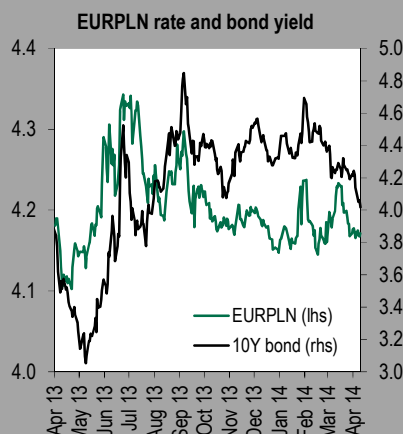
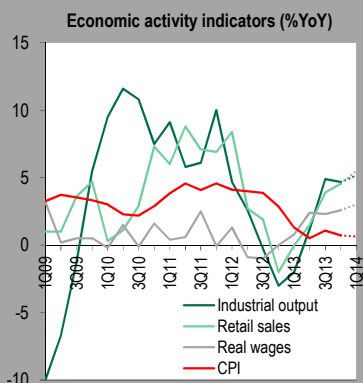


MACROscope

Polish Economy and Financial Markets

April 2014

Spring-time optimism



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■ **Polish economic data released recently provide clear support for the spring optimism regarding the pace of the ongoing revival.** Decent growth of the industrial output and visible rebound in construction and assembly output (even if partly driven by the favourable weather conditions), acceleration of the retail sales, high pace of growth of exports, and significant improvement in the labour market – all of these factors justify hopes that pace of GDP growth in Q1 exceeded 3% for the first time in two years. Additionally, these positive trends should be continued in the following quarters and the Polish economy may be growing by almost 4%YoY at the end of the year (and 3.5% on average in 2014). We are pleased to note that the scenario anticipated by us for some time has been actually materializing – quickly growing external demand is being accompanied by two additional growth engines – private consumption and investments. Consequently, this year's economic growth is likely to be not only faster, but also more balanced and less susceptible to any turbulences.

■ **Recovery in the world's most developed economies is also gaining steam.** The IMF claims in its recent update of global economic forecasts that strengthening growth in the richest countries (US, Great Britain, Germany) diminishes the risk of next global downturn. On the other hand, the outlook for developing countries has deteriorated, in particular for China. Also the conflict between Russian and the US/EU concerning Ukraine remains vital risk factor for global economic growth and foreign trade volumes. We still do not anticipate a scenario of events abroad that could make us revise downwards our GDP forecasts for Poland.

■ **While the economic growth accelerates, inflation remains subdued worldwide and this has clear impact on the central banks' policies.** The US Fed continues QE3 tapering but is unlikely to hurry with an interest rate hike despite some hawkish, in the market's view, remarks at the first press conference of Janet Yellen as a Fed governor. At the same time, the ECB seems to be getting more and more convinced to the need of taking nonstandard measures in order to avoid deflation in the euro zone. Polish MPC has entered a stand-by mode again after it extended its forward guidance in March. It has signalled very clearly that no changes in the communication should be expected before July and if nothing extraordinary happens until then, it may declare that interest rates will remain stable until the end of the year.

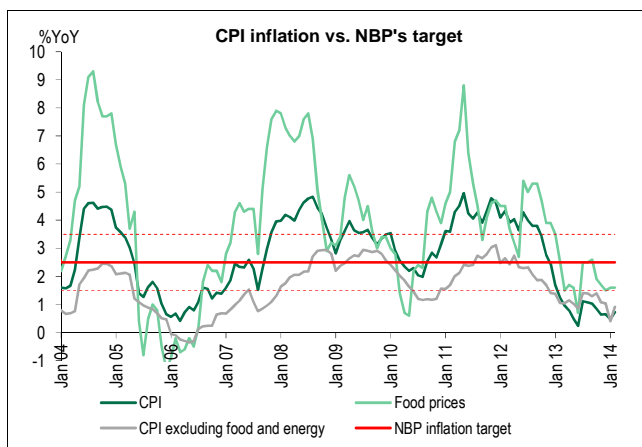
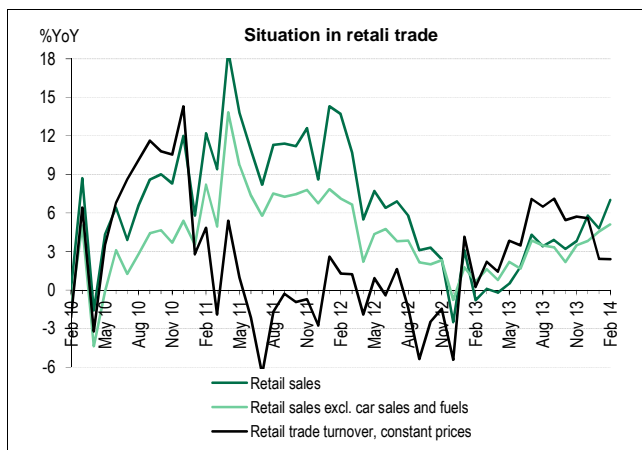
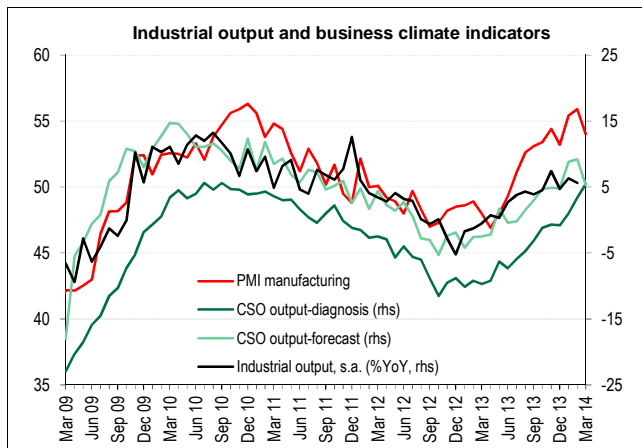
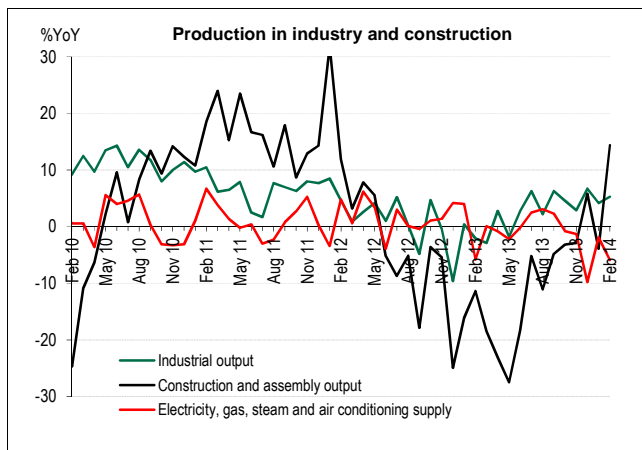
■ **Spring mood seems to be present also in the financial markets.** The US and European stock indexes have set new all-time highs in April and investors are again getting more interested in the emerging markets, despite the risk factors persisting in the global environment (situation in Ukraine, slowdown in China). This might have partly been due to changes of expectations regarding next decisions of the main central banks. The domestic currency and Polish bonds were supported by this positive sentiment, and additionally by dovish signals from the MPC. Although the situation in Ukraine still cannot be erased from the list of risk factors may still trigger some corrections in the Polish FX market, we expect the domestic currency to appreciate in the medium term due to sound fundamentals of the Polish economy. Note at the same time, that the upward trend of Polish bond yields expected by us for some time may be actually weaker and slower as the suggestion on quantitative easing by the ECB may diminish the negative impact that Fed's QE3 tapering has on the European curves.

Financial market on 10 April 2014:

NBP deposit rate	1.00	WIBOR 3M	2.72	EURPLN	4.1710
NBP reference rate	2.50	Yield on 2-year T-bond	2.92	USDPLN	3.0092
NBP lombard rate	4.00	Yield on 5-year T-bond	3.49	CHFPLN	3.4262

This report is based on information available until 10.04.2014

Economic update



Source: CSO, Markit, BZ WBK

Output going up, correction in PMI index

- Industrial output expanded in February by 5.3%YoY. Output growth in manufacturing accelerated to 7.3%YoY from 5.9%YoY one month earlier, with the most considerable increases in export-oriented branches, like production of furniture (18%YoY). Output in electricity, gas, steam and air conditioning supply declined by 5.9%YoY probably mainly due to mild winter.

- Construction and assembly output surprised to the upside, showing a leap by 14.4%YoY. This was the highest growth rate in this sector for two years, but we should not neglect the positive weather effect. Main drivers of growth are: construction of buildings (16.8%YoY) and specialized construction activities (25.4%YoY), while civil engineering, i.e. sector strongly connected to public investments, is stagnating (0.1%YoY).

- Data on industrial and construction output indicate a continuation of positive tendencies in the economy. These trends should persist in the coming months, leading to acceleration of economic growth. We maintain our annual forecast of GDP growth at 3.5%YoY.

- PMI for Polish manufacturing plunged in March to 54.0pts from 55.9pts in February. The index fell to the lowest level since December 2013. The decline was partially triggered by uncertainty due to events in Ukraine. However, in our view the index was rising too strongly recently, overshooting the underlying economic growth. Thus, we treat this decline as a correction of too optimistic expectations and not as a harbinger of slowdown, especially as the index is still running at a very high level. Let us note that CSO business climate index (seasonally adjusted) for industry climbed in March to the highest level since December 2010, while subindex for output recorded the second highest value since April 2008 after the third strong increase in a row.

Consumer demand supported by labour market recovery

- February brought an acceleration of retail sales growth to 7%YoY, the highest level since May 2012. This was partially due to high sales of personal cars registered as trucks and low statistical base. However, according to our estimates, retail sales excluding cars and fuels also accelerated - to 4.2%YoY (the highest growth rate since August 2012).

- High growth rate of sales and, in general, of consumer demand is underpinned by recovery of the labour market, which results in faster growth of personal income and improving consumer confidence.

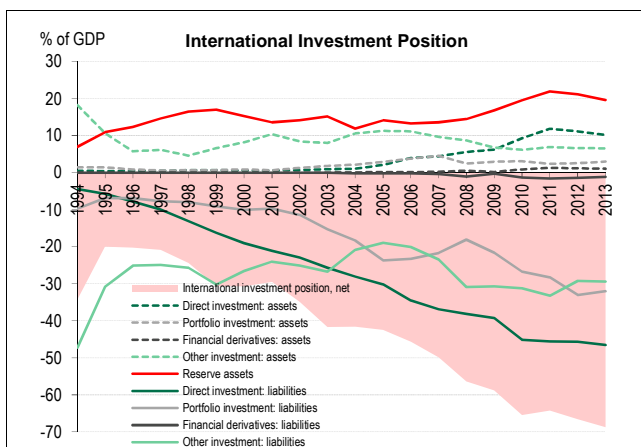
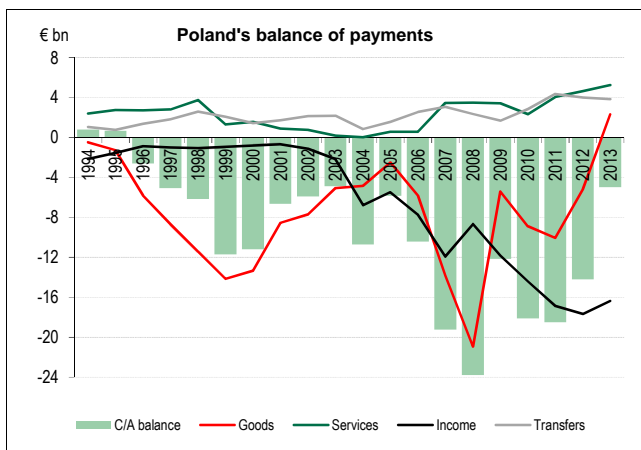
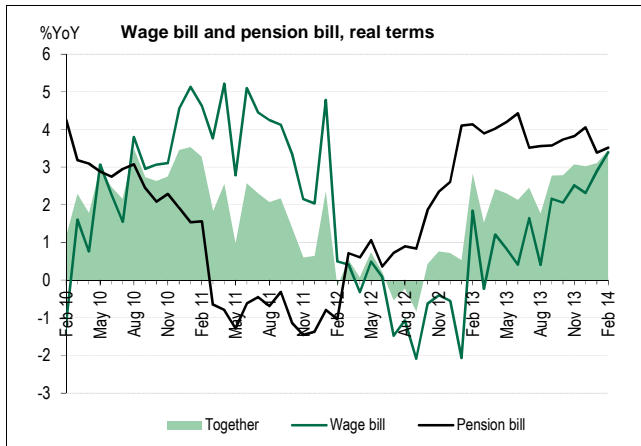
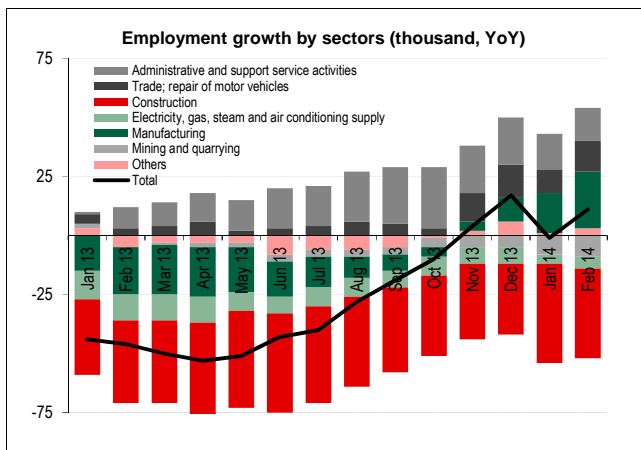
Inflation still low

- February's inflation reached 0.7%YoY, below expectations, and flash January's release was revised downward by 0.2pp to 0.5%YoY due to changes of weights in the inflation basket. In our opinion, the update of weights will have a significantly less impact on the end-year CPI than on the January's number (December's CPI may be lower by 0.02-0.03pp).

- Pace of price growth is expected to remain subdued for the better part of the year, and will rather not deviate significantly above the level of 1%YoY. Only in the final quarter of 2014 we expect some more visible rebound of inflation.

- In the last decade or so, periods of substantial rise of inflation in Poland were usually preceded by sharp acceleration of growth of food prices. One cannot exclude, that this will be the case also this time. First, we can already observe a significant increase of cereals prices in the global commodity markets (the effect of draughts and crisis in Ukraine). Secondly, in a few months' time this may be accompanied by much lower supply of pork (as Polish breeders significantly limited the production after the information about detection of African swine fever virus).

Economic update



Source: CSO, NBP, BZ WBK

Employment in firms weak, but labour market recovery present

- Employment in corporate sector increased in February by 0.2%YoY. It is worth to remind that one month earlier data on employment clearly disappointed (0.0%YoY), which we had explained by the change of the sample of companies covered, and we had suggested that next months will show an improvement. And it indeed happened in the following month, when 2.1k of workplaces were added on monthly terms – the first increase of employment in February since 2011. Rise of employment was generated mainly in industrial manufacturing, retail trade and administrative and support service activities. Employment in wholesale trade and transport is still stagnating, while construction is posting negative results. The improvement of situation in construction will probably eventually translate into higher employment in this sector, while the general improvement of economic situation should support the wholesale trade and transport. Thus, even if potential for employment growth in leading sectors “runs out of fuel”, then higher employment in the whole corporate sector will still be secured.

- Data on wages surprised to the upside showing growth by 4.0%YoY. This is the fastest pace of wage growth for twelve months. Total wage bill in corporate sector increased in February by 4.2%YoY in nominal terms and by 3.4%YoY in real terms. These are the highest growth rates since January 2012 and provide an important support for private consumption in 1Q2014.

- According to data of the labour ministry, in March the registered unemployment rate declined to 13.6%, while number of jobseekers declined by 72k in one month. This was the best March's result since 2008, i.e. since the pre-crisis boom. In YoY terms unemployment rate fell by as much as 0.7pp, while in December it was still at level seen one year before. Unemployment is falling really fast and this is generated mainly by labour market revival, as scale of the Labour Ministry intervention is more or less the same as one year before.

Positive tendencies in balance of payments

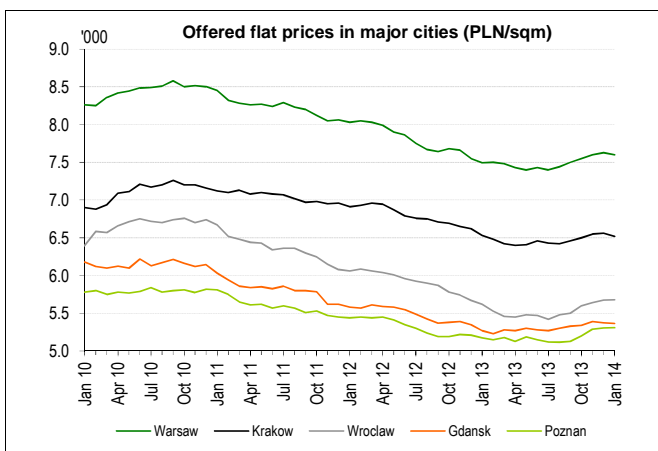
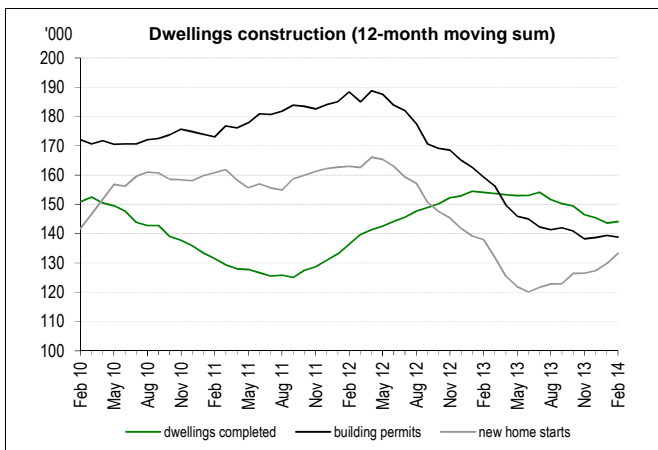
- The year 2013 was exceptional as regards balance of payments tendencies. For the first time since early 90s the value of Polish exports exceeded the value of imports, while current account deficit fell to a mere 1.3% of GDP (the lowest level since 1995). Moreover, the sum of current and capital accounts was positive, which means that for the first time since 1994 the Polish economy was not dependent on external financing.

- This development resulted in a slowdown of upward tendency in external debt – its value at the end of 2013 reached €275bn (ca. €2br less than in 2012), while its relation to GDP fell for the second year in a row (to 70%). The short-term external debt rose at the end of 2013 to €75.5bn (ca. 7%YoY), but – as we wrote in February's MACROscope edition – its financing should not cause major worries, especially as an important part of short-term debt is made of liabilities versus direct investors and within capital groups (as explained in details in the special box in the latest NBP's *Inflation report*).

- Poland's net International Investment Position reached all-time high at -1.12bn at the end of 2013, i.e. 68.7% of GDP and this was the eighteenth yearly increase of this number in a row. However, in our view the rise of IIP last year was primarily due to change of prices of assets and changes in exchange rates.

- Recent data are showing a continuation of positive tendencies in foreign trade – in January the pace of growth of Polish exports remained above 10%YoY for the second time in a row and trade balance showed a surplus (€419m). We are expecting the trade balance to remain in the positive territory also in the upcoming quarters, so current account deficit will decline to ca. 0.7% of GDP. Thanks to that, external debt and net IIP should not expand this year.

Housing market



Continuation of revival on the housing market in 2014?

- 2013 saw a deceleration of rise of house supply in Poland. Number of dwellings completed (145.4k) fell by ca. 5%YoY, house starts (127.4k) by ca. 10% and building permits (138.7k) by 16%. Even though house starts are rebounding slowly, supply of new houses in 2014 will be probably lower again (ca. 140k).
- On the other hand, we have seen an activation of demand for houses. According to REAS data, in 4Q2013 sales on the primary market in Poland's biggest cities increased by as much as 17%, at the same time, according to ZBP (Polish banks' association), value of newly signed mortgage loan contracts amounted to PLN36.5bn in 2013, which is the lowest level in a couple of years, so demand was driven mainly by so-called "cash clients", who took the opportunity of low prices. Let us note that currency loans almost vanished from the market – 99.07% of loans granted in 2013 were PLN-denominated.
- Lower imbalance between supply and demand stopped the downward tendency of prices, observed for a couple of years. At the end of 2013 and at the start of 2014 prices were even a bit higher than one year earlier. Still, price growth is still weak (1-2%YoY).
- In the upcoming quarters we are expecting a rise of demand for flats, especially financed via loans, given continuation of labour market recovery, better economic outlook and low interest rates. Supply remains subdued, which can translate into a gradual rise of average prices. Some cap of demand growth can be put by restrictive credit conditions, like rising margins or abandonment of zero-LtV loans. In a couple of years horizon, potential for rise of demand for dwellings is quite considerable in our view, as along with rising income levels there will be a natural trend to improve quality of housing (which still significantly lags behind European average).

Monetary policy watch

Fragments of MPC communiqué after April's meeting

Growth in global economic activity remains moderate, although the economic situation varies across countries. (...) Moderate growth in global economic activity is conducive to maintaining low inflation in many countries.

Data on domestic economic activity confirm a continuation of the gradual recovery in Poland. In the first months of 2014 industrial output and retail sales growth accelerated. In February construction and assembly output increased as well. Activity growth in the subsequent quarters is signalled by favourable business climate indicators.

The recovery is gradually being transmitted into labour market conditions. Signs of employment growth in the enterprise sector, as well as a decline in unemployment have been observed. However, despite a slightly fall in February, the unemployment rate remains at an elevated levels, which restricts wage growth.

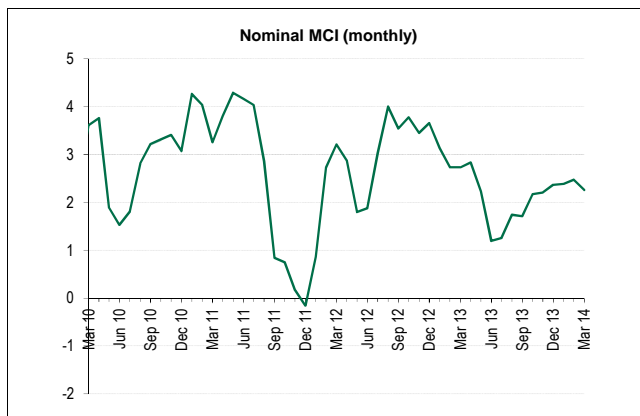
In February 2014 CPI inflation amounted to 0.7%, thus remaining markedly below the NBP inflation target of 2.5%. Core inflation also continued at a low level. At the same time producer prices declined further. This is accompanied by low inflation expectations.

In the opinion of the Council, gradual economic recovery is likely to continue in the coming quarters, however, inflationary pressures will remain subdued. Therefore, the Council decided to keep NBP interest rates unchanged. In the Council's assessment NBP interest rates should be kept unchanged for a longer period of time, i.e. at least until the end of the third quarter of 2014.

Tone of the statement unchanged until July

- In line with expectations, the MPC kept interest rates unchanged at its April meeting. The tone of the statement also has not changed when compared to the March statement. This was no surprise at all, as only one month ago the MPC has extended its forward guidance until at least the end of the Q3-14 and no breaking macro data has emerged since then that could have altered substantially the GDP and CPI outlook.
- NBP governor, Marek Belka, said during the press conference that if nothing special happens, then one should not expect any changes in the MPC tone and its bias until July (when fresh NBP projections will be available). This means that there are two rather unexciting MPC meetings ahead, which outcomes are easy to predict.
- At the same time, Belka reminded that numerous comments of the MPC members have recently indicated that the period of stable interest rates may be extended beyond the end of the 3Q14. This seems to be a clear suggestion, that in July the MPC may extend its forward guidance once again (probably until the end of 2014), provided that economic outlook does not change significantly until then.
- We uphold our stance that NBP's official rates will remain stable till year-end, while at the beginning of 2015 the MPC will decide to hike rates. It will be justified by strengthening of economic growth and upward revision of inflation forecasts (in our opinion inflation rate will start rising faster than predicted in recent NBP's projection).

Restrictiveness of the Monetary Policy (Council)



Slight decline of MCI, but this is only a deviation from trend

- In line with our expectations, the MCI monetary policy restrictiveness index posted an insignificant decline in March, mainly under influence of the weakening Polish currency (average EURPLN in March amounted to 4.20 versus 4.18 in February) amid stabilization of money market rates.
- However, in our opinion this move was only a deviation from trend, triggered by temporary factors (uncertainty about situation in Ukraine) – we are expecting a strengthening of the zloty amid improving economic outlook and approaching hikes of interest rates by the MPC (in a longer horizon) and these will cause a tightening of monetary conditions and will push the MCI upwards.



Rzońca (1.44)

Winiecki (1.45)

Bratkowski (0.58)

Kaźmierczak (1.41)

Hausner (1.03)

Belka (0.96)

Zielińska-Głębocka (0.81)

Głapiński (1.38)

Chojna-Duch (0.73)

Osiatyński



Index is between 0 and 2. A vote for the majority view is given a score of 1. A vote for a more hawkish (less dovish) decision than the majority view has a score of 2 and a vote for a less hawkish (more dovish) decision than the majority view has a score of 0. Value of the index for a given MPC member is a weighted average of points for all votes. Recent votes have higher weights, more distant – lower.

Numbers directly by the name are values of the index for period since the beginning of current term of office of the current MPC and NBP governor.

Direction of the restrictiveness axis reflects our expectations regarding direction of interest rate changes in the nearest 12 months.

As there was no vote on the rate change for a long time, the positioning of MPC members on the axis is based mainly on our assessment, as we took into account comments of MPC members in recent period.

More and more MPC members supporting stable rates till year-end

Numerous comments of the MPC members expressed in recent weeks clearly point that the majority of them is in favour of extending the forward guidance until the end of 2014. Jerzy Hausner, who has not been excluding the launching the monetary policy tightening cycle this year not that long ago has changed his mind and postponed the timing of the first rate hike. Andrzej Bratkowski still does not rule out a hike of interest rates in 4Q-14, but sees rising changes for a longer stabilization of the monetary policy parameters. Most dovish member of the Council, Jerzy Osiatyński is even ready to keep rates at all-time low until the end of 2015. NBP governor, Marek Belka, admitted recently in an interview, that sentiment in the MPC is getting more “dovish” because of the current economic environment and reminded of the rising number of members supporting stable rates beyond the Q3 during the last MPC press conference. All of this suggests that the forward guidance is likely to be extended, this time until the year-end, after the Council gets acquainted with the fresh NBP projection in July.

Situation in Ukraine and ECB actions may have an impact on the MPC

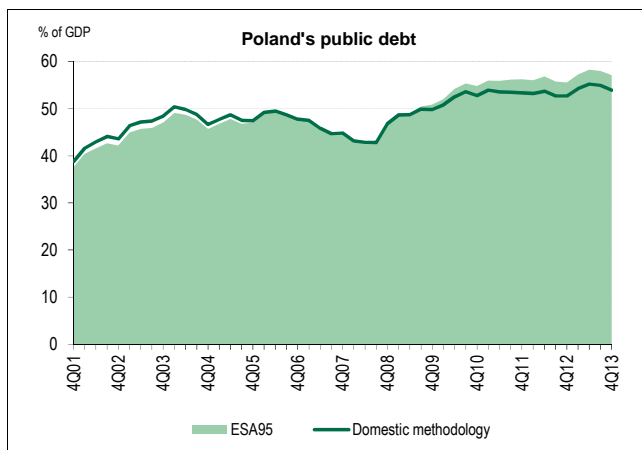
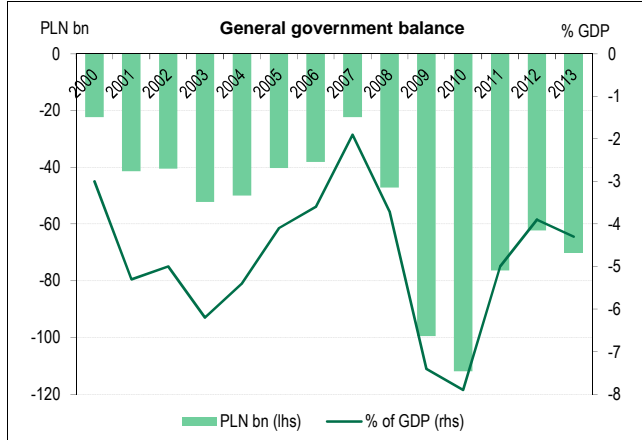
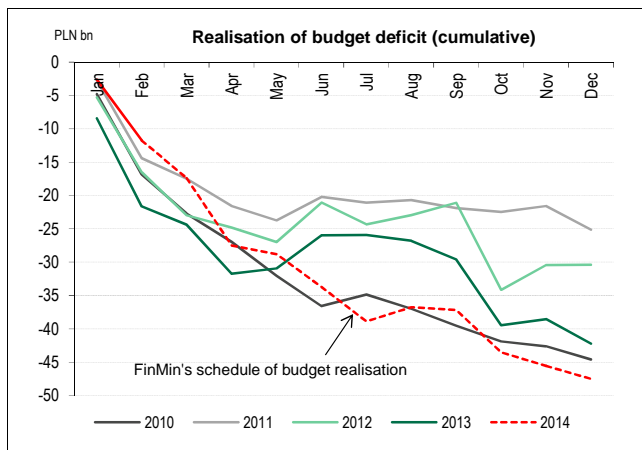
Marek Belka said during the press conference that a recession in Ukraine and sluggish growth in Russia, connected with possible trade sanctions, may have a downward impact on inflation and GDP growth. Recall, that already last month he mentioned that situation in Ukraine accelerated the decision on extending the forward guidance and it seems that this factor will be monitored by the central bank very closely. However, Belka admitted, that the influence of these disturbances on Polish economy shall not be tremendous.

Belka said also that a potential start of asset purchases program by the ECB may change the environment for the monetary policy in Poland – inflation might be tamed due to, among others, zloty's appreciation. He reminded, however, that on the other hand the US central bank is withdrawing its monetary stimulus and we may face a sooner-than-expected monetary policy tightening in the UK.

Increase in number of MPC members only in 2015?

Deputy minister of finance suggested that an amendment to the act on the National Bank of Poland, which will increase temporary the number of the MPC's members to 12 persons, probably would come into effect only in 2015. As we wrote in December's MACROscope, if a new three board members had macroeconomic view closed to the new Council's member Mr Osiatynski, it would shift balance of power towards more dovish side. However, postponing the time when the number of MPC's members will be extended, lowers, in our opinion, risk that the Council will be delaying the start of the monetary policy tightening excessively long. We uphold our stance that the first rate hike will take place at the beginning of 2015, i.e. just before the extension of the number of the MPC members.

Fiscal policy watch



	Spread vs. Bunds (10Y) in bp			CDS (5Y USD)		
	10.04	change since 11.03.14	change since 31.12.13	10.04	change since 11.03.13	change since 31.12.13
Poland	247	-14	9	72	-8	-6
Czech	50	-7	-9	58	-1	-3
Hungary	414	-23	37	232	-8	-24
Greece	439	-93	-222	80	13	44
Spain	162	-6	-59	91	-26	-63
Ireland	138	-3	-14	74	-14	-46
Portugal	233	-37	-176	173	-37	-173
Italy	161	-13	-54	114	-25	-55
France	50	-8	0	47	-3	-7
Germany	-	-	-	21	-3	-5

Source: MoF, GUS, EC, Reuters, BZ WBK

Economic recovery boosts tax revenues

▪ Budget deficit after February amounted to PLN9.5bn, while after 1Q, according to Ministry, it may have reached the level of PLN17.4bn or 36.6% of annual plan. Current budget deficit realisation path is visibly lower than in previous years. It results from economic activity revival, in particular in domestic demand, which consequently increases tax income inflows to the budget (VAT revenues grew by 27%YoY after February). We still expect this year budget deficit to be lower than planned at the end of year.

The 2013 fiscal deficit below forecasts

▪ According to unofficial data, the general government deficit increased to 4.3% of GDP in 2013, up from 3.9% GDP in previous year. It was slightly below the European Commission's forecast (4.4%) and earlier Finance Ministry's projection (4.8%).

▪ Better than expected realisation (the official data will be released by the Statistical Office on April, 16) is not a surprise. It comes from on the one hand economic growth acceleration, which strengthened in H2 2013, and from lower realisation of deficits of the central budget (by ca PLN9bn vs plan after amendment) and of municipal governments (by ca PLN8bn).

▪ This year, due to implemented pension system reform, the general government sector (ESA95) will show one-time surplus worth 4.4% of GDP (our forecast is very close to the European Commission). In 2015 further consolidation of fiscal policy is expected. Detailed plan of the Finance Ministry will be presented in the 2014 updated convergence program, which will be published till end-April. Earlier this month minister of finance Mateusz Szczurek announced further steps, which will allow to permanently decrease deficit below 3% of GDP, in line with EC suggestions.

The public debt increased in 2013, but this year it declines

▪ Ministry of Finance announced that public debt in 2013 amounted to PLN880.2bn, or 53.9% of GDP (vs 52.7% of GDP in previous year). At the same time the general government debt (ESA95) increased to 57.1% of GDP from 55.6% of GDP in 2012. The highest growth in debt (in both cases) resulted from financing net borrowing requirements, which in 2013 amounted to PLN57.4bn.

▪ Implementation of pension reform caused open pension funds to transfer to Social Insurance Institution (ZUS) securities in the total value of PLN153.2bn. Consequently, it will result in reduction of public debt by more than 8% of GDP and of general government debt (ESA 95) by more than 9% of GDP.

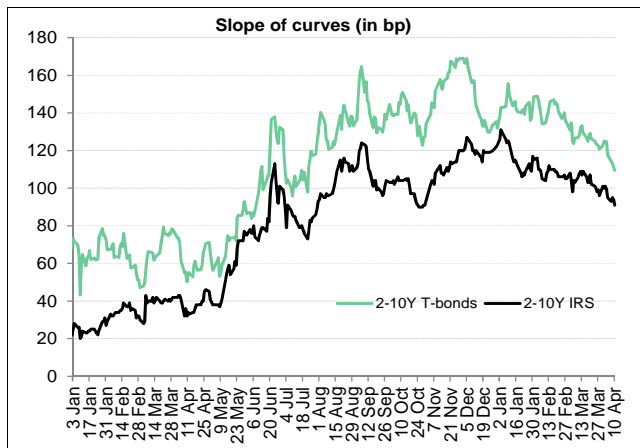
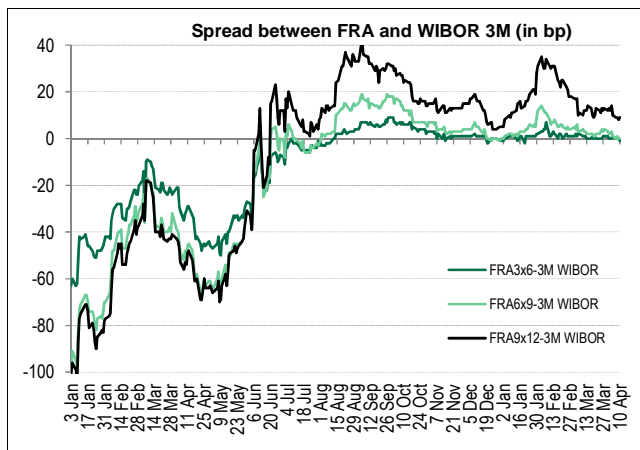
▪ According to Fitch Ratings, recent changes of the pension system are neutral for Polish sovereign ratings. The agency judges, that the reduction in public debt (as well as debt-servicing costs) is offset by an increase in long-term pension liabilities. Fitch assumes that fiscal consolidation will be continued (despite looming elections) due to convenient economic conditions, but the agency wants to wait for the effects of this process before it will make a decision about upward revision of Poland's credit rating.

ECB's promises supported global debt markets

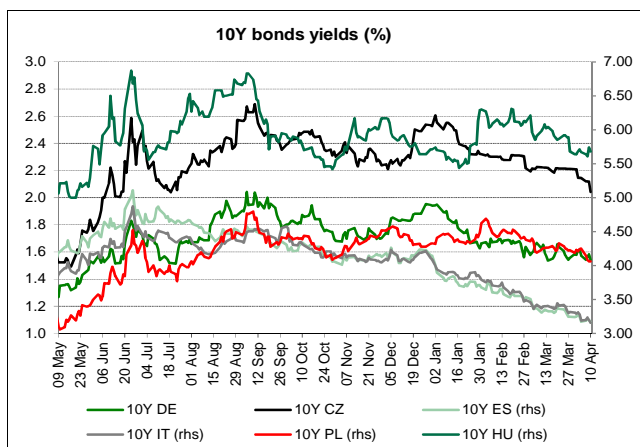
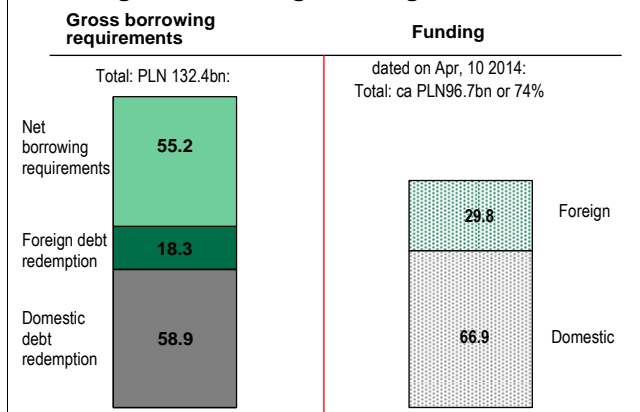
▪ March and the beginning of April brought continuation of positive tendencies on core market. Yield of 10Y Bund, after short-lived increase above 1.60%, stabilised slightly below this level. On the other hand better perspectives of economic growth for peripheral countries supported further decline in yields of these countries, in which Spanish and Italian 10Y benchmarks reached the lowest level in history. What is more, measures of the risk assessment improved – spread over Bunds narrowed, while CDS declined.

▪ Perspectives that ECB may again act to fight against deflationary risk should stabilise yields of Bunds near current levels. Consequently, it should support stabilization of yields of peripheral debt in coming weeks. Notwithstanding, more visible signals of improving economy should bring pressure of yields increase in mid to long term horizon.

Interest rate market



The 2014 gross borrowing financing



Source: Reuters, BZ WBK

The MPC's rhetoric stabilises money market rates

▪ WIBOR rates between 1M and 9M stayed unchanged in March while 12M rate inched up by 1bp despite extending forward guidance until Q3-14 by the MPC. At the same time, FRA adjusted to the new MPC rhetoric and dropped by 1-4bp, leading to FRA-3M WIBOR spread narrowing. After the March decision of the Council, investors shifted their expectations for a first rate hike to one year horizon (temporarily the market was even pricing-in slightly longer period of stable rates).

▪ This month's domestic data should confirm the continuation of the positive economic tendencies amid lack of inflation pressure. Perspectives of further extension of forward guidance by the MPC till year-end and still low inflation rate (we expect CPI inflation to stay below 1%YoY in upcoming months) should stabilise FRA rates near current levels. On the other hand, continuation of downward trend in T-bonds yields and IRS rates may (in short run) result in further decline of FRAs.

Hopes for ECB actions support the interest rate market

▪ March and early April saw a significant plunge of IRS and bond yields. This move was driven by several factors, of which the most important were as follows: (1) March decision of the MPC to extend the forward guidance and suggestions of the Council's members that it may be extended even further, (2) lack of escalation of the Ukraine crisis (though this factor gained strength in early April) and (3) the suggestion by the ECB that it may finally take additional measures (quantitative easing, negative interest rates). Middle and long end of the curves benefited the most, while the short ends remained relatively stable. This led to 2-10Y spreads narrowing – to 109bp in case of T-bonds (lowest since July 2013) and to 91bp for the IRS (lowest since October 2013). Yield of the 10Y benchmark tested 4% while the 10Y IRS fell slightly below 3.90% and established fresh 2014 lows.

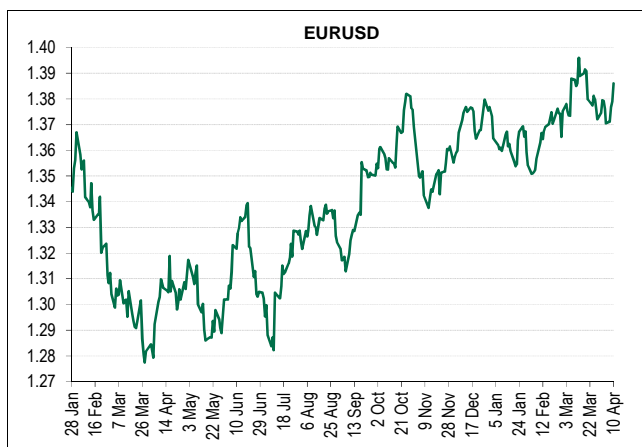
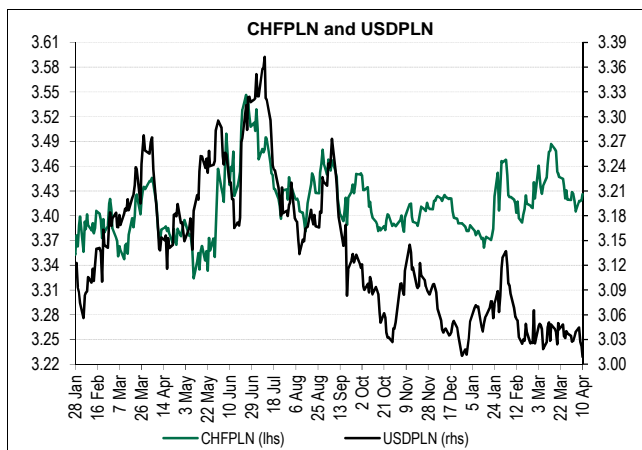
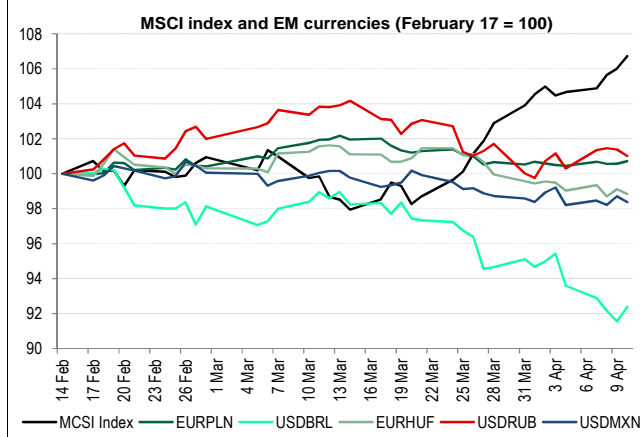
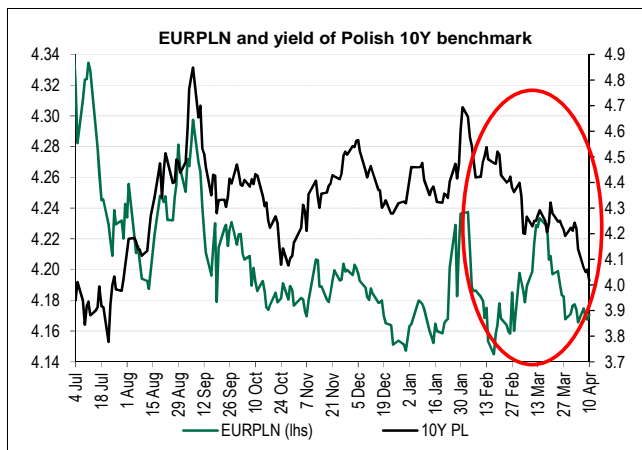
▪ Auction results have also been supportive for the market mood. Demand claimed by investors was solid and this enabled the Ministry of Finance to issue debt at market prices (or even slightly higher than on the secondary market). Consequently, the 2014 gross borrowing needs are covered in ca. 73% after the first April auction. If high demand for Polish bonds persists (this is supported by current market environment), there is a high probability that coverage ratio will reach 80% at the end of the month and 100% at the end of June.

We still expect higher rates in the medium term

▪ During the first weeks of April Polish bonds gained quite significantly as compared to other markets in the EM universe. Expectations for more ECB actions (including the option of introducing the quantitative easing program) may provide further support for the Polish bonds in coming weeks.

▪ Developments in the core markets remain crucial for domestic mid- and long-term bonds. Further decline of German bonds yields may drag yields of Polish debt deeper to the south or at least stabilize around current levels. Additionally, more flattening of curves cannot be excluded if no negative factors emerge. However, stronger signals confirming the continuation of the economic recovery are likely to generate an upward pressure for yields in the medium term. Still, the pace of yields and IRS increase may be slower than we had expected so far.

Foreign exchange market



Sources: CSO, Reuters, BZ WBK

Zloty may gain at slower pace

▪ After the second wave of risk aversion seen in the first weeks of March, second half of the month saw a visible recovery – the zloty benefited from lack of Ukraine-Russia conflict escalation after the Crimean referendum. Furthermore, the IMF agreed a loan to this country and package of anti-crisis reforms has been approved by the Ukrainian parliament. In these circumstances, the zloty pared nearly all losses suffered versus the euro in the first half of March – EURPLN declined from 4.25 to around 4.16. In our opinion, this move was supported partly also due to global weakness of the single currency (find more in the next paragraph).

▪ Taking a broader glance on the Polish FX market, we see that recent eight weeks in case of EURPLN are very similar to mid-January/mid-February period. After three weeks of an upward move of EURPLN recorded at that time (triggered by high risk aversion in the emerging markets), next two weeks saw a move down from 4.26 to 4.14.

▪ It is worth to notice, that Polish bonds suffered significantly only during the first wave of risk aversion seen this year. The following months brought a significant plunge of yields and this trend has been only temporarily accompanied by the zloty's appreciation. Additionally, MSCI index for emerging markets increased by nearly 7% since the situation in Ukraine has deteriorated (in mid-February). Similarly, positive changes have been recorded also in case of the LatAm currencies, which gained 5-8% vs. the euro or the dollar. At the same time, among CEE currencies best performers (next to the ruble that has recovered at fastest pace after it has depreciated most) were the forint (2.6% gain vs. the euro) and the zloty (0.5% gain vs. the dollar).

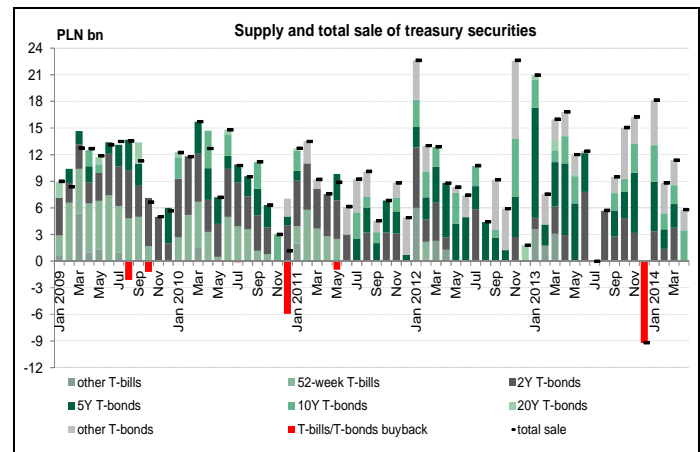
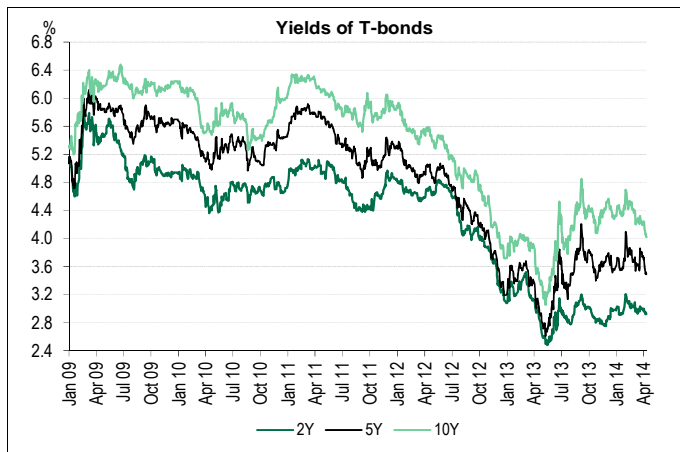
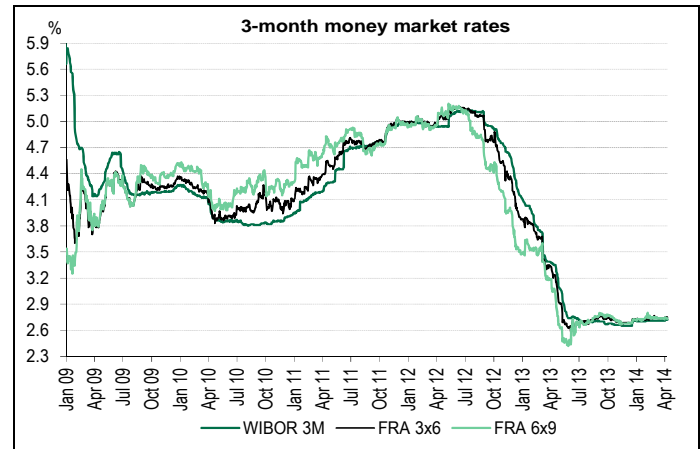
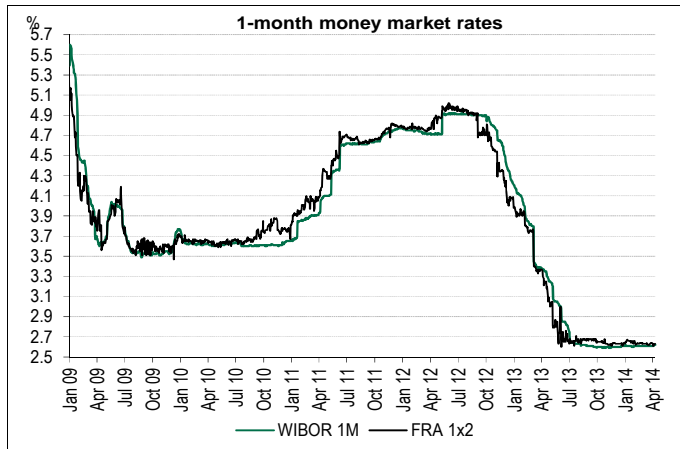
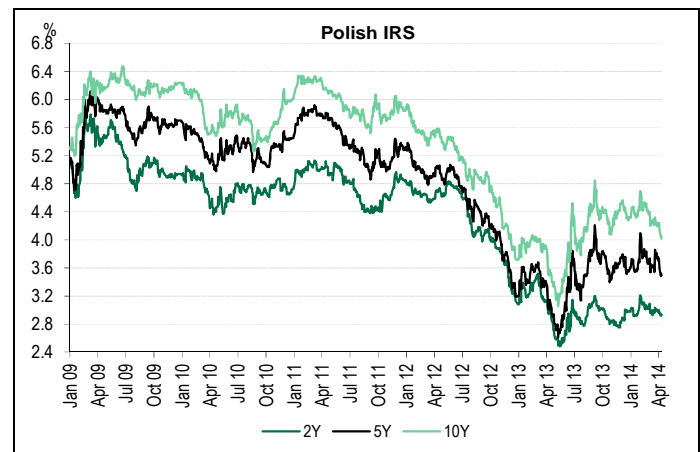
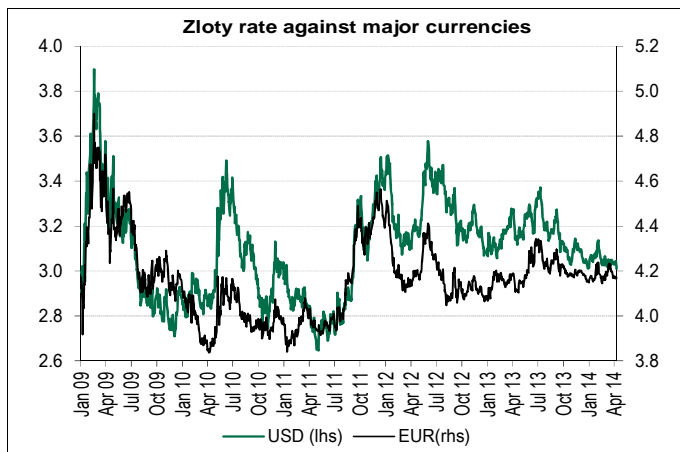
▪ The above circumstances suggest, that the issue of Ukraine is not – at least for the time being – the most important factor driving the global market moods anymore as Western countries are reluctant to engage more in the conflict. However, we think it would be premature to erase this issue from the list of risk factors for the zloty's appreciation scenario given recent events beyond our eastern border. Although the zloty may appreciate to 4.14 per euro, we would not perceive this move as a sustainable given turmoil and separatists activity in eastern Ukraine. On the other hand, we do not expect the exchange rate to break peaks of last upward waves (4.25-4.26) any time soon. Expectations for more monetary policy easing by the ECB may support risky assets, including the zloty. We expect EURPLN to remain in 4.14-4.25 range in April.

April's inflation in the centre of attention

▪ Euro's weakening recorded in recent weeks in the global market indicates that ECB officials, who have been repeating for several weeks the bank's readiness to take further actions in order to defend the euro zone against deflation, have reached their goal – EURUSD recorded three consecutive weeks of a decline (from 1.39 to nearly 1.37). Since the market sentiment has improved after the Crimea referendum, the single currency depreciated vs. nearly all EM currencies (except the Ukraine hryvnia or the Argentine peso) and vs. the majority of core currencies. At the same time, the US dollar was supported by surprisingly hawkish statement after the FOMC meeting, followed by comments of the Committee's members, and decent US macro releases.

▪ During the press conference after the April ECB meeting, Mario Draghi fuelled hopes for further easing actions aimed at fighting the risk of deflation. He stressed the importance of April's inflation data, as a factor influencing the decision. Flash HICP for April is due to be released on the last day of this month and the FOMC decision will be announced the same day. Thus, late April may be quite a volatile period for EURUSD. We sustain our scenario of euro's appreciation vs. the dollar on the course of 2014, but launching the QE program in the euro zone or cutting the deposit rate below 0% would be a significant risk factor for these forecasts.

Market monitor



Treasury bond auctions in 2013/2014 (PLNm)

month	First auction				Second auction			Switch auction			
	date	T-bonds	offer	offer	date	T-bonds	offer	offer	offer		
April '13	11.04	DS1023/WZ0124	3000-5000	5029.1	23.04	OK/WZ/PS	5000-10000	11788.6			
May	9.05	PS0718	3500-5500	6498.0	16.05	DS/WZ/WS	2000-6000	5505.4			
June	6.06	PS0718/WZ0119	3000-5000	4606.5					19.06	OK0713/DS1013	
July	-	-	-	-							
August	7.08	OK0116	3000-5000	5695.0							
September	5.09	OK0112/PS0718	5000-7000	5706.8					25.09	DS1013/OK0114	WZ0119/DS1023
October	3.10	PS0718	2500-4500	3008.0	22.10	OK0116/IZ0823/DS1023	6000-12000	12019.9	16.10	EUR20140203**	445.0
November	7.11	OK0116/PS0718	4000-7000	7964.2	13.11	USD20140115**	100	132.2	20.11	OK0114/PS0414	DS1023/WS/WZ/IZ
December									5.12	OK0114/PS0414	PS0416/WZ0119
January '14	9.01	PS0718/WZ0124	3000-5000	6013.0	23.01	OK/PS/WZ/DS	6000-10000	12129.7			
February	6.02	OK0716/WZ0119	2000-4000	4810.0	13.02	PS0718/DS1013	3000-5000	4011.0			
March	6.03	OK0716/WZ0119	2500-5500	6573.0					20.03	PS0414/OK0714	PS0718/DS1023
April	3.04	DS1023/WZ0119	3000-5000	5781.0	23.04	OK0716/PS1016/PS0718	5000-10000				

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

Economic calendar

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
7 April CZ: Industrial output (Feb) DE: Industrial output (Feb)	8	9 PL: MPC decision CZ: CPI (Mar) US: FOMC minutes	10	11 PL: Balance of payments (Feb) HU: CPI (Mar) US: Flash Michigan (Apr)
14 PL: Money supply (Mar) EZ: Industrial output (Feb) US: Retail sales (Mar)	15 PL: CPI (Mar) DE: ZEW index (Apr) US: CPI (Mar)	16 PL: Core inflation (Mar) PL: Wages and employment (Mar) EZ: HICP (Mar) US: House starts / Building permits (Mar) US: Industrial output (Mar) US: Fed Beige Book	17 PL: Industrial output (Mar) PL: PPI (Mar) PL: MPC minutes US: Philly Fed index (Apr)	18
21 PM: Market holiday	22 US: Home sales (Mar)	23 CN: Flash PM – manufacturing (Apr) DE: Flash PMI – manufacturing (Apr) EZ: Flash PMI – manufacturing (Apr) US: New home sales (Mar)	24 PL: Retail sales (Mar) PL: Unemployment rate (Mar) DE: Ifo (Apr) US: Durable goods orders (Mar)	25 US: Michigan index (Apr)
28 US: Pending home sales (Mar)	29 HU: Central bank decision US: Consumer confidence index (Apr)	30 PL: Inflation expectations (Apr) EZ: Flash HICP (Apr) US: ADP report (Apr) US: Advance GDP (Q1) US: Fed decision	1 May PL: Market holiday US: Personal income (Mar) US: Consumer spending (Mar) US: ISM – manufacturing (Apr)	2 PL: PMI – manufacturing (Apr) CN: PMI – manufacturing (Apr) DE: PMI – manufacturing (Apr) EZ: PMI – manufacturing (Apr) US: Non-farm payrolls (Apr) US: Unemployment rate (Apr)
5 US: ISM – services (Apr)	6 EZ: PMI – services (Apr) DE: PMI – services (Apr)	7 PL: MPC decision DE: Industrial orders (Mar) CZ: Industrial output (Mar) CZ: Central bank decision	8 EZ: ECB decision DE: Industrial output (Feb)	9 DE: Exports (Mar)
12 CZ: CPI (Apr)	13 HU: CPI (Apr) DE: ZEW index (May) US: Retail sales (Apr)	14 PL: CPI (Apr) PL: Money supply (Apr) EZ: Industrial output (Mar)	15 PL: Advance GDP (Q1) PL: Core inflation (Apr) PL: Balance of payments (Mar) GE, CZ, HU, EZ: Flash GDP (Q1) EZ: HICP (Apr) US: CPI (Apr) US: Industrial output (Apr) US: Philly Fed index (May)	16 US: House starts / Building permits (Apr) US: Flash Michigan (May)

MPC meetings and data release calendar for 2014

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
ECB meeting	8	6	6	3	8	5	3	7	4	2	6	4
MPC meeting	7-8	4-5	4-5	8-9	6-7	2-3	1-2	19	2-3	7-8	4-5	2-3
MPC minutes	23	20	20	17	22	20	-	21	18	23	20	18
Flash GDP*	-	14	-	-	15	-	-	14	-	-	14	-
GDP*	-	28	-	-	30	-	-	29	-	-	28	-
CPI	15	14 ^a	14 ^b	15	14	13	15	13	15	15	13	15
Core inflation	16	-	14	16	15	16	16	14	16	15	17	16
PPI	21	19	19	17	20	18	17	20	17	17	20	17
Industrial output	21	19	19	17	20	18	17	20	17	17	20	17
Retail sales	24	24	25	24	-	-	-	-	-	-	-	-
Gross wages, employment	20	18	18	16	19	17	16	19	16	16	19	16
Foreign trade	about 50 working days after reported period											
Balance of payments*	2		31			30						
Balance of payments	17	12	17	11	15	13						
Money supply	14	14	14	14	14	13						
Business climate indices	23	21	21	23	22	23	22	22	22	22	21	19

* quarterly data. ^a preliminary data for January. ^b January and February; Source: CSO, NBP, Ministry of Finance, Reuters, Bloomberg

Economic data and forecasts

Monthly economic indicators

		Mar 13	Apr 13	May 13	Jun 13	Jul 13	Aug 13	Sep 13	Oct 13	Nov 13	Dec 13	Jan 14	Feb 14	Mar 14	Apr 14
PMI	pts	48.0	46.9	48.0	49.3	51.1	52.6	53.1	53.4	54.4	53.2	55.4	55.9	54.0	54.2
Industrial production	%YoY	-2.9	2.8	-1.8	2.8	6.3	2.2	6.3	4.6	2.9	6.7	4.2	5.3	5.9	5.6
Construction production	%YoY	-18.5	-23.1	-27.5	-18.3	-5.2	-11.1	-4.8	-3.2	-2.9	5.8	-3.9	14.4	10.6	16.9
Retail sales ^a	%YoY	0.1	-0.2	0.5	1.8	4.3	3.4	3.9	3.2	3.8	5.8	4.8	7.0	4.7	10.8
Unemployment rate	%	14.3	14.0	13.5	13.2	13.1	13.0	13.0	13.0	13.2	13.4	14.0	13.9	13.6	13.2
Gross wages in enterprises sector ^a	%YoY	1.6	3.0	2.3	1.4	3.5	2.0	3.6	3.1	3.1	2.7	3.4	4.0	3.6	3.2
Employment in enterprises sector	%YoY	-0.9	-1.0	-0.9	-0.8	-0.7	-0.5	-0.3	-0.2	0.1	0.3	0.0	0.2	0.4	0.7
Export (€)	%YoY	-1.2	11.0	0.3	5.4	7.4	2.8	9.0	3.8	2.3	10.1	10.6	8.1	14.3	11.4
Import (€)	%YoY	-1.3	1.6	-6.1	-1.9	3.1	-0.3	4.2	4.6	0.6	0.0	6.6	8.5	6.1	11.0
Trade balance	EURm	-502	630	1	570	137	299	660	259	-25	-85	419	410	517	753
Current account balance	EURm	-272	569	-176	100	-566	-618	-907	162	-803	-430	-1 135	-344	199	#N/D!
Current account balance	% GDP	-3.1	-2.8	-2.8	-2.3	-1.9	-1.9	-1.9	-1.7	-1.6	-1.3	-1.2	-1.1	-1.0	#N/D!
Budget deficit (cumulative)	PLNbn	-24.4	-31.7	-30.9	-26.0	-25.9	-26.8	-29.6	-39.5	-38.5	-42.2	-2.6	-11.7	-17.4	-27.5
Budget deficit (cumulative)	% of FY plan	47.3	61.6	60.0	50.4	50.3	51.9	57.4	76.5	74.7	81.8	5.6	24.7	36.6	57.9
CPI	%YoY	1.0	0.8	0.5	0.2	1.1	1.1	1.0	0.8	0.6	0.7	0.5	0.7	0.7	0.7
CPI excluding prices of food and energy	%YoY	1.0	1.1	1.0	0.9	1.4	1.4	1.3	1.4	1.1	1.0	0.4	0.9	1.0	0.9
PPI	%YoY	-0.7	-2.1	-2.5	-1.3	-0.8	-1.1	-1.4	-1.4	-1.5	-1.0	-1.0	-1.4	-0.9	-0.4
Broad money (M3)	%YoY	6.6	7.4	6.5	7.0	6.6	6.1	6.1	5.9	5.7	6.2	5.4	5.3	4.5	5.4
Deposits	%YoY	6.6	7.1	6.0	6.5	5.6	5.8	6.0	5.9	5.2	6.0	4.9	4.7	4.0	4.3
Loans	%YoY	3.5	2.3	1.4	3.5	3.7	3.3	3.7	2.9	3.8	4.0	4.2	4.7	4.7	5.4
EUR/PLN	PLN	4.16	4.14	4.18	4.28	4.28	4.23	4.24	4.19	4.19	4.18	4.18	4.18	4.20	4.18
USD/PLN	PLN	3.21	3.18	3.22	3.25	3.27	3.18	3.17	3.07	3.10	3.05	3.07	3.06	3.04	3.05
CHF/PLN	PLN	3.39	3.39	3.36	3.47	3.46	3.43	3.43	3.40	3.40	3.41	3.39	3.42	3.45	3.43
Reference rate ^b	%	3.25	3.25	3.00	2.75	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50
WIBOR 3M	%	3.48	3.29	2.86	2.74	2.70	2.70	2.69	2.67	2.65	2.67	2.70	2.71	2.71	2.71
Yield on 2-year T-bonds	%	3.26	2.89	2.55	2.86	2.87	2.98	3.07	2.90	2.80	2.94	2.99	3.06	2.99	2.95
Yield on 5-year T-bonds	%	3.46	3.03	2.80	3.43	3.36	3.67	3.86	3.62	3.64	3.65	3.67	3.79	3.68	3.50
Yield on 10-year T-bonds	%	3.93	3.50	3.28	3.95	3.97	4.31	4.50	4.28	4.38	4.41	4.42	4.47	4.26	4.10

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

Quarterly and annual economic indicators

		2011	2012	2013	2014	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14
GDP	PLNbn	1 528.1	1 596.4	1 635.7	1 703.7	377.9	395.7	404.3	453.9	391.5	413.1	422.1	477.1
GDP	%YoY	4.5	2.0	1.6	3.5	0.5	0.8	1.9	2.7	3.1	3.5	3.6	3.8
Domestic demand	%YoY	3.6	-0.1	0.0	3.0	-0.9	-1.7	0.5	1.2	1.7	3.5	3.0	3.7
Private consumption	%YoY	2.6	1.3	0.8	2.4	0.0	0.2	1.0	2.1	2.2	2.3	2.5	2.6
Fixed investments	%YoY	8.5	-1.6	-0.2	4.6	-2.1	-3.2	0.6	1.3	1.5	2.0	5.0	7.0
Industrial production	%YoY	7.7	1.0	2.3	5.0	-2.0	1.2	4.9	4.7	5.2	4.7	4.6	5.7
Construction production	%YoY	12.3	-1.0	-10.3	10.9	-15.6	-22.9	-7.0	0.0	7.2	15.5	11.8	8.9
Retail sales ^a	%YoY	11.2	6.0	2.6	6.9	0.9	0.8	4.0	4.5	5.7	7.3	6.5	8.0
Unemployment rate ^b	%	12.5	13.4	13.4	12.4	14.3	13.2	13.0	13.4	13.6	12.3	12.1	12.4
Gross wages in national economy ^a	%YoY	5.2	3.7	3.4	4.4	2.6	3.3	4.0	3.6	3.9	4.3	4.5	4.6
Employment in national economy	%YoY	0.6	0.0	-0.8	0.4	-0.7	-1.1	-1.2	-0.1	0.0	0.4	0.5	0.5
Export (€)	%YoY	12.1	5.9	5.0	11.6	3.2	5.5	6.5	5.0	11.0	11.4	11.8	12.0
Import (€)	%YoY	12.2	2.3	0.0	9.9	-2.0	-2.2	2.4	1.8	7.0	11.0	10.0	11.5
Trade balance	EURm	-10 059	-5 175	2 309	5 124	-139	1 203	1 094	151	1 345	1 489	1 919	371
Current account balance	EURm	-18 519	-14 191	-4 984	-2 926	-2 313	486	-2 086	-1 071	-1 280	-61	-855	-730
Current account balance	% GDP	-5.0	-3.7	-1.3	-0.7	-3.1	-2.3	-1.9	-1.3	-1.0	-1.1	-0.8	-0.7
General government balance	% GDP	-5.0	-3.9	-4.3	4.4	-	-	-	-	-	-	-	-
CPI	%YoY	4.3	3.7	0.9	1.0	1.3	0.5	1.1	0.7	0.6	0.9	0.8	1.6
CPI ^b	%YoY	4.6	2.4	0.7	1.9	1.0	0.2	1.0	0.7	0.7	1.1	1.2	1.9
CPI excluding food and energy prices	%YoY	2.4	2.2	1.2	1.1	1.2	1.0	1.4	1.2	0.8	1.1	1.0	1.4
PPI	%YoY	7.6	3.4	-1.3	-1.4	-0.7	-2.0	-1.1	-1.3	-1.1	-1.0	-2.3	-1.1
Broad money (M3) ^b	%YoY	12.5	18.6	8.1	8.8	6.6	7.0	6.1	6.2	4.5	4.8	6.1	7.0
Deposits ^b	%YoY	11.7	20.6	9.8	9.1	6.6	6.5	6.0	6.0	4.0	3.9	5.2	6.7
Loans ^b	%YoY	14.4	36.6	8.7	8.8	3.5	3.5	3.7	4.0	4.7	3.6	3.7	4.8
EUR/PLN	PLN	4.12	4.19	4.20	4.09	4.16	4.20	4.25	4.19	4.19	4.14	4.04	3.99
USD/PLN	PLN	2.96	3.26	3.16	2.97	3.15	3.22	3.21	3.08	3.06	3.02	2.93	2.87
CHF/PLN	PLN	3.34	3.47	3.41	3.28	3.38	3.41	3.44	3.40	3.42	3.38	3.22	3.11
Reference rate ^b	%	4.50	4.25	2.50	2.50	3.25	2.75	2.50	2.50	2.50	2.50	2.50	2.50
WIBOR 3M	%	4.54	4.91	3.02	2.74	3.77	2.96	2.70	2.66	2.71	2.72	2.74	2.78
Yield on 2-year T-bonds	%	4.81	4.30	2.98	3.01	3.29	2.77	2.98	2.88	3.01	2.95	3.02	3.08
Yield on 5-year T-bonds	%	5.44	4.53	3.46	3.63	3.49	3.09	3.63	3.64	3.71	3.50	3.60	3.72
Yield on 10-year T-bonds	%	5.98	5.02	4.04	4.22	3.95	3.58	4.26	4.36	4.38	4.03	4.13	4.33

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates;

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

This analysis is based on information available until 10.04.2014 has been prepared by:

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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.

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