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Comment on the upcoming data and forecasts

On Wednesday MPC's meeting ends with interest rate level announcement. January "Minutes" showed significant change in MPC's assessment of current economic situation in Poland towards great optimism (yet confirmed by January PMI reading) along with upside revisions of inflation forecasts for 2012. However, we assess those statements as directed to eliminate expectations for cuts rather than move towards hikes. In our base scenario significant PLN exchange rate appreciation and explicit inflation decrease in the forthcoming months will dampen MPC wording on monetary policy tightening and lengthen period without interest rates changes.

Polish data to watch: February 6 to February 10

Publication	Date	Period	BRE	Consensus	Prior
NBP repo rate (%)	8.02.	Feb	4.5	4.5	4.5

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Last yield (%)	Prev auction
52 Week T-bills	2/27/2012	2000	4.510	1/30/2012
2Y T-bond OK0114	2/9/2012	6000	4.724	1/19/2012
5Y T-bond PS1016	2/9/2012	4000	5.246	10/16/2012
10Y T-bond DS1021	3/21/2012	3000	5.511	2/1/2012
20Y T-bond WS0429	2/16/2012	3600	5.931	1/12/2011

Macroeconomic forecasts

Wskaźnik	2008	2009	2010	2011	2012 F
GDP y/y (%)	5.1	1.6	3.8	4.3	2.8
CPI Inflation y/y (average %)	4.3	3.5	2.8	4.3	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	12.5	13.6
Repo rate (end of period %)	5.0	3.5	3.5	4.5	4.0

	2011 Q1	2011 Q2	2011 Q3	2011 Q4	2012 Q1 F	2012 Q2 F
GDP y/y (%)	4.5	4.3	4.2	4.0	3.6	3.0
CPI Inflation y/y (average %)	3.7	4.2	4.1	4.6	4.1	3.7
Repo rate (end of period %)	4.0	4.5	4.5	4.5	4.5	4.5

F - forecast

Economics

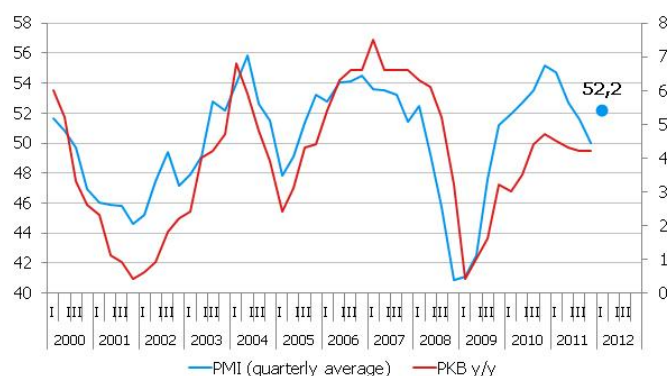
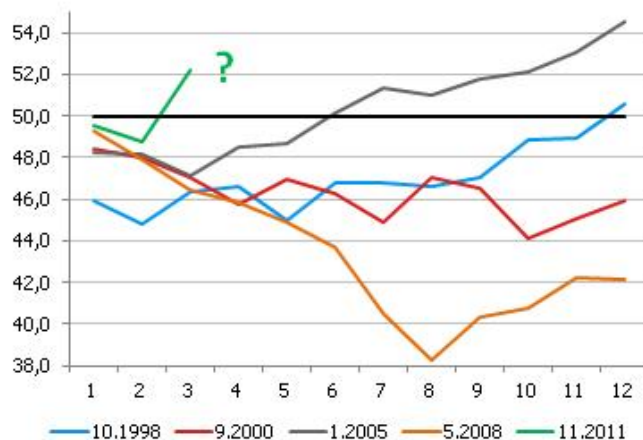
Significant growth of PMI in Poland

PMI in Polish manufacturing sector grew by 3.4 pts to 52.2 pts and returned after two months to recovery-levels above 50 pts. Contrary to previous months firms reported an increase in new orders, which in turn generated faster production growth and halted the decline in employment initiated one month before. Central to the recovery in momentum in January was a resumption of new business growth, which increased at the sharpest pace since last August. As a result in January also new orders to production ratio reversed after half year decline. Survey data signaled a robust increase in new export orders revealing improvement in European demand, which was also mentioned directly by respondents. Exporters' activity is supported by relatively weak Zloty, which acts as an automatic stabilizer in the economy.

January reading confirmed our expectations of recovery in manufacturing sector, although the scale of growth surprised upwards. In the whole survey history such an increase was reported only twice in 2009 and initiated PMI's return to the growing trend. Nevertheless, it may result from the change of current assessment vs. expectations distribution similar to patterns revealed by European indices (e.g. ZEW and Ifo) - after few months of undervaluation (forecasts lower than actual readings) and lack of negative scenario materializing in the real sphere, entrepreneurs seem to reverse their expectations' path upwards. In Polish PMI it is somehow reflected in employment and new orders sub-indices (stabilization and growth respectively), which are often treated as leading indicators in manufacturing. One should also notice that current cycle reveals specific patterns - historically after decrease below 50pts PMI lasted there for 17 months on average (minimum period was 5 months) while in January it returned above 50 pts after only 2 months (see chart).

Comparing Polish index with its euro zone counterparts reveals that in the last half year Polish PMI stayed on average higher (similarly to the path in 2009 - see chart), however, their changes move in the same direction (which is confirmed also by an increase in new export orders and demand). Therefore trend reversal in European economic indicators and rumors on forecasts revisions in euro zone and Germany (this time upwards) are also positive factors influencing Polish reading. However, we have to stress that only longer-lasting increases will imply trend reversal in economic indicators. January sentiment recovery strongly supported by ECB's liquidity actions may turn out to be only short-lived with no solution to fundamental matters in Europe. In Poland, however, the key determinants of further changes in sentiment are real data releases for January. Our forecasts remain relatively positive and above market consensus - in industrial output we expect about 10.5% y/y growth supported by better economic indicators, an additional working day and shorter „long weekend” with 6th January. As there are no signs of manufacturing slow-down PMI should remain above 50 pts, although slight correction from high 52.2 pts is still possible. PMI reading and expected positive publications from the real sphere are to support latest MPC's hawkish rhetoric and wait-and-see stance but with no changes in interest rate level in the months to come due to rapid zloty appreciation.

Historical PMI paths after first decline below 50 mark





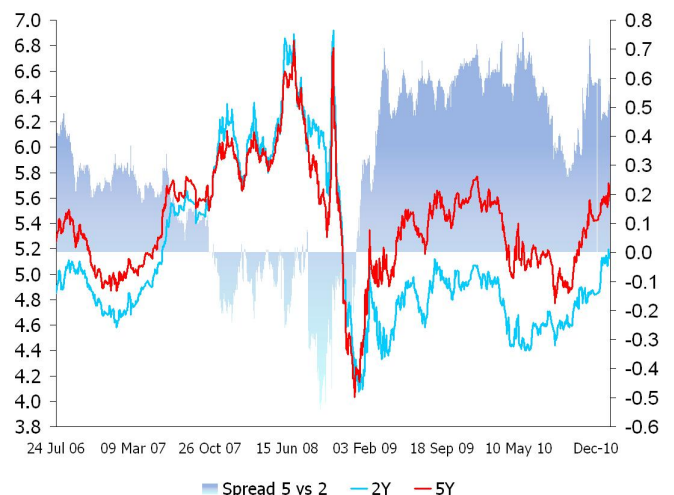
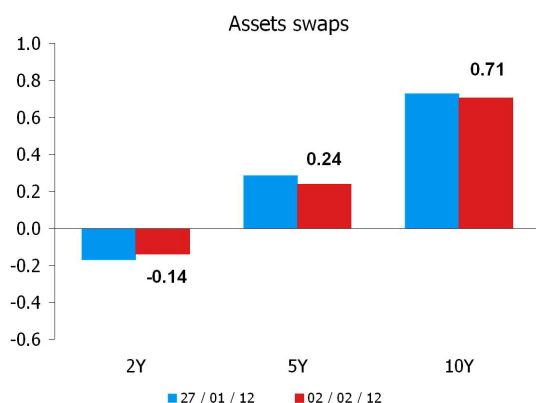
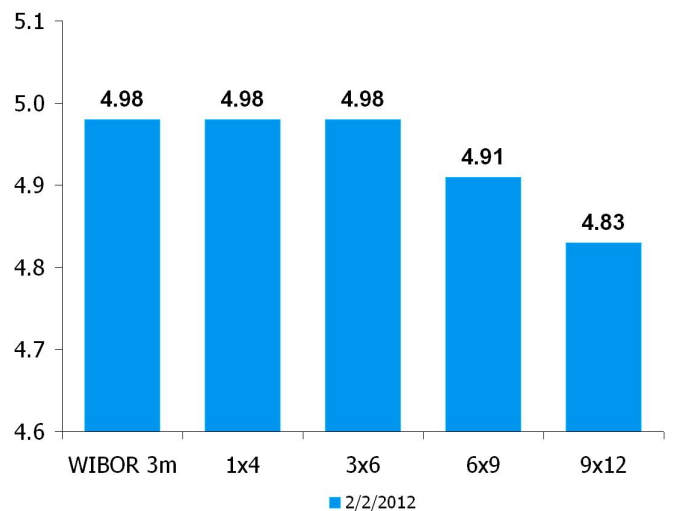
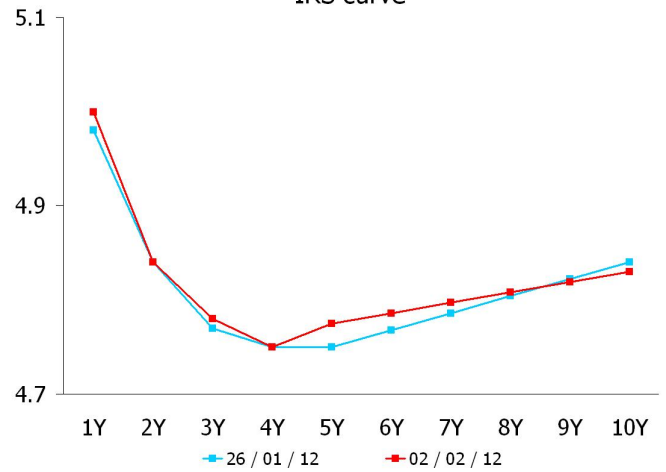
Fixed income

Consolidation phase

Beginning of the week was quite positive on the bond market. Ironically strongest wave of buying happened just before Wednesday's bond auction, when 10Y bond yield touched 5.50%, level not observed since September last year. FinMin successfully placed 3bio of DS1021, but it seems that this rally has somehow run out of steam. Later on market prices pulled back by some 5bp. Front end rates, which has repriced significantly previous week after really hawkish comments from Mr. Belka, have also recovered (9x12 pulled back by almost 10bp) and therefore curve steepened both in 2y5y and 2y10y.

In the longer term we remain bullish on PLN rates practically in all sectors - we think bonds in 5y and 10y sectors have a lot to gain. We disagree with market reluctance to price in rate cuts in 1y1y forward. Nevertheless what currently prevails in MPC's rethorics, we think will not turn into actual policy tightening and it's also matter of time when CPI starts falling and economy starts showing clearer signals of a slowdown and next move in rates will be a cut not a hike and that will happen sooner that what shape of the yield curve indicates. However from short term perspective, we think that some correction is due. Rally lasted for quite a while now, there is a decent profit to be collected, it's hard to expect some supportive news, either locally or globally. Next week's MPC statement will rather be hawkish than dovish (next CPI projection won't be published until next month), EURPLN is consolidating here and won't be supporting rates as it has been in January. Trying to be short bonds however is a dangerous strategy, so we'd rather stay on the sidelines for a while and if we're right and some correction happens, we'll be looking to reenter long bonds position, preferably ahead of CPI data on 15th.

IRS curve





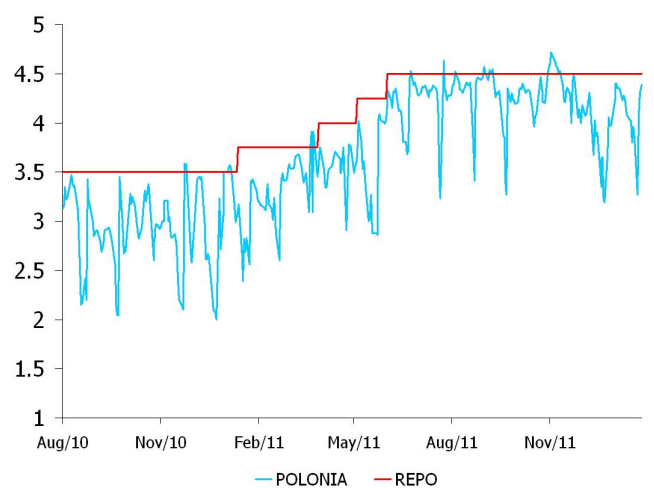
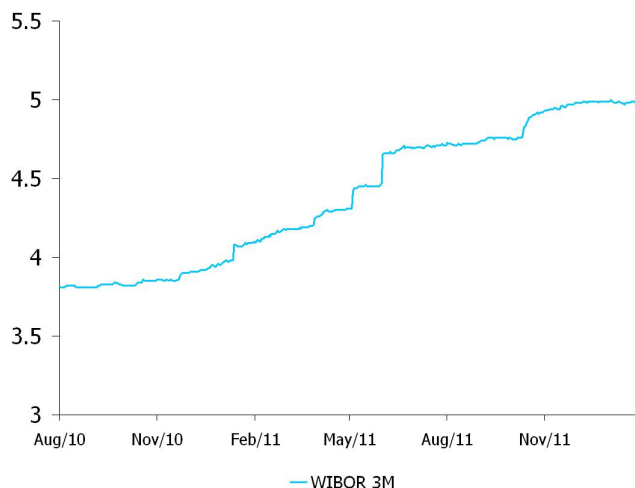
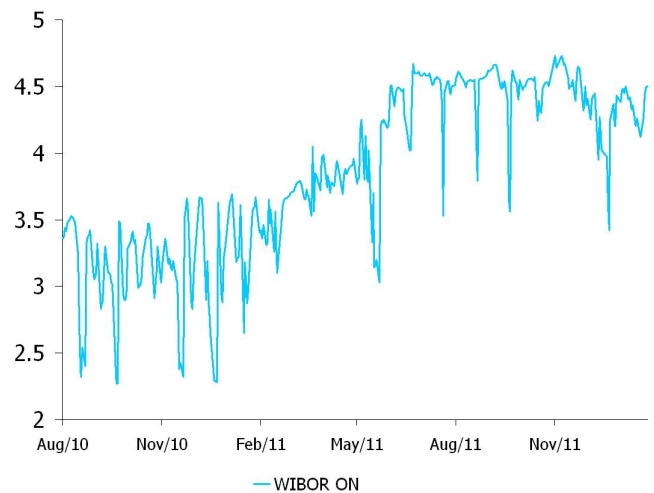
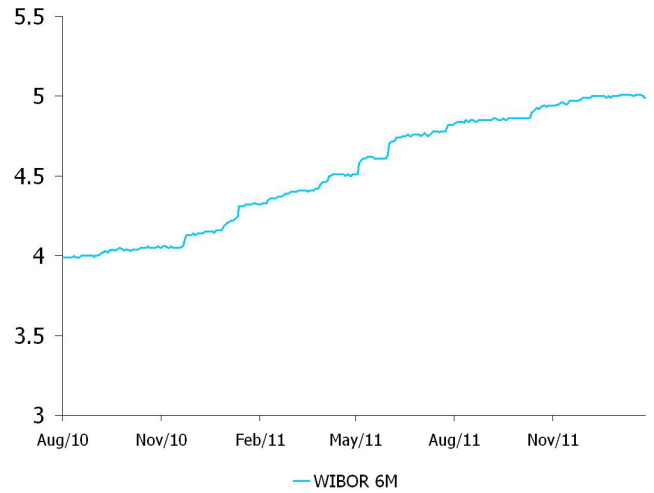
Money market

Carry stabilised as a new reserve started. Figures support bears, global sentiment supports bulls. Sort supply of T-bills in February.

After very cheap end of the reserve requirement settlement period we approached a new one with the stable rates nearby the main market rate. We think that another week is going to be similar and without any disturbances. We estimate the polonia index to be around 4.2%.

Very high inflation expectations (5.2%) plus extraordinary rebound of the PMI Index (above 52 vs last reading 48.8) indicate further hawkish bias of the MPC. However, good week for stock exchange along with the further strengthening of the zloty partially put out the bearish figures. All in all sentiment for rates has improved pushing the front end a bit lower. We still think it is a good idea to keep payers, since the probability of the hike event (which is not our base scenario but still) is not priced in. Therefore, we consider last drops as a good opportunity to overweight the payers in a core position. Next week we have MPC meeting and voting a hike is a very likely scenario. Set of figures for January should also support the bears.

Expected T-bills auctions were cancelled, and the next one is as far as on 27th of February. This will definitely support the prices of on the run issues. Short supply will also influence potential yields of the new papers. To sum up T-bills should be really expensive as a result (last auction was more expensive that the previous one and this trend should be sustained).





Forex

4,2150 support 200 days MA is broken EUR/PLN has broken the very important 4.2150 support (200 days MA), but it did not spur the selling spill. The low so far was 4.1820, the market found it's equilibrium around 4.1900. The move from 4.5250 looks stretched, and at least small correction would be healthy. But with a global thirst for any return so big, playing on correction is quite a risky game. Today's NFP may give a market fresh signal, to either side...

Vols unchanged The implied volatility curve is stable/unhanded from last week. 1month EUR/PLN ATM is 10 % mid with 1 year EURPLN ATM is 12 %. What is worth mentioning that curve is unchanged even the spot is totally boxed in 4.1820/4.2050 for last several sessions. The risk reversals 25D are also flat with last week, but the currency spread (USD/PLN minus EUR/PLN) is 0.25% higher, 8% from 7.75 %.

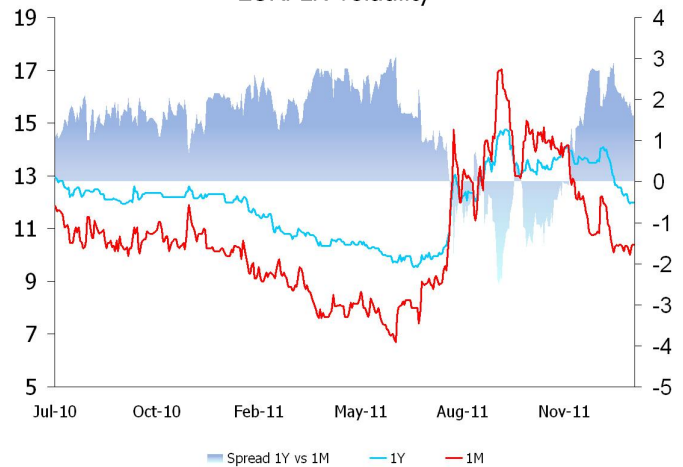
Short-term forecasts.

Main supports and resistances
EUR/PLN: 4.1400 / 4.2600
USD/PLN: 3.1500 / 3.3500

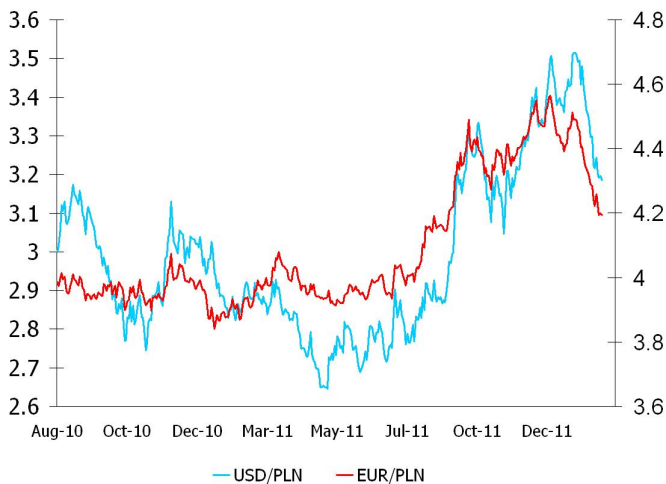
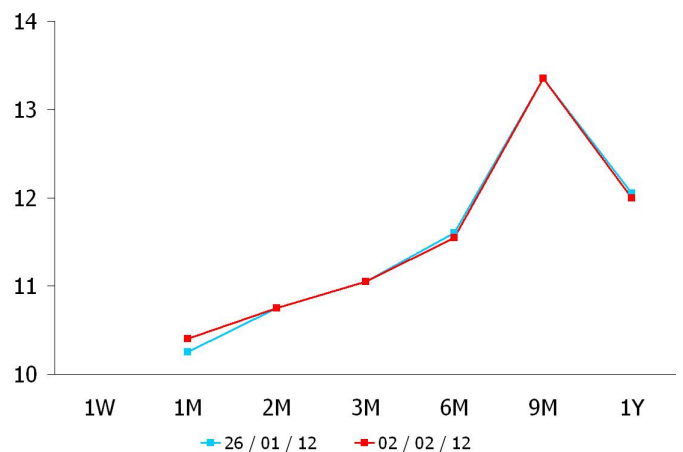
Spot. We got rid of the longs EURPLN from last week. We have gone a long way from 4.5250 and the move is very fast. We are mentally not ready, to chase that move and buy PLN here, but the trend is very strong and we will not stay on its way ... at least not yet.

Derivatives The picture is blur. The implied volatility is still well above it's historic ones. Same with Skew... but the ATM's are much lower then the beginning of the year and the Risk reversals also, so we are not chasing that move .. waiting sidelined for some further developments...

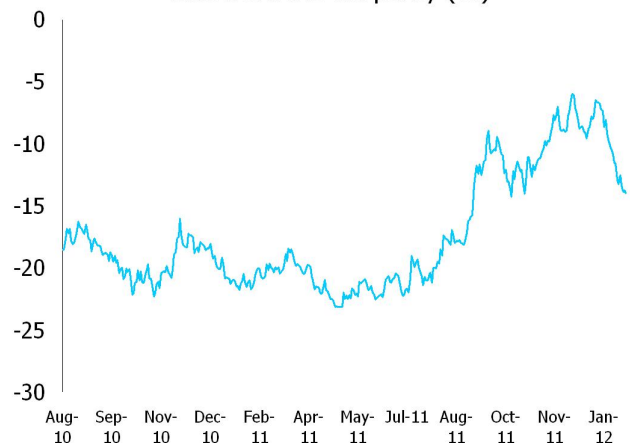
EURPLN volatility



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
1/27/2012	4.77	4.98	4.78	6.49	4.78	6.59	4.99	5.02	4.96	4.88	4.73	4.98
1/30/2012	4.63	4.99	4.50	4.91	4.50	4.91	5.01	5.03	4.94	4.87	4.73	4.97
1/31/2012	4.63	4.99	4.66	4.90	4.66	4.90	5.00	5.02	4.97	4.91	4.80	5.02
2/1/2012	4.61	4.99	4.53	4.90	4.58	4.90	5.00	5.02	4.95	4.90	4.76	5.00
2/2/2012	4.81	4.98	4.80	4.89	4.80	4.89	4.98	4.98	4.91	4.83	4.68	4.94

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	DS1019
1/27/2012	6.590	4.645	4.900	4.730	4.810	5.095	4.880	5.610
1/30/2012	4.910	4.662	4.910	4.760	4.850	5.136	4.920	5.664
1/31/2012	4.900	4.658	4.895	4.691	4.790	5.029	4.870	5.584
2/1/2012	4.900	4.510	4.888	4.710	4.765	5.004	4.820	5.548
2/2/2012	4.890	4.510	4.840	4.701	4.775	5.014	4.830	5.536

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY
Date	1M	3M	6M	1Y	1M	1Y	1Y
1/27/2012	10.00	10.85	11.45	11.95	11.95	3.40	0.99
1/30/2012	10.25	11.05	11.55	12.00	12.00	3.40	0.99
1/31/2012	10.40	11.05	11.55	12.00	12.00	3.40	0.79
2/1/2012	10.40	11.05	11.55	12.00	12.00	3.40	0.79
2/2/2012	10.40	11.05	11.55	12.00	12.00	3.40	0.74

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
1/27/2012	4.2223	3.2163	3.4966	4.1801	1.4349	0.1679
1/30/2012	4.2589	3.2433	3.5335	4.2278	1.4399	0.1688
1/31/2012	4.2270	3.2032	3.5054	4.1995	1.4410	0.1680
2/1/2012	4.1933	3.1913	3.4824	4.1935	1.4285	0.1663
2/2/2012	4.1995	3.1955	3.4861	4.2010	1.4352	0.1669

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