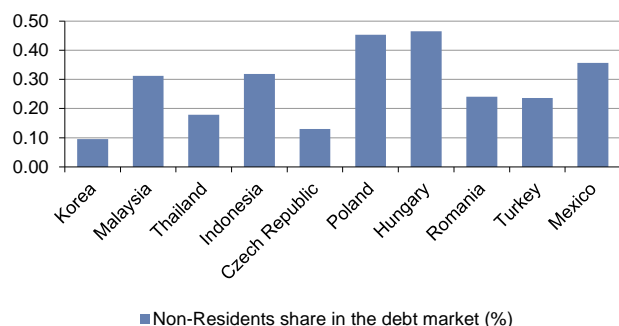


## PLN: Pension overhaul, PLN s-t negative, m-t positive due to fiscal boost

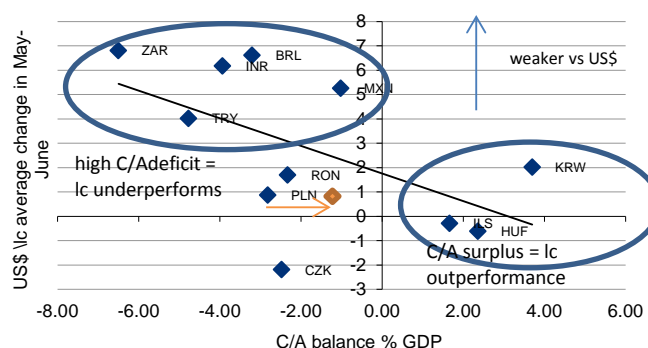
The government decided to: **1) Take-over the entire bond part** of the private pensions' (OFE) assets, the bonds should be redeemed and changed to pension liabilities in ZUS. The positives for the FI market are better fiscal metrics, e.g. public debt lower by 7.5% of GDP to about 47.5% of GDP and slower growth in the future. But FI market negative is higher relative reliance on external investors as their share rises from 35.7% to 45% (even if absolute stays flat), **2) The equity part should stay within OFE books** and still be managed by them, so there is no risk of fierce cashing of the current equity holdings. But simultaneously "the biased voluntary choice" between OFE and ZUS was proposed, but only with respect to the new contributions paid. At best about 30% of members would still pay its contribution to new OFE (effectively equity fund with high volatility of return), so net flow to equity market via OFE should drop from about PLN5.4bn yearly to PLN-0.6bn (also due to point 3). So private pension funds would become net seller vs almost permanent net buyer so far. They will also try to rebalance their portfolio (lower share of equity, increase share of corporate bonds), so overall this changes are definitely negative for equity market. 3) **The capital of OFE clients who are 10 (and less) years before the retirement age will be moved from OFE to ZUS.** This is for the better stability of pensioners' capital before the pension age. But effectively this means cash transfer of PLN10bn to ZUS in 2014, also a relief for central budget. The second relief comes from the lower participation/subsidies to OFE. As a result, **the sector deficit would be lower by 1.1% of GDP (MinFin estimates 0.5% of GDP), or alternatively this can be used to support GDP growth in 2014.** 4) The government declares that debt thresholds would be lowered, accordingly to the value of assets moved from OFE to ZUS (by about 7.5% of GDP), in order to prevent future fiscal expansion caused by less binding debt rules. But even with lower debt threshold we see about 1% of GDP extra space for fiscal stimulus in 2014. Also the local news agency claims 2014 central budget should be planned close to 2013 revised deficit at PLN51.6bn, which in our view is already about PLN5-6bn too high, given recent economic acceleration. So there is possibility of 1-2% of GDP fiscal expansion in 2014. Boosting growth before the elections in Autumn 2015 would be a very strong temptation for the governing Civic Platform. Thus we see think about 1pp upside risk to our 2014 GDP forecast at 2.4%YoY. 5) The government proposed a complicated set-up of bonds handover, with the bond price stabilising mechanism, which we estimate, would force OFE to buy bonds should their price decrease (in order to reach the fixed value of the government bond portfolio which needs to be handed over).

Fig 1 Poland will stand out with non-res exposure



Source: Reuters, GUS, Parkiet, ING forecast and estimates

Fig 2 But improving C/A balance is very PLN positive



Source: GUS, ING forecast and estimates

Overall, **the holders of PLN bonds** would get better fiscal metrics in exchange for more volatile markets, and be more exposed to foreign bond holders. Also the share of PLN bonds in EM bond indexes should drop, which can also **additionally fuel PLN bonds sell-off**. This is a tricky set up in the current environment where we see 14 weeks of outflows from EM bond funds, while Poland so far opposed this tendency. So, at least until September Fed tapering we expect further weakening of PLN bonds. But further on, the PLN bonds can still outperform the EM space as Poland has improving C/A balance (we expect the 2013 12M C/A deficit to shrink to 0-0.5% of GDP and stay close to 1% in 2014). The economy is also experiencing a rapid recovery of the production sector. The proposed changes should improve the (official) debt level, lower deficit and borrowing needs. Also with the less burden associated with the funding of pension system (it was very costly because the government ran two systems simultaneously: PAYGO and capital with OFE) the government can afford to boost growth before 2015 elections and would be very well prepared for the absorption of EU funds from the new European budget. **Thus we think the changes could end up long term supportive for PLN bond market.** Also rating agencies said this doesn't change their assessment of the creditworthiness. **For equity market, the new set up prevents the sell-off of the current equity holding, but still new OFE** looks set to become a permanent equity seller as opposed to its current role of permanent buyer. Fortunately, the foreign investors holding in PL equity market is very low so its impact on PLN would be limited. **FX market wise**, the s-t bond market correction we expect should cause weaker PLN, with possible testing of 4.32-4.35/€, but further on we expect the PLN to outperform EM space, exactly as we have seen since the beginning of recent EM sell-off. [rafal.benecki@ingbank.pl](mailto:rafal.benecki@ingbank.pl)

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