BRE BANK SA

THE BEST FINANCIAL INSTITUTION FOR DEMANDING CUSTOMERS

FINANCIAL MARKETS DEPARTMENT

PAGES: 9

WARSAW, SEPTEMBER 18, 2009

POLAND WEEKLY REVIEW

MACROECONOMICS AND FINANCIAL MARKETS

PREVIEW: The week of September 18th to September 24th

Indicator	Date of release	Period	BRE forecast	Consensus	Last	Comment
Core Inflation y/y	Sep 22	Aug	**2.9%**	2.9%	2.9%	Moderate growth in core categories but too high to bring annual index down. Core inflation is likely to stay elevated for some months.
Retail Sales y/y	Sep 23	Aug	**5.8%**	5.6%	5.7%	Good data on auto sales combined with solid business tendency indicators and possible run for holiday spending in Poland are likely to fuel elevated levels of retail sales.

In Focus / Macroeconomics

Decent real sphere data and elevated inflation

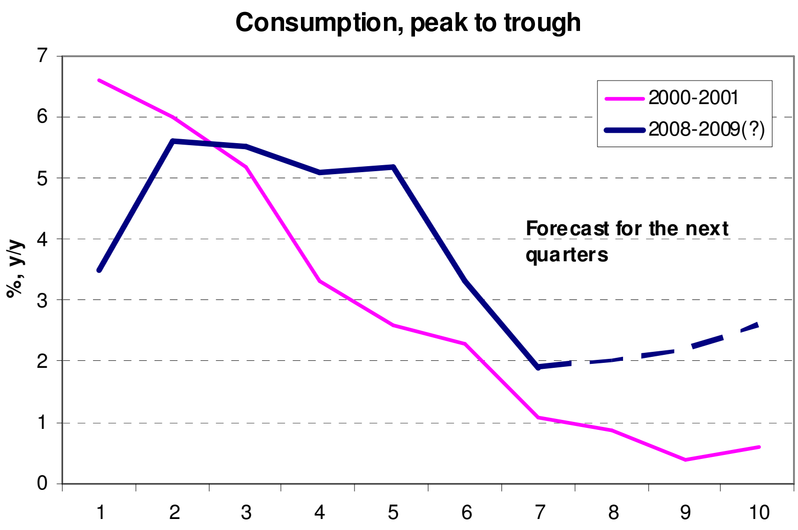
This week failed to give definitely clear picture of the real sphere. Although the data in no circumstances can be regarded as worse, it seems we have to wait until the holiday period is over to thoroughly assess existing trends. However, **employment and industrial output give a flavor of the resilience of the Polish economy and pose quite solid base for the coming months**. All this happens in the environment of elevated core and headline inflation. When we add the expansionary 2010 budget it is really hard to imagine MPC cutting rates. Quite the opposite – we expect the monetary policy stance to be altered to neutral in October meeting.

CPI inflation met earlier predictions of the Ministry of Finance, exceeding only by a notch market expectations. CPI fell by 0.4% on monthly terms and rose to 3.7% on annual basis (from 3.6% reported in July). Food prices behaved quite close to seasonal pattern (-1.3% m/m vs. August average of -1.1% m/m). We witnessed some ease in case of fuel prices (-1.9% m/m) and wearing apparel (seasonal sales); there is also some kind of moderation in other core categories – recreation and culture, health, communications and other goods and services. Core inflation remained intact in August at 2.9% y/y and will stay elevated for some time.

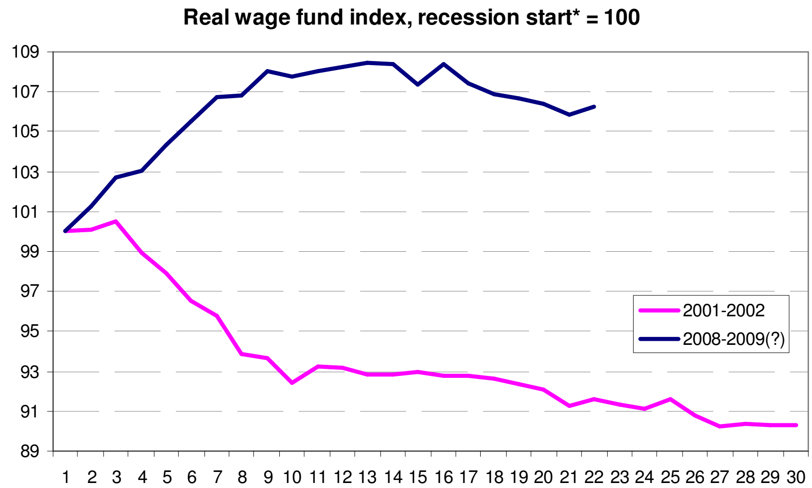
Next month is going to bring some moderation in CPI level. However, inflation outlook is far from benign at the moment (elevated core, quite resistant labor market, supply side expansion on the horizon, expansionary 2010 budget – not only in terms of doubled deficit but also higher spending to GDP ratio).

Wage growth showed a slight moderation by rising at 3.0% annual rate. However, compared with the previous months, the trend seems to be steeper, not flatter. Employment growth stabilized in August at -2.2% y/y and enterprise sector shed only 3k jobs on monthly basis (new cycle high). Such a circumstances can be truly named stabilization.

In our opinion, labor market may prove much more resistant than in previous recession episodes. Such a situation may be linked to greater flexibility of enterprises (mind that the majority of jobs was shed in the very beginning of the slowdown, along with decent drop of sentiment) which allowed them to preserve profit margins. Also government programs contributed to the contemporary situation by introducing flexible working hours (is seems enterprises exercised natural trade-off between working hours and employment in favor of the latter). Next months may bring more job cuts (end of seasonal employment in trade and construction) although a solid turnaround is on the horizon in the year end as supply side expansion sets in (manufacturing).



That is why we expect private consumption to have reached a trough in the current cycle already in Q2 (see the graph when in which we compare recession episodes: this one may be not only relatively shallow, but also shorter). The subsequent rise of the unemployment rate is unlikely to take its toll as it is related to the inflow of alumni, who – to be honest – does not alter their material status at all: they have been excluded from labor force and they will become unemployed (both cases entail no earnings). We are skeptical as far as the stories of ailing wage fund go. Back-of-the-envelope calculations show that during this slowdown episode the real wage fund (seasonally adjusted) have not yet fell below the initial level (from October 2007) whereas the correction during the 2001-2002 was much more abrupt. What is more, analyses basing on the income side neglect quite important wealth effects: turnaround in the stock exchange and lower payments connected with servicing mortgage debt (lower interest and much stronger zloty compared with the start of the year).



* Quite arbitrarily we set the start of the slowdown phase at the quarter with the highest real GDP growth (measured annually). X-axis starts then (we increased frequency to months) October 1999 (in case of 2001-2002 recession) and October 2007 (in case of 2008-2009(?) recession). In both cases we present seasonally adjusted data within 30 months peak to trough.

Industrial output in August fell by 0.2% y/y behaving slightly worse than expected by market consensus (+0.3%). Seasonally adjusted output posted a fall by -3.1% which may be regarded as an improvement compared with -5.3% print last month. To give a better taste of industrial output momentum one may look at seasonally adjusted growth on monthly basis which amounted to 0.5% this month, quite close to the results recorded in western economies.

Once again we are forced to admit that hard data point only to a minor moderation of falling trend which stands in opposition to brisk performance of business tendency indicators (especially PMI which “output” sub index breached 50pts barrier in August). It seems likely that the trend may be properly assessed after the holiday season. It leads us to sustain the scenario of growth (stabilization) of supply side in the coming months, connected with global business cycle embodied in expectations of the German upswing (which almost automatically translates into higher Polish exports of intermediate and capital goods).

Once again we recorded a positive (as expected) surprise from construction (+11.0% y/y versus 10.7% lat month and close to null H1 average): it almost definitely bodes well for investment activity in Q3 and speaks in favor of the scenario of prosperity of the EU investment connected sectors.

Producer prices surprised a bit to the downside (-0.2% m/m and 2.5% y/y vs. consensus 0.0% m/m and 2.7% y/y) speaking in favor of continuing disinflation. Slight EURPLN depreciation in September may slow temporarily slow down the whole process (along with input prices – especially. However, in mid-term we expect disiflation in supply side to continue as spare capacities stay high and wage growth remains subdued (especially compared with the roaring 2007-2008).

We expect the contemporary MPC to left the policy scene with 3.5% reference rate and decide to change monetary policy stance to neutral in October meeting following the release of new inflation projection. However, interest rate hikes are unlikely to be seen before H2 2010.

MID-TERM FORECATS

Indicator	2006	2007	2008	2009	2010
GDP y/y (%)	6.1	6.5	4.8	1.1-1.5	2.0-3.0
Inflation rate (%, average)	1.0	2.4	4.3	3.5	>1.8
Current account (% of GDP, average)	-2.1	-4.5	-5.3	0.2	-2.9
Unemployment rate (end-of-year)	14.9	11.4	9.5	12.3	12.8
NBP repo rate (end-of-year)	4.00	5.00	5.00	3.50	4.00

Indicator	2008		2009			
	Q3	Q4	Q1	Q2	Q3	Q4
GDP y/y (%)	4.7	2.9	0.8	1.1	**1.2**	**2.7**
Inflation rate (%, average)	4.7	3.8	3.2	3.7	3.5	3.6
NBP repo rate (end-of-quarter)	6.00	5.00	3.75	3.50	3.50	3.50

Bold denotes chages from the last release with arrows showing the direction of chages

Fixed Income

All about the "news".

Last week we saw some volatility on the curve. Week started with sell off in the middle long end of the curve as future supply fears started to weigh on the market. ASW were widening especially in the longer tenors, swap curve moved to 5.70 in 5y and 5.10 in 2y marking the local highs. After that the market was rather influenced by official statements rather than economic releases. First market mover was announcement of 1y repo operation with NBP which triggered very good buying in the 2y sector of the curve (bonds moved by 30bp in yield). After rather 3 poor tbills/tbonds auctions Ministry of Finance hinted opportunity of limited supply in long term maturities in the last quarter of 2009. Impact on the curve was really impressive (long bonds dropped by 15 bp in yield with WS0922 marking more that 100 cents gain in one day). Economic data came close to consensus and didn't have much impact on the market. Our opinion is still unchanged (though we are a little surprised by the price action) and we believe we will see higher yields in 1-3 months perspective. Supply is definitely not out (one should remember first of all about borrowing needs in 2010, additionally there is road program to finance by BGK bonds (7-8 bio to go) this year, possible ARP program (4 bio to go)) so apart from good marketing we are really looking forward to see how the actual execution will go. Second part is our view about recovery, we think that next few months can impress market in terms of CPI, IP, retail sales dynamics. So while carry game is still in place, we advice a little more cautious approach.

TRADE IDEAS:

stay pay in 1y3s (we are long at 4.45, market 4.42, we stop at 4.20), stay pay in 5y (we are long at 5.65, market 5.55 we stop at 5.40)

AUCTIONS

	next auc.	offer	avg yield last	last auction date
13 Week T-bills	-	-	6.142%	12/9/2008
26 Week T-bills	-	-	4.456%	5/4/2009
52 Week T-bills	9/21/2009	-	4.468%	9/14/2009
2Y T-bond OK0112	10/7/2009	-	5.130%	9/2/2009
5Y T-bond PS0414	10/7/2009	-	5.550%	9/9/2009
10Y T-bond DS1019	-	-	6.340%	5/20/2009
20Y T-bond WS0429	-	-	6.340%	5/20/2009

Money Market

Expensive short term interbank rates

Friday's CB bills tender made market square. Banks bought all 41,5 bln PLN papers from the offer. There was even small reduction – 2%. After the tender short term rates increased above 3% and will stay at this level till the next OMO.

This week was quite expensive that is why we expect next NBP tender to be under bidded especially that the end of reserve requirement period is coming.

T-bill's yields up at the

At the 6M repo on Tuesday demand was 480 mln in comparison to 62 mln PLN last month.

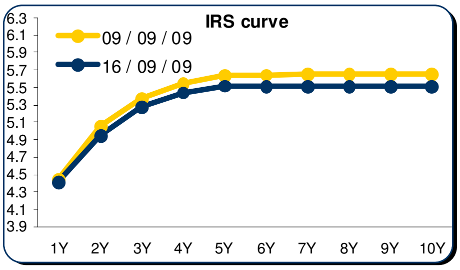
tender

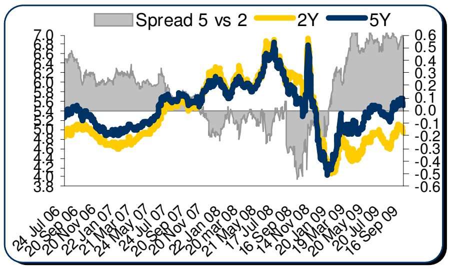
The average yield on Polish 52-week T-bills at primary tender up to 4,468% from 4,388%. Banks bidded 1,5 billion PLN and the Ministry sold 0,803 billion papers from the offer.

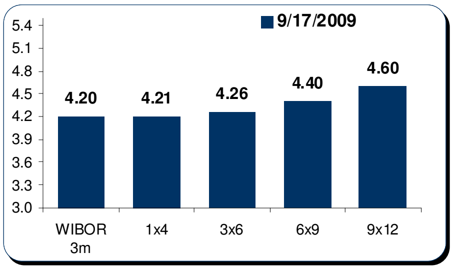
TRADE IDEAS:

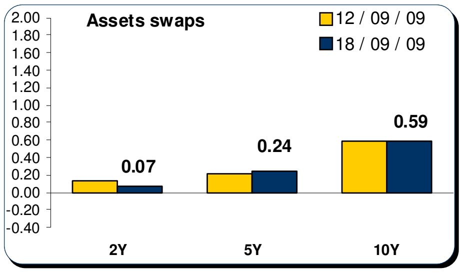
Offer 1W OIS at current level

FIXED INCOME & MONEY MARKET CHARTS









Foreign Exchange

Zloty weaker but still in range

Despite breaking 4.2000 and reaching 4.2500 on Monday, zloty strengthen to 4.1000 once again. Zloty reflected budget deficit worries but good global sentiment generated stronger signal.

Implied volatility stays steady

Volatility curve follows spot 1M was paid at 15.5 while 4.25, 13.5 was given at 4.1000. 1Y was traded in 13.00-13.50 range.

TRADE IDEAS:

SPOT

Main supports / resistances:
EUR/PLN: 4.0650 / 4.2700
USD/PLN: 2.8000 / 3.0000

Look for testing 4.06

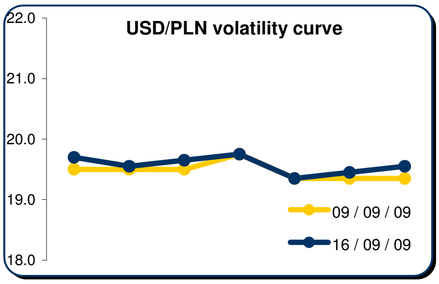
Zloty is trapped between 4.065 (Fibonacci) and 4.20 (EURPLN short entry level). Breaking of 4.2000 failed. If global sentiment stays so good testing of lower band is matter of time.

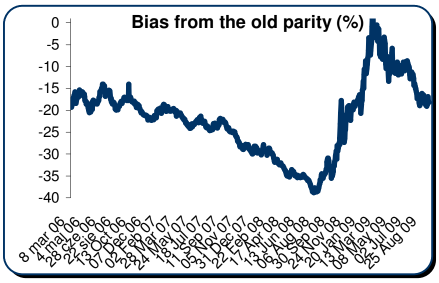
Short gamma

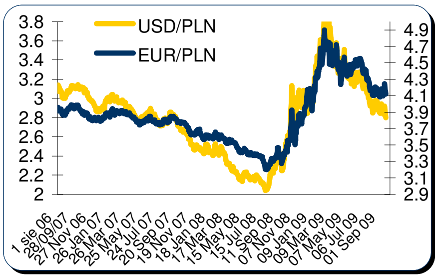
OPTIONS

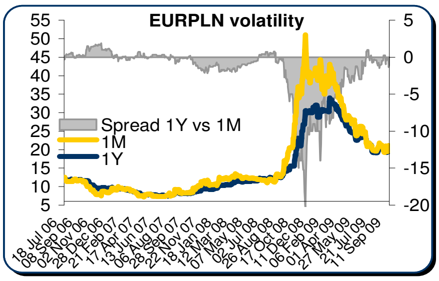
Short gamma seems to be good idea, testing of 4.06 shouldn't be aggressive.

FX CHARTS









MARKET PRICES UPDATE

MONEY MARKET RATES

Money market rates (Closing mid-market levels)

date	3M		6M		1Y	
	FXSW	WIBOR	FXSW	WIBOR	FXSW	WIBOR
10/09/09	4.13%	4.18%	4.22%	4.23%	4.40%	4.39%
11/09/09	4.14%	4.18%	4.22%	4.23%	4.39%	6.59%
14/09/09	3.99%	4.18%	4.22%	6.49%	4.45%	4.40%
15/09/09	3.99%	4.18%	4.22%	4.24%	4.40%	4.40%
16/09/09	4.00%	4.20%	4.23%	4.24%	4.37%	4.41%

FRA MARKET RATES

FRA Market Rates (Closing mid-market levels)

date	1X4	3X6	6X9	9X12	6X12
10/09/09	4.21%	4.28%	4.42%	4.64%	4.64%
11/09/09	4.21%	4.28%	4.43%	4.64%	4.63%
14/09/09	4.20%	4.27%	4.44%	4.65%	4.65%
15/09/09	4.20%	4.36%	4.44%	4.65%	4.65%
16/09/09	4.19%	4.28%	4.44%	4.66%	4.64%

FIXED INCOME MARKET RATES

Fixed Income Market Rates (Closing mid-market levels)

date	1Y		2Y		5Y		10Y	
	WIBOR	TB	IRS	OK0709	IRS	PS0511	IRS	DS1017
10/09/09	4.39%	4.43%	5.05%	5.20%	5.64%	5.86%	5.66%	6.26%
11/09/09	6.59%	4.37%	5.06%	5.20%	5.65%	5.86%	5.67%	6.26%
14/09/09	4.40%	4.37%	5.05%	5.20%	5.65%	5.90%	5.65%	6.28%
15/09/09	4.40%	4.37%	5.03%	5.12%	5.62%	5.86%	5.61%	6.25%
16/09/09	4.41%	4.34%	4.95%	5.02%	5.52%	5.76%	5.51%	6.10%

PRIMARY MARKET RATES

Last Primary Market Rates

	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	09/09/14	10/09/14	95.678	4.47%	1000	1495	803
OK0112	09/08/05	12/01/25	88.708	4.97%	4500	11232	4502
PS0414	09/09/09	14/04/26	100.003	5.74%	2000	2159	1108
DS1017	09/04/08	19/10/25	94.460	6.22%	2500	4846	1820

FX VOLATILITY

	USD/PLN 0-delta stradle				25-delta RR		25-delta FLY	
date	1M	3M	6M	1Y	1M	1Y	1M	1Y
10/09/09	19.50	19.75	19.35	19.35	2.75	4.00	1.00	1.10
11/09/09	19.55	19.75	19.35	19.55	2.75	4.00	1.00	1.10
14/09/09	21.05	20.25	19.75	19.70	2.75	4.00	1.00	1.10
15/09/09	20.55	20.00	19.55	19.55	2.75	4.00	1.00	1.10
16/09/09	19.55	19.75	19.35	19.55	2.75	4.00	1.00	1.10

PLN SPOT PERFORMANCE

PLN spot performance

date	USD/PLN	EUR/PLN	bias
10/09/09	2.8651	4.1699	-19.11%
11/09/09	2.8675	4.1858	-18.69%
14/09/09	2.9183	4.2461	-18.75%
15/09/09	2.8514	4.1640	-16.88%
16/09/09	2.8239	4.1501	-17.93%

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

Contact Details

BRE BANK SA

Ul. Senatorska 18
00-950 Warszawa
P.O. Box 728
Poland

Reuters Pages: BREX, BREY, and BRET

Bloomberg: BRE

SWIFT: BREXPLPW

www.brebank.pl

Forex (BREX) - FX Spot &Options
Marcin Turkiewicz (+48 22 829 01 84) Marcin.turkiewicz@brebank.pl
Jakub Wiraszka (+48 22 829 01 73)
Tomasz Chmielarski (+48 22 829 01 78)

Fixed Income (BREP) - FRA, IRS, T-Bonds, T-Bills
Łukasz Barwicki (+48 22 829 01 93) Lukasz.barwicki@brebank.pl
Paweł Białczyński (+48 22 829 01 86)

MM (BREP) - MM, FX Swaps
Bartłomiej Małocha (+48 22 829 01 77) Bartlomiej.malocha@brebank.pl
Tomasz Wołosz (+48 22 829 01 74)

Structured Products (BREX)
Jaroslaw Stolarczyk (+48 22 829 01 67) Jaroslaw.stolarczyk@brebank.pl
Jacek Derezinski (+48 22 829 01 69)

Institutional Sales (BRES)
Inga Gaszkowska-Gębska (+48 22 829 12 05)

Research
Ernest Pytlarczyk (+48 22 829 01 66) Research@brebank.pl
Marcin Mazurek (+48 22 829 0183)

Financial Markets Department
Phone (+48 22 829 02 03)
Fax (+48 22 829 02 45)

Treasury Department
Phone (+48 22 829 02 02)
Fax (+48 22 829 02 01)

Financial Institutions Department
Phone (+48 22 829 01 20)
Fax (+48 22 829 01 21)

Back Office
Phone (+48 22 829 04 02)
Fax (+48 22 829 04 03)

Custody Services
Phone (+48 22 829 13 50)
Fax

Disclaimer

Distribution and use of this publication