



TOP NEWS FROM THE POLISH MARKET

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MACROECONOMICS

CPI in March at inflation target 2.5%

Services prices start to grow more significantly

NBP chairman Skrzypek: currently no reason for rates hike but new data may change this view

MPC member Nieckarz: A pre-emptive hike may be needed

MPC member Wasilewska – Trenkner: High March inflation increases the probability of hike in April

MPC member Czekaj: Projection crucial for MPC decision

Consumer prices grew in March by 0.5% as compared with February and by 2.5% on the annual basis (BRE forecast: 2.4%, consensus: 2.4%). It is the first month for almost two years that inflation has hit the inflation target. The growth of the annual index has been caused mostly by the high growth of food prices (0.8% m/m) and the growth of fuel prices by 4.9% m/m. These data show, however, that services prices have started to grow more significantly. The prices of dental services increased by 0.4%, medical services by 0.1%, the hair services by 0.4% m/m. According to our preliminary estimates net inflation grew in March to 1.8% y/y. We expect CPI in April to be at 2.2-2.3% and at the end of year at 2.5-2.6%.

The published data show that the inflation pressure in the economy comes from the services sector. The growing costs in industry can be partly recompensed by productivity growth but in the services the growth of productivity is rather limited.

NBP chairman Sławomir Skrzypek said that the overheating of the Polish economy is not a danger and the strong data for Q1 may be distorted by favourable weather conditions. He believes that data for April and May will be more reliable. Moreover he added that the inflation projection is more optimistic for inflation than expected. Thus this "optimism" concerns the short term (till the end of this year) while for monetary policy the inflation path in 2008 is more important, which in our opinion will not be lower than in the January projection. His announcement indicates that he would like the delay of the first hike to be till May or June. On the other hand he said that "currently there is no reason for the correction of interest rates but before the MPC meeting we will know some new data, which could change the outlook and influence the final decision". In our opinion this comment indicates that if in April the MPC forms a majority ready to hike the rates Mr Skrzypek will support this decision. We believe that he will avoid losing the vote and aim to increase his credibility.

The tightening bias has been visible in the announcements of another dovish MPC member, Dr Stanisław Nieckarz. So far he has been an opponent of monetary policy tightening but last week he partly changed his view. He said that the risk balance for inflation is less favourable mostly due to large emigration and limited supply on the labour market, in particular in non-tradable sectors. Nieckarz didn't exclude a pre-emptive hike to cool the domestic demand. However Nieckarz added that in the longer term the growth of investments should increase the potential output and limit the inflationary pressure. Moreover the substitution of labour by capital should diminish the wages pressure. Mr Nieckarz doesn't see a danger for inflation in the longer-term but he agreed to vote for a pre-emptive strike. It is very likely that Nieckarz is one more MPC member who will support the hike in the coming months.

We have no doubt that Dr Halina Wasilewska – Trenkner will vote for the hike as well. She agreed with chairman Skrzypek that the inflation projection shows lower CPI in the short term but in her opinion in the longer term the projection will be similar to the previous projection. She repeated her previous view that the MPC should take the lead and hike the rates by 25 bps as quickly as possible. Wasilewska – Trenkner believes that the MCP will form a majority to hike the rates in April.

MPC members Prof. Jan Czekaj and Prof. Mirosław Pietrewicz said that CPI in March at 2.5% is roughly in line with the previous expectations. In their opinion the next inflation projection will be very important for further moves in monetary policy. Prof. Czekaj added that the increase of the rates will be an issue of the coming months, not quarters.

Our comment: The MPC seems certain to increase the rates by 25 bps in the next few months. The only open question is the precise timing of the hike. In our opinion it is very likely that the March projection will show the increase of inflationary pressure being a good argument for such

We expect hike by 25 bps in April, 75 bps in 2007

a decision. This projection will be strengthened by data published in April (higher inflation at 2.5%, good industry output and retail sales, high wages). We maintain our view that the MPC will hike the rates by 25 bps in April and by 25 bps in July. We don't exclude one more hike in October/November.

Money supply in March grew by 0.4% m/m and 18.1% y/y

Money supply M3 increased in March by 0.4% as compared with February, which gives an annual growth of 18.1%. Despite a lower figure than we expected (BRE forecast :19.5%), the growth rates of loans for households and enterprises remained at a very high level – at 37.8% and 17.5% respectively, which confirms that recovery in the Polish economy is sustainable.

C/A deficit in February to EUR 424 m

The current account deficit in February amounted to EUR 424 m. Exports grew roughly in line with expectations by 16.3% y/y but imports increased less than expected by only 13.4% (the three month average was equal to 19.7%). The trade gap dropped to EUR 60 m. We expect that due to strong domestic demand the dynamic of imports will return to the higher levels observed in the previous months, which will lead to a deterioration of the C/A balance. We expect that the C/A to GDP ratio will grow from 2.1% to 2.5% at the end of year.

In February the net inflow of FDIs amounted to EUR 910 m but it has been balanced by an outflow of EUR 1100 m worth of portfolio investments.

FIXED INCOME

Calm week despite economic surprises

Last week was rather quiet on the market, as usual in recent weeks. Bond auction, even with slightly bigger size drew little attention, as price was close to the secondary market. Even slightly higher than expected CPI number (2.5 versus 2.4 expected) have not influenced market in a great way. What we observe is clarification of the up trend in the yields, especially in the 5y sector. We basically agree that rates should be higher. Apart from paying 9x12 we think that pay position in 5y is also good trade.

RECOMMENDATION:

We are bearish PLN rates

MONEY MARKET

Carry still high

Probability of rates hike this month is growing

Shorter post holiday week was boring and quite. Carry still above the main rate with similar nearest future prospects. Open market operation a bit too high in our opinion (19,5 billion pln 18.5 expected) so no chance for sudden relief.

As for longer terms waiting for Friday's CPI figure. 2.5% surprised the market (2.4% expected) and strengthen the bearish sentiment. Next figures in coming week, as of now probability of hike this month grew to 60%.

RECOMMENDATION:

Pay 1,2 months.

FOREIGN EXCHANGE

Zloty stronger

Last week the Zloty continuing its appreciating trend. The trend was even strengthened by the bullish Friday's CPI data (headline inflation of 2.5%yoy, just 0.1p.p. above market consensus). EUR/PLN declined further to 3.82500 whereas USD/PLN, mainly due to rallying EUR/USD (1.3550 top) to 2.8230.

Volatility lower

As a result of the still stronger Zloty, the volatilities edged lower again last week. 1Y EUR/PLN traded down by 0.2 to 6.1 (mid) on Friday close, 1Y USD/PLN down by 0.5 to 7.7 (mid). 1M EUR/PLN dropped from 6.1 to 6.0, whereas 1M USD/PLN from 8.1 to 7.5.

RECOMMENDATION:

Zloty stable/bullish

Spot:
Main supports / resistances:
EUR/USD: 1.3375 / 1.3600
EUR/PLN: 3.8200 / 3.8600
USD/PLN: 2.8000 / 2.8500

In the following week we still may see Zloty trade within a range. The correction is still plausible, however due to recent stronger than expected CPI data and MPC members' comments on the need for immediate rate hike, we think the EUR sellers will dominate this week. That is why we recommend selling EUR/PLN on tops this week.

Options:

Short Gamma

Given that EUR/PLN still remains within a range and realized volatility is very low by historical comparison (around 4.0-4.5% monthly realized volatilities), we still recommend shorting Gamma.

MARKET PRICES UPDATE**MONEY MARKET RATES**

Money market rates (Closing mid-market levels)						
date	3M		6M		1Y	
	FXSW	WIBOR	FXSW	WIBOR	FXSW	WIBOR
09-04-07	4.23%	4.29%	4.41%	4.47%	4.66%	4.68%
10-04-07	4.25%	4.29%	4.42%	4.48%	4.65%	4.68%
11-04-07	4.26%	4.29%	4.42%	4.47%	4.66%	4.68%
12-04-07	4.26%	4.29%	4.42%	4.46%	4.66%	4.68%
13-04-07	4.28%	4.29%	4.44%	4.46%	4.68%	4.67%

FRA MARKET RATES

FRA Market Rates (Closing mid-market levels)					
date	1X4	3X6	6X9	9X12	6X12
	09-04-07	4.42%	4.59%	4.76%	4.86%
10-04-07	4.42%	4.59%	4.77%	4.87%	4.82%
11-04-07	4.42%	4.59%	4.76%	4.87%	4.80%
12-04-07	4.42%	4.59%	4.76%	4.87%	4.80%
13-04-07	4.43%	4.60%	4.77%	4.86%	4.81%

FIXED INCOME MARKET RATES

Fixed Income Market Rates (Closing mid-market levels)								
date	1Y		2Y		5Y		10Y	
	WIBOR	TB	IRS	OK1208	IRS	PS0511	IRS	DS1017
09-04-07	4.68%	4.38%	4.88%	4.62%	5.07%	5.02%	5.14%	5.21%
10-04-07	4.68%	4.37%	4.90%	4.61%	5.08%	5.04%	5.16%	5.24%
11-04-07	4.68%	4.36%	4.90%	4.59%	5.08%	5.04%	5.17%	5.24%
12-04-07	4.68%	4.39%	4.91%	4.61%	5.14%	5.05%	5.21%	5.27%
13-04-07	4.67%	4.38%	4.91%	4.60%	5.14%	5.09%	5.24%	5.31%

PRIMARY MARKET RATES

Last Primary Market Rates							
	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	07-04-02	08-04-02	95.766	4.37%	900	1543	900
OK0709	07-04-04	09-07-25	89.970	4.69%	1000	2463	1000
PS0412	07-03-21	12-04-25	99.009	4.97%	1800	4979	1800
DS1017	07-04-11	17-10-25	99.976	5.24%	1800	3473	1800

FX VOLATILITY

date	USD/PLN 0-delta stradle				25-delta RR		25-delta FLY	
	1M	3M	6M	1Y	1M	1Y	1M	1Y
09-04-07	7.50	8.00	8.20	8.20	1.20	1.30	0.35	0.60
10-04-07	7.50	8.00	8.20	8.20	1.20	1.30	0.35	0.60
11-04-07	7.50	8.00	8.20	8.20	1.20	1.30	0.35	0.60
12-04-07	7.50	8.00	8.20	8.20	1.20	1.30	0.35	0.60
13-04-07	7.50	7.80	8.00	8.00	1.20	1.30	0.35	0.60

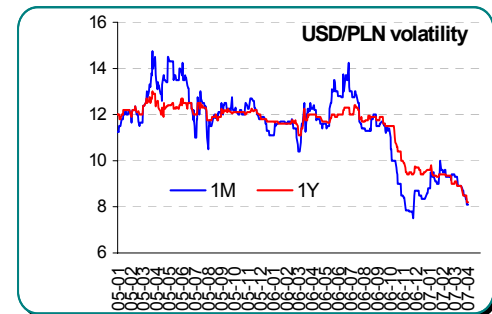
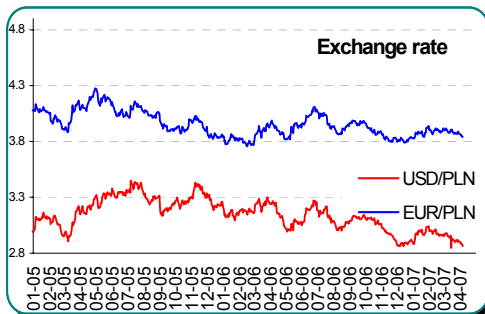
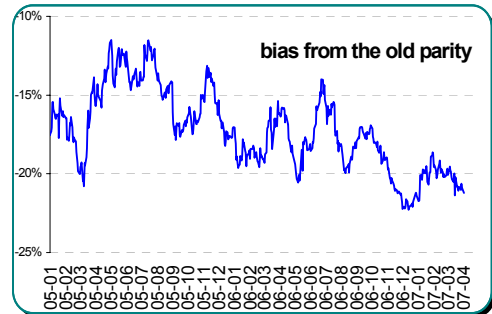
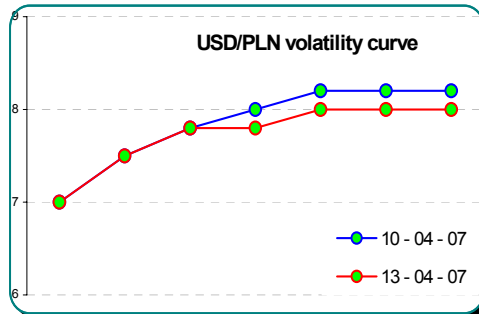
PLN SPOT PERFORMANCE

PLN spot performance			
date	USD/PLN	EUR/PLN	bias
09-04-07	2.8629	3.8415	-21.80%
10-04-07	2.8653	3.8420	-21.77%
11-04-07	2.8509	3.8279	-22.10%
12-04-07	3.8331	2.8499	-22.48%
13-04-07	3.8410	2.8405	-22.50%

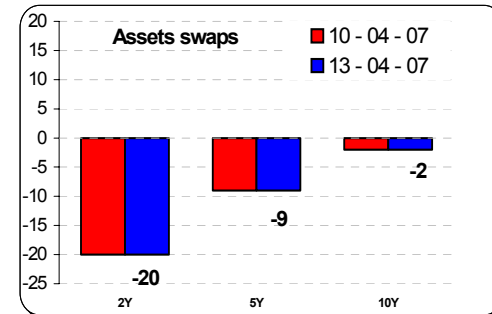
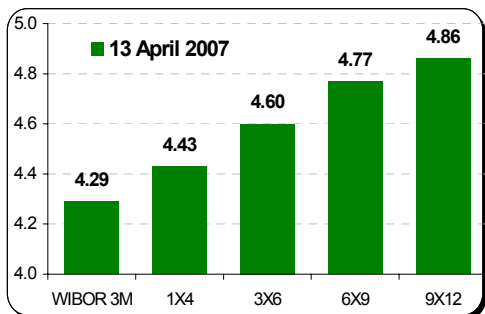
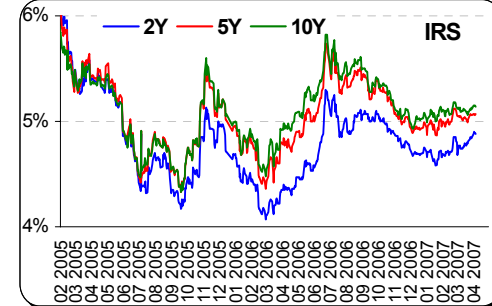
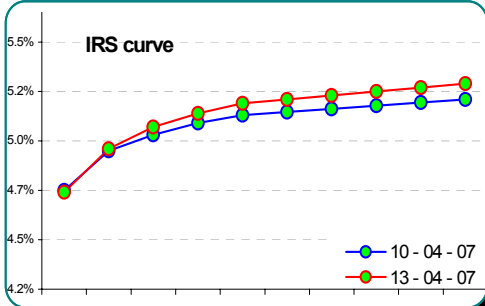
Note: parity on 11/04/00 – USD= 4.3806, EUR=4.2196, basket share 50:50
Mid-market volatility of vanilla option strategies

CHARTS

Foreign Exchange



Fixed Income



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CALENDAR

Macro

	January	February	March	Data Release	BRE Bank forecast
CPI m/m	0.4%	0.3%	0.5%	15-05-07	
CPI y/y	1.6%	1.9%	2.5%	15-05-07	
PPI m/m	0.6%	0.3%		20-04-07	0.7%
PPI y/y	3.1%	3.6%		20-04-07	3.5%
Industrial production growth m/m	0.2%	-2.1%		20-04-07	15.3%
Industrial production growth y/y	15.4%	12.9%		20-04-07	11.8%
Average wages in enterprise sector [PLN]	2663.6	2687.5		17-04-07	2791.0
Average wages in enterprise sector y/y	7.8%	6.5%		17-04-07	6.8%
Unemployment	15.1%	14.9%		24-04-07	14.6%
Budget realisation (%)	-10.3%	10.1%	16.1%	15-05-07	
Current account [EUR mn]	-733	-424		18-05-07	
Balance of foreign trade in goods (transaction basis) [EUR mn]	-398	-60		18-05-07	
Exports growth y/y (transaction basis)	15.5%	16.3%		18-05-07	
Imports growth y/y (transaction basis)	21.5%	13.4%		18-05-07	
Current account [% of GDP]	-2.1%	-2.2%		18-05-07	
Money supply (M3)	485.3	490.6	492.7	14-05-07	498.7
Money supply growth y/y	19.3%	17.9%	18.1%	14-05-07	19.5%
Total PLN loans [PLN bn]	376.6	383.6	392.4	14-05-07	
Households PLN loans	194.2	197.1	203.6	14-05-07	
Corporate PLN loans	144.4	148.2	151.4	14-05-07	
Total PLN deposits [PLN bn]	404.7	410.7	410.9	14-05-07	
Households PLN deposits	226.3	228.6	227.1	14-05-07	
Corporate PLN deposits	124.1	126.1	125.5	14-05-07	
NBP intervention rate	4.00%	4.00%	4.00%	30-04-07	4.25%

Auctions

	next auc.	offer	avg yield last	last auction date
13 Week T-bills	-	-	4.208%	16-01-06
26 Week T-bills	-	-	3.943%	24-04-06
52 Week T-bills	23-04-07	-	4.373%	02-04-07
2Y T-bond OK1208	06-06-07	-	4.694%	04-04-07
5Y T-bond PS0412	18-04-07	-	4.967%	21-03-07
10Y T-bond DS1017	11-11-07	-	5.244%	11-04-07
20Y T-bond WS0922	12-09-07	-	5.309%	14-03-07

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