



## POLAND WEEKLY REVIEW

### MACROECONOMICS AND FINANCIAL MARKETS

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### PREVIEW: The week of June 3<sup>rd</sup> to July 9<sup>th</sup>

Indicator	Date of release	Pe-riod	BRE forecast	Consen-sus	Last	Comment
NO SIGNIFICANT RELEASES						

## In Focus / Macroeconomics

### Polish FinMin sees lower inflation in June

As the market consensus stood at 3.6%, FinMin's inflation forecast of 3.4% proved to be a real shocker for both analysts and investors (the yields rose by about 15bps across the curve). As for the breakdown, FinMin's forecast hinges on an estimated pronounced drop in food prices of 1.5% m/m, which contrasts with our estimate of unchanged prices in this category. The FinMin's estimates of core inflation are pretty much in line with analyst consensus of 2.7%.

We see a significant upside risk for FinMin's inflation forecast related to the estimates of very volatile food prices (inflation basket had been, as usual, expanded with seasonal fruits and vegetables starting in June). Taking into account our estimates of food and tobacco prices in June, which we still believe in, inflation may well rise up to 3.9% y/y. Thus, the final reading would prove to be even more shocking for the market as the FinMin's forecast.

Turning to the mid-term perspectives, we see inflation to decline at a very slow pace this year and a more pronounced drop in annual inflation rate in 2010 owing to high statistical base effects. The risk to this scenario is skewed upwards, as one cannot rule out VAT rate hikes next year. As far as the monetary policy is concerned, we see the easing cycle coming to the end (at most one corrective rate cut in Autumn). However, rate hikes are very unlikely to materialize before 2010.

### Marginal growth of PMI

June saw only marginal growth of the Polish PMI. It advanced to 43.0pts. from 42.5pts. a month ago. The index describing current production noted progress of the same scale. After a quite abrupt rebound at the beginning of the year, Polish purchasing managers seem to lag behind the respondents in the euro zone (see both PMI and Ifo Index) and growth rate of the PMI has recently lost momentum.

It seems that Polish PMI has been lately kept in check by deteriorating credit conditions (not only the unprecedented rise of the WIBOR rates after the consecutive cuts, but also tapping the volume of credit). Moreover, Polish respondents do not have to automatically react to some bits of optimism abroad (still no confirmation in hard data). In these circumstances we expect PMI momentum to lag behind as long as business confidence abroad is driven mainly by expectations. That is why we expect PMI to start improving swiftly as soon as current assessment of the economy goes decisively north, but this requires green shoots to constitute for good in the hard data.

#### MID-TERM FORECASTS

Indicator	2006	2007	2008	2009	2010
GDP y/y (%)	6.1	6.5	4.8	0.0	2.0
Inflation rate (% , average)	1.0	2.4	4.3	3.4	1.8
Current account (% of GDP, average)	-2.1	-4.5	-5.3	<b>-1.0</b> ↑	<b>-2.9</b> ↑
Unemployment rate (end-of-year)	14.9	11.4	9.5	12.8	13.5
NBP repo rate (end-of-year)	4.00	5.00	5.00	3.25	3.75

Indicator	2008		2009			
	Q3	Q4	Q1	Q2	Q3	Q4
GDP y/y (%)	4.7	2.9	0.8	-0.7	-1.1	0.5
Inflation rate (% , average)	4.7	3.8	3.2	3.6	3.5	3.4
NBP repo rate (end-of-quarter)	6.00	5.00	3.75	3.50	3.25	3.25

*Bold denotes changes from the last release with arrows showing the direction of changes*

## Fixed Income

*Who is right about CPI?*

The main event in the FI market was the release of Ministry of Finance's CPI forecast. To general surprise (we expected 3.9% y/y) CPI is to fall to 3.4% (from 3.6% previous month). Reaction was very positive, curve moved down some 10 bp. in 2y IRS and even more in 10y IRS as curve is flattening a lot. Wibor rates are also coming lower and they are 23 bp lower from the cut. Sentiment is positive, which comes from generally stable demand on the primary market, relatively small volatility and strengthening in PLN. For this week we are staying neutral, we think that curve flattening is premature, we also see high risk to the CPI release that is why we are not participating in the move down in yields. If anything we will be paying 2y IRS or 1y1y IRS on the dips. We also like holding 0711 in ASW and maintain our view about OIS.

**RECOMMENDATION:**

Stay receive in ASW, stay receive in OIS, outright neutral.

**AUCTIONS**

	next auc.	offer	avg yield last	last auction date
13 Week T-bills	-	-	6.142%	12/9/2008
26 Week T-bills	-	-	4.456%	5/4/2009
52 Week T-bills	7/6/2009	-	4.495%	6/22/2009
2Y T-bond OK0112	8/5/2009	-	5.410%	6/3/2009
5Y T-bond PS0414	7/15/2009	-	5.783%	6/3/2009
10Y T-bond DS1019	9/9/2009	-	6.340%	5/20/2009
20Y T-bond WS0429	9/9/2009	-	6.340%	5/20/2009

## Money Market

*Half year end did not disturb the MM much*

The new reserve started with nice surplus and short rates slightly below the main rate. Half year end did not disturb the market much; however activity was significantly restricted for MM. If the surplus of the cash will be sustained, there are huge chances for another cheap month, which is reflected in current OIS curve. Huge amount of the money bills the central bank is forced to offer to keep the market square, will be probably under bided (mainly due to psychological reasons), and therefore supporting low carry.

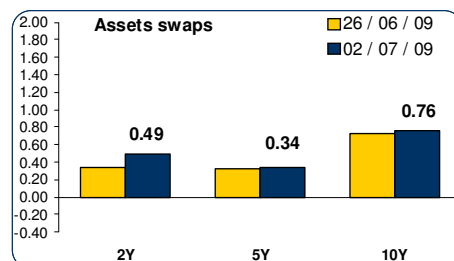
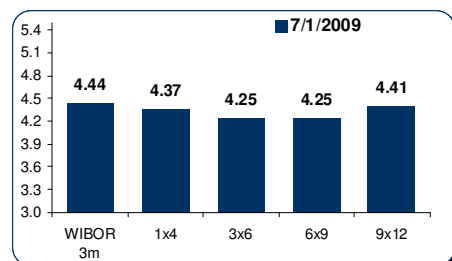
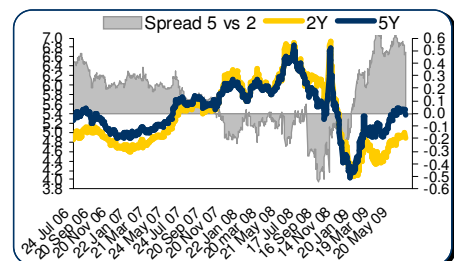
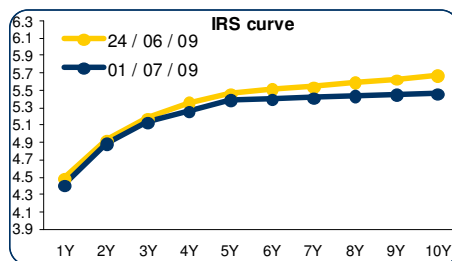
*Bullish CPI projection by the MinFin*

CPI projection made by the MinFin (3.4% versus 3.6% consensus) triggered bullish sentiment despite of the MPC member's comments that the easing cycle is nearly done. We still think that one more cut is coming after summer which along with the cheap carry gives bullish outlook for OISs.

**RECOMMENDATION:**

Sell 1M polonia.

**FIXED INCOME & MONEY MARKET CHARTS**



## Foreign Exchange

*Zloty stronger*

This week zloty has opened at 4.5200 and strengthened to 4.3450. Improving in both regional and global sentiment were reasons

*Implied volatility lower*

Few weeks of range trading plus lower spot made EURPLN curve hit new low with all curve flat at 15.00.

**RECOMMENDATION:**

SPOT

Main supports / resistances:  
 EUR/PLN: 4.2600 / 4.5200  
 USD/PLN: 3.9600 / 3.3000

*Sell upticks*

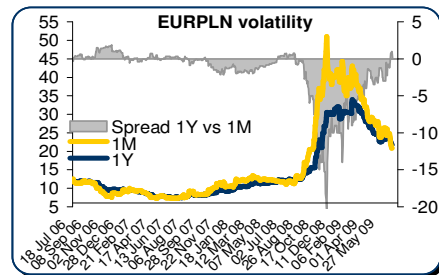
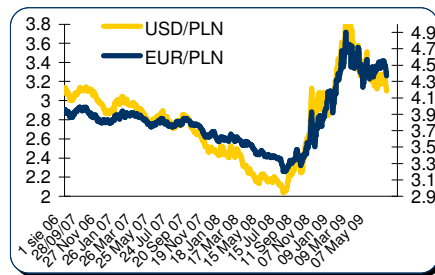
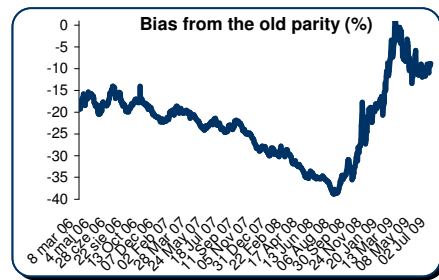
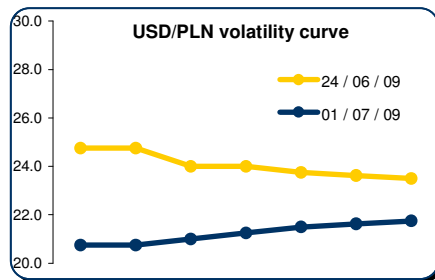
Good sentiment all over the world plus thin summer market are Zloty chances to touch Fibonacci 4.26. Market is pretty short so we will be looking for selling upticks 4.45/4.48.

*Sell gamma*

OPTIONS

Curve is much lower but we still see chance for short gamma trade to be profitable  
 For hedging we suggest buying KO options as it is cheaper due to barrier pricing on high volatility market.

**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
25/06/09	4.33%	4.63%	4.52%	4.65%	4.71%	4.90%
26/06/09	4.32%	4.62%	4.54%	4.65%	4.70%	6.59%
29/06/09	4.38%	4.47%	4.50%	6.49%	4.68%	4.73%
30/06/09	4.30%	4.45%	4.52%	4.53%	4.72%	4.72%
01/07/09	4.25%	4.44%	4.50%	4.53%	4.70%	4.72%

**FRA MARKET RATES**

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

date	1X4	3X6	6X9	9X12	6X12
25/06/09	4.51%	4.31%	4.29%	4.44%	4.45%
26/06/09	4.51%	4.31%	4.29%	4.44%	4.46%
29/06/09	4.47%	4.25%	4.23%	4.40%	4.42%
30/06/09	4.46%	4.29%	4.31%	4.45%	4.49%
01/07/09	4.43%	4.31%	4.29%	4.46%	4.49%

**FIXED INCOME MARKET RATES**

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

date	1Y		2Y		5Y		10Y	
	WIBOR	TB	IRS	OK0709	IRS	PS0511	IRS	DS1017
25/06/09	4.90%	4.60%	4.93%	5.39%	5.48%	5.88%	5.66%	6.44%
26/06/09	6.59%	4.59%	4.93%	5.27%	5.47%	5.80%	5.63%	6.36%
29/06/09	4.73%	4.49%	4.97%	5.31%	5.49%	5.79%	5.65%	6.31%
30/06/09	4.72%	4.39%	4.98%	5.40%	5.45%	5.78%	5.52%	6.29%
01/07/09	4.72%	4.39%	4.89%	5.38%	5.38%	5.72%	5.47%	6.23%

**PRIMARY MARKET RATES**

## Last Primary Market Rates

	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	09/06/29	09/06/29	95.653	4.50%	1200	4663	1200
OK0112	09/07/01	12/01/25	87.362	5.41%	4500	4431	4006
PS0414	09/06/03	14/04/26	99.835	5.78%	1000	1614	971
DS1017	09/04/08	19/10/25	94.460	6.22%	2500	4846	1820

**FX VOLATILITY**

date	USD/PLN 0-delta stradle				25-delta RR		25-delta FLY	
	1M	3M	6M	1Y	1M	1Y	1M	1Y
25/06/09	23.75	23.75	23.50	23.25	3.50	5.10	1.25	1.25
26/06/09	22.50	23.00	22.75	22.75	3.25	5.00	1.25	1.25
29/06/09	21.75	22.25	22.25	22.50	3.00	5.00	1.25	1.25
30/06/09	21.25	21.75	21.75	22.00	2.75	4.75	1.25	1.25
01/07/09	20.75	21.25	21.50	21.75	2.75	4.75	1.25	1.25

**PLN SPOT PERFORMANCE**

## PLN spot performance

date	USD/PLN	EUR/PLN	bias
25/06/09	3.2345	4.5166	-10.92%
26/06/09	3.2110	4.5073	-9.65%
29/06/09	3.2084	4.4908	-8.91%
30/06/09	3.1733	4.4696	-9.34%
01/07/09	3.1375	4.4157	-8.83%

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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