



## POLAND WEEKLY REVIEW

### MACROECONOMICS AND FINANCIAL MARKETS

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#### PREVIEW: The week of February 21<sup>st</sup> to March 28<sup>th</sup>

Indicator	Date of release	Period	BRE fore-cast	Consensus	Last	Comment
Core inflation	Mar 21	Feb	2.9%	2.5%	1.7%	Core inflation is rising on the back of administrative price changes and gradually increasing "demand" categories. The publication concerns January and February reading as the weights have been revised.
Retail sales	Mar 26	Feb	19.1%	20.1%	20.9%	We expect reading slightly below the figure released for January as the effect of seasonal sales faded in February.
MPC decision	Mar 26	-	5.75%	5.75%	5.50%	All the figures released this month support another rate hike and back the scenario of further rate increases. 6.0% likely to be reached by May. Then wait-and-see. Resumption of hikes likely in late summer.

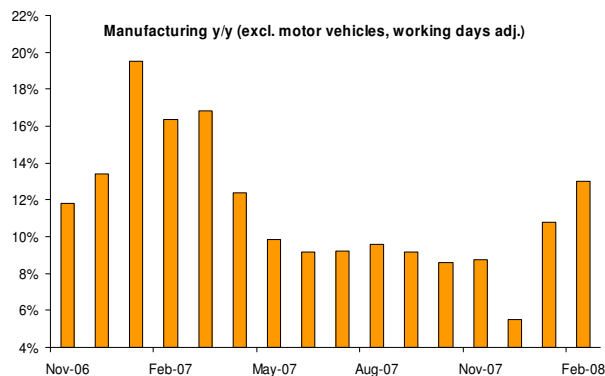
## In Focus / Macroeconomics

### Green light for the MPC

Wages in February surprised on the upside reaching a growth rate of 12.8%, reaching thereby the highest pace of expansion in the ongoing business cycle phase. We expect the figure to have been disturbed by the bonuses in mining, however, the lion's share of the expansion rate stems from recently granted remuneration increases. The contemporary trend of wage growth hovers around 10% and, in the light of our research conducted in the largest enterprises, this expansion is likely to be continued through the whole 2008. Taking into account the inflation running at 4.3% in February, real average wage expanded at slightly above 8% rate.

Industrial output has also beaten market expectations reaching 14.9% annual pace. The growth is mostly attributable to rises recorded in manufacturing – the structure is thus (similar to the January figure) healthy. The data adjusted for working days effect and excluding volatile automotive production shows a solid expansion of 12.5%, versus 10.3% recorded in January. As for the reasons for solid growth of output, our earlier assumptions of accounting tricks have been rejected by the data – it seems we are experiencing seasonal structural change, led mainly by construction industry (last year's story fully repeats itself) and exports.

*The data fully backs our scenario of fast rate hikes. Rising wages confirm the mounting demand and cost tension whereas high growth of industrial production shatters growth worries.*



The data fully backs our scenario of fast rate hikes. Rising wages confirm the mounting demand and cost tension whereas high growth of industrial production shatters growth worries. It is then pretty comfortable situation for the MPC to proceed with further hikes. The necessity for continued monetary tightening is going to be stressed by tomorrow's reading on core inflation.

It is worth to mention, though, that the combination of high industrial output may trigger adverse reasoning among some MPC dissenters, based on widening spread between labor productivity growth and real wage dynamics. Following this line of thought, some MPC members may point to decelerating cost pressure. We regard such arguments as those missing the point. The aggregate cost pressure is stemming mainly from services, securing modest productivity rises. Higher wage increases recorded in manufacturing are spilt over services what ultimately leads to higher prices, quoted independently as they belong to non-tradables category.

#### MEDIUM-TERM FORECASTS

Indicator	2006	2007	2008
GDP y/y (%)	6.1	6.5	5.6
Inflation rate (%)	1.0	2.4	4.0
Current account (% of GDP)	-2.1	-4.5	-5.3
Unemployment rate (end-of-year)	14.9	11.4	9.8
NBP repo rate (end-of-year)	4.00	5.00	<b>&gt;6.0</b>

Source: GUS, NBP, BRE Bank, **bold** change on last week

## Fixed Income

*Relatively calm week.*

Last week was rather calm on the FI. Rates stayed in stable range despite economic releases came at much higher range than market expected. We also got some hawkish statements from MPC members suggesting that hike this month is a done deal. The situation on the ASW market calm down a little bit as levels at around 25-30 bp bonds over swap proved to be quite attractive. Our view remains unchanged from last week, we see value in paying 9x12 FRA and paying spread 6x9 ag 21x24 at current levels. We wish you Happy Easter and good luck.

**RECOMMENDATION:**

pay 9x12 FRA and spread 6x9 ag 21x24 at current levels

**AUCTIONS**

	next auc.	offer	avg yield last	last auction date
13 Week T-bills	-	-	4.208%	1/16/2006
26 Week T-bills	-	-	3.943%	4/24/2006
52 Week T-bills	4/14/2008	-	6.230%	3/10/2008
2Y T-bond OK0709	4/4/2008	-	6.189%	1/2/2008
5Y T-bond PS0413	5/7/2008	-	6.167%	3/5/2008
10Y T-bond DS1017	4/9/2008	-	5.785%	2/13/2008
20Y T-bond WS0922	5/14/2008	-	5.794%	1/9/2008

## Money Market

*Chances for cheap end of the reserve are growing*

Stable carry all the week with growing surplus of the cash in the system. Tomorrow open market operation should be quite similar to the last one (underbidding) since just before Easter players will be more likely to posses excess cash then to take liquidity risk. Hence, chances for cheap end of the reserve are growing.

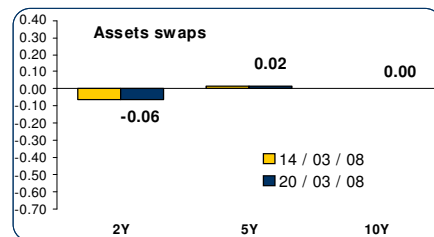
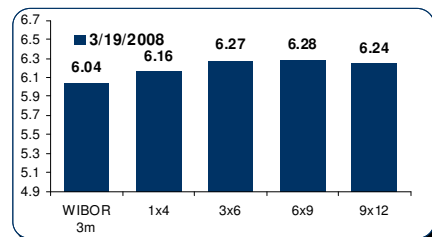
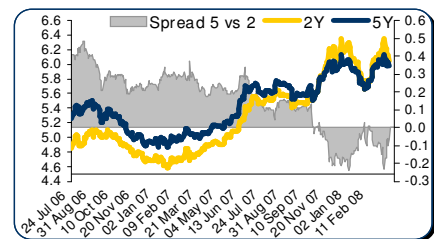
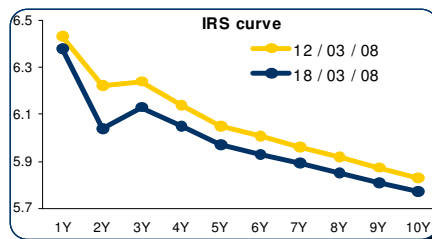
*Is a rate cut possible this year? Not really in our opinion*

As for trading, two bearish figures (wages 12.8 vs 11.5 and industrial output 14.9 vs 10.4% expected) and explosion of bullish sentiment...Some big London players really need to see some rates cut (or strong expectations at least) this year (growing disparities with USD and Euro zones is explanation behind it). However we do not share this point of view at all. In our opinion probability of rates growing above 6.5% is much bigger then to see them falling after two more fast hikes. Hence, we think now is an excellent time to take pay position for longer end.

**RECOMMENDATION:**

Pay synthetic 9\*12 in OISs.

**FIXED INCOME & MONEY MARKET CHARTS**



## Foreign Exchange

### Zloty in range trading

Since Friday the zloty was traded between 3.5650 and 3.5250 and besides Monday's trading we may make it more narrow – 3.5450-3.5250. As main factor providing volatility we may name US banks liquidity problems what induced bad performance of stocks exchanges.

### Volatility curve slightly higher

Narrowing of range and pricing in Easter holidays lowered 1M EURPLN from 7.2 to 6.8 with long end staying untouched.

### **RECOMMENDATION:**

Spot:  
Main supports / resistances:  
EUR/PLN: 3.5200 / 3.5700  
USD/PLN: 2.2300 / 2.3600

### Sell on upticks

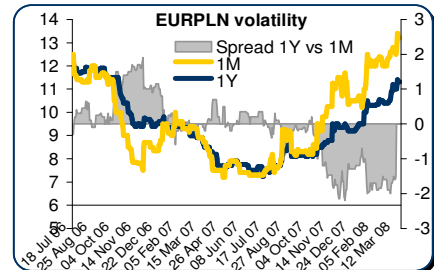
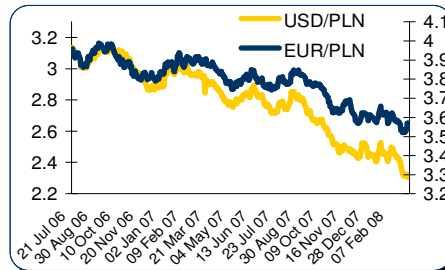
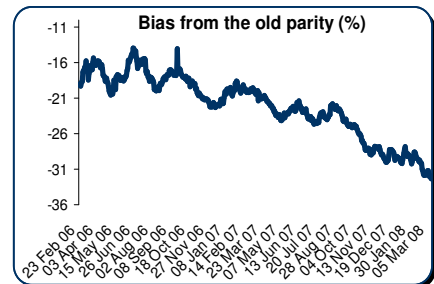
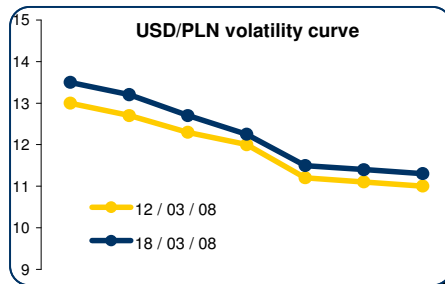
Market reaction suggest there is no big engagement in PLN positions what helps zloty more easily go through global uncertainty. Because it's most likely to stay in range we still see 3.57 as good EURPLN selling level with potential S/L 3.59 and P/T 3.52.

### Options:

### Short EURPLN gamma

We advise to trade short EURPLN gamma as spot market is likely to still trade range-bound.

## FX CHARTS



**MARKET PRICES UPDATE****MONEY MARKET RATES**

## Money market rates (Closing mid-market levels)

date	3M		6M		1Y	
	FXSW	WIBOR	FXSW	WIBOR	FXSW	WIBOR
12/03/08	5.92%	5.91%	6.15%	6.20%	6.32%	6.35%
13/03/08	5.95%	5.93%	6.25%	6.22%	6.49%	6.36%
14/03/08	5.89%	5.91%	6.19%	6.20%	6.34%	6.34%
17/03/08	5.85%	5.93%	5.95%	6.21%	6.15%	6.35%
18/03/08	5.95%	5.93%	6.20%	6.23%	6.40%	6.37%

**FRA MARKET RATES**

## FRA Market Rates (Closing mid-market levels)

date	1X4	3X6	6X9	9X12	6X12
12/03/08	6.15%	6.35%	6.38%	6.34%	6.39%
13/03/08	6.13%	6.29%	6.32%	6.25%	6.31%
14/03/08	6.08%	6.27%	6.29%	6.28%	6.34%
17/03/08	6.14%	6.30%	6.34%	6.31%	6.38%
18/03/08	6.17%	6.30%	6.32%	6.29%	6.35%

**FIXED INCOME MARKET RATES**

## Fixed Income Market Rates (Closing mid-market levels)

date	1Y		2Y		5Y		
	WIBOR	TB	IRS	OK0709	IRS	PS0511	IRS
12/03/08	6.35%	5.08%	5.57%	5.29%	5.72%	5.69%	5.73%
13/03/08	6.36%	5.05%	5.57%	5.29%	5.71%	5.68%	5.72%
14/03/08	6.34%	5.05%	5.57%	5.34%	5.71%	5.67%	5.71%
17/03/08	6.35%	5.05%	5.56%	5.30%	5.71%	5.65%	5.72%
18/03/08	6.37%	5.03%	5.56%	5.34%	5.70%	5.68%	5.70%

**PRIMARY MARKET RATES**

## Last Primary Market Rates

	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	08/03/10	09/03/10	94.074	6.23%	1000	296132	10000
OK0710	08/01/02	09/07/25	85.730	6.19%	1800	2047	1654
PS0413	08/03/05	13/04/25	95.950	6.17%	1500	2019	1500
DS1017	08/02/13	17/10/25	96.048	5.79%	2000	2785	2000

**FX VOLATILITY**

date	USD/PLN 0-delta stradle				25-delta RR		25-d
	1M	3M	6M	1Y	1M	1Y	1M
12/03/08	12.60	12.00	11.20	11.00	0.75	0.90	0.30
13/03/08	12.50	12.00	11.20	11.00	0.75	0.90	0.30
14/03/08	12.70	12.00	11.20	11.00	0.75	0.90	0.30
17/03/08	13.40	12.50	11.60	11.40	0.75	0.90	0.30
18/03/08	13.20	12.40	11.60	11.30	0.75	0.90	0.30

**PLN SPOT PERFORMANCE**

## PLN spot performance

date	USD/PLN	EUR/PLN	bias
12/03/08	2.2664	3.5307	-32.29%
13/03/08	2.2560	3.5613	-32.05%
14/03/08	2.2440	3.5420	-32.42%
17/03/08	2.2442	3.5370	-32.47%
18/03/08	2.2841	3.5333	-32.06%

Note: parity on 11/04/00 – USD= 4.3806, EUR=4.2196, basket share 50:50  
Mid-market volatility of vanilla option strategies

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