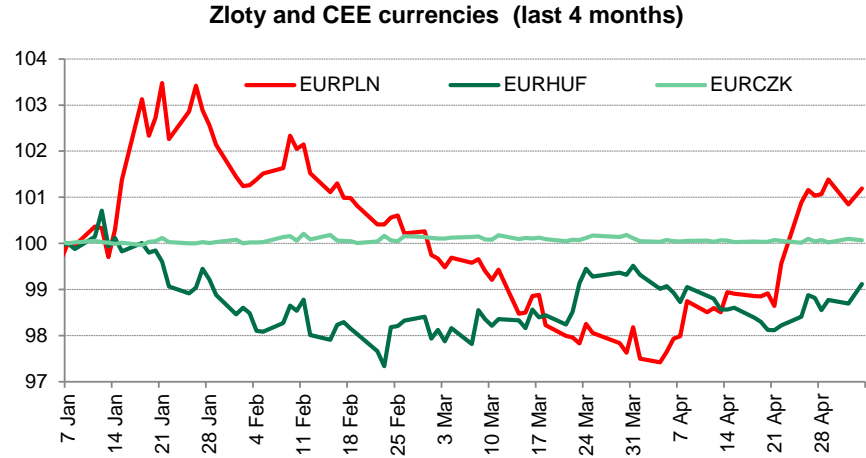
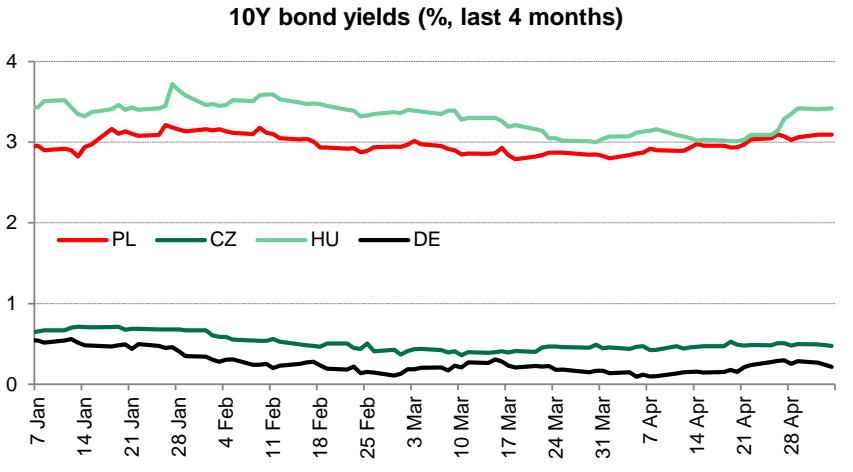
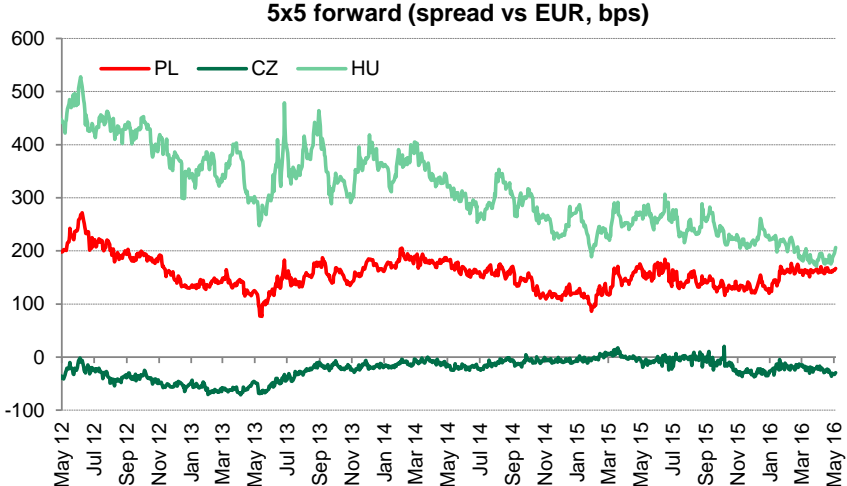
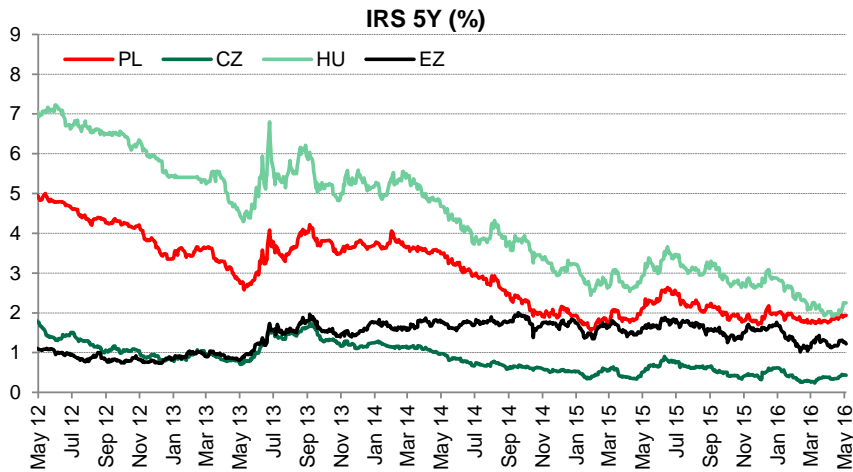


# 5. Poland vs. Other Countries (cont.)



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

# 5. Poland vs. Other Countries (cont.)



Source: Reuters, BZ WBK.

## 6. Central Bank Watch

		Last	2015	2016E	Expected changes (bp)			Comments
					1M	3M	6M	
<b>Euro zone</b>	Forecast	0.00	0.05	0.00				As expected, the ECB kept monetary policy unchanged, however moderate, but improving nominal growth and super-loose ECB policy generates increasing potential risk. We currently expect no fresh measures from the ECB at the June meeting and there is no May meeting.
	Market implied »				-1	-2	-3	
<b>UK</b>	Forecast	0.50	0.50	0.75				We expect the BoE to keep rates unchanged in the light of UK macro data that have remained lukewarm-to-healthy. In our view, the UK's EU referendum has provided a convenient narrative to explain the fall in UK market rates.
	Market implied »				1	1	4	
<b>US</b>	Forecast	0.25-0.50	0.25-0.50	1.00				The April FOMC statement did not close the door to a hike at the next few meetings. Comments from Fed members also suggest that an interest rate hike is a real option in the near future. All in all, we expect a 25bp rate hike to be delivered in June/July if the US macro data remain solid.
	Market implied »				44	63	91	
<b>Poland</b>	Forecast	1.50	1.50	1.50				We think there will be no surprises at all at the MPC meeting. Interest rates should remain on hold, in our view, and the tone of the MPC's statement should not change much from March. Recent comments by MPC members clearly suggest that they see no need for an interest rate reduction in the nearest months.
	Market implied »				-1	-4	-11	
<b>Czech Republic</b>	Forecast	0.05	0.05	0.05				The Czech National Bank (CNB) kept monetary conditions unchanged in May. We think it is likely to reiterate its medium-term commitment to a EUR/CZK floor. The new CNB macro forecast will be published this month. Currently, the inflation rate is 60bp below the latest CNB forecast and this should be reflected in the new forecast.
	Market implied »				0	-3	-8	
<b>Hungary</b>	Forecast	1.05	1.35	1.00				In April, the Hungarian central bank (MNB) continued its monetary easing, cutting rates by another 15bp. The base rate was trimmed to 1.05%, a new minimum level. However, the MNB surprised the market with its unexpectedly hawkish statement. The new forward guidance suggests that the room for more rate cuts may be limited and that expectations of more aggressive easing are overdone.
	Market implied »				-15	-25	-26	

This analysis is based on information available through May 5, 2016 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
<b>Long / Buy</b>	Buy the bond for an expected average return of at least 10bp in 3 months (decline in the yield rate), assuming a directional risk.	<b>Long / Receive fixed rate</b>	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.
<b>Short / Sell</b>	Sell the bond for an expected average return of at least 10bp in 3 months (increase in the yield rate), assuming a directional risk.	<b>Short / Pay fixed rate</b>	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		
<b>Long a spread / Play steepeners</b>	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).		
<b>Short a spread / Play flatteners</b>	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		
<b>Long / Buy</b>	Appreciation of a given currency with an expected return of at least 5% in 3 months.		
<b>Short / Sell</b>	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.

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