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Comment on the upcoming data and forecasts

On Wednesday CPI will be published - our forecast (0.1pp lower than consensus) is based on slight fuel prices decline and relatively low growth of food prices (0.5% m/m). Our calculations point to 2.7% y/y growth of core CPI in May, the same as in April. On Thursday NBP will announce money supply M3 growth rate for May. We expect further deterioration of household deposits (however statistical base from 2011 raises annual growth rate) and seasonal growth of coporate deposits volume. About 2-3pp. are added by Zloty depreciation. The week ends with April current account data. There is a possibility of a sizeable outflow from income account due to interest payments, we see also significant uncertainty regarding the import and export after the last surprise (EUR 12000 mln export, EUR 12500 mln import). Net transfers from the EU should be at lower level.

Polish data to watch: June 11th to June 15th

Publication	Date	Period	BRE	Consensus	Prior
CPI y/y (%)	13.06.	May	3.8	3.9	4.0
M3 y/y (%)	14.06.	May	10.4	10.2	10.3
C/A (mln EUR)	15.06.	Apr	-800	-923	-228

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Last yield (%)	Prev auction
52 Week T-bills	-	3000	4.470	3/26/2012
2Y T-bond OK0114	6/20/2012	7500	4.759	4/19/2012
5Y T-bond PS1016	6/20/2012	4200	5.047	5/18/2012
10Y T-bond DS1021	7/11/2012	4000	5.349	5/10/2012
20Y T-bond WS0429	7/11/2012	4000		5/10/2012

Macroeconomic forecasts

Wskaźnik	2008	2009	2010	2011	2012 F
GDP y/y (%)	5.1	1.6	3.9	4.3	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	12.5	13.6
Repo rate (end of period %)	5.0	3.5	3.5	4.5	4.75

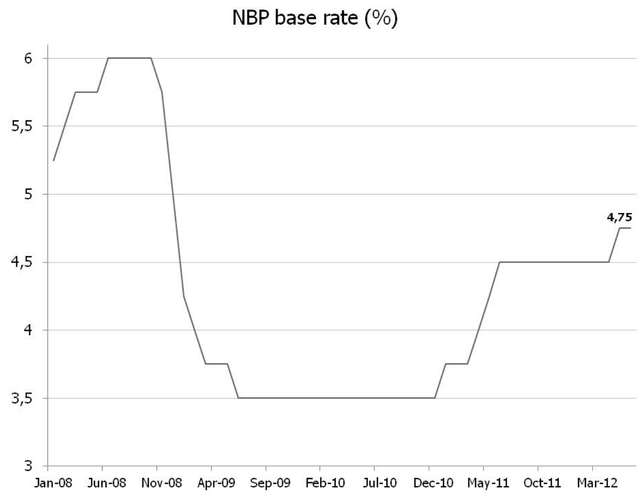
	2011 Q1	2011 Q2	2011 Q3	2011 Q4	2012 Q1	2012 Q2 F
GDP y/y (%)	4.6	4.2	4.2	4.3	3.5	2.8
CPI Inflation y/y (average %)	3.7	4.2	4.1	4.6	3.9	4.2
Repo rate (end of period %)	4.00	4.50	4.50	4.50	4.50	4.75

F - forecast

Economics

MPC left interest rates unchanged and did NOT announce further tightening in July

In line with expectations MPC did not decide to change interest rates on June meeting - the reference rate stayed at 4.75% on an annual basis. MPC pointed to weakening economic activity in Poland and globally, although governor Belka claims that in Poland it will remain only moderate. As we expected, in June - similarly to May - the following sentence appeared in the statement: „Incoming data, as well as the NBP's July macroeconomic projection, will enable a more comprehensive assessment of the scale of economic slowdown and future inflation developments in Poland, thus allowing for the assessment whether another adjustment of interest rates will be justified". It does not mean, however, that further tightening is on the cards, which was clearly stated by governor Belka during the conference. We assess that the importance of July inflation projection declined and even if it foresees higher inflation, it will not necessarily signal rate hike in July, especially that the global rate policy moves recently rather in the opposite direction.

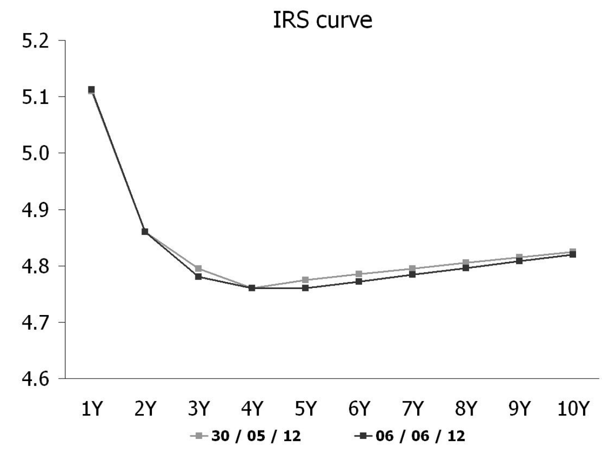


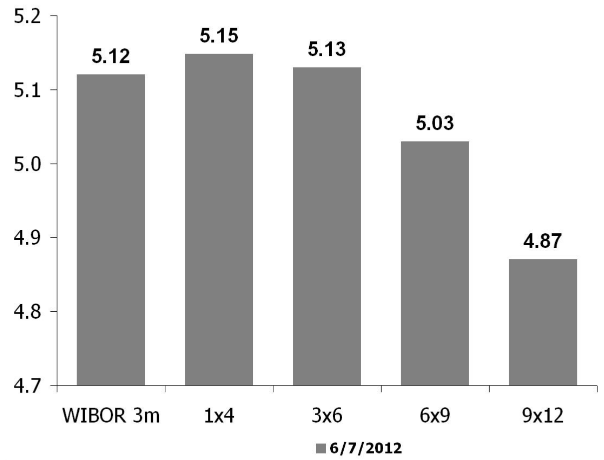
Polish monetary policy cannot be analyzed without the context of global central banks' decisions. Firstly, although on the June meeting the ECB's Governing Council did not announce further monetary loosening and distanced itself from debt crisis solving, governor Draghi stated that „a few" Council members called for a rate cut already in June and the bank „stands ready to act" if downside risks for growth materialize. Even more suggestive are recent unexpected People's Bank of China rate cut and Fed representatives suggestions on operation twist extension, which all together cast doubts on the continuation of monetary tightening in Poland. PBoC and Fed's actions not only support risky assets (bear market correction), but also indicate serious concerns about global economic growth and risks of European debt crisis spread as was mentioned lately by Bernanke. Besides global factors also analysts' opinions and more and more convincing signs of slow down will put pressure on MPC hawkish rhetoric. Slowdown in Poland remains mild (without rapid changes like in 2008/09), but its causes are yet not only external (lower growth in Europe, weakening Polish exports) but also internal (internal cycle components are reversing - e.g. rebuilding of savings rate, lower consumption, infrastructural and private investment). Such a scenario should not heighten Polish credit risk and therefore lead to strengthening of Polish bonds. On the one hand, their short term volatility may depend on sentiment and fears of European stability. On the other hand, however, these are local factors (weaker data from the real economy and inflation decline - although connected with almost 1% statistical base, it will eventually lead to the correction of expected NBP rate path) and global low rates environment that support uptrend on Polish bond prices.

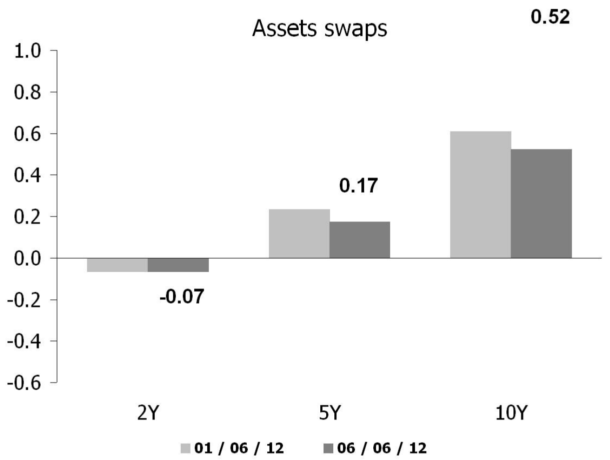
Fixed income

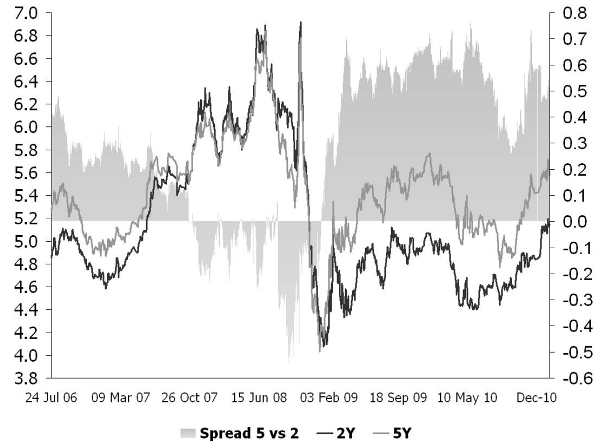
There's still room for a rally

Last week didn't really support activity on the FI market - awaiting for the MPC amid absence of London players followed by local holiday on Thusrday kept the turnover low. However positive sentiment prevailed and bonds in the long end of the curve rallied significantly by some 8-11bp. The MPC left rates unchanged and to our opinion shifted their rethorics slightly towards less hawkish stance. Future path of the rates still depends on the outcome of next inflation projection, but neither was another hike annouced, nor was any automated decision signalled, had the CPI outlook worsened in July's report. Market reaction in the front end of the curve was very limited, there's no hike priced in at all and first easing in the Q1 2013. Such rates path seems quite reasonable to us, however we see some risk coming from Wibor rates, which have recently kept pushing slightly up. We don't think this move can accelerate, but without much chances for a shift in depo market it wouldn't reverse either. That, and the inverted shape of forward curve up to 2Y makes receiving quite costly. That's why we stick with our preference for bonds over rates, especially in 5Y sector. After recent move some correction looks likely, but any sell-off there would only create nice buying opportunity.









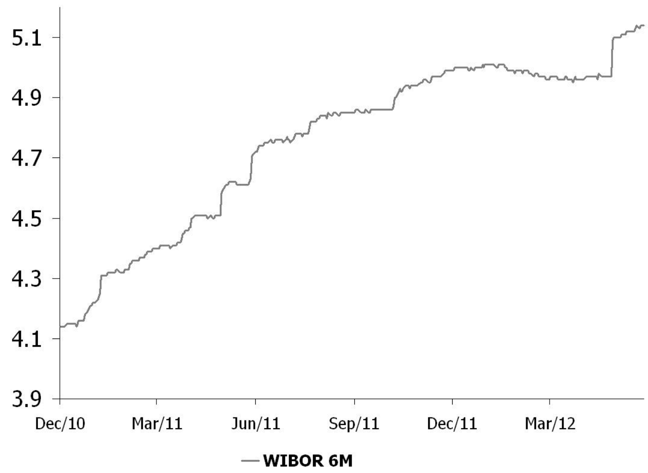
Money market

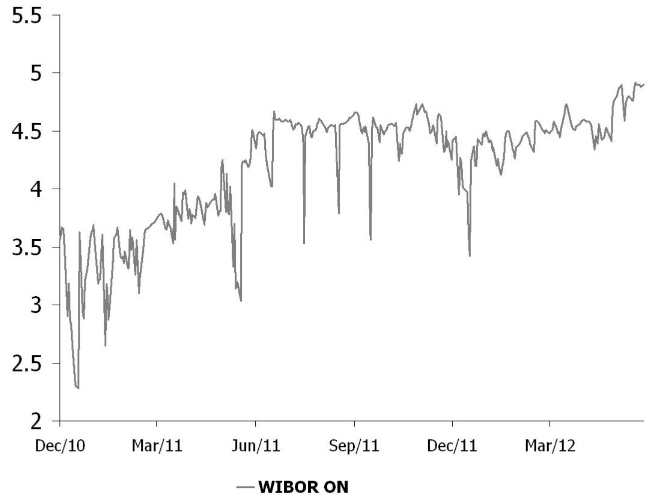
More cash in the system for the coming week. July less likely in the terms of hike.

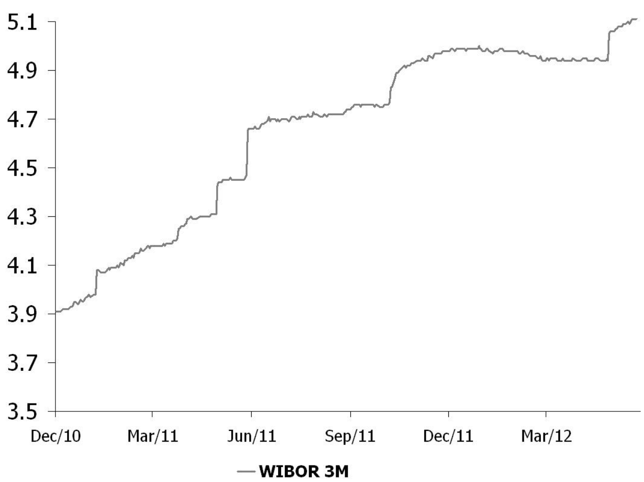
Liquidity should be improved for the coming days, since the demand for money bills was 3 billion lower then the supply (82.6 vs 85.5 bln pln). However, just because the reserve settlement period has just started we would not expect the shortest rate to go down by much.

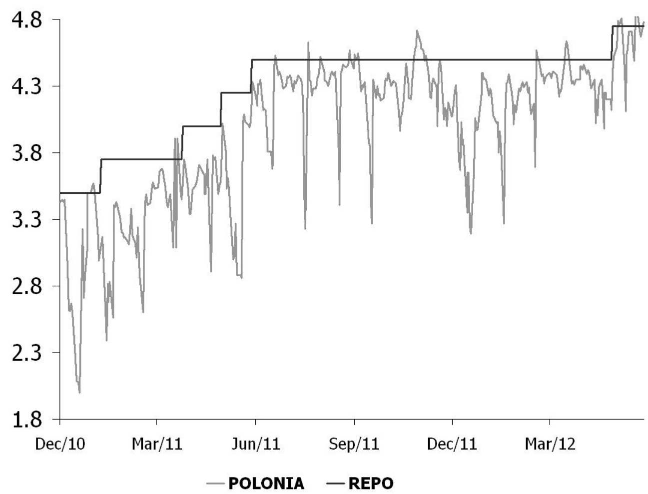
The week with the holiday and the commencement of the EURO2012 could not be busy. The MPC and the ECB did not change the parameters of the monetary policy. July becomes less likely for the hike unless the figures or/and the CPI projection are surprising. September is also questionable because the slowdown should be well visible by then. The highest probability is for no change mode scenario this year, however at current levels paying front end is a zero cost hedge against the hike, which can not still be excluded.

Stay pay in the front end.





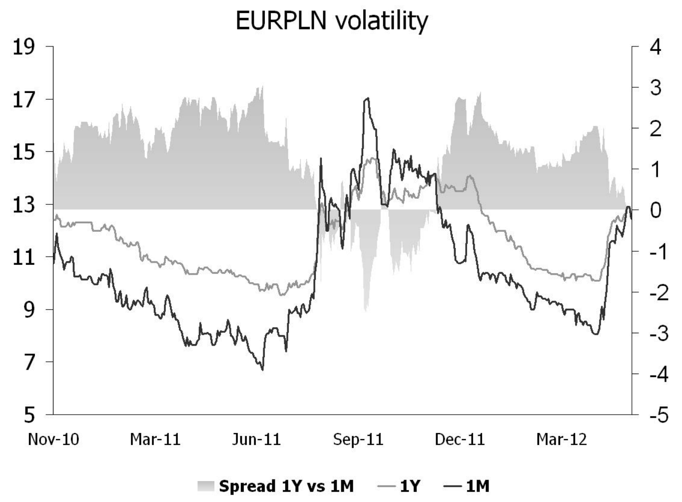




Forex

The bad news is a good news. After reaching the 4.4300 high just after the bad NFP, the Zloty has railed savagely touching briefly 3.2320 low (Thursday). Just to come back to the 4.30 level on Friday... My theory is, that the fear of the US printing press was so big that lead to massive liquidation of good portion of the long USD/PLN positions. There is no relation with the fundamentals, just a stop/loss hunting in my view. What next for here? I would expect that as Greek election, Spain are still the source of all bad news, the possible move to the upside is still likely... the positioning is much lighter now.

The realized volatility shoot up! The implied volatility curve hasn't really changed from the last week. The 1 month EUR/PLN ATM is still 12.5% and 1 year EUR/PLN 12.7%. What makes the difference is that short term realized volatility shoot up significantly! The EUR/PLN 1 week realized vol is 13.3%, for USD/PLN, the realized vol marks 21.36 %. If the realized volatilities stay that high we can have next leg higher in XXX/PLN vol space... The skew got sold on the knee-jerk reaction to the stronger PLN ...

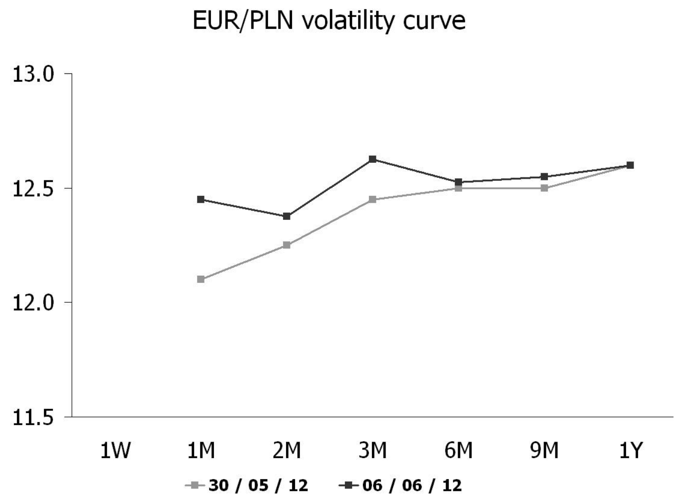


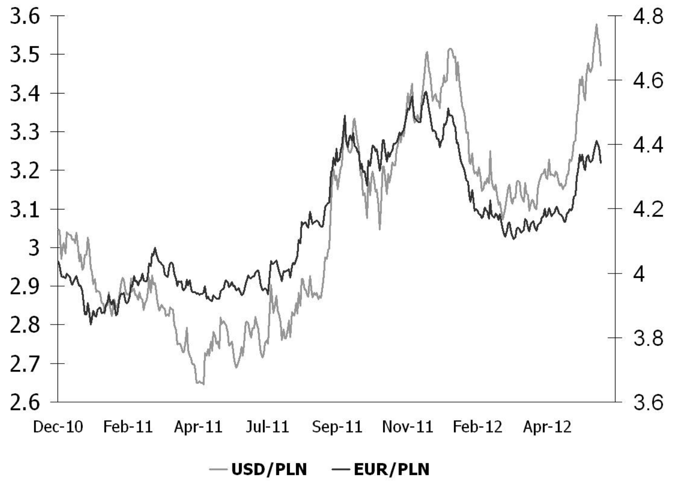
Short-term forecasts.

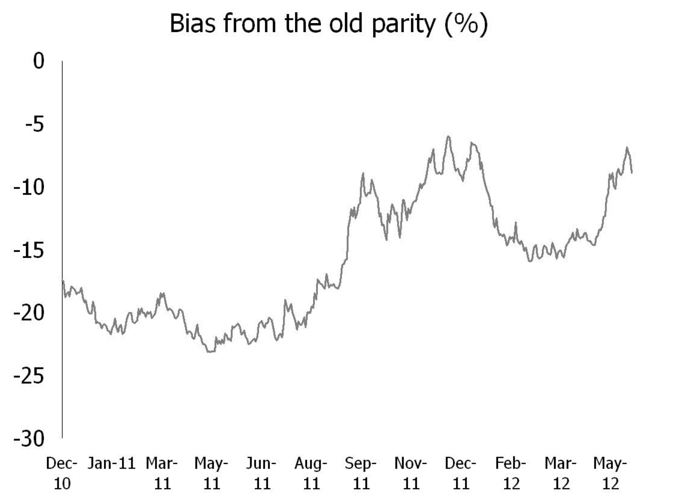
Main supports and resisances
EUR/PLN: 4.2300 / 4.4300
USD/PLN: 3.3500 / 3.6000

Spot. It was not a correction, it was a wild washout of the long XXX/PLN, which took a number of the markets stops (ourselves included at 4.35). Despite the depth of the correction, which is shocking... we think it was caused more by the market positioning and has little rationale. We would like to try to ideally go long at 4.25/4.28 region with a stop bellow 4.23 and hopes for 4.35+ still to come.

Derivatives The level of uncertainty is higher and higher. So in current environment we are strongly exposed to higher levels, the last year highs 15% at 1 month and 14% at 1 year are strongly in sight. Even a relief rally will not change much as the move will keep the gamma being valuable, in other words still bid.







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
5/31/2012	4.61	5.11	4.91	5.03	4.94	5.04	5.15	5.14	5.05	4.90	4.71	5.04
6/3/2012	4.80	5.11	4.91	6.49	4.94	6.59	5.15	5.15	5.01	4.87	4.64	5.02
6/4/2012	4.90	5.11	4.85	5.03	4.78	5.04	5.14	5.13	5.03	4.87	4.65	5.02
6/5/2012	4.94	5.12	5.10	5.04	5.06	5.04	5.14	5.14	5.02	4.86	4.67	5.01
6/6/2012	4.92	5.12	5.10	5.04	4.90	5.04	5.15	5.12	5.03	4.86	4.65	5.02

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
5/31/2012	5.040	4.813	4.860	4.814	4.765	5.032	4.810	5.464
6/3/2012	6.590	4.813	4.860	4.794	4.765	4.999	4.810	5.419
6/4/2012	5.040	4.813	4.875	4.782	4.760	4.964	4.810	5.386
6/5/2012	5.040	4.813	4.875	4.826	4.760	4.943	4.810	5.369
6/6/2012	5.040	4.813	4.860	4.795	4.760	4.933	4.820	5.342

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY
Date	1M	3M	6M	1Y	1M	1Y	1Y
5/31/2012	12.40	12.40	12.55	12.60	12.60	4.01	0.46
6/3/2012	12.90	12.80	12.90	12.90	12.90	4.01	0.46
6/4/2012	12.90	12.80	12.90	12.90	12.90	4.03	0.66
6/5/2012	12.90	12.80	12.90	12.90	12.90	4.03	0.66
6/6/2012	12.45	12.63	12.53	12.60	12.60	4.03	0.66

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
5/31/2012	4.3889	3.5372	3.6545	4.4833	1.4610	0.1708
6/3/2012	4.4126	3.5777	3.6743	4.5731	1.4508	0.1710
6/4/2012	4.4007	3.5431	3.6651	4.5401	1.4462	0.1705
6/5/2012	4.3922	3.5359	3.6570	4.5213	1.4492	0.1709
6/6/2012	4.3423	3.4703	3.6159	4.3855	1.4473	0.1702

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