

EYEOPENER

27 September 2017

Government approves 2018 budget draft

- **Government approved 2018 budget draft**
- **Zloty, forint and ruble under pressure, EURUSD at its lowest since late August**
- **No big changes on the bond market**
- **Today Czech central bank decision and next US data**

The government agreed yesterday on the 2018 budget draft. It assumes a fiscal deficit of PLN41.5bn, revenues at PLN335.7bn and expenditures at PLN397.2bn. The underlying macro assumptions look realistic. The real GDP growth at 3.8% is slightly above our forecast (3.6%), but it is the other way round when it comes to 2017 so the assumed nominal level of GDP in 2018 is only a bit lower than our estimate. Some assumptions, like wage growth, even seem rather conservative. Total budget revenues are to grow by 3.5% from the expected 2017 full-year result, which seems feasible. Tax revenues are assumed to grow PLN20.5b and their rate of growth is 6.6% which is a bit above the nominal pace of GDP.

Project assumes that closing of tax revenue gap should add PLN10.8bn to the budget revenues. The higher budget revenues will be reached owing to new tax regulation, which should help to improve tax collection. We estimate that closing of the VAT gap will add PLN11-13bn to the budget revenues this year (assuming that current trend will maintain). In our opinion, it means that 2018 budget plan looks realistic. The expenditures limit for 2018 will be raised by PLN20.4bn (5.4% y/y). The main part of this amount will be consumed by higher cost of key governments programs (decrease of the state pension age, child benefit subsidies program 500+, house subsidies program dwelling+, defense expenditures). It means that the room for the other expenditures (like investments) will be limited. Expenditures to GDP ratio is expected to decrease to 19.3%, to lowest level since 2015.

The draft assumes a 2018 general government (GG) deficit of 2.7% GDP, which would constitute a moderate fiscal easing despite high GDP growth. As a reminder, the spring update of the Convergence Programme had GG deficit at 2.9% for 2017 and 2.5% for 2018. We feel that as long as the figure is markedly below 3% GDP it should not worry neither investors nor the European Commission. However, no progress in fiscal consolidation at the time of supportive economic climate raises doubts about fiscal performance when the next cyclical slowdown comes.

On Tuesday, core debt markets remained relatively stable for most of the day. Data on consumer sentiment in the US showed

a slight deterioration, which did not have a significant impact on bonds. Yields went up slightly in the early afternoon, responding to the upside opening on the US stock market. Overall, the volatility across the day was minor, the US yields rose 1-2bp across the curve, whilst the German one by only 1bp at the long end and belly.

Fed governor Janet Yellen had a speech on Tuesday evening. She said that rates still need to be raised despite uncertain inflation outlook. In her view, normalization of monetary policy cannot wait until inflation goal is reached. Her comment is in line with the tone of the last FOMC meeting, where American central bankers maintained the declaration that there will be another rate hike still this year.

The domestic market followed the US debt by shifting the bond curve and the IRS curve by 2bp at the belly and long end of the curve and by 1bp at the short end. Polish investors ignored the information on the budget 2018 approval. Also the Monday afternoon information that the President withdrew from the court bills did not influence the market.

Over the next few days, we expect a slight rebound in domestic bond yields after a significant decline at the beginning of the week. In our opinion, this move will concern primarily the long end and belly of the curve.

On Tuesday the dollar gained as a result of market pricing the outcome of the German elections. In effect, EURUSD fell to 1.178 from 1.186, breaching the lower end of the horizontal trend within which it has been staying since the end of August.

When it comes to the domestic currency, the zloty weakened vs. the euro and the dollar. Since the Friday closing, four out of the five weakest EM currencies are from the CEE region (the zloty performing the worst). This suggests that political issues in Europe can exert some negative pressure on the market. Yesterday EURPLN rose to 4.295 and USDPLN to 3.65. EURHUF rebounded to 311 from about 310. The ruble also weakened given the downwards correction after the recent oil price increase.

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FX market

Today's opening

EURPLN	4.2907	CZKPLN	0.1649
USDPLN	3.6458	HUFPLN*	1.3775
EURUSD	1.1769	RUBPLN	0.0629
CHFPLN	3.7511	NOKPLN	0.4612
GBPPLN	4.8846	DKKPLN	0.5767
USDCNY	6.6373	SEKPLN	0.4479

*for 100HUF

Last session in the FX market

26/09/2017

	min	max	open	close	fixing
EURPLN	4.271	4.296	4.280	4.291	4.282
USDPLN	3.604	3.651	3.614	3.642	3.6234
EURUSD	1.176	1.186	1.185	1.178	-

Interest rate market

26/09/2017

T-bonds on the interbank market**

Bond (term)	%	Change (bps)	Last auction	Paper offered	Average yield
OK0419 (2Y)	1.67	1	23.03.2017	OK0419	2.049
PS0422 (5Y)	2.62	2	23.03.2017	PS0422	2.945
DS0727 (10Y)	3.30	2	23.03.2017	DS0727	3.568

IRS on the interbank market**

Term	PL	US	EZ
%	Change (bps)	%	Change (bps)
1L	1.79	1	-0.26
2L	1.96	2	-0.18
3L	2.09	2	-0.06
4L	2.23	1	0.07
5L	2.36	2	0.21
8L	2.67	4	0.62
10L	2.82	3	0.85

WIBOR rates

Term	%	Change (bps)
O/N	2.03	27
T/N	1.96	20
SW	1.61	0
2W	1.62	0
1M	1.66	0
3M	1.73	0
6M	1.81	0
9M	1.83	0
1Y	1.85	0

FRA rates on the interbank market**

Term	%	Change (bps)
1x4	1.73	0
3x6	1.75	0
6x9	1.80	1
9x12	1.85	0
3x9	1.84	0
6x12	1.88	0

Measures of fiscal risk

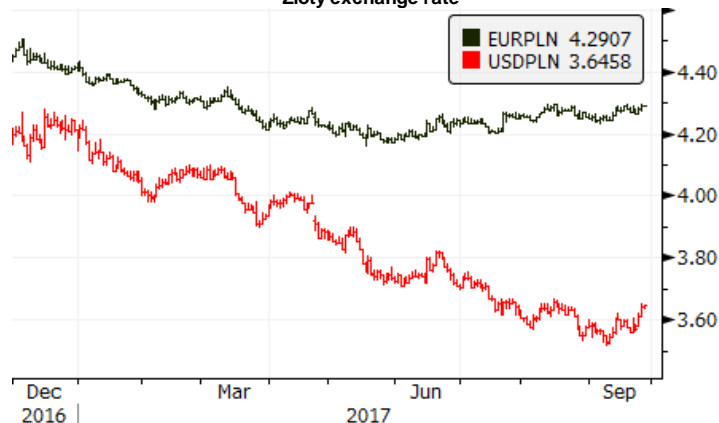
Country	CDS 5Y USD		10Y spread*	
	Level	Change (bps)	Level	Change (bps)
Poland	71	-1	2.88	1
France	21	0	0.29	-1
Hungary	116	1	2.05	-2
Spain	64	-2	1.18	-2
Italy	144	1	1.69	-2
Portugal	131	-1	1.96	-2
Ireland	32	-1	0.29	-1
Germany	13	1	-	-

* 10Y treasury bonds over 10Y Bunds

**Information shows bid levels on the interbank market at the end of the trading day

Source: Bloomberg

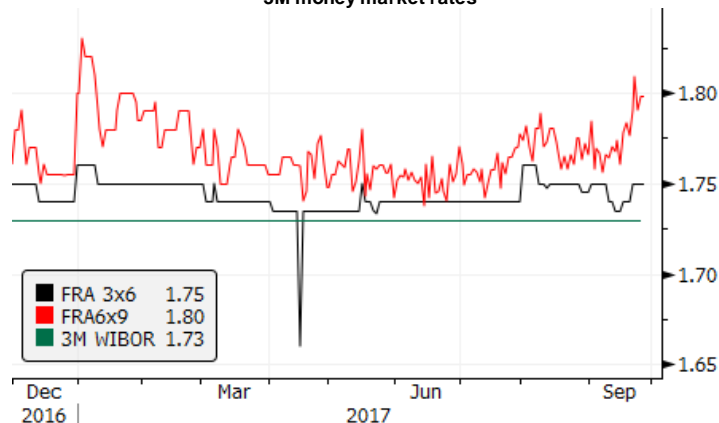
Zloty exchange rate



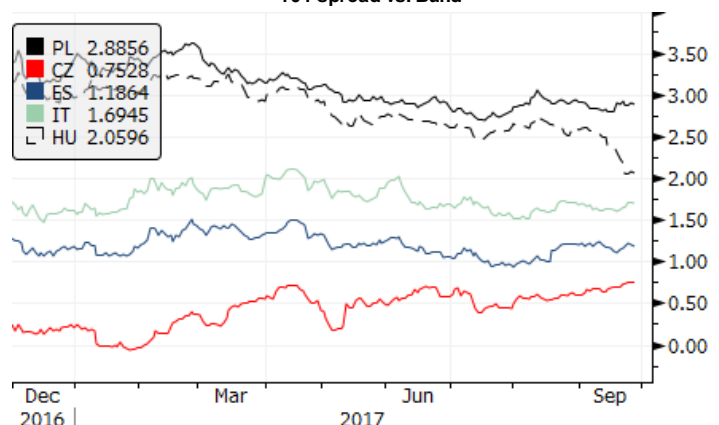
T-bonds yields



3M money market rates



10Y spread vs. Bund



Economic calendar

Economic calendar									
TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST		ACTUAL VALUE	LAST VALUE*	
					MARKET	BZWBK			
FRIDAY (22 September)									
9:30	DE	Flash PMI – manufacturing	Sep	pts	59.0	-	60.6	59.3	
9:30	DE	Flash PMI – services	Sep	pts	53.7	-	55.6	53.5	
10:00	EZ	Flash PMI – manufacturing	Sep	pts	57.2	-	58.2	57.4	
10:00	EZ	Flash PMI – services	Sep	pts	54.8	-	55.6	54.7	
10:00	PL	Unemployment rate	Aug	%	7.0	7.0	7.0	7.1	
14:00	PL	Money supply	Aug	% y/y	5.2	5.3	5.5	5.0	
MONDAY (25 September)									
10:00	DE	Ifo index	Sep	pts	115.9	-	115.2	115.9	
16:30	US	Dallas Fed index	Sep	pts	13.0	-	21.3	17.0	
TUESDAY (26 September)									
16:00	US	New home sales	Aug	% m/m	2.9	-	-3.4	-9.4	
16:00	US	Consumer confidence	Sep	pts	120	-	119.8	122.9	
WEDNESDAY (27 September)									
13:00	CZ	Czech central bank decision		%	0.25	-		0.25	
14:30	US	Durable goods orders	Aug	% m/m	0.9	-		-6.8	
16:00	US	Pending home sales	Aug	% m/m	-0.3	-		-0.8	
THURSDAY (28 September)									
14:00	DE	Flash CPI	Sep	% y/y	1.8			1.8	
14:30	US	GDP	2Q	% q/q	3.1	-		3.0	
14:30	US	Initial jobless claims	week	k	-	-		259	
FRIDAY (29 September)									
11:00	EZ	Flash CPI	Sep	% y/y	1.6	-		1.5	
14:00	PL	Flash CPI	Sep	% y/y	2.0	1.9		1.8	
14:30	US	Consumer spending	Aug	% m/m	0.1	-		0.3	
14:30	US	Personal income	Aug	% m/m	0.3	-		0.4	
15:45	US	Chicago PMI index	Sep	pts	57.5	-		58.9	
16:00	US	Michigan index	Sep	pts	95.2	-		95.3	

Source: BZ WBK, Reuters, Bloomberg

* in case of the revision the data is updated

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