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Comment on the upcoming data and forecasts

On Tuesday CPI and C/A will be published. We expect further growth in food (1.3% m/m) and fuels (3.4% m/m) prices. Effect of Zloty depreciation becomes more and more visible in most categories in CPI basket. We expect C/A deficit to widen; our models are consistent in exports (11860 mln EUR) and imports (12433 mln EUR) forecasts, each of them points in the same direction. On Wednesday NBP will publish M3 money supply - excluding FX and statistical base effects we expect annual growth similar to October. „Deposits war” seems to be in the cards. On Friday labor market data will be published. As far as wages are concerned, the growth rate is mostly affected by seasonal shifts of bonuses in mining. As far as employment goes, economic indicators stabilized at low levels, comparison of employment path now and in 2008 favors current situation - therefore observed slowdown may be called only „slow erosion”.

Polish data to watch: December 12 to December 16

Publication	Date	Period	BRE	Consensus	Prior
CPI y/y (%)	13.12.	Nov	4.7	4.5	4.3
C/A (mln EUR)	13.12.	Nov	-2230	-1897	-1901
M3 y/y (%)	14.12.	Nov	10.5	10.6	10.3
Employment y/y (%)	16.12.	Nov	2.3	2.3	2.5
Wages y/y (%)	16.12.	Nov	4.6	5.1	5.1

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 PS1016	-	2500	5.147	11/16/2011
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 (%)	5.1	1.6	3.8	4.0	2.8
CPI Inflation y/y (average %)	4.3	3.5	2.8	4.2	3.6
Current account (%GDP)	-5.3	-1.6	-4.5	-4.9	-3.6
Unemployment rate (end of period %)	9.5	12.1	12.4	12.6	12.8
Repo rate (end of period %)	5.0	3.5	3.5	4.5	4.0

	2010	2010	2011	2011	2011	2011
	Q3	Q4	Q1	Q2	Q3	Q4 F
GDP y/y (%)	4.4	4.7	4.5	4.3	4.2	3.6
CPI Inflation y/y (average %)	2.6	2.9	3.7	4.2	4.1	4.4
Repo rate (end of period %)	3.5	3.5	4.0	4.5	4.5	4.5

F - forecast



Economics

MPC left interest rates unchanged

In line with expectations MPC left interest rates unchanged. According to the statement MPC retains hawkish bias focusing attention mainly on inflation perspectives and devoting less space for the real sphere. In general the statement is quite similar to the one from the previous month (some paragraphs remained literally unchanged).

MPC acknowledged better GDP data for Q3'2011 (which „confirm continuously relatively high and stable growth“) and anti-cyclical behavior of net exports. Similarly to previous statement MPC states the possibility of „flagging economic activity in the subsequent quarters“ and annual CPI persistence at a heightened level (primarily due to the previous sharp rise in global commodity prices and the zloty depreciation of recent months). In the context of inflation expectations MPC seems to be more hawkish (stating that households' inflation expectations „remained elevated“ rather than „shifted somewhat upwards“), which probably results from last reading aberration (only small decrease of expectations in spite of higher decrease of CPI; the behavior somehow negates adaptive nature of expectations). Inflation perspectives remained unchanged as the sentence concerning implemented tightening („the significant monetary tightening implemented in the first half of 2011 should enable inflation to return to the target in the medium term“) remained in the statement. The Council maintained also possibility for further monetary policy adjustments, should the outlook for inflation's return to the target deteriorate.

In Q&A part during the conference Belka committed to further FX interventions in case of zloty destabilization (but not defense of certain level). What seems interesting, Belka positively assessed fiscal policy plans for the next year.

If there was a motion of a hike a for hike submitted (Każmierczak) we will get to know only from the „Minutes“. But even without this information we claim that MPC maintains consistent stance focusing attention on current factors which may endanger CPI's return to target (high current CPI level, relatively good current real sphere condition) and devoting less attention to the future risk-factors (the scale of the slowdown). The topic of rate cuts will return at the beginning of 2012 not only with lower growth and easing inflation (statistical base effect), but also due to improvement in monetary policy transmission via a change in the FX structure of new mortgage loans (new loan creation in foreign currencies will be brought to none). Then rate cuts would influence not only FX market (in a way that stands in contrast with efficient monetary transmission - stronger PLN after a rate hike, thereby lowering the costs for foreign loans holders) but also housing market and households' spending and investments.

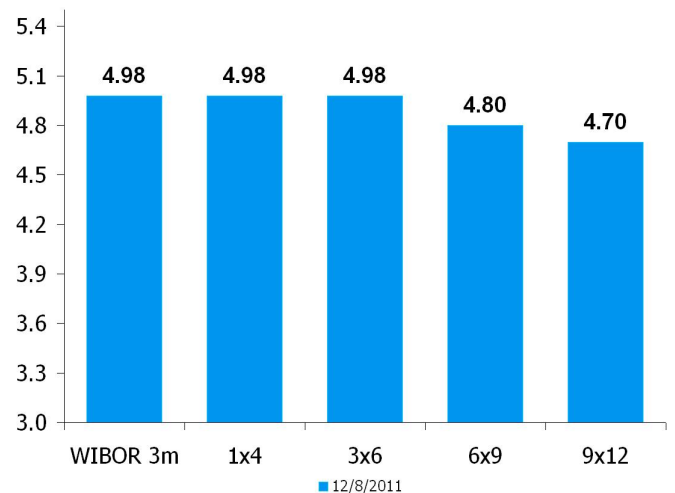
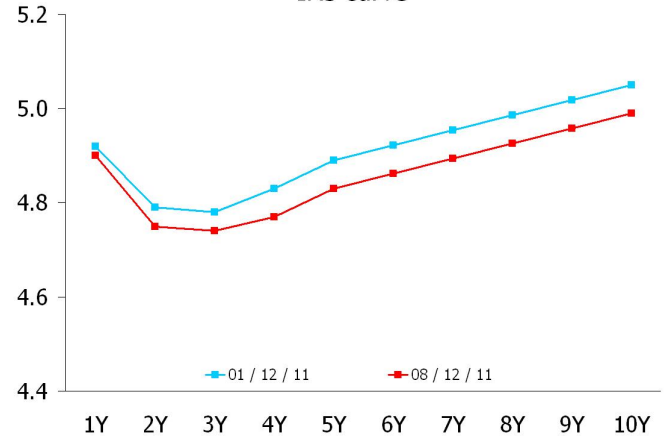


Fixed income

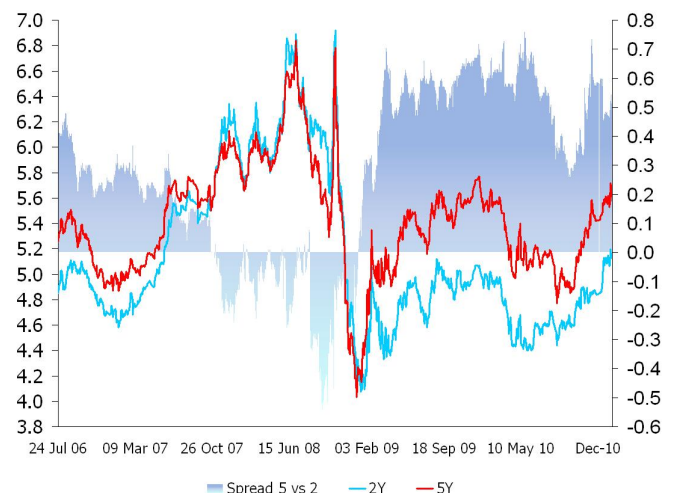
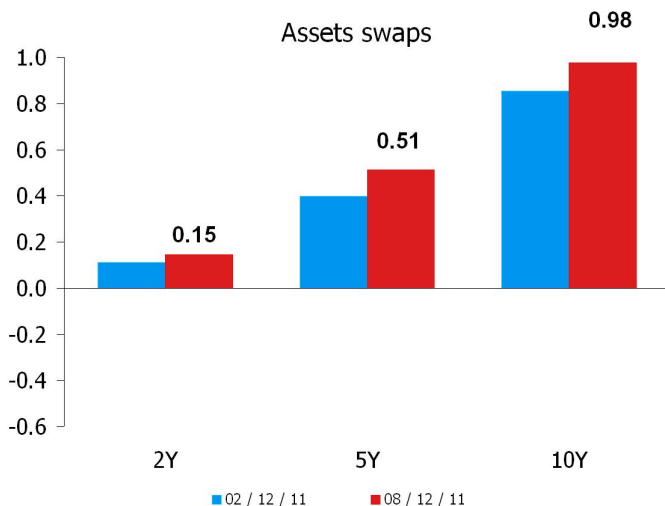
The Gravity

Last week we experienced phenomena of December market, nice volatility and very little liquidity. Rates traded in nice range of 4.74/4.84 in the 2y, 5y IRS range was even wider (4.82/4.94), bonds traded in 10y almost full point up or down depending on risk market sentiment. Local data and events (such as MPC meeting, budget approval) had secondary meaning. Sentiment is very fragile and market swings from euphoria into tears within hours. The only sustained trade was wider ASW prices and cheaper funding despite NBP efforts to sterilize excessive market liquidity. Next week we will have last bits of important data, CPI, which we think will come very high (we look for 4.7% yty) and we will have switch auction, where MinFin will probably yet again offer all bonds and will not be shy to lock as much as possible to further prefund next year borrowing needs. The theme of this weekly is rather physics than economy since it doesn't really seem to matter (nor to work). „Gravity” will finally start to push lower CPI, especially early next year, growth is on the falling path resembling physics of the downward spiral. Polish economy is also like a moon to the bigger EU planet and we will be strongly influenced by developments in our main trading partners. We are referring to satellites and planets hoping it will not change into black hole phenomena, as it would have much more serious and rather unpredictable consequences. We are looking forward to receiving rates especially in 2y and 5y sectors, we think that investors will be coming back to the bonds market early next year, 5y bonds seem to offer the biggest value. MPC can be on the wait and see mode, but the experiment we are witnessing at mom it reminds very much what happened in winter 2008. Markets usually don't allow us to repeat same experiments twice, but there you go ... Gravity works after all.

IRS curve



Assets swaps



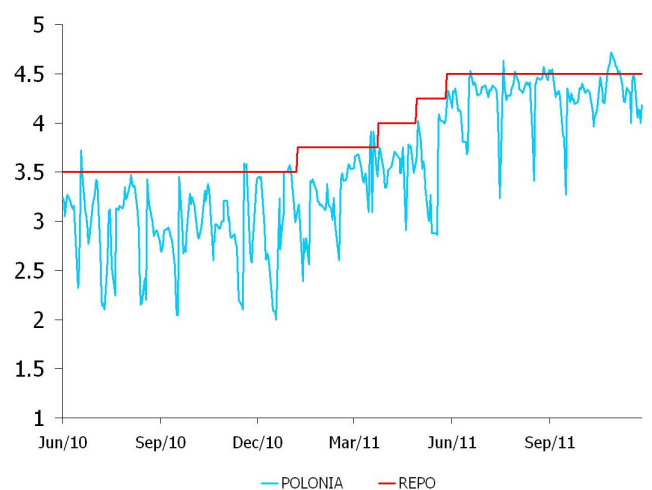
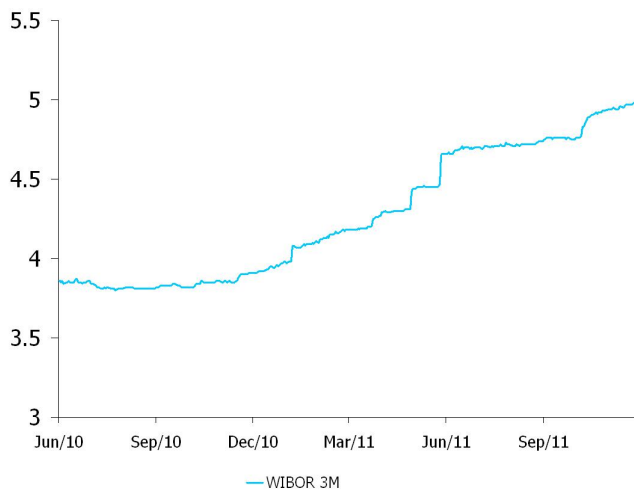
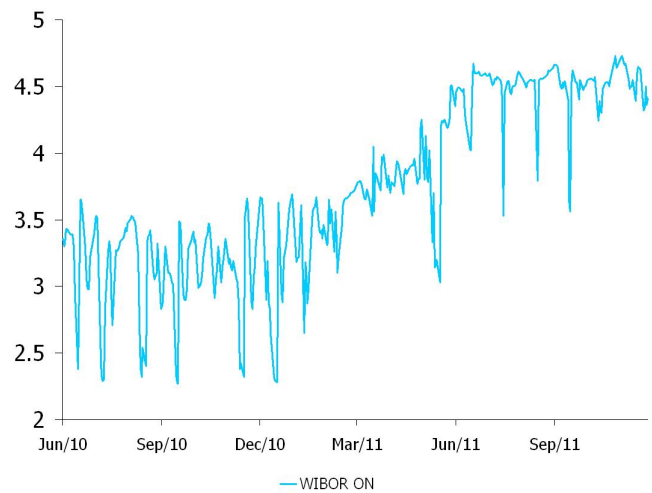
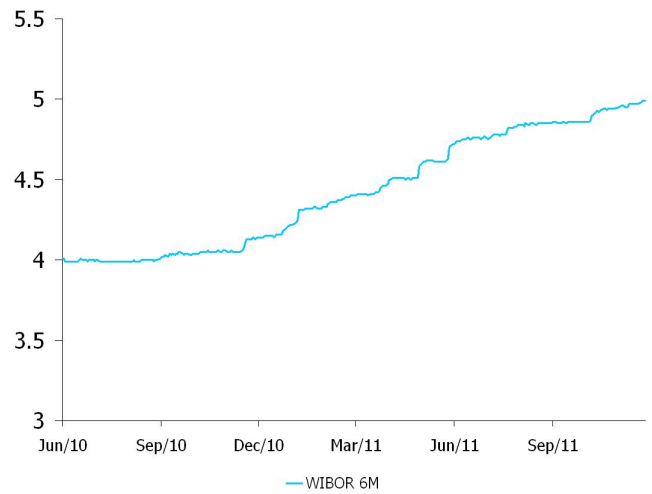


Money market

Cheap carry despite additional OMOs. MPC, ECB in line. CPI crucial figure this month.

Cash is cheap, around 50 bps below the main market rate and should be lower and lower as we are approaching Christmas, year end, end of the reserve... Additional OMOs are not successful since increased risk aversion is being mollified by the increased cash levels on the accounts. Today's OMO was also in the scenario with the intake of only 89 billion pln out of 97 billion on the offer.

The MPC did not change any of the monetary policy parameters just in line with expectations. ECB also in line with the 25 bps cut. CPI figure can add some colour next week since the figure can be higher than consensus, which itself is higher than the last month's figure. It can push the front end higher and give additional argument for hawks. EU summit is the global highlight and volatility is following any news.





Forex

Still in the range. The story repeats itself one more time... High expectations for EU salvation event were left unfulfilled. Even ECB announcements, were not able to constantly change the trend for EU peripheral's bonds and as consequence the risk off hit the market again. The range for EUR/PLN still holds, with 4.4430 and 4.5550 marking this week low and high.

Volts lower. The Xmass sell off continues, this hit hard especially the frontend of the curve (1 week was given at 11.5%), the 1 month mid fixed at 12.00 % about 1.5 % lower then the week before. The backend sale is much less impressive with 1 year EURPLN vol now at 13.5 % mid (13.9 last week). The risk reversals and currency spread (difference between USD/PLN and EUR/PLN vol) both lower, roughly 0.25% each.

Short-term forecasts

Main supports and resistances

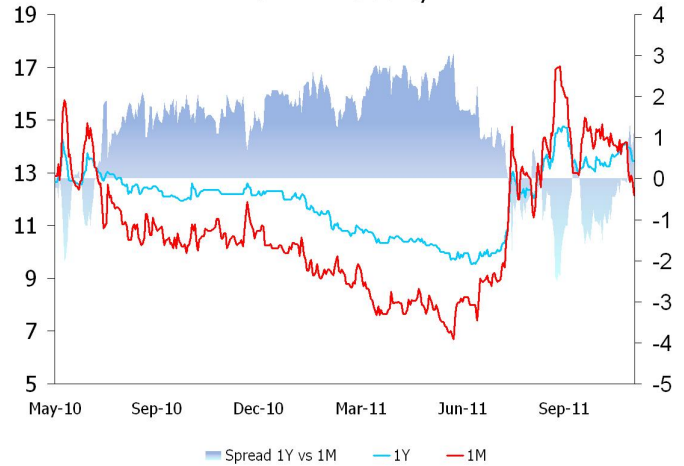
EUR/PLN: 4.4000 / 4.6000

USD/PLN: 3.2500 / 3.5000

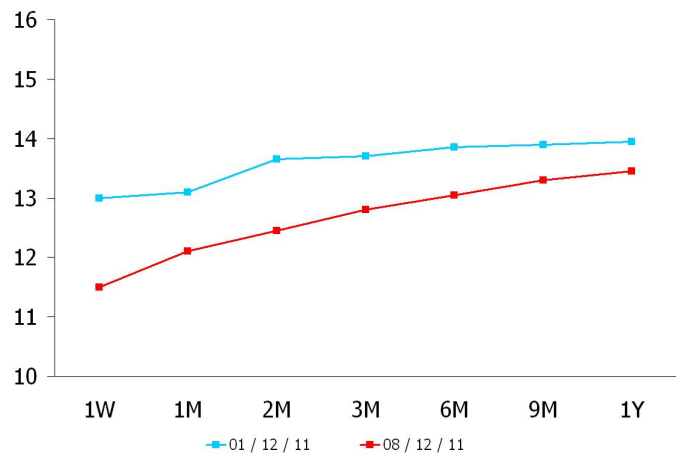
Spot. Unchanged from last week. The wide range of 4.4300-4.6200 is still intact. We would play it opportunistically and be very disciplined with executing stop losses as the thin liquidity may create market gaps. Stay sidelined or use extremes.

Derivatives. Unchanged from last week. We are core long 3/6 months sector in ATMS in EUR/PLN. The short dated gamma we have bought last week paid it's Theta bill with a small profit but we are letting it expire and not adding more gamma to the book. Would like to average Vega bellow 13% , but we doubt we will have this opportunity this year. Poor liquidity and wide spreads are the things we better got used to in current environment.

EURPLN volatility



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
12/2/2011	4.79	4.97	4.91	6.49	4.78	6.59	4.97	4.98	4.80	4.71	4.61	4.82
12/5/2011	4.82	4.97	4.84	4.88	4.83	4.88	5.00	4.97	4.80	4.71	4.58	4.83
12/6/2011	4.74	4.97	4.89	4.89	4.76	4.89	5.01	4.99	4.80	4.70	4.56	4.84
12/7/2011	4.76	4.98	4.98	4.89	4.80	4.89	4.98	4.96	4.77	4.67	4.57	4.80
12/8/2011	4.78	4.98	4.85	4.89	4.80	4.89	4.98	4.98	4.80	4.70	4.59	4.82

Last primary market rates							
Paper	Au. date	Maturity	Avg. price	Avg. yield	Supply	Demand	Sold
52W TB	5/30/2011	5/30/2012	95.57	4.58	600	2667	505
OK0114	8/10/2011	1/25/2013	89.58	4.58	5000	4934	1889
PS1016	10/19/2011	10/25/2016	98.44	5.11	3600	11200	3638
DS1021	7/21/2011	10/25/2021	99.53	5.80	3000	5608	3000

Fixed income market rates (closing mid-market levels)							
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0113	5Y IRS	PS0416	10Y IRS
12/2/2011	6.590	4.806	4.790	4.901	4.880	5.277	5.045
12/5/2011	4.880	4.685	4.740	4.843	4.830	5.198	4.990
12/6/2011	4.890	4.810	4.750	4.849	4.830	5.239	4.980
12/7/2011	4.890	4.689	4.750	4.888	4.845	5.292	4.990
12/8/2011	4.890	4.821	4.750	4.896	4.830	5.343	4.990

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY	
Date	1M	3M	6M	1Y	1M	1Y	1M	1Y
12/2/2011	12.65	13.65	13.75	13.95	13.95	5.03	0.43	0.90
12/5/2011	12.90	13.45	13.55	13.75	13.75	5.03	0.43	0.90
12/6/2011	12.75	13.05	13.20	13.45	13.45	4.83	0.34	0.96
12/7/2011	12.15	12.80	13.05	13.45	13.45	4.83	0.89	0.91
12/8/2011	12.10	12.80	13.05	13.45	13.45	4.83	0.59	0.86

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
12/2/2011	4.4812	3.3235	3.6275	4.2696	1.4725	0.1771
12/5/2011	4.4773	3.3276	3.6155	4.2696	1.4856	0.1777
12/6/2011	4.4711	3.3429	3.6089	4.3031	1.4886	0.1771
12/7/2011	4.4690	3.3310	3.6010	4.2883	1.4892	0.1770
12/8/2011	4.4692	3.3359	3.6107	4.3087	1.4858	0.1770

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