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FINANCIAL MARKETS DEPARTMENT

PAGES: 9

WARSAW, SEPTEMBER 24, 2009

POLAND WEEKLY REVIEW

MACROECONOMICS AND FINANCIAL MARKETS

PREVIEW: The week of September 25th to October 1st

Indicator	Date of release	Period	BRE forecast	Consensus	Last	Comment
MPC decision	Sep 30	-	**3.50%**	3.50%	3.50%	No surprise. According to the latest "Minutes" the MPC is already quite split on the indirect monetary policy stance. We expect some words on a possibility of changing monetary policy mode to neutral, which is going to officially take place in October, along with inflation projection.
PMI Index	Oct 1	Sep	**48.5**	-	48.2	Significant improvement of the business tendency indicators abroad. Polish PMI not once proved to be quite independent in the very short-run. This time we expect only a minor increase, having in mind large drop of business orders and quite disappointing industrial output in August.

In Focus / Macroeconomics

Retail sales rises although a notch slower than expected

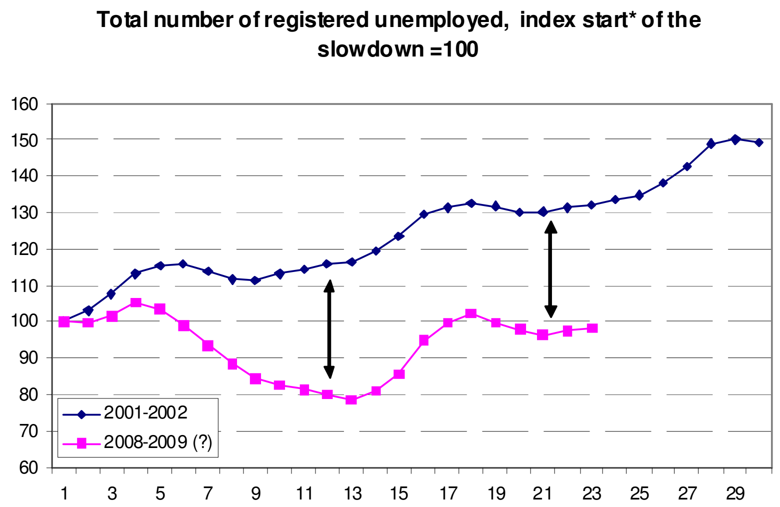
Retail sales came in a notch lower than expected in August. Despite the positive working days effect, the aggregate rose by 5.2% y/y vs. 5.7% y/y recorded in July. August sales figure, similarly to that in July, has been boosted by food sales (above 11% y/y) and pharmaceuticals (15.9% y/y), which may reflect the fact that more Poles spent their holidays in Poland this year. A significant improvement has been recorded in auto sales this summer (-1.9% y/y vs. -5.0% y/y in July). Sales of home appliances slowed to -4.9% y/y from 2.4% in July.

One has to note, however, that after a pronounced decline in sales excluding food and fuel in the first months of 2009 August was the third consecutive month characterized by a significant growth in the so called core categories (the sub-index accelerated from 4.5% y/y in June to 7.7% y/y and 6.2% y/y in July and August, respectively).

We uphold our opinion that the outlook for retail sales and consumer spending in general has improved and more and more hard data point to rising consumer confidence. We expect the individual consumption to at least stabilize in terms of y/y/ dynamics in the quarters to come. For our reasoning and more insightful analysis of one of the most important consumer spending determinants analysis see the piece below.

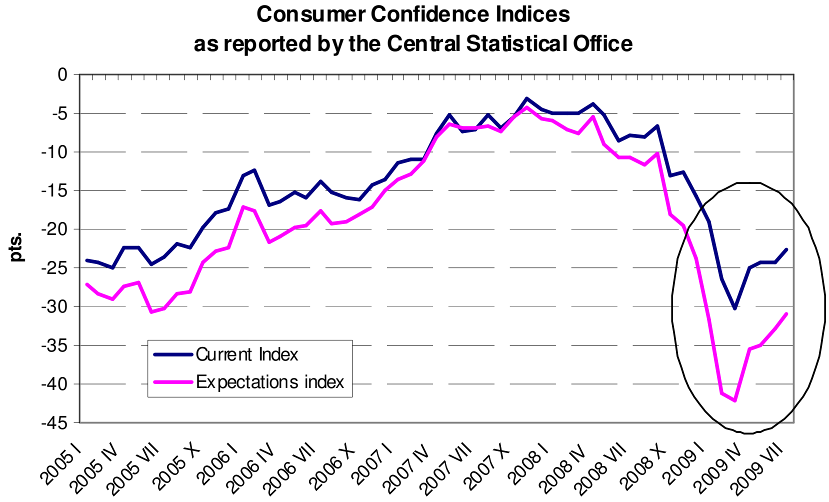
Is labor market strong enough? It seems it is.

Along with retail sales data, the Central Statistical Office announced that the unemployment rate stabilized at 10.8% in the end of the holiday season (August). In our opinion, recent trends in the labor market speak in favor of at least stabilization of individual consumption in the coming quarters. In order to present our view we rely on the flows in the labor market and analyze current employment situation. Our forecast hinges on the assumption that consumers react not only to changes in their current income (the issue we dealt with in the previous issue of weekly report) but also to its permanent component which is assessed by the households on the basis of formulated expectations.

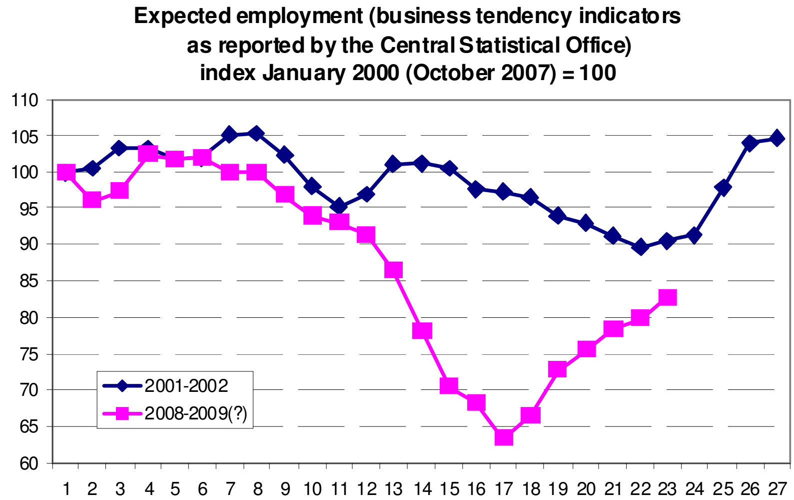


* Quite arbitrarily we set the start of the slowdown phase at the quarter with the highest real GDP growth (measured annually). X-axis starts then (we increased frequency to months) October 1999 (in case of 2001-2002 recession) and October 2007 (in case of 2008-2009(?) recession). In both cases we present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

When we compare the inflow of unemployed citizens with the previous slowdown episode there is no visible upward trend, contrary to what we observed some years ago (see the graph above). Such a tendency may sustain the purchasing power of consumers (mind the fast deterioration in the last cycle) and, at the same time, reinforce more favorable expectations; to back up our view by the data we present consumer confidence indices (see another graph, this time below) which are now trending upwards (after a period of deterioration which went hand in hand with considerable drops in employment). During the cycle we do not expect a radical inflow of the unemployed. In the most pessimistic scenario (in which tendencies form 2001-2002 replicate now) the number of unemployed may grow by 250-300k (we rationally expect this slowdown to be no longer than the previous one) which translates into unemployment rate at 12.8% (top value) in the end of 2010.



Turning to employment, situation has stabilized in the last few months (we elaborated on the causes of such situation in the last weekly report). Although we admit the wave of lay-offs may struck in Autumn (lagged effects of firms bankruptcies and group lay-offs, factor already included in the past market sentiment), the scale of this (negative) process is likely to be subdued as business tendency indicators are relentlessly pointing upwards (see the graph below). We expect then employment trends (as measured by the annual index) to turnaround at the turn of the year. Such a behavior of the employment series may again back up expectations (support to the valuation of the permanent income) and prevent expenditures from fading.



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

Surprisingly good auction.

Most interesting event of the passing week was the WS0922 bond auction held on Wednesday. 2 bio supply met very decent demand (bid/cover ratio close to 2). After the auction the bond gained some 5bp. Beside that, market was relatively quiet, with slight pressure on lower yields. However market seems a little vulnerable - temporary currency weakening was enough to push yields up by a spread. Economic data published this week were quite in line with expectations and didn't have any impact on the curve. Next week's MPC meeting isn't likely to bring anything new to the picture, as council members will probably wait till next month to see the latest inflation projection. We didn't change our view, still see yields higher in few month perspective, strengthening on the market seems just an opportunity to add to pay positions, especially in the front end (1y3s seems a very cheap option here, with 3x6 only few bp over spot Wibor, while historically Wibors tend to move higher in December, 9x12 not actually pricing a full rate hike which is in our opinion likely to happen in the beginning of 2H2010)

TRADE IDEAS:

Stay pay 1y3s (we entered at 4.45, currently at 4.41, with s/l at 4.20), stay pay in 5y (we entered at 5.65, currently at 5.52, s/l 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	9/29/2009	-	4.411%	9/21/2009
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	-	-	6.300%	9/23/2009

Money Market

Cheap end of the reserve

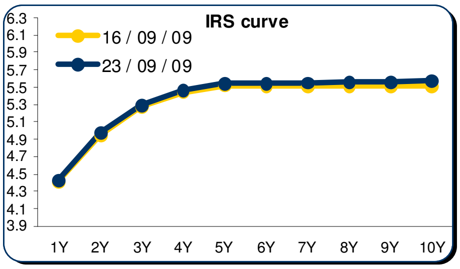
T-bills yields down during the tender

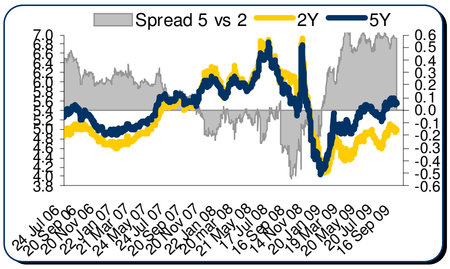
Very cheap week before the end of the reserve and no chances to see higher shortest rates till Wednesday (start of the new reserve). With hugely overbuilt current reserve, tomorrow's OMO becomes irrelevant for the next few days. Then the new OMO will try to balance the market.
Benchmark T-bill average yield lower by 6 bps comparing to the previous auction (at 4,41%).
Nothing new for trading, still consensus is for first rate hikes coming in the middle of the next year. The MPC is not expected to do anything next week.

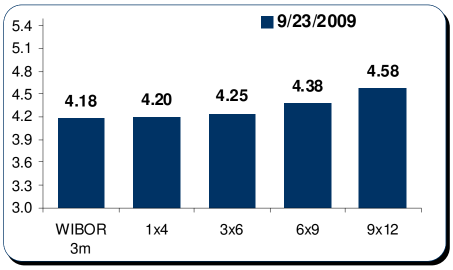
TRADE IDEAS:

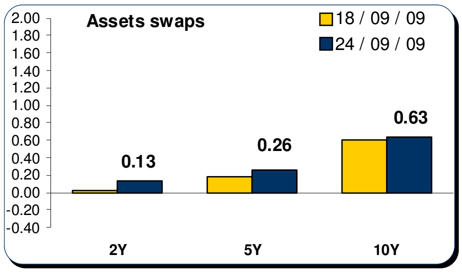
Sell 3M polonia on hikes.

FIXED INCOME & MONEY MARKET CHARTS









Foreign Exchange

Zloty weaker but still in range

This week EURPLN opened at 4.1450, weakened to 4.2075 and retraced to 4.1550. Still trading the same range but in worse sentiment. Once again budget deficit worries followed by possible decent outflow order forced market to close PLN longs.

While EURPLN is trapped in range, volatility curve stays pretty untouched. 1M is traded at 13.5, 1Y at 12.5.

Implied volatility stays steady

SPOT

TRADE IDEAS:

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

Wait if 4.27 hold

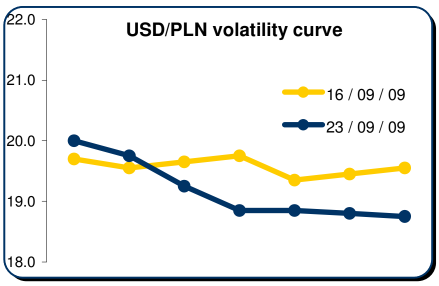
Zloty is trapped between 4.065 (Fibonacci) and 4.20 (EURPLN short entry level). On one hand market became slightly short PLN on the other huge outflow is likely. If won't happen probability of retesting 4.06 is huge.

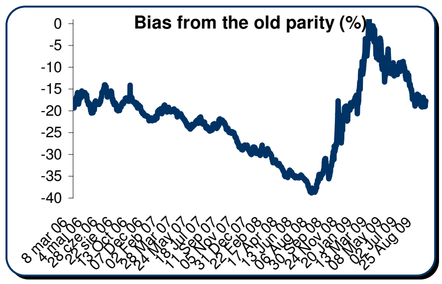
Stay away

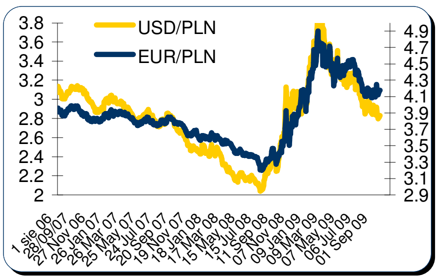
OPTIONS

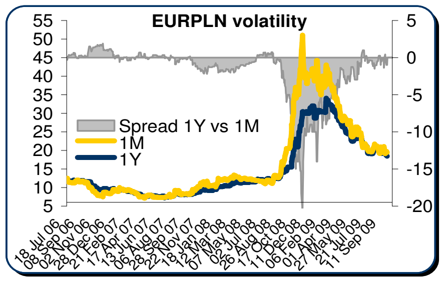
Wait for spot reaction. Selling gamma/vega if order turned rumour or will be done is next obvious move.

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
17/09/09	4.00%	4.20%	4.23%	4.25%	4.37%	4.41%
18/09/09	4.12%	4.19%	4.23%	4.26%	4.41%	6.59%
21/09/09	4.06%	4.17%	4.22%	6.49%	4.36%	4.39%
22/09/09	4.05%	4.17%	4.22%	4.24%	4.37%	4.38%
23/09/09	4.04%	4.18%	4.25%	4.23%	4.37%	4.38%

FRA MARKET RATES

FRA Market Rates (Closing mid-market levels)

date	1X4	3X6	6X9	9X12	6X12
17/09/09	4.19%	4.28%	4.44%	4.66%	4.64%
18/09/09	4.21%	4.27%	4.41%	4.63%	4.64%
21/09/09	4.21%	4.24%	4.37%	4.57%	4.56%
22/09/09	4.21%	4.26%	4.40%	4.60%	4.61%
23/09/09	4.22%	4.27%	4.40%	4.61%	4.60%

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
17/09/09	4.41%	4.37%	4.97%	5.01%	5.54%	5.73%	5.51%	6.12%
18/09/09	6.59%	4.37%	5.03%	5.05%	5.61%	5.79%	5.59%	6.19%
21/09/09	4.39%	4.37%	5.01%	5.06%	5.58%	5.82%	5.57%	6.21%
22/09/09	4.38%	4.36%	4.96%	5.05%	5.53%	5.81%	5.53%	6.22%
23/09/09	4.38%	4.36%	4.98%	5.11%	5.54%	5.80%	5.57%	6.20%

PRIMARY MARKET RATES

Last Primary Market Rates

	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	09/09/21	10/09/21	95.730	4.41%	1000	3658	1000
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
17/09/09	19.10	19.05	18.95	19.55	2.75	4.00	1.00	1.10
18/09/09	19.30	19.05	18.95	19.05	2.75	4.00	1.00	1.10
21/09/09	19.30	19.05	18.95	19.00	2.75	4.00	1.00	1.10
22/09/09	19.50	18.85	18.85	18.75	2.75	4.00	0.90	1.10
23/09/09	19.75	18.85	18.85	18.75	2.75	4.00	0.90	1.10

PLN SPOT PERFORMANCE

PLN spot performance

date	USD/PLN	EUR/PLN	bias
17/09/09	2.7969	4.1204	-18.20%
18/09/09	2.8228	4.1447	-18.30%
21/09/09	2.8295	4.1498	-19.03%
22/09/09	2.8094	4.1565	-18.93%
23/09/09	2.8214	4.1742	-17.89%

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

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