



## TOP NEWS FROM THE POLISH MARKET

### MACROECONOMICS

- Polish corporate wages surge in March to 9.1% y/y
  - PPI rose by 3.3% y/y
  - Industrial output up by 11.3%
  - A. Sławiński: single rate hike would not hurt growth rate
  - A. Wojtyna: small rate hike may prove necessary
  - S. Skrzypek: inflationary projection significantly lower than in January
  - H. Wasilewska-Trenkner: assumptions for projection overly optimistic
  - We expect 25 bps hike this week
  - Budget deficit amounted to 4.8 bn PLN after March
- pages 2-3

### FIXED INCOME

- Time for rate hikes
- pages 3-4

### FI RECOMMENDATION

- Stay pay

### MONEY MARKET

- Expensive week behind
  - Mixed after PPI and IO figure
- page 4

### MM RECOMMENDATION

- Sell short polonia

### FOREIGN EXCHANGE

- Zloty stronger
  - Volatility falling
- pages 4-5

### FX RECOMMENDATION

- Correction to 3.85
- Long Vega, short Gamma

### MARKET PRICES CHARTS CALENDAR CONTACT LIST

- page 6
- page 7
- page 8
- page 9

## MACROECONOMICS

**Polish corporate wages surge in March to 9.1% y/y**

Polish corporate wages surged in March to 9.1% y/y, far above the market consensus of 6.4%. In our opinion this may be a delayed effect of the rising demand for labour (however, having no access to the detailed data we cannot rule out that the record dynamics resulted from one-off events). Corporate employment was up by 4.5% y/y in March. Corporate wages rising at such a high pace may impact producer prices and further CPI inflation in the near future. In addition, we expect that a rise in the labour fund will stimulate private consumption.

Note that the reading of the corporate wage figure and the headline inflation is that inflation pressure has increased and the currently priced interest hikes may prove insufficient to curb inflation.

Last week, Polish Finance Minister Zyta Gilowska revealed her forecasts for unemployment. She sees the unemployment rate falling to below 12% in December from the 14.4% recorded in March. Even though we are more pessimistic and expect unemployment to fall to 12.5% by the end of the year, it is clear now (see the comment above) that labour demand surges and stimulates domestic demand.

**PPI rose by 3.3% y/y**

PPI in March rose by 0.5% m/m, which gives 3.3% y/y (consensus and BRE forecast 3.5%). The lower than expected figure results from a lower rise in mining prices (1.7% despite a significant rise in metal prices). On the other hand, the rise in manufacturing was in line with our expectations (0.5%). In April, due to base effect a drop in PPI should occur – our preliminary estimates show a drop to 2.1% y/y. In the summer months we may see levels at around 1%, but it must be noticed that this is visibly higher than was expected a few months ago.

**Industrial output up by 11.3%**

Industrial output was up by 11.3% y/y in March, a touch above the consensus forecast of 10.5%. In February a 12.9% industrial output growth was recorded. A drop in the annual figure was due to high base effect and the lower number of working days in March 2007. The seasonally adjusted figure is estimated at 13.3%, which in our opinion clearly indicates that the current condition of Polish industry is excellent.

**A. Sławiński: single rate hike would not hurt growth rate**

A. Sławiński of the MPC thinks the inflationary outlook remains fairly positive, but inflationary pressure may arise with time. He is afraid that the high pace of growth may lead to more rapid tensions on the labour market (given the March data on the labour market, we may see those fears materializing). The economic growth is, in his opinion, stable, with 3 pillars behind it – strong demand in Germany, rising inflow of FDI and high business confidence among Polish entrepreneurs. In summary, he thinks a single hike would not harm economic growth, but would help in stabilizing inflationary expectations.

**A. Wojtyna: small rate hike may prove necessary**

A. Wojtyna reckons a small hike in interest rates may prove necessary in order to control the sustained pick up in inflation rate next year. He expects the new inflationary projection to show a somewhat lower path of CPI throughout the projection horizon, but it will still show a high risk of target overshooting in 2009, which must be considered a serious risk. Such a path would be in line with our expectations, but we must underline that the projection did not include the March CPI and wages data – both indicating a significant risk of CPI rebound. Besides, even Prof. Wojtyna referred to the labour market data, admitting that the uncertainty regarding wages growth would lead to inflation risk.

**S. Skrzypek: inflationary projection significantly lower than in January**

**H. Wasilewska-Trenkner: assumptions for projection overly optimistic**

**We expect 25 bps hike this week**

**Budget deficit amounted to 4.8 bn PLN after March**

Also, S. Skrzypek stressed that the inflationary projection should be significantly lower than the one prepared in January. He also underlined that the CPI in Q1 was actually lower than anticipated in the projection. The NBP President thinks the economy has entered a phase of balanced growth, which is set to last for the next few years. He admitted that the MPC monitors private consumption growth, but added that current levels should not cause additional inflationary pressure.

The discussion on the inflationary projection was summarized by Dr Wasilewska-Trenkner, who indicated that the preliminary assumptions for the projection may prove overly optimistic as the projection does not include March CPI data indicating a rise in services prices (this must be supplemented by the wages data, also pointing to a more significant risk than was previously expected).

In our opinion the majority of the MPC is aware of the fact that the assumptions may be too optimistic and will rather focus on current data than on the inflationary projection.

**Our comment:**

In our opinion the inflationary risks are becoming more and more visible, which is not yet fully acknowledged by the majority in the MPC. We think the MPC will hike rates by 25 bps this week, which in our opinion should be regarded as the first hike in the cycle. Because in our opinion the forthcoming information would point to a risk in the pick up of CPI, we think the next hike will have taken place by July.

The Finance Ministry announced that the budget deficit after March amounted to 4.8 bn PLN, i.e. 16.1% of the plan. This figure is only slightly worse than the earlier estimates of the MinFin (14-15%) and the 22% scheduled at the beginning of the year. Higher than scheduled were the tax revenues. Budget spending amounted to 23.4% compared to the 24.8% scheduled. Finance Minister Zyta Gilowska wished that the whole year's budget figure were as good as for the year before (25 bn PLN), but it may not be easy given the tax cuts to be implemented in 2007.

Moreover, we note that the budget revenues may be lower by about 750 mn PLN in the summer due to lower than planned dividends paid by the PZU, Poland's biggest insurer, in which the state has a majority stake. This will, however, have no impact on the whole year figure. Higher tax revenues, which are attributable to superior economic conditions, will compensate for the decline in dividends.

## **FIXED INCOME**

**Time for rate hikes**

This week most important event is the MPC decision to be announced on Wednesday. We see 25bp hike followed by slightly hawkish statement. In our opinion the market is a bit too optimistic about future rate scenario, and expectations of the Council doing just one preemptive strike and then considering their job as done will not be fulfilled. We expect MPC to be more aware of future inflation risks and therefore become more data dependent. In such circumstances we don't see much room for lower rates and serious chances for rates going significantly up. We recommend staying pay and using any strengthening to add to this position.

**RECOMMENDATION:**

Stay pay

**MONEY MARKET****Expensive week behind**

Last week was even more expensive than we were forecasting in our last report, but the direction was very good. Next week will be different. Get prepared for the cheap end of reserve.

**Inflation, wages above market forecasts**

As for longer terms everyone was waiting for figures. First of them (wages) on Tuesday, was substantially above the market expectations (9.1% vs. 6.4%) supporting the fast rates hike view. PPI numbers was lower than expected but still near a multi-month high (3.3%), and IO rose 11,3 percent y/y faster than expected. Our probability distribution of this scenario (hike in April) grew again and now is 80:20.

**Next T-bill auction on April 23<sup>rd</sup>**

Poland's finance ministry said Friday it will offer 900 million zlotys in 52-week treasury bills at auction Monday. The offer value is at the bottom end of the ministry's preliminary range of 0.9-1.0 billion zlotys.

**RECOMMENDATION:**

Sell short polonia

**FOREIGN EXCHANGE****Zloty stronger**

Zloty is in strengthening trend started at 3,9100 with major bottom around 3,7600. Even other CE4 turbulences did not change overall view. Last week started at 3,8280 for EURPLN and ended at 3,7830. Week opening for USDPLN was at 2,8230 with 2,7820 on Friday close.

**Volatility falling**

Last week the implied volatility has reached the lowest level since ever. On average, (EUR/PLN options) 1M was traded at 5.9, whereas 12M at 6.1. Looking at these levels it seems that the volatility curve has found its support. USD/PLN volatility curve has decreased also. 1M traded at about 7.5 and 12M at 7.7.

**RECOMMENDATION:**

Spot:  
Main supports/resistances:  
EUR/USD 1.3525 / 1.3670  
EUR/PLN 3.7600 / 3.8500  
USD/PLN 2.7700 / 2.8030

**Correction after side trend**

This week the market will be still following global sentiment as this will indicate the local sentiment for Polish Zloty.  
Positive trend last from 3,9100 and breaking of 3,8000 triggered massive S/L taken by large bank on Friday. We expect 3,7600 to be held and with 1-2 days side trend we see correction target at 3,8500.

**Long Vega, short  
Gamma****Options:**

We think that during next week options should continue to trade on a bid tone (especially because of holiday during the first week of May). That's why we recommend short position in gamma.

Because of the very low historical volatilities we still recommend positive vega position.

**MARKET PRICES UPDATE****MONEY MARKET RATES**

Money market rates (Closing mid-market levels)						
date	3M		6M		1Y	
	FXSW	WIBOR	FXSW	WIBOR	FXSW	WIBOR
16-04-07	4.28%	4.29%	4.43%	4.48%	4.68%	4.69%
17-04-07	4.28%	4.29%	4.44%	4.49%	4.68%	4.69%
18-04-07	4.31%	4.32%	4.47%	4.50%	4.69%	4.72%
19-04-07	4.32%	4.35%	4.47%	4.51%	4.72%	4.72%
20-04-07	4.32%	4.35%	4.48%	4.51%	4.72%	4.73%

**FRA MARKET RATES**

FRA Market Rates (Closing mid-market levels)					
date	1X4	3X6	6X9	9X12	6X12
16-04-07	4.43%	4.61%	4.78%	4.88%	4.85%
17-04-07	4.43%	4.61%	4.77%	4.89%	4.85%
18-04-07	4.44%	4.62%	4.78%	4.88%	4.85%
19-04-07	4.44%	4.62%	4.79%	4.89%	4.87%
20-04-07	4.45%	4.62%	4.79%	4.89%	4.87%

**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
16-04-07	4.69%	4.38%	4.92%	4.62%	5.15%	5.10%	5.25%	5.31%
17-04-07	4.69%	4.37%	4.93%	4.62%	5.17%	5.12%	5.27%	5.31%
18-04-07	4.72%	4.38%	4.93%	4.66%	5.16%	5.11%	5.25%	5.31%
19-04-07	4.72%	4.37%	4.94%	4.66%	5.17%	5.11%	5.25%	5.31%
20-04-07	4.73%	4.36%	4.95%	4.66%	5.17%	5.12%	5.25%	5.33%

**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	07-04-18	12-04-25	98.416	5.11%	1800	8876	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
16-04-07	7.50	7.60	7.60	7.70	1.20	1.30	0.35	0.60
17-04-07	7.50	7.60	7.60	7.70	1.20	1.30	0.35	0.60
18-04-07	7.50	7.60	7.60	7.70	1.20	1.30	0.35	0.60
19-04-07	7.50	7.50	7.50	7.50	1.20	1.30	0.35	0.60
20-04-07	7.50	7.50	7.50	7.50	1.20	1.30	0.35	0.60

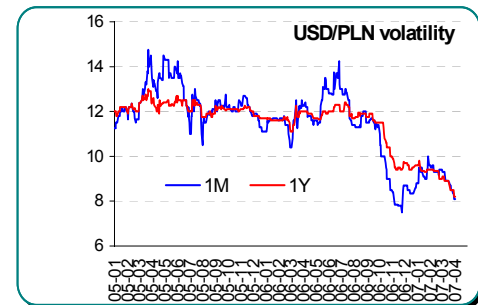
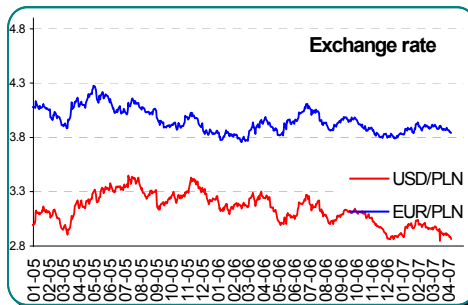
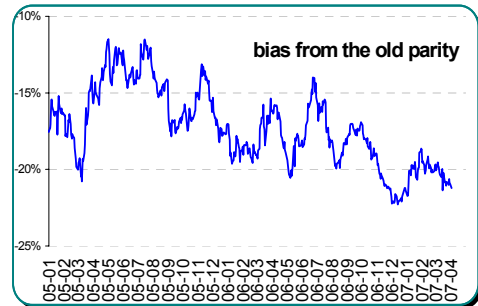
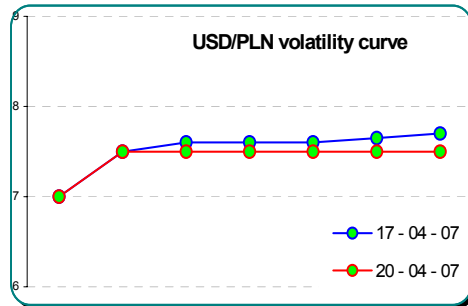
**PLN SPOT PERFORMANCE**

PLN spot performance			
date	USD/PLN	EUR/PLN	bias
16-04-07	3.8248	2.8217	-22.91%
17-04-07	3.8231	2.8241	-22.90%
18-04-07	3.8080	2.8005	-23.35%
19-04-07	3.8124	2.8049	-23.25%
20-04-07	3.7941	2.7894	-23.64%

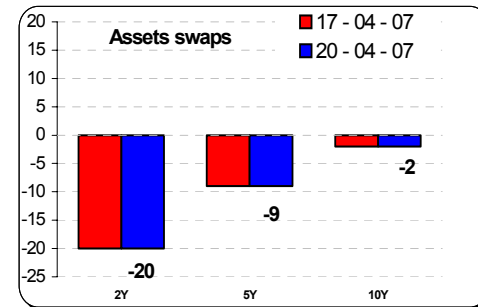
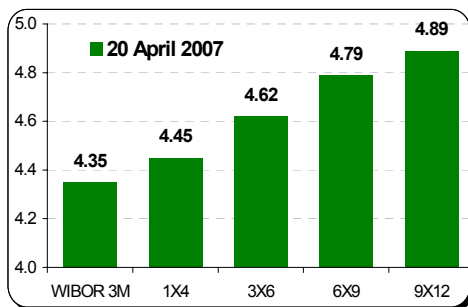
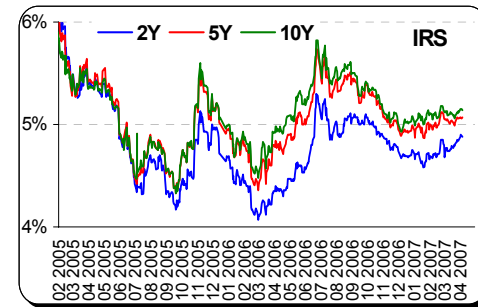
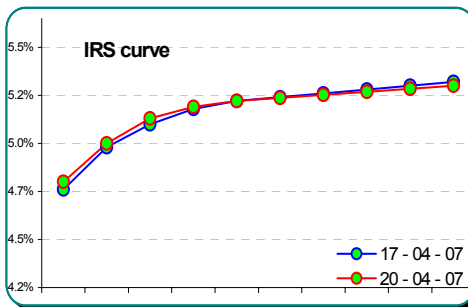
Note: parity on 11/04/00 – USD= 4.3806, EUR=4.2196, basket share 50:50  
Mid-market volatility of vanilla option strategies

**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%	0.5%	21-05-07	
PPI y/y	3.1%	3.5%	3.3%	21-05-07	
Industrial production growth m/m	0.2%	-2.1%	14.7%	21-05-07	
Industrial production growth y/y	15.4%	13.0%	11.3%	21-05-07	
Average wages in enterprise sector [PLN]	2663.6	2687.5	2852.7	17-05-07	
Average wages in enterprise sector y/y	7.8%	6.5%	9.1%	17-05-07	
Unemployment	15.1%	14.9%		25-04-07	14.4%
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	
Money supply growth y/y	19.3%	17.9%	18.1%	14-05-07	
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%	25-04-07	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	900	4.373%	02-04-07
2Y T-bond OK1208	06-06-07	-	4.694%	04-04-07
5Y T-bond PS0412	16-05-07	-	5.111%	18-04-07
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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