

**Bureau of Economic Analysis**
(research)

Ernest Pytlarczyk, PhD, CFA
chief economist
tel. +48 22 829 01 66
ernest.pytlarczyk@brebank.pl

Marcin Mazurek, PhD
senior analyst
tel. +48 22 829 01 83
marcin.mazurek@brebank.pl

Paulina Ziembinska
analyst
tel. +48 22 829 02 56
paulina.ziembinska@brebank.pl

Artur Pluska
analyst
tel. +48 22 526 70 34
artur.pluska@brebank.pl

Financial Markets Department
(business contacts)

Lukasz Barwicki
head of trading
tel. +48 22 829 01 93
lukasz.barwicki@brebank.pl

Inga Gaszkowska-Gebska
institutional sales
tel. +48 22 829 01 67
inga.gaszkowska-gebska@brebank.pl

Bartłomiej Malocha, CFA
money market
tel. +48 22 829 01 77
bartlomiej.malocha@brebank.pl

Jaroslav Stolarczyk
structured products
tel. +48 22 829 01 67
jaroslav.stolarczyk@brebank.pl

Marcin Turkiewicz
fx market
tel. +48 22 829 01 67
marcin.turkiewicz@brebank.pl

Reuters pages:
BREX, BREY, BRET

Bloomberg:
BRE

SWIFT:
BREXPLPW

BRE Bank S.A.
18 Senatorska St.
00-950 Warszawa
P. O. BOX 728
tel. +48 22 829 00 00
fax. +48 22 829 00 33
http://www.brebank.pl

Table of contents

Economics	page 2
• MPC left interest rate unchanged	
Fixed income	page 3
• Return of investors into polish government bonds	
Money market	page 4
• Cheap month start	
• MPC meeting - hawkish governor Belka	
FX market	page 5
• Zloty stronger	
• Volatility lower	

Comment on the upcoming data and forecasts

On Thursday inflation and current account data will be published. The fall in CPI growth results from stronger than seasonal decline in food prices and 1.5% lower fuel prices (core inflation growth is set to top 2.8-2.9% y/y). In balance of payments we expect exports and imports to break seasonal patterns (upwards - due to higher than expected August industrial production and retail sales data), we also look forward to better balance of income and slightly higher transfers from EU. Higher growth of M3 results from money outflow from mutual funds, PLN depreciation and increasing competition on deposits market.

Polish data to watch: October 3 to October 7

Publication	Date	Period	BRE	Consensus	Prior
CPI y/y (%)	13.10.	Sep	4.0	4.1	4.3
C/A (mln EUR)	13.10.	Aug	-1055	-1273	-1644
M3 y/y (%)	14.10.	Sep	8.7	9.2	8.5

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Last yield (%)	Prev auction
52-week T-Bills	-	600	4.578	5/30/2011
2Y T-bond OK0114	-	3000	4.469	8/10/2011
5Y T-bond PS0416	10/19/2011	3000	5.256	8/10/2011
10Y T-bond DS1021	-	3000	5.803	7/21/2011
20Y T-bond WS0429	-	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	3.5	3.2
CPI Inflation y/y (average %)	4.3	3.5	2.8	4	3.4
Current account (%GDP)	-5.3	-1.6	-4.5	-4.9	-3.4
Unemployment rate (end of period %)	9.5	11.9	12.3	12.3	12.8
Repo rate (end of period %)	5.00	3.5	3.5	4.5	4.0

	2010	2010	2011	2011	2011	2011
	Q3	Q4	Q1	Q2	Q3 F	Q4 F
GDP y/y (%)	4.2	4.5	4.4	4.3	3.6	3.4
CPI Inflation y/y (average %)	2.6	2.9	3.7	4.2	4.1	3.9
Repo rate (end of period %)	3.5	3.5	4.0	4.5	4.5	4.5

F - forecast



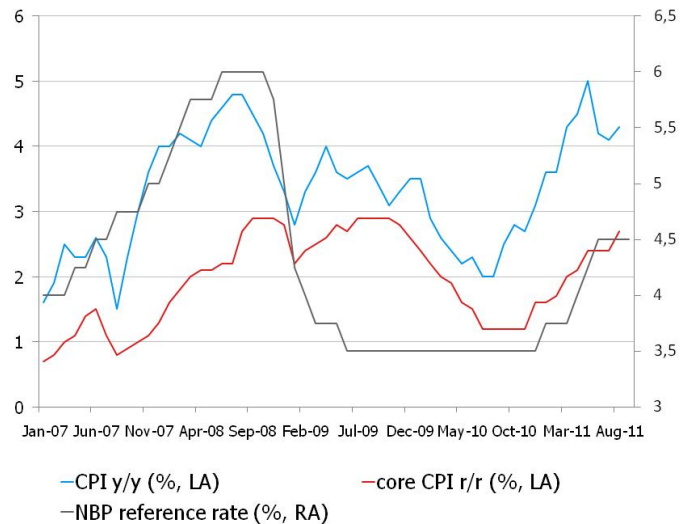
Economics

MPC left interest rate unchanged

In line with expectations MPC left repo rate unchanged at the 4.5% level. The statement makes clear that macroeconomic perspectives have darkened further due to global economic activity weakening, deterioration of economic indicators (despite surprisingly good industrial production and retail sales data in August, which we consider one-offs), stagnation on labor market. However, inflation is stuck at high level and will be there for some time (in spite of the fact that growth of August CPI reading to 4.3% resulted mainly from communications category).

Part of the statement concerning future monetary policy remained the same: „The Council does not rule out the possibility of further monetary policy adjustment, should the outlook for inflation’s return to the target deteriorate”, what market interpreted as relatively hawkish attitude (e. g. by FRA rates growth). The main risk factor for inflation’s return to the target remains PLN depreciation (Belka highlighted that current EURPLN rate do not reflect properly Polish fundamentals and deviate from fundamental equilibrium levels).

After the conference it is clear that it is high FX market volatility what prevents MPC from monetary loosening and keeps relatively hawkish rhetoric still on. Had we seen the opposite attitude it could call into question launched in September by NBP FX intervention policy. Simultaneously Belka highlighted that NBP is not defending particular PLN levels, but fights against speculation and aims to calm FX market. What is more, he announced that interventions will be continued, which together with risks of capital outflow and high inflation indicates maintenance of relatively hawkish rhetoric in the forthcoming months. In our opinion the first moment for change in MPC tone and following rate cuts will be beginning of the next year with lower (mainly due to statistical base effects) inflation (attention focused also on new November NBP inflation projection) assuming smaller FX market volatility (and more tranquility in global financial markets) and greater investors’ approval for Polish fiscal policy. Therefore, we sustain our previous assessment of unchanged rates till the end of 2011.





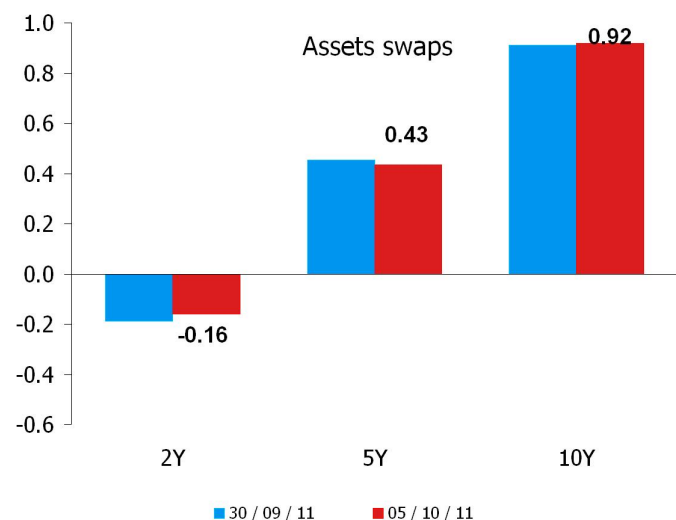
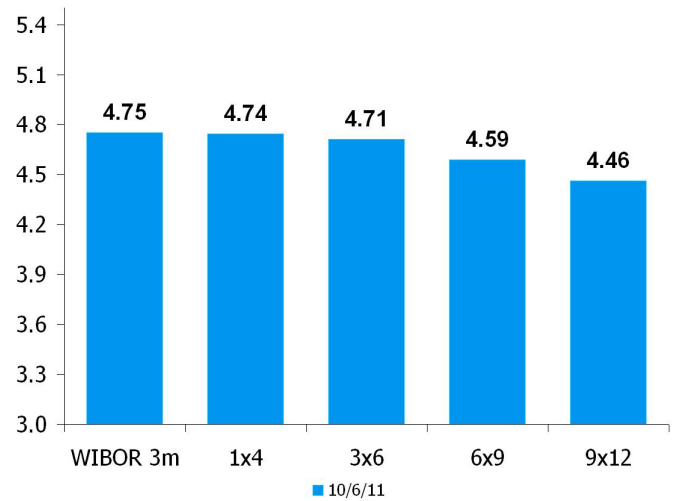
Fixed income

Return of investors into polish government bonds

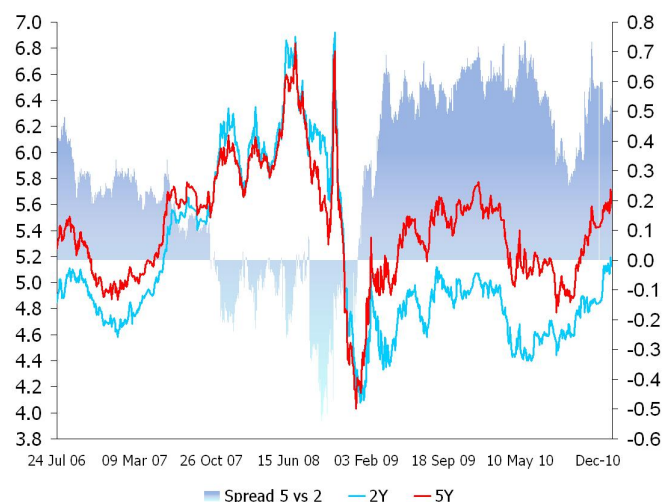
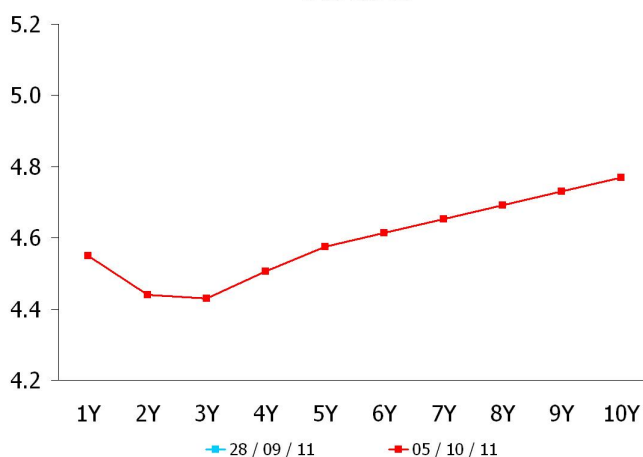
Last week we had seen return of investors into polish government bonds. Most preferred sector was 5y (PS0416) which moved 100 cents from last week. 10y bonds also enjoyed nice rally over performing swaps. 5y5y forward have narrowed to 175 bp from 250 bp high in previous weeks. 5y10y is stable relatively unchanged trading at 18 bp, but big flattening happened in 2y5y which moved from 20 bp to just 14 bp. 1y2y has flattened also after Belka gave rather hawkish statement about rates and FX interventions which are aimed to curb CPI pressures.

Over weekend we will have general elections, current polls show that PO will be winner, but it is unclear who will be in the coalition, our view is that PO and PSL (peasant party) will not have enough majority and with SLD (socialist party) will move PO more into compromises making any kind of fiscal adjustments hard to pass (all three main rating agencies have spoken that they are looking forward to speeding up structural reforms process after elections in Poland). With recent rally in the risk and narrowing of ASW spreads we are skeptical that the rally can move forward.

Ministry of Finance is doing good job with tactical moves, but we think that it was story of last year, 2012 will be the year with most likely lower growth, budget assumptions thus far were conservative but at the moment they look to be on the very optimistic side. Coalition talks will not be easy and with data suggesting real economy is starting to put on brakes, curve should price in risk long end of the curve. 5y5y can move again to 250 target and ASW will not like it also, especially with basis swaps narrowing making funding of new bond positions more and more expensive.



IRS curve



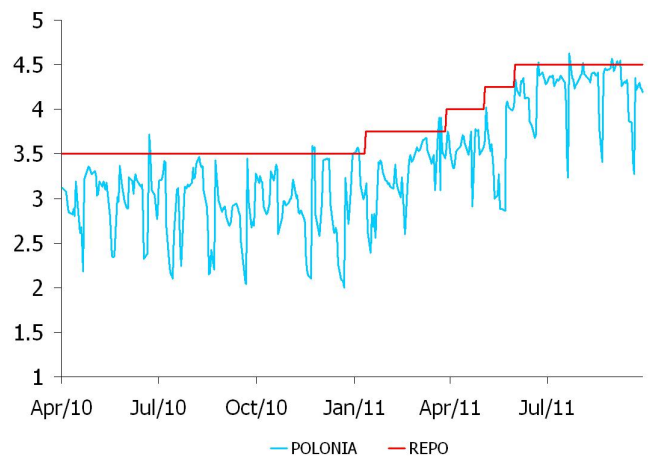
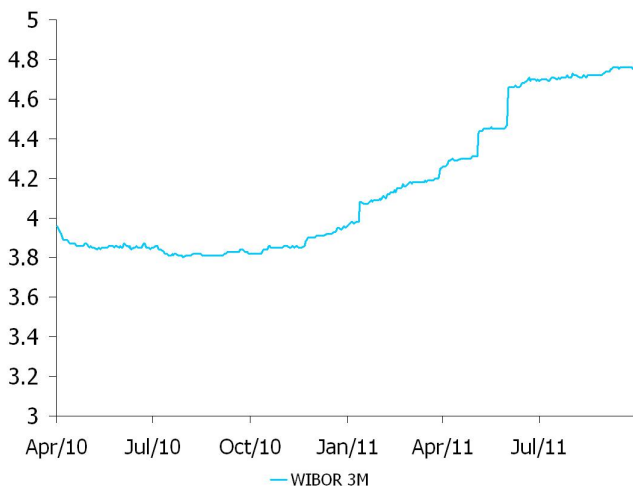
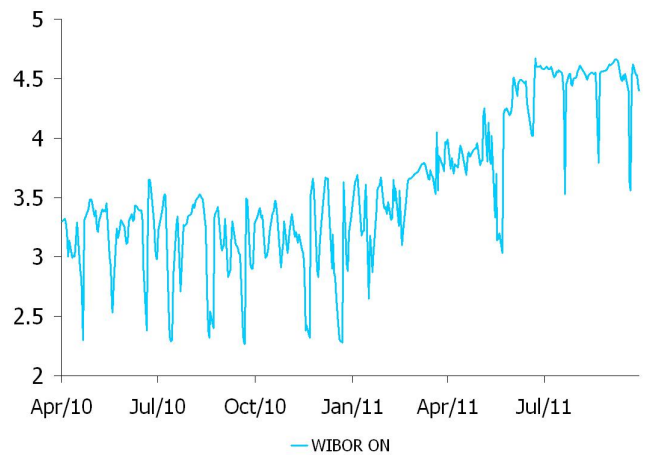
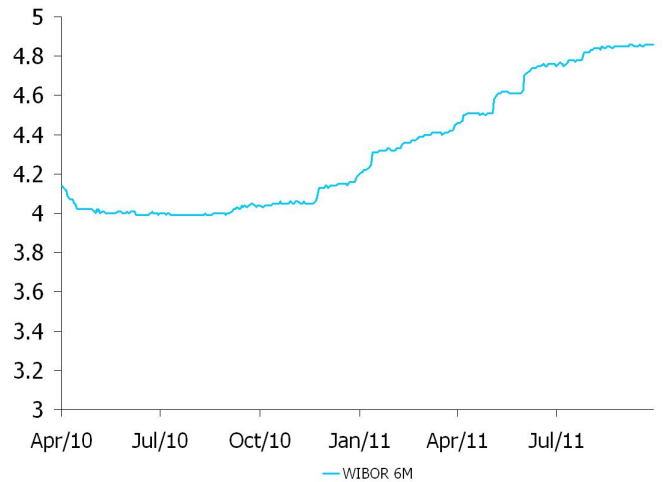


Money market

Cheap month start. MPC meeting - hawkish governor Belka

Unexpectedly we had quite low polonia fixings in the first week of the month. After last Friday's OMO, market left itself around PLN 8 bn surplus. Given that, we wonder why the NBP hasn't done additional operation? Adding a low end of the reserve period, average Polonia fixing for last 30 days came at 4.22. That is 8 pips lower than it used to be for the last few months.

October's no change was no surprise to the market and during the press conference Belka reiterated that MPC is ready to hike rates if needed. Reaction to that comment was smaller than last month. Market was driven by expectations for a cut from ECB.





Forex

Zloty stronger In the beginning of the week the Central European currencies extended losses because of existing concerns over the global financial system, the only exception was the zloty. Poland's central bank intervened on the foreign exchange market again, on Monday selling euros and buying zlotys. The three recent interventions, and the threat of the new ones, improved global market sentiment in second part of the week, helped to lift the zloty roughly 1.5 percent to the euro from last week closing.

Volatility lower As the zloty was traded in the narrow range during last week, we experienced the short volatility collapse. 1 month EUR/PLN is now trading 3 % lower than last week (16.5% vs. 13.5% now). In fact the theta bills forced some Vega selling especially in the 1-3m space : the 3m EURPLN fell down from 15.6% to 13.75%, 1Y fell from 14.6 to 14.0. Currency spread (USDPLN against EURPLN) is still very high at 10.25 - but it's because of the turbulences in EURUSD.

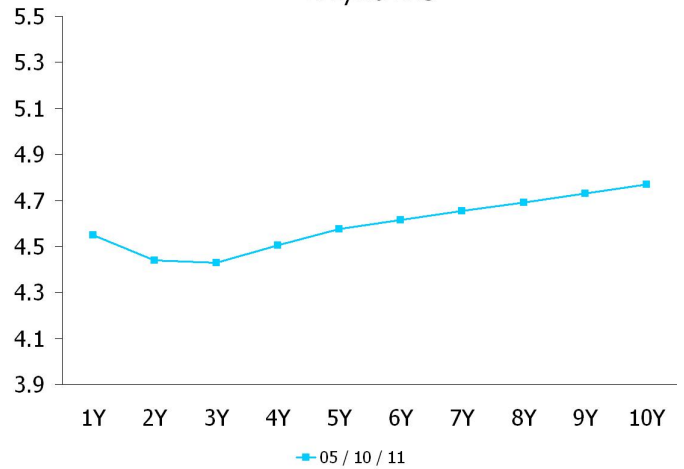
Short-term forecasts

Main supports and resistances
EUR/PLN: 4.3200 / 4.4500
USD/PLN: 3.1500 / 3.3500

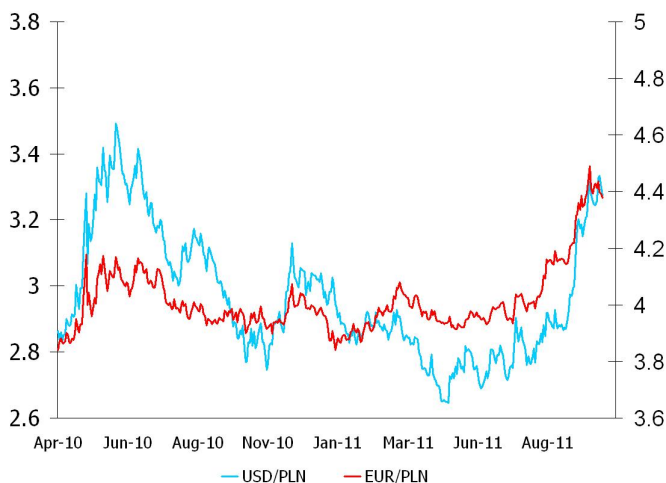
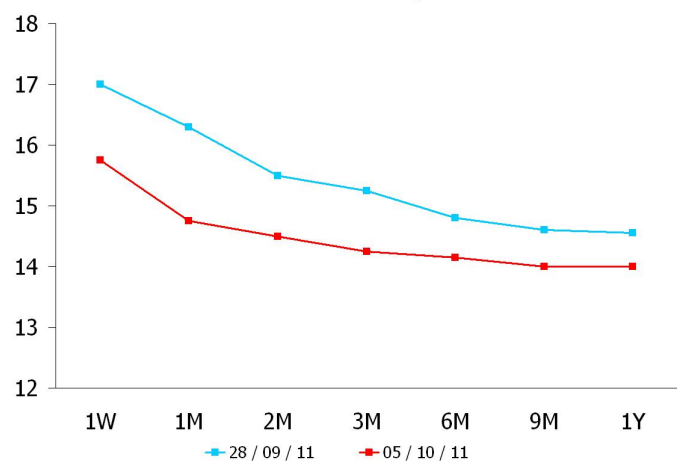
Spot. There are still many risks connected with debt crisis, data signaled slowing global economic growth and parliamentary election in Poland on Sunday. Nevertheless the presence of NBP on the market allow as to think the Zloty is still going to play and hold the range 4.34-4.44.

Derivatives. We think that EUR/PLN will be capped below 4.5 even till the end of the year. So there is potential for to the move lower in the implied volatility. That's why we still suggest being short vega especially in 1m-3m tenors as Polish authorities are likely to increase their activity near the end of the year. The options below 1month sold off really heavily, so we have decided to close that pure gamma bets.

Krzywa IRS



EUR/PLN volatility curve



Bias from the old parity (%)





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
9/29/2011	4.59	4.76	4.60	4.75	4.69	4.79	4.74	4.70	4.58	4.48	4.40	4.70
9/30/2011	4.58	4.76	4.61	4.76	4.76	6.59	4.74	4.71	4.60	4.49	4.42	4.68
10/3/2011	4.56	4.76	4.73	6.49	4.68	4.78	4.74	4.72	4.59	4.46	4.40	4.64
10/4/2011	4.54	4.76	4.67	4.76	4.62	4.78	4.77	4.73	4.61	4.50	4.43	4.69
10/5/2011	4.59	4.76	4.67	4.76	4.61	4.79	4.75	4.73	4.61	4.50	4.43	4.69

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
9/29/2011	4.790	4.570	4.641	4.504	4.821	5.272	4.986	5.919
9/30/2011	6.590	4.530	4.670	4.483	4.840	5.295	5.005	5.917
10/3/2011	4.780	4.530	4.660	4.481	4.830	5.300	4.995	5.949
10/4/2011	4.780	4.570	4.645	4.482	4.815	5.308	4.995	5.945
10/5/2011	4.790	4.570	4.610	4.451	4.785	5.219	4.965	5.885

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY	
Date	1M	3M	6M	1Y	1M	1Y	1M	1Y
9/29/2011	16.00	15.20	14.95	14.75	14.75	4.98	0.65	0.86
9/30/2011	16.00	15.20	14.95	14.75	14.75	4.98	0.65	0.86
10/3/2011	15.85	15.05	14.90	14.70	14.70	5.01	0.63	0.86
10/4/2011	15.85	15.05	14.90	14.70	14.70	5.03	0.64	0.85
10/5/2011	14.75	14.25	14.15	14.00	14.00	5.03	0.64	0.87

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
9/29/2011	4.4293	3.2451	3.6298	4.2453	1.5227	0.1807
9/30/2011	4.4112	3.2574	3.6165	4.2385	1.5097	0.1791
10/3/2011	4.4370	3.3265	3.6511	4.3315	1.5042	0.1785
10/4/2011	4.3957	3.3337	3.6180	4.3481	1.4749	0.1766
10/5/2011	4.3918	3.2966	3.5794	4.2983	1.4698	0.1769

Disclaimer

Distribution and use of this publication The review note is based on the information available to the public. This review creates exclusively a marketing information as defined in Paragraph 9 Section 1 of the Decree of Minister of Finance dated November 20, 2009 on procedures and conditions to be followed by investment firms and banks mentioned in Article 70 Section 2 of Law on Trading in Financial Instruments dated July 29, 2005 as well as by custody banks. This review note is provided to you for information purposes only and is not intended as advice on any particular matter or as recommendation, offer or solicitation for purchase of sale of any financial instrument and should not be taken as such. BRE Bank SA, its directors, officers, executives, managers, servants or agents expressly disclaim all liability to any person in respect of any-thing, and in respect of the consequences of anything, done or omitted to be done, wholly or partly, in reliance upon the whole or any part of the contents of this review note. The opinions and estimates contained herein reflect the current judgment of the author(s) on the date of this document and are subject to change without notice. The opinions pointed in review do not necessarily correspond to the opinions of BRE Bank SA. The past performance of financial instruments is not indicative of future results. No assurance can be given that any financial instrument or issuer described herein would yield favourable investment results. BRE Bank and/or its principals or employees may have a long or short position or may transact in the financial instrument(s) and/or securities referred to herein or may trade in such financial instruments with other customers on a principal basis. No client or other reader should act or refrain from acting on the basis on any matter contained in it without taking specific independent professional advice on the particular facts and circumstances in issue. Copyright protection exists in this publication and it may not be, even partially, reproduced or distributed without the prior written agreement with BRE Bank SA.

©BRE Bank 2011. All rights reserved.