



TOP NEWS FROM THE POLISH MARKET

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- Central Bank governor, despite his quite hawkish comments, in our opinion, unlikely to back interest rate hike this year

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- We stick to the "stay pay and pay dips" strategy, one can try to catch a short term bullish move from here though

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- Buy synthetic 3*6 in OISs

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- Zloty weaker
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MACROECONOMICS

Polish MinFin correct downward the budget deficit estimates for May

According to preliminary estimates of the MinFin the budget deficit after May reached 14-15% of the annual plan. The previous estimates indicated that the figure may be a notch higher and amount to 16-17%. Given that the Ministry is now able to estimate the budget revenues more precisely (a few days ago Deputy Finance Minister E. Suchocka-Roguska pointed to higher budget spending in May), it seems that revenues continue to surprise on the upper side. The budget deficit in May 2007 at 2.5 bn PLN also would be much lower compared to the 4.5 bn PLN recorded in May 2006. Hence, we uphold our view that the whole year figure will be by 6-8 bn PLN lower than the 30 bn planned.

Unemployment rate down to 13.0% in May

The registered unemployment rate dropped by 0.7 percentage points, to 13.0%, in May. The number of unemployed declined by 116,600 compared to April. In the corresponding period of 2007 a 120,600 drop had been recorded. According to the official statement of the Ministry of Labour the decline in the registered unemployment was owing to various activation schemes implemented by the labour offices. This notwithstanding, we uphold our view that the economic recovery is the main factor affecting the unemployment figure. Given that demand for labour rises more significantly in the later phase of economic recovery, we expect the official unemployment figure to drop to 12.7% in June and to 11.4% in December 2007. The latter, according to our estimates, would be pretty close to the rate of structural unemployment.

Central Bank governor, despite his quite hawkish comments, in our opinion, unlikely to back interest rate hike this year

The Polish Central Bank governor, S. Skrzypek, underlined that the inflation rate would not breach the upper part of the target band within the coming 12 months. In an interview Mr. Skrzypek frequently reiterated that the Central Bank would guard the stability of prices and stabilize economic growth. He also stated that the adoption of the common currency is inevitable in the future. The only statement which one may directly link to the implementation of the monetary policy this year is that "the mounting inflationary risks owing to higher wages will be taken into account while deciding on interest rates in the future". In our opinion, however, it would be an exaggeration to interpret the above quotation as an announcement of a prompt interest rate hike. Judging by his earlier comments, especially those made directly after the May MPC meeting, S. Skrzypek is very unlikely to back the interest rate hike this year.

M. Noga: period of non-inflationary growth may be soon over

Contrary to quite dovish comments made by S. Skrzypek and, later on, by professor Pietrewicz, professor Noga reiterated that the period of non-inflationary economic growth in Poland may be soon over. In his opinion the output gap would widen in the coming months resulting in rising inflation. Furthermore, professor Noga, quoting the projections of the Central Bank staff, underlined that inflation would breach 3.5%, i.e. the upper band of the target, by the mid of 2008. As he perceives inflation rate of "slightly below" 2.5% as the most favorable for Polish enterprises and argues that higher inflation would adversely affect the competitiveness of Polish enterprises, in his opinion the MPC should anchor the inflationary expectations and eliminate the risk of higher inflation by hiking the rates in two steps this year.

Our comment:

As long as the headline inflation stays below the 2.5% target and the discussion concentrates solely on the future risks to inflation, the median voters (Owsiak and Czekaj) seem to be unlikely to vote for the rate hike. As the Polish MPC seem to be increasingly data dependent, the interest rate outlook may change significantly after the release of the monthly data for May.

FIXED INCOME**Friday, bloody Friday**

The beginning of the week seemed like the trading wasn't about to start at all - no data, no auction, long weekend ahead. But it turned out completely different. Firstly, quite a significant flow on Wednesday pushed the curve some 10-12bp up. As market perception was that it had just been a s/l order, rates relaxed by some 5bp at the end of the session. Friday's opening was already another 10bp higher after significant weakening on core markets and during the day we reached 5.29 and 5.55 on 2y and 5y respectively.

We think this move is just a part of an upward trend the market is in. However after such a big move in just a few days a correction is very likely before and we can touch 5.45% on 5Y before we move up again.

This week main issues will be CPI data scheduled on Wednesday - but since MinFin set up expectations at 2.1 y/y, we do not see it to impact market a lot, even though we see upside risk to this figure, 2.2 should still be quite neutral. Also new 30y bond (WS0437) scheduled on Wednesday should go well, which would also improve the outlook in the short term.

RECOMMENDATION:

We stick to the "stay pay and pay dips" strategy, one can try to catch a short term bullish move from here though

MONEY MARKET**Boring week waiting for figures**

Boring last week with quite stable carry. Open market operation 23 billion pln, however market bought only 20.8 billion pln, hence the carry should be lower next week.

T-bills yields down during the tender

Sentiment still weak and situation in region does not help, especially Thursday in Hungary dominated last week's closing. CPI on Wednesday should show whether last month's figures were just the break or not.

T-bills average yield down during the tender – 4,38% vs 4,48%. Bid-to cover ratio significantly up (3.9 up from 1.5) as the result of reduced supply. The Ministry of Finance sold 500 mio pln in the 52-week benchmark paper.

RECOMMENDATION:

Buy synthetic 3*6 in OISs

FOREIGN EXCHANGE**Zloty weaker**

Last week the Zloty traded range-bound between 3.7965 and 3.8580.

EUR/USD also traded between 1.3320 and 1.3555. USD/PLN traded between 2.8130 and 2.8900.

Volatility consolidating

Slow uptrend on EURPLN made implied volatilities consolidated at 6.6 for EURPLN 1M, and 6.25 for EURPLN 1Y.

RECOMMENDATION:***Zloty weaker******Long smile***

Spot:

Main supports / resistances:

EUR/USD: 1.3250 / 1.3400

EUR/PLN: 3.8100 / 3.8600

USD/PLN: 2.8350 / 2.9200

Low nominal polish interests rates, confronting with EUR, USD, NZD, AUD, CAD and rumors about dividend payments are, in our opinion, enough strong reasons to weaken PLN. In that case, in the following week we still may see EUR/PLN trade higher, that is why we recommend buying EUR/PLN around 3.81 with target 3.8850 in the following week.

Options:

With EURPLN breaking 3.85 levels we recommend long smile position, long upgamma and long upvega.

MARKET PRICES UPDATE**MONEY MARKET RATES****Money market rates (Closing mid-market levels)**

date	3M		6M		1Y	
	FXSW	WIBOR	FXSW	WIBOR	FXSW	WIBOR
04-06-07	4.42%	4.45%	4.53%	4.61%	4.78%	4.81%
05-06-07	4.42%	4.46%	4.55%	4.61%	4.80%	4.81%
06-06-07	4.42%	4.46%	4.55%	4.61%	4.80%	4.81%
07-06-07	4.42%	4.46%	4.55%	4.61%	4.80%	4.81%
08-06-07	4.44%	4.47%	4.58%	4.62%	4.86%	4.79%

FRA MARKET RATES**FRA Market Rates (Closing mid-market levels)**

date	1X4	3X6	6X9	9X12	6X12
04-06-07	4.50%	4.62%	4.83%	5.01%	4.96%
05-06-07	4.51%	4.61%	4.82%	5.00%	4.95%
06-06-07	4.52%	4.65%	4.86%	5.08%	5.02%
07-06-07	4.52%	4.65%	4.86%	5.08%	5.02%
08-06-07	4.52%	4.68%	4.90%	5.12%	5.04%

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
04-06-07	4.81%	4.38%	5.08%	4.56%	5.29%	5.15%	5.32%	5.30%
05-06-07	4.81%	4.40%	5.11%	4.57%	5.33%	5.17%	5.35%	5.32%
06-06-07	4.81%	4.41%	5.16%	4.60%	5.39%	5.25%	5.42%	5.37%
07-06-07	4.81%	4.41%	5.16%	4.60%	5.39%	5.25%	5.42%	5.37%
08-06-07	4.79%	4.45%	5.22%	4.60%	5.51%	5.37%	5.54%	5.48%

PRIMARY MARKET RATES**Last Primary Market Rates**

	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	07-06-04	08-06-04	95.759	4.38%	500	1931	500
OK0709	07-04-04	09-07-25	89.970	4.69%	1000	2463	1000
PS0412	07-05-16	12-04-25	98.360	5.13%	1500	8541	1500
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
04-06-07	7.75	7.75	7.75	7.75	1.20	1.30	0.35	0.60
05-06-07	7.75	7.75	7.75	7.75	1.20	1.30	0.35	0.60
06-06-07	7.75	7.75	7.75	7.75	1.20	1.30	0.35	0.60
07-06-07	7.75	7.75	7.75	7.75	1.20	1.30	0.35	0.60
08-06-07	7.75	7.75	7.75	7.75	1.20	1.30	0.35	0.60

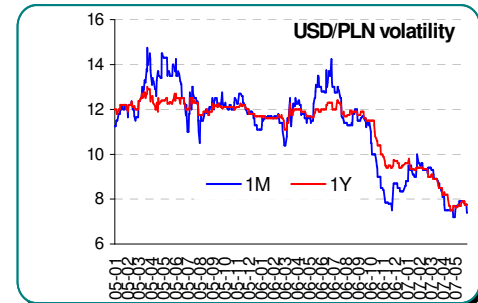
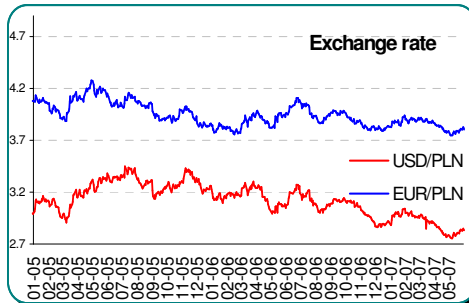
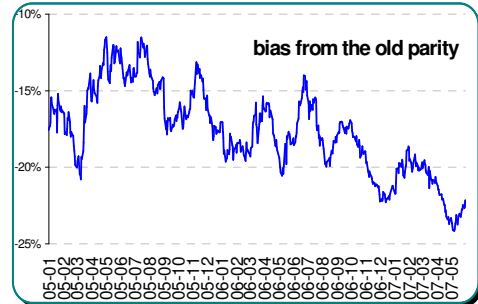
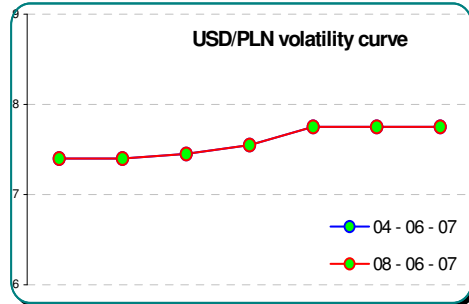
PLN SPOT PERFORMANCE**PLN spot performance**

date	USD/PLN	EUR/PLN	bias
04-06-07	2.8212	3.7940	-22.84%
05-06-07	2.8163	3.8050	-22.77%
06-06-07	2.8257	3.8216	-22.46%
07-06-07	2.8257	3.8216	-22.46%
08-06-07	2.8732	3.8485	-21.60%

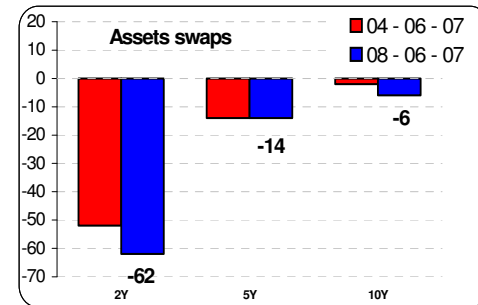
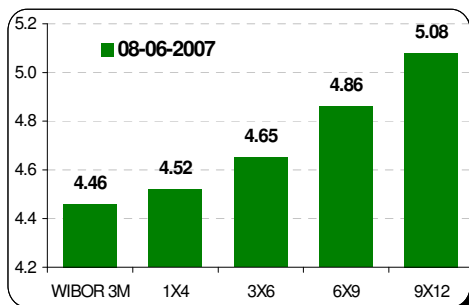
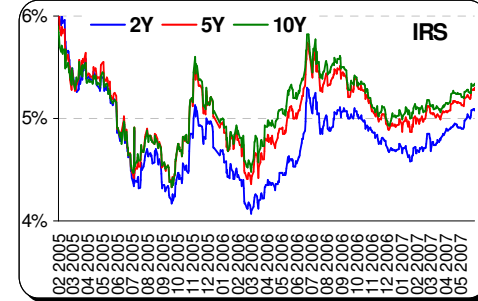
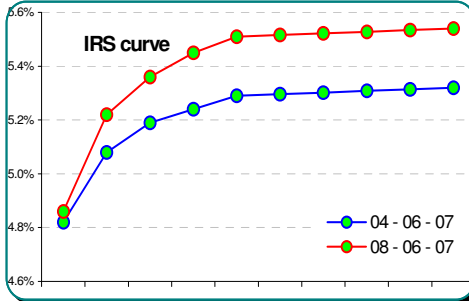
Note: parity on 11/04/00 – USD= 4.3806, EUR=4.2196, basket share 50:50
Mid-market volatility of vanilla option strategies

CHARTS

Foreign Exchange



Fixed Income



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CALENDAR

Macro

	March	April	May	Data Release	BRE Bank forecast
CPI m/m	0.5%	0.5%		13-06-07	0.4%
CPI y/y	2.5%	2.3%		13-06-07	2.2%
PPI m/m	0.5%	0.6%		20-06-07	0.1%
PPI y/y	3.3%	2.3%		20-06-07	2.1%
Industrial production growth m/m	14.7%	-8.7%		20-06-07	5.9%
Industrial production growth y/y	11.3%	12.4%		20-06-07	11.0%
Average wages in enterprise sector [PLN]	2852.7	2786.3		19-06-07	2781.7
Average wages in enterprise sector y/y	9.1%	8.4%		19-06-07	9.1%
Unemployment	14.4%	13.7%		22-06-07	13.0%
Budget realisation (%)	16.1%	6.9%		15-06-07	14.2%
Current account [EUR mn]	-539			15-06-07	-564
Balance of foreign trade in goods (transaction basis) [EUR mn]	-627			15-06-07	-554
Exports growth y/y (transaction basis)	15.8%			15-06-07	16.0%
Imports growth y/y (transaction basis)	21.7%			15-06-07	22.0%
Current account [% of GDP]	-2.2%			15-06-07	-2.2%
Money supply (M3)	492.8	498.7		14-06-07	
Money supply growth y/y	18.1%	17.8%		14-06-07	
Total PLN loans [PLN bn]	392.6	402.8		14-06-07	
Households PLN loans	203.7	209.6		14-06-07	
Corporate PLN loans	151.4	155.2		14-06-07	
Total PLN deposits [PLN bn]	410.8	414.4		14-06-07	
Households PLN deposits	227.1	225.2		14-06-07	
Corporate PLN deposits	125.4	126.7		14-06-07	
NBP intervention rate	4.00%	4.25%	4.25%	27-06-07	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	09-07-07	-	4.380%	04-06-07
2Y T-bond OK1208	04-07-07	-	4.694%	04-04-07
5Y T-bond PS0412	20-06-07	-	5.127%	16-05-07
10Y T-bond DS1017	11-07-07	-	5.244%	11-04-07
20Y T-bond WS0922	12-09-07	-	5.309%	14-03-07

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