



POLAND WEEKLY REVIEW

MACROECONOMICS AND FINANCIAL MARKETS

**IN FOCUS /
MACROECONOMICS**

- Polish government reconstruction • page 2

FIXED INCOME

- Quiet market. Another good auction. • pages 2-3
- Close outright 1y3s. Pay FRA spreads: 3x6 ag 9x12 at +30, 6x9 ag 12x15 at +50.

FI TRADE IDEAS
MONEY MARKET

- Successful T-bond auction and T-bills buy back • page 3
- Repo with the central bank should be supported this month by the maturing 3M operation held in July.

MM TRADE IDEAS

- Sell 6M polonia.

FOREIGN EXCHANGE

- Zloty in range • page 4
- Implied volatility stays steady

FX TRADE IDEAS

- Sell 4.27/4.30
- Sell vega

**MARKET PRICES
CONTACT LIST
DISCLAIMER**

- page 5
- page 6
- page 7

PREVIEW: The week of October 9th to October 15th

Indicator	Date of release	Pe-riod	BRE forecast	Consensus	Last	Comment
C/A balance EUR	Oct 13	Aug	+67 mln	-110 mln	-565 mln	Trade deficit narrowed a bit but it is an income account which is driving the improvement in the whole aggregate, along with better transfer payments. There is a risk of a significant downward revision of the past data.
M3 Supply y/y	Oct 14	Sep	8.6%	8.8%	9.2%	Meager growth of firms' deposits (restoring higher inventory level, credit repayment) accompanied by the inflow of funds towards mutual funds.
CPI Inflation y/y	Oct 14	Sep	3.3-3.4%	3.5%	3.7%	Despite higher MinFin estimate at 3.5% we remain bearish on this months inflation outlook, mainly on favorable outlook for food (we expect monthly drop) and fuels (another monthly drop of prices). Net inflation leveling off a bit to 2.8% y/y.

In Focus / Macroeconomics

Polish government reconstruction

On Wednesday press conference Polish PM D. Tusk announced the broad reconstruction of his cabinet. He ousted ministries of Interior, Justice and Sports affairs along with Deputy Minister of the Economy. All the dismissals were related to their alleged involvement in a so-called gambling gate (in which some ministers are blamed to have offered help concerning favorable changes in the forthcoming gambling bill). Tusk also announced his aim to dismiss the Head of Central Anti-corruption Bureau (the guy who disclosed the corruption scandal but is blamed for acting on behalf of opposition party).

The very moment of Tusk's conference correlated with quite dynamic zloty depreciation. However, the developments on the FX are hardly to be directly associated with government reconstruction, though. We saw parallel changes in EURUSD and weakening across all CEE currencies due to rumors that Czech Central Bank plans currency interventions to weaken its currency. At the same time the investors rushed to buy Polish bonds at the 2 year tender (11.9 bn demand, prices very close to the secondary market, positive sentiment and lower yields at the front end of the curve as the result).

The opinion polls at hand indicate that the ruling party is still very popular (support running at 48-50%) and the impact of the gambling gate does not exceed measurement error. We do not think the gambling gate had any impact on the stability of the ruling coalition whatsoever. Finally, it did not negatively affect the popularity of PM Tusk and his chances to win the presidential election (Autumn 2010). We think that it is the Tusk's popularity running so high (and clearly presidential election being so distant event) that prevented markets from overreacting.

In our opinion, the so-called political risk is to be more important factor for 2010 – investors see Tusk's presidency (now very likely outcome) as a chance for fiscal reforms (now being impossible due to President Kaczynski's veto). Fluctuations in Tusk's popularity are thus to be closely monitored by investors and are expected to be more and more critical for the markets with the passage of time.

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	-1.2	-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 changes from the last release with arrows showing the direction of changes

Fixed Income

Quiet market. Another good auction.

Market was relatively stable this week, fluctuating within a narrow range amid low turnover, though the curve has steepened by few bp. Most interesting event was the 2Y bond auction OK0112 on Wednesday, which attracted close to 12 bio in bids against 4.5 bio of supply. Cheap cash and perspectives for the 1Y repo operation in 1Q10 still give support for the bonds in the front end. Next week major event will be the inflation data, to be published on Wednesday. Our forecast is 3.3-3.4%, which is slightly lower than recent MinFin's estimate of 3.5%. As that would likely push front end even lower, we decided to close our pay position in 1y3s, taking some 7-8bp loss. Instead we prefer to pay FRA spreads, 3x6 ag 9x12 and 6x9 ag 12x15 are our favorites. They currently trade at +30 and +50 respectively, which seems very low to us, as the first

leg fixes at the beginning of next year, in period of lowest CPI, and second leg is already when tightening cycle is likely to have started (yet the spreads hardly price in single 25bp hike.)

TRADE IDEAS:

Close outright 1y3s. Pay FRA spreads: 3x6 ag 9x12 at +30, 6x9 ag 12x15 at +50.

AUCTIONS

	next auc.	offer	avg yield last	last auction date
13 Week T-bills	-	-	6,142%	2008-12-09
26 Week T-bills	-	-	4,456%	2009-05-04
52 Week T-bills	2009-10-12	-	4,397%	2009-09-29
2Y T-bond OK0112	2009-11-10	-	5,115%	2009-09-02
5Y T-bond PS0415	2009-12-02	-	5,550%	2009-10-07
10Y T-bond DS1019	-	-	6,340%	2009-05-20
20Y T-bond WS0429	-	-	6,300%	2009-09-23

Money Market

Successful T-bond auction and T-bills buy back

Very cheap beginning of the new reserve, as the central bank's supply of the money bills was not matched by the demand (45 vs 42.5 billion pln). Surplus of the cash supported the demand for the OK0112 auction, which reached 12 billion pln and 5.5 billion pln of the papers was sold. The average yield was 5.12%. T-bills buy back by the MinFin was also quite successful, and caused 2 billion pln inflow to the system.

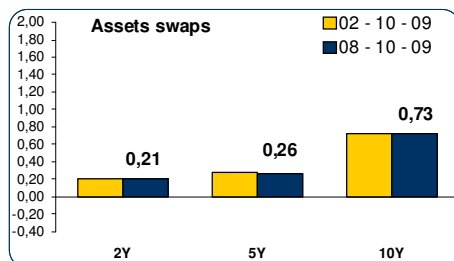
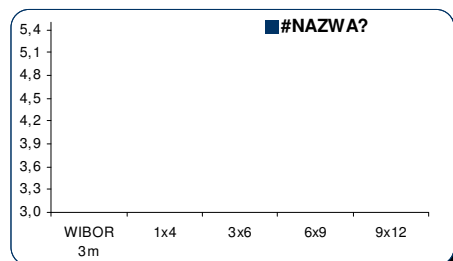
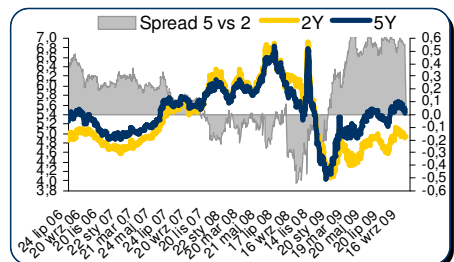
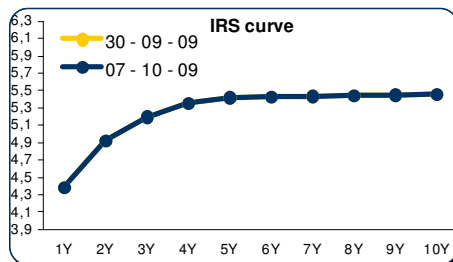
Repo with the central bank should be supported this month by the maturing 3M operation held in July.

OIS curve remains low, which indicates strong expectations for another cheap month as far as cost of carry, is concerned. Next week we have 3M repo facility with the central bank. We expect the demand to be much higher than in previous month, since 1.3 billion pln from the July auction is maturing on Thursday. Therefore either 3M auction or 6M auction this month should be nicely supported.

TRADE IDEAS:

Offer 1M polonia.

FIXED INCOME & MONEY MARKET CHARTS



Foreign Exchange

Zloty in range

This week EURPLN opened at 4.2050 and had been traded in 4.1700-4.2450 range. Amount of PZU dividend is known so Zloty is once again driven by global sentiment. Only local factor is government reconstruction.

Implied volatility stays steady

Despite quiet EURPLN trading, longer we stay above 4.20 short vols are a bit bidden, 1M had been paid at 14.7 while 1Y stays at 12.5 level.

TRADE IDEAS:

SPOT

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

Sell 4.27/4.30

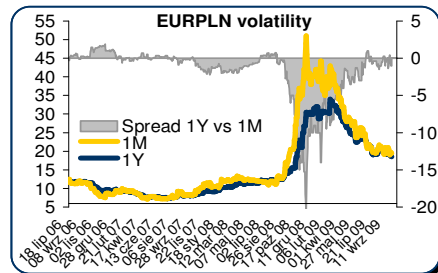
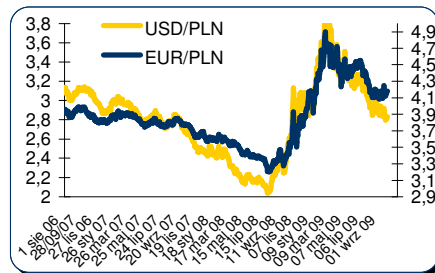
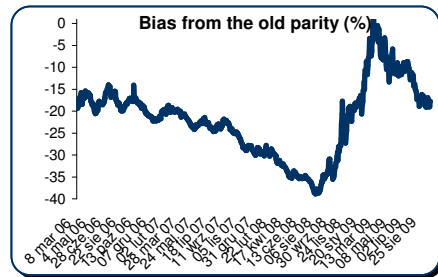
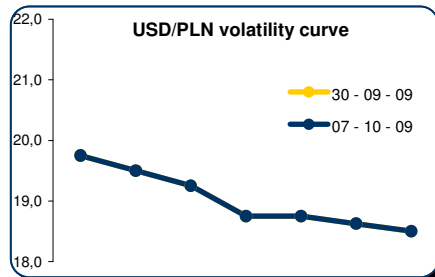
Economy performs well, Eureka outflow proved to be lower than expected. Despite government problems, wavy global sentiment we see these levels as selling opportunity (especially 4.35). First target is 4.15, 4.07 and 4.00 next ones.

Sell vega

OPTIONS

We like idea being short 6M 25D delta put. On other hand being short 1M/2M Risk Reversals should provide profitable gamma structure.

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
01-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?
02-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	6,59%
05-10-09	#NAZWA?	#NAZWA?	#NAZWA?	6,49%	#NAZWA?	#NAZWA?
06-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?
07-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?

FRA MARKET RATES

FRA Market Rates (Closing mid-market levels)					
date	1X4	3X6	6X9	9X12	6X12
	01-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?
02-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?
05-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?
06-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?
07-10-09	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?	#NAZWA?

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
01-10-09	#NAZWA?	4,30%	4,97%	5,15%	5,46%	5,73%	5,51%	6,22%
02-10-09	6,59%	4,35%	4,96%	5,16%	5,47%	5,75%	5,51%	6,23%
05-10-09	#NAZWA?	4,36%	4,91%	5,15%	5,42%	5,74%	5,47%	6,23%
06-10-09	#NAZWA?	4,35%	4,89%	5,12%	5,42%	5,71%	5,48%	6,20%
07-10-09	#NAZWA?	4,30%	4,89%	5,10%	5,44%	5,70%	5,47%	6,20%

PRIMARY MARKET RATES

Last Primary Market Rates							
	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	09-09-28	10-09-28	95,743	4,40%	1000	2485	848
OK0112	09-09-07	12-01-25	89,179	5,12%	4500	11890	4500
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

date	USD/PLN 0-delta straddle				25-delta RR		25-delta FLY	
	1M	3M	6M	1Y	1M	1Y	1M	1Y
01-10-09	19,50	18,75	18,75	18,50	2,75	4,00	0,90	1,10
02-10-09	19,50	18,75	18,75	18,50	2,75	4,00	0,90	1,10
05-10-09	19,50	18,75	18,75	18,50	2,75	4,00	0,90	1,10
06-10-09	19,50	18,75	18,75	18,50	2,75	4,00	0,90	1,10
07-10-09	19,50	18,75	18,75	18,50	2,75	4,00	0,90	1,10

PLN SPOT PERFORMANCE

PLN spot performance			
date	USD/PLN	EUR/PLN	bias
01-10-09	2,8309	4,1780	-17,67%
02-10-09	2,8309	4,1780	-17,67%
05-10-09	2,8309	4,1780	-17,67%
06-10-09	2,8309	4,1780	-17,67%
07-10-09	2,8309	4,1780	-17,67%

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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