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Comment on the upcoming data and forecasts

On Tuesday GDP for 2nd quarter will be published. We expect slight 0.2pp deterioration compared to 4.4% in 1st quarter and in our view it will the be the last quarter with above 4% growth this year, with high consumption and especially investment (our call for 7.5% should be marked with an upside bias). On Thursday we expect PMI figure to ease after last month's upward adjustment. Our view is supported by deteriorating euro zone (and most significant German) economic indicators (PMI, Ifo, ZEW) and less favorable outlook for industrial production.

Polish data to watch: August 29 to September 2

Publication	Date	Period	BRE	Consensus	Prior
GDP y/y	30-08	Q2	4.2	4.2	4.4
Inflation expectations y/y	31-08	Aug			4.7
PMI	01-09	Aug	51.5		52.9

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Last yield (%)	Prev auction
52-week T-Bills	10/3/2011	600	4.578	5/30/2011
2Y T-bond OK0114	10/12/2011	3000	4.469	8/10/2011
5Y T-bond PS0416	10/19/2011	3000	5.256	8/10/2011
10Y T-bond DS1021	10/19/2011	3000	5.803	7/21/2011
20Y T-bond WS0429	9/22/2011	250	6.246	1/12/2011

Macroeconomic forecasts

Wskaźnik	2008	2009	2010	2011 F	2012 F
GDP y/y (%)	4.8	1.7	3.8	3.8	3.2
CPI Inflation y/y (average %)	4.3	3.5	2.8	4.3	3.1
Current account (%GDP)	-5.3	-1.6	-4.5	-4.9	-4.3
Unemployment rate (end of period %)	9.5	11.9	12.3	11.9	11.5
Repo rate (end of period %)	5.00	3.5	3.5	4.5	4

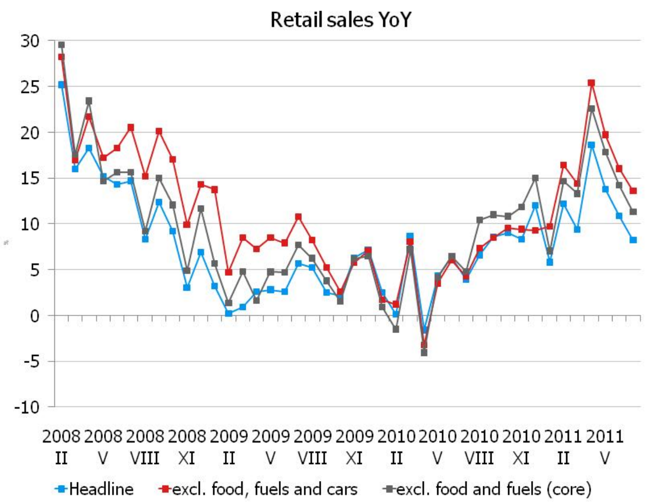
	2010 Q3	2010 Q4	2011 Q1	2011 Q2 F	2011 Q3 F	2011 Q4 F
GDP y/y (%)	4.2	4.5	4.4	4.2	3.7	3.7
CPI Inflation y/y (average %)	2.6	2.9	3.7	4.2	4.2	4.2
Repo rate (end of period %)	3.5	3.5	4	4.5	4.5	4.5

F - forecast

Economics

Retail sales weaker than expected

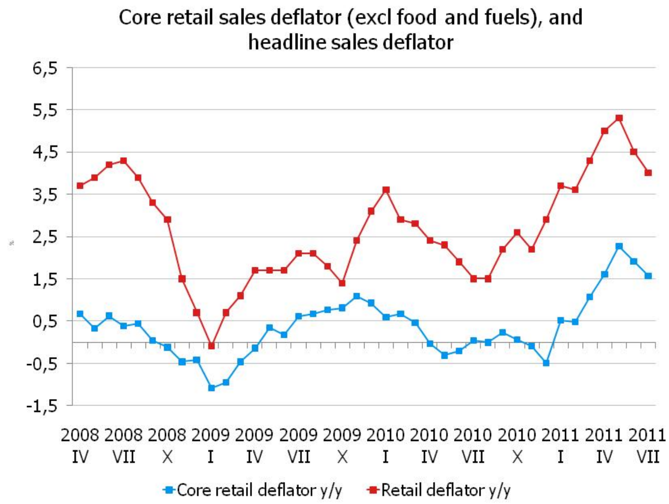
July retail sales data was surprisingly low comparing to market consensus (10.1%) and our more pessimistic forecast (9.4%). Growth rate declines third month in a row, what confirms a reliable break (speaking more in a language of technical analysis) of the rising trend of this category (similar pattern is visible after excluding food and fuels or food, fuels and cars sales).



Turning to details - almost 2 pp. decrease is due to wide „others" category (growth rate drop from 17% to about 10% after stable 17-19% during last few months), we also observe lower car sales (1.6% from 4.2% in June) and food sales (1.4% from 4.1%). Surprisingly sales of clothing/ footwear and furniture/TV/ household appliances categories increased significantly (17.1% and 6.4% respectively), which are neither price nor statistical base effects (easily seen in monthly data).

From the chart above we conclude that peaks of those categories are yet in the past and recently appear only small upward adjustments. Fundamental reasoning based on analysis of disposable income (higher loan installments and inflation) speaks in favor of further drops. Therefore we sustain our previous statements of decelerating private consumption growth and parallel behavior of retail sales.

Additionally, as usual, we calculated retail sales deflators (4% headline and 1.6% core), which both indicate that inflation peak has already been seen in May (see chart).



Historical MPC „Minutes" as consensus moved to the dovish side

Published yesterday, MPC „Minutes" carry only historical message. During the meeting on 6th July, MPC stated that previous rate hikes should be sufficient in bringing inflation back to the target (view most likely influenced by NBP inflation projection), but in case of second round effects MPC is still ready to take further tightening measures. However, this was MPC's reasoning under assumptions of only risks to economic growth (escalation of debt crisis in euro zone, symptoms of slow-down in USA), which yet have been materializing in an unfolding global slowdown. Therefore, „Minutes" may be treated as historical while recent MPC view is better expressed by its members' lately statements.

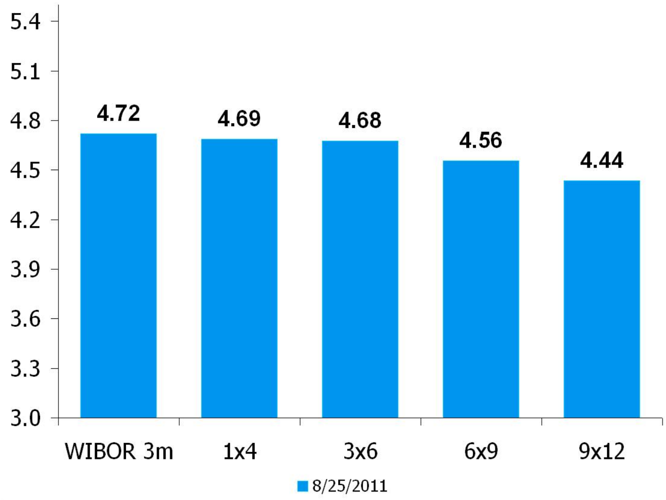
Both Bratkowski and Gilowska suggest that MPC is now in a state close to wait-and-see mood as economic slowdown is somehow undeniable but its depth remains uncertain. However, they are not unanimous as Bratkowski assess that economy can sustain 4% growth in 2012 and upward rate movements are still more likely than the other way round (as inflation will decrease to target level in line with NBP projection more slowly than stipulated by the projection) and Gilowska somewhat takes slowdown for granted (and thinks a fall of inflation is a safe bet). As a matter of fact and as always the vast amount of information comes with Belka's statements, which are clearly dovish. Particularly, governor says openly that "recently a slowdown scenario is more probable than in the first half of this year" and as a result risk balance shifts towards lower inflation (what is more, a slowdown implies also lower pressure on commodities prices assessed by most MPC members as main driving force of current inflation). Nevertheless, Belka highlights that projected 3.2% GDP growth in 2012 is not a "dramatic" slowdown.

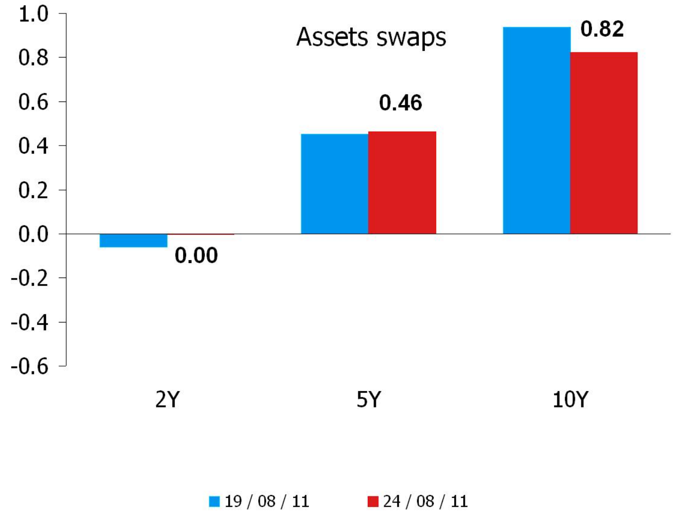
September MPC meeting is not going to be a definite game changer - therefore we do not expect any declaration of easing. Rather there may be a definite statement about a balance of risks (lower growth and inflation). Moreover, we may also look for a kind of insurance, materializing in a commitment to act flexibly on incoming information. More pronounced changes in rhetoric will be still discouraged by high inflation (NBP forecasts point to even higher reading in August than in July, which we also assess as quite probable), high wages growth rate and lack of significant slowdown in real sphere data. In fact we think that until MPC sees more significant downturn in national accounts data for 3rd quarter it will not change its bias, especially regarding recent fragile equilibrium in the FX market. However, a window of opportunity opens at the turn of 2011 and 2012, when inflation and wages growth rate decrease. It should be noticed that with 3-4% CPI, even 50bp rate cut may translate into even higher real rate than now, which seems to be a reference number for some MPC members. We think that is such circumstances MPC will not miss an opportunity to support GDP growth.

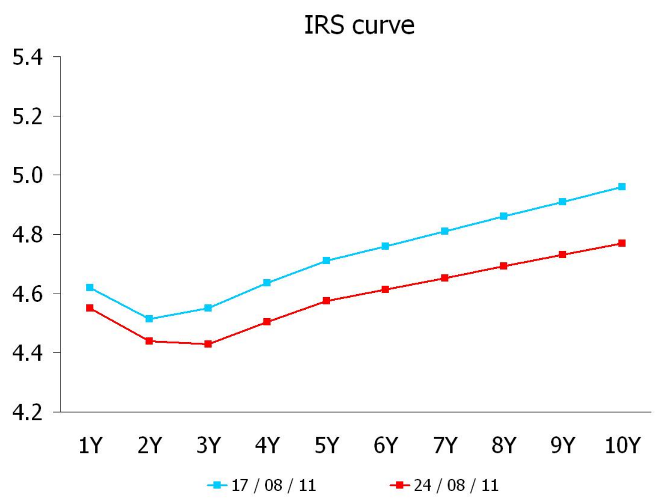
Fixed income

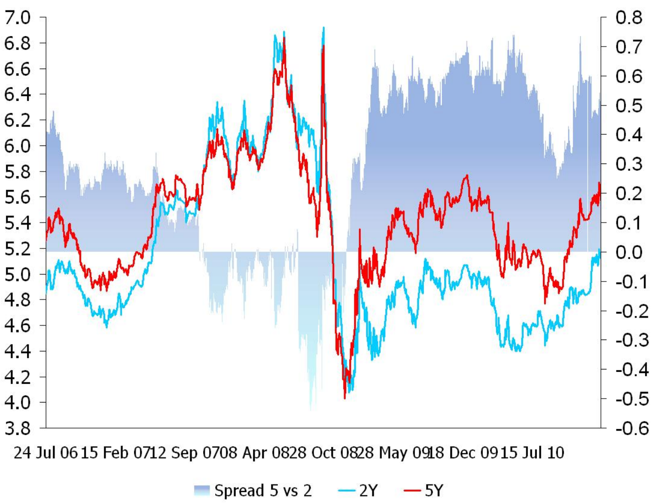
Quite big volatility on the FI market

Last week we had quite big volatility on the FI market. Range on the 2y was 20 bp (4.42/4.62), 5y traded between 4.58 and 4.73. Bonds were also very volatile and we had few when prices moved by more than 100 cents during 24H period. Economic data generally surprised on the downside as retail sales, industrial production points for slower economic growth. The lowest levels on the rates we saw before interviews given by policy members, which played down risk of immediate rate cuts, but overall statements showed that RPP is gradually changing bias towards more neutral. One have to bear in mind that RPP had very little time to discuss developments in the markets and economy and we start to think that next few meetings can bring even more dovish statements especially if inflation will be slowly creeping lower. We expect the communication to soften a little in the coming meeting already, but to see a real change in monetary policy most likely we will have to wait till 1Q of 2012. Our favorite call is to receive 5y here or play 2y5y flattener as it is carry positive and should react very well is economic revisions (GDP lower, CPI lower) process is to be continued. As for the bonds, we prefare long positions in 5y bonds. MinFin is doing very good job in funding borrowing needs, position in 5y bonds is not overcrowded (unlike 10y), as issuance on the primary market wasn't huge recent months, basis in is very favorable for international players, it is sometimes possible to lock spread on the 5y bond with spread better than CDS.







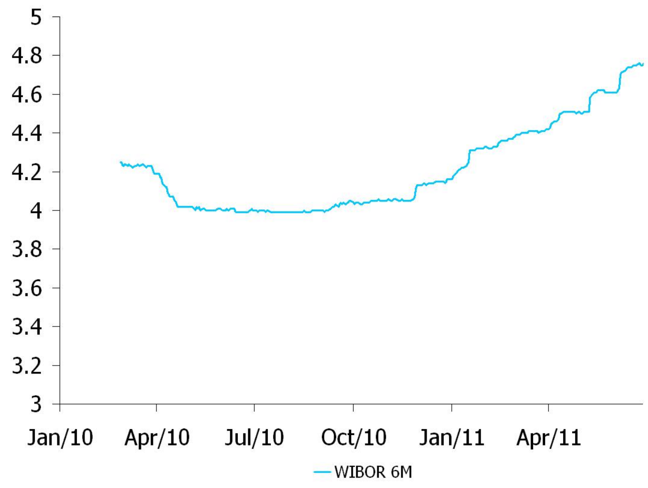


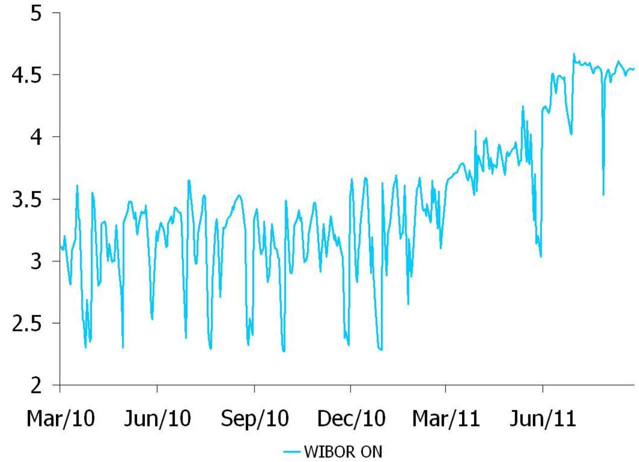
Money market

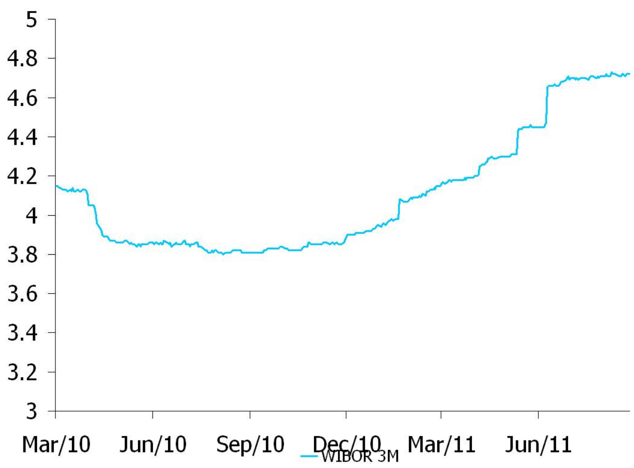
Temporary drop in cost of carry. MPC less pessimistic than the market.

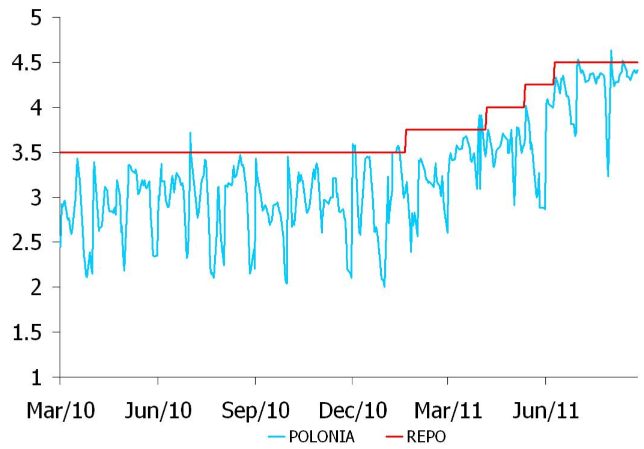
Today's drop in cost of carry due to lower demand for money bills (pln 97 bln against 103,5 bln offer) is just a temporary one. On Tuesday we have the end of the reserve requirement settlement period, therefore additional OMO and probably spike of the shortest rates on a historical basis. Then we will enter the new reserve period with the cost of carry at 4.3+ levels.

Slight move up on a curve after almost 2-week rally, mainly on a few MPC comments with the governor himself. The MPC is protagonist for wait and see strategy. They even do not exclude another hike after a long pause, which we consider a scenario with a negligible potential. Cuts are more likely but not as fast as the market was assuming for the last 2 weeks. However, if the local real economy and moreover the global outlook turns out into the black scenarios, they may got panicked and change their bias accordingly. As of now we bet on a moderate scenario in which two cuts (end of the first and the second quarter 2012) occur.





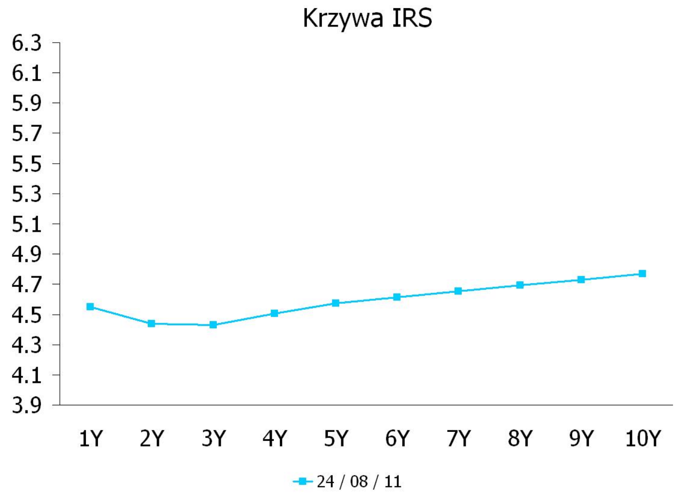




Forex

Range Zloty was played in the range (4.1350- 4.2000 for EUR/PLN) during this week, as the market participants were awaiting Bernanke from Jackson Hole. We don't really know what to expect later, but it is always nice to take a break, and have a perfect excuse for it.

Still wide, range The market is still wide and nervous, 12.0/13.5 constitutes the run, for the whole EUR/PLN curve. The market is positioned himself in the front of the event. The risk reversals are still high (4.5 % 1m and 5% 1Y) and currency spread (USD/PLN - EUR/PLN) is down a little 8% mid now. The Currency spread for CHF/PLN (CHF/PLN - EUR/PLN) was seen at the same level.. (which means considerable correction lower for CHFPLN curve).

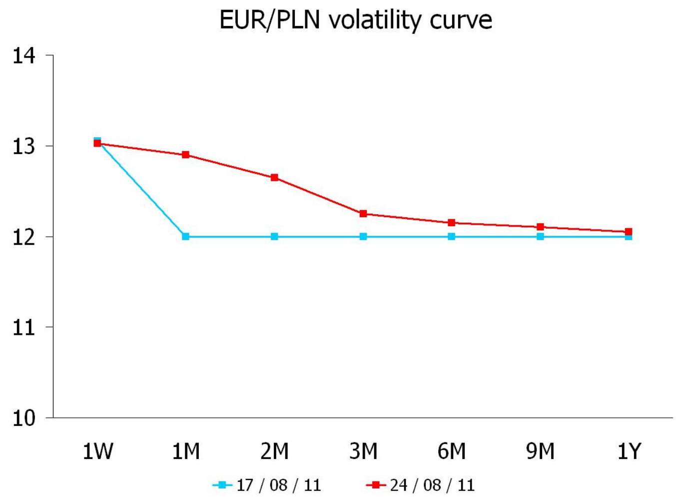


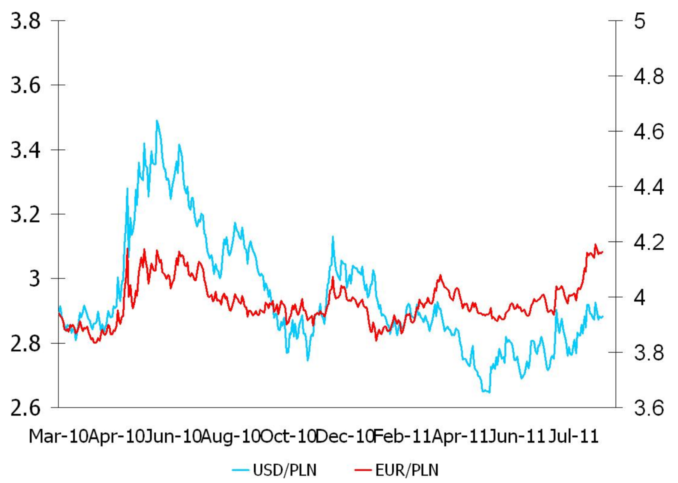
Short-term forecasts

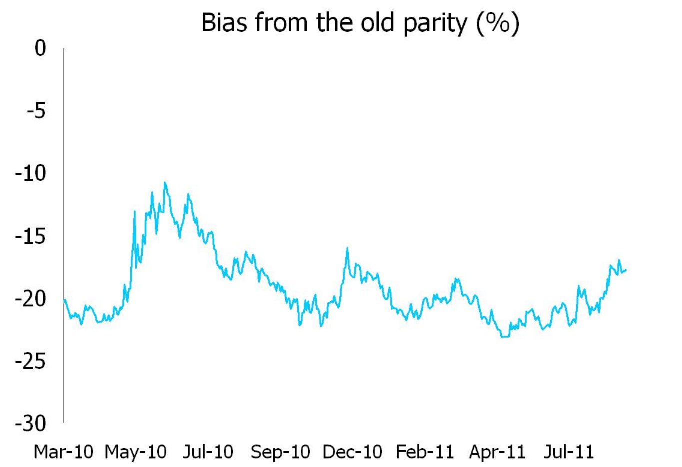
Main supports and resisances
EUR/PLN: 4.1300 / 4.2500
USD/PLN: 2.8500 / 3.0000

Spot. View unchanged from the last week. Play a range, with a skew to the upside (zloty downside), as risk aversion is creeping back on the radar. We are not worried about Jackson Hole or Jean-Caude Trichet, everything they may say or do is probably already priced in. It is Finland collateral request or German constitutional court which are not getting the market attention it should . . . in our opinion.

Derivatives. Unchanged from the last week. We have bought back same of the long Vega position at around 12.50%. And to be honest we have a deya vu of the 2008 (one may call it experience, others the old uncured trauma). Whatever it is, being long Vega and Gamma, you at least know what is your possible loss (Theta, even if it may be very high). . . Being short Vega, Gamma, Vanna or Volga is a big unknown. Overall we are better bids for above ...







Market prices update

Money market rates (mid close)								FRA rates (mid close)				
Date	FXSW 3M	WIBOR 3M	FXSW 6M	WIBOR 6M	FXSW 1Y	WIBOR 1Y	1x4	3x6	6x9	9x12	12x15	6x12
8/18/2011	4.62	4.71	4.72	4.74	4.76	4.77	4.67	4.63	4.50	4.38	4.28	4.56
8/19/2011	4.69	4.72	4.74	4.73	4.77	6.59	4.65	4.63	4.51	4.41	4.31	4.57
8/22/2011	4.61	4.71	4.77	6.49	4.73	4.78	4.67	4.58	4.44	4.31	4.19	4.53
8/23/2011	4.62	4.72	4.74	4.74	4.78	4.77	4.68	4.60	4.45	4.31	4.19	4.52
8/24/2011	4.60	4.72	4.74	4.74	4.77	4.78	4.66	4.62	4.47	4.33	4.19	4.53

Last primary market rates							
Paper	Au. date	Maturity	Avg. price	Avg. yield	Supply	Demand	Sold
52W TB	1/31/2011	1/31/2012	95.84	4.35	2000	2968	1961
OK0113	4/13/2011	1/26/2013	89.16	5.16	5500	7385	4758
PS0416	1/5/2011	4/25/2016	97.08	5.64	6500	2795	1140
DS1020	1/12/2011	4/25/2019	93.02	6.21	2250	4252	2250

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0113	5Y IRS	PS0416	10Y IRS	DS1019
8/18/2011	4.770	4.570	4.440	4.379	4.575	5.027	4.770	5.708
8/19/2011	6.590	4.530	4.440	4.379	4.575	5.027	4.770	5.708
8/22/2011	4.780	4.530	4.450	4.443	4.606	5.049	4.781	5.621
8/23/2011	4.770	4.570	4.460	4.456	4.615	5.079	4.795	5.618
8/24/2011	4.780	4.570	4.535	4.478	4.685	5.131	4.865	5.554

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY	
Date	1M	3M	6M	1Y	1M	1Y	1M	1Y
8/18/2011	13.00	12.25	12.25	12.25	12.25	4.61	0.43	0.61
8/19/2011	13.00	12.25	12.25	12.25	12.25	4.61	0.43	0.61
8/22/2011	13.25	12.25	12.25	12.25	12.25	4.54	0.53	0.78
8/23/2011	13.00	12.50	12.40	12.40	12.40	4.52	0.54	0.78
8/24/2011	12.90	12.25	12.15	12.05	12.05	4.51	0.55	0.77

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
8/18/2011	4.1417	2.8722	3.6112	3.7517	1.5274	0.1697
8/19/2011	4.1913	2.9270	3.6972	3.8324	1.5313	0.1715
8/22/2011	4.1728	2.8943	3.6783	3.7727	1.5302	0.1706
8/23/2011	4.1533	2.8713	3.6485	3.7510	1.5315	0.1703
8/24/2011	4.1601	2.8823	3.6439	3.7643	1.5276	0.1702

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