



## POLAND WEEKLY REVIEW

### MACROECONOMICS AND FINANCIAL MARKETS

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#### PREVIEW: The week of December 11<sup>th</sup> to December 17<sup>th</sup>

Indicator	Date of release	Pe-riod	BRE forecast	Consensus	Last	Comment
C/A (EUR)	Dec 11	Oct	+114 mln	-190mln	-57mln	Relative solid exports (-10.8% y/y on good manufacturing performance and overall, global outperformance of exports) and weakness of imports (-21.5% y/y on weak wholesale sales). Other accounts without major surprises.
M3 supply y/y	Dec 14	Nov	8.6%	9.0%	11.8%	PGE IPO effect petered out, return to trend.
CPI inflation y/y	Dec 15	Nov	3.4%	3.3%	3.1%	Period of downward surprises in food prices ended – confirmation in the data from the Czech Rep. We see food prices at 0.8-0.9% m/m and fuels at more than 2%. Core inflation 2.9%.
Employment y/y	Dec 16	Nov	-2.2%	-2.3%	-2.4%	Solid uptrend in business activity indicators. There are some signs of hiring (!) in various manufacturing sections. We expect only a marginal monthly fall of employment at 2k on seasonal factors.
Wages y/y	Dec 16	Nov	3.2%	2.7%	2.0%	Low statistical base effect from the last year. Some bonuses in mining (KGHM) but some postponed till December what lowers considerably the growth of the aggregate.
Producer prices y/y	Dec 17	Nov	2.4%	2.2%	2.0%	Core PPI stable. Minor increases of oil prices and base metals. Firms expecting moderate growth of prices. PMI

						output prices on the rise for the first time in several months.
<b>Industrial output y/y</b>	Dec 17	Nov	<b>6.6%</b>	6.2%	-1.2%	Positive working days effect (+1). Low statistical base from the last year – strong effect. Restocking continues.

## In Focus / Macroeconomics

### The New MPC – further steps closer to the final composition

Nine out of ten member body are to be replaced at the beginning of 2010. Although we are still quite far from the exact personal composition of the new MPC, we are getting closer and closer. Recent developments on this field give a good opportunity to sum up official nominees and the other potential picks. So far, 3 Sejm (the Lower House of the Parliament) candidates have been determined including 2 PO nominees (Bratkowski and Zielińska-Głębocka) and 1 PSL (junior coalition party) candidate (Chojna-Duch). 3 highly likely Senate (the Upper House of the Parliament) candidates are to be Pawłowicz, Winiński and Rzońca. Among 3 presidential candidates will most likely appear Kaźmierczak, Glapiński and Bugaj or Roszkowski. The exact timing of replacements is given in the table below.

Member	Appointed by...	End of tenure
Jan Czekaj	Lower chamber (Sejm)	January 9
Mirosław Pietrewicz	Lower chamber (Sejm)	January 9
Dariusz Filar	President	February 18
Andrzej Sławiński	President	February 18
Andrzej Wojtyna	President	February 18
Stanisław Nieckarz	Lower chamber (Sejm)	February 7
Halina Wasilewska-Trenkner	Upper chamber (Senat)	January 23
Stanisław Owsiak	Upper chamber (Senat)	January 23
Marian Noga	Upper chamber (Senat)	January 23

**Lower chamber candidates (Sejm).** The candidates put through the lower chamber of the parliament have all been announced by now. E. Chojna-Duch (university professor) supported by the Peasants Party, has academic achievements far from economics (law faculty); economic ties can be seen only in her professional career (Deputy Finance Minister), but still fiscal policy is far away from monetary policy. Politically-correct candidate, rather in the dovish camp but not against the EMU accession. On the other hand A. Zielińska-Głębocka (nominee professor) has economic background (professor of economic sciences) and her research focuses on the issues of economic integration (quite narrow specialization as for the MPC member, but seemingly on time – possible another euro enthusiast); rather political candidate (quite unfortunate opinions quoting the exact level of interest rates in H2 2010 at 3.75%). Last but not least, A. Bratkowski (Ph. D.) is probably the best suited candidate with wide economic experience within monetary policy (former NBP vice-governor). His academic interests concentrate on monetary policy and the effects of euro adoption. Possibly the most devoted euro-enthusiast, closely connected with J. Rostowski (co-author of the papers on a unilateral euroization of Poland).

**Upper chamber candidates (Senat).** Only L. Pawłowicz (university professor) has been recently confirmed. Apart from quite wide academic interests (no leading field), he has some experience in business (management boards, supervisory boards). Similar to Zielińska-Głębocka, he is one of Gdańsk liberals (the group associated with the PM Tusk). As for the other candidates, potential picks are A. Rzońca (Ph. D.) and J. Winiński (university professor). The former is known as a close associate of L. Balcerowicz (the same foundation they work for – FOR) and his relatively fast career. Although he may be considered expert, he majors rather in public finance and his academic papers concentrate on this field. As for the latter candidate, J. Winiński is one of the most frequently cited Polish economists in 80' and 90'. However, the glow from the past faded in the course of years. Professor Winiński (although he is advisor at West LB) does not participate actively in public debate on the conduct of monetary policy (nor he is frequently cited by the press) although he declares himself monetarist.

**Presidential candidates.** As for those prospective MPC members, only A. Kaźmierczak (nominee professor), professor at the Warsaw School of Economics, has been officially confirmed. He may be regarded as a declared dove. Although in some circles he is perceived as an expert in monetary policy field, the textbooks he writes are conceptually still in 70ties. Another candidate is also deeply rooted in Warsaw School of Economics. A. Glapiński (university professor) focuses his academic research on the history of economic ideas, closely connected to Schumpeterian

development theory. He is known as being closely connected with Kaczyński brothers. Summing up: competences loosely connected with monetary economics, loyal supporter of Law and Justice policy. The pick of the third presidential MPC member is likely to come from R. Bugaj (Ph. D.) or W. Roszkowski (nominee professor): both intellectuals, although the former more politician than economist whereas the latter more historian. Presidential camp (along with the contemporary governor Skrzypek) is adversary to the other members in terms of euro adoption.

The most likely MPC composition, as highlighted above, indicates there is a good chance that the absolute majority (including one PSL candidate) will see the euro adoption as a top priority in the years ahead. Such a change of the strategic monetary policy goal will probably not impact the MPC's decisions in the next few months. In fact, we even expect the rate hike expectations to subside on the back of falling inflation (see the massive base effects from 2009).

As the euro adoption is the strategic goal of the Polish government and the MPC seems to be responsible for its partial implementation (see the need to meet the inflation convergence criterion), we may well expect the monetary policy to be more restrictive in the mid-term. On balance, we see the NBP rates to rise to 4% by the end of 2010 and by at least 100bp in 2010.

### MID-TERM FORECASTS

Indicator	2007	2008	2009	2010	2011
GDP y/y (%)	6.5	4.8	1.7	3.0	4.5
Inflation rate (% average)	2.4	4.3	3.5	2.3	2.9
Current account (% of GDP, average)	-4.5	-5.3	-1.2	-2.9	-3.7
Unemployment rate (end-of-year)	11.4	9.5	12.0	12.5	10.5
NBP repo rate (end-of-year)	5.00	5.00	3.50	4.00	5.50

Indicator	2009				2010	
	Q1	Q2	Q3	Q4	Q1	Q2
GDP y/y (%)	0.8	1.1	1.7	3.2	3.2	2.9
Inflation rate (% average)	3.2	3.7	3.5	3.5	3.3	2.1
NBP repo rate (end-of-quarter)	3.75	3.50	3.50	3.50	3.50	3.50

*Bold denotes changes from the last release with arrows showing the direction of changes*

## Fixed Income

NFP, Greece, Spain ...  
Poland

Last week, we finally saw a little bit of volatility. Friday, surprise reading in NFP triggered significant move in EURPLN which, however, was not accompanied by rally on bonds. Actually, after successful 2y and 5y combo auction prices started to go south. After the downgrades of Greece and Spain sell-off continued to mount. Lowest prices were seen after (we must admit successful) road bonds auction. WS0922 lost 100 cents in one week, and spread between 2y and 10y bonds widen some 10bp in yield. Our view remains unchanged, we are still believing in two things. First is differentiating trade, local fundamentals are sound, economy seems to be very balanced with main concern being the fiscal side. We have underlined several times that Ministry of Finance is coming up with many alternative emergency strategies, building up liquidity pillow, sticking to conservative budget assumptions, postponing tax refunds to 2012 etc. They haven't touched the fiscal reform per se, but with political calendar we must give them some credit. However, there are rumors that some elements of the fiscal reform are likely to be announced in the coming week, which will be a support for the differentiating trades among fiscal problems noted within EMU periphery. Second thing is the CPI and our view of how fast and how low it can get after December reading (see our research about statistical base effects that will bring CPI close to lower band of NBP target). Said this we stick to our strategy of holding 2y2y forward IRS (currently at 6.15, same level when we opened it, but we are slightly better off with carry on that trade). We also used this sell-off to load some long dated bonds. Finally, we start to think about warmly off-the-run 20y bond with entry level at 6.35 in yield.

### TRADE IDEAS:

Stay receive in 2y2y, buy long bonds with yield 6.35%

### 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	1/4/2010	-	4.223%	10/26/2009
2Y T-bond OK0712	1/6/2010	-	5.099%	12/2/2009
5Y T-bond PS0415	1/13/2010	-	5.736%	12/2/2009
10Y T-bond DS1019	1/13/2010	-	6.340%	5/20/2009
20Y T-bond WS0429	1/13/2010	-	6.300%	9/23/2009

## Money Market

*Another cheap week during this reserve requirement period*

*Significant demand on 3M repo*

### TRADE IDEAS:

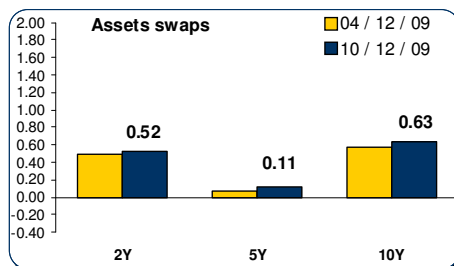
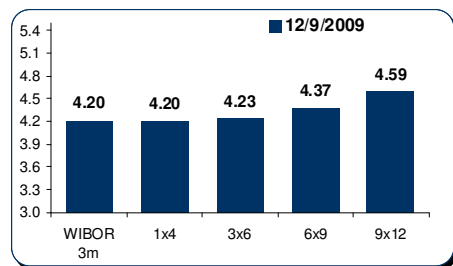
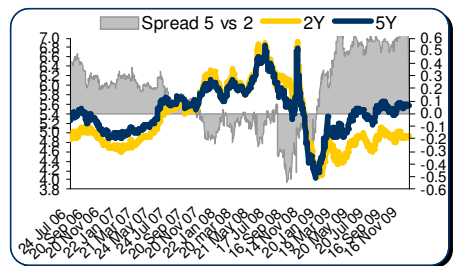
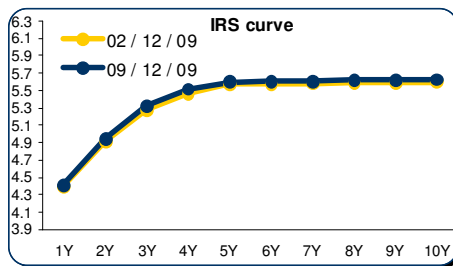
### **FIXED INCOME & MONEY MARKET CHARTS**

It was another cheap week during this reserve requirement period. Last Friday banks bought 51.3 bln PLN NBP bills from 57 bln PLN offer. We can expect same behavior on tomorrow's tender and the short-term rates should be low till the end of December.

Coming year end causes increase in WIBOR rates as usual. 1M WIBOR increased from the beginning of December by 8 bps.

Despite the fact that there are huge cash surpluses in the system there was significant demand on 3M repo on Tuesday. NBP accepted almost 3,5 bln PLN in comparison to 750 million maturing.

Offer 1Y OIS POLONIA



## Foreign Exchange

*Zloty bumpy ride*

*Implied Volatility mixed*

The eruption of optimism, after last Friday's job data from USA, was strong enough to brake the very strong technical support at 4.0650 to EUR/PLN. On the waves of the stop loss selling of the hard currency, the Zloty touched 4.0370 (7days Low). But later the Ben Bernake testimony, German production figures and the downgrade of Greece have hit hard the global sentiment again, and the EUR/PLN briefly reached the 4.1750 (7days High). We still view EUR/PLN in the wide range 4.0350/4.2350.

As usually, the implied volatility was mimicking the moves of spot. As the consequence the volatility curve was better offered, then bid in panic (2mth EUR/PLN paid at 14.50), only to end offered again (1mth sold 13.25). The risk reversals were dancing to the same tune.

**TRADE IDEAS:**

**SPOT**

Main supports / resistances:  
 EUR/PLN: 4.0350 / 4.2250  
 USD/PLN: 2.6500 / 2.9000

*Stay aside*

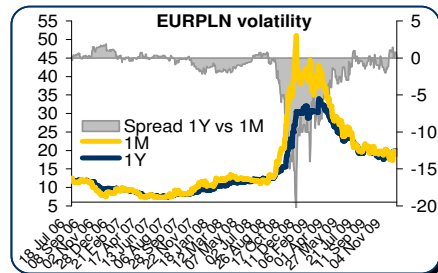
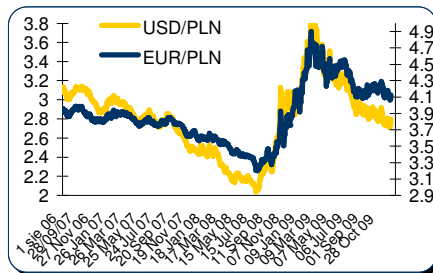
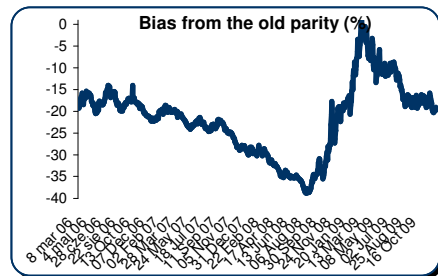
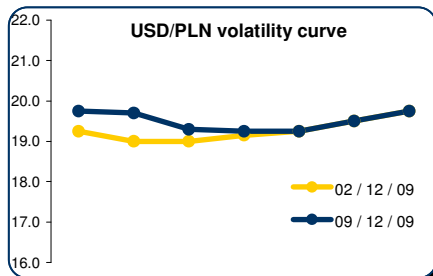
The false break of the (supposed to be a pivotal) 4.0650 level, made us a little bit more cautious about further Zloty perspectives. We still keep to our mid/ longer term Zloty positive scenario, mainly due to good fundamentals. This said, we would stay aside at the moment or resell EUR/PLN at 4.24/4.27 area with the stop loss at 4.3200.

**OPTIONS**

*Keep short Vega*

The historic volatilities are well below the implied volatility, especially in the front end. That is supporting our view of keeping the short Vega positions. Due to high correlation between the spot and volatility we tend to keep long Vanna position.

**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
03/12/09	4.08%	4.19%	4.22%	4.20%	4.39%	4.38%
04/12/09	4.06%	4.20%	4.21%	4.20%	4.39%	6.59%
07/12/09	4.11%	4.20%	4.20%	6.49%	4.34%	4.38%
08/12/09	4.10%	4.20%	4.23%	4.20%	4.40%	4.38%
09/12/09	4.12%	4.20%	4.20%	4.20%	4.38%	4.38%

**FRA MARKET RATES**

## FRA Market Rates (Closing mid-market levels)

date	1X4	3X6	6X9	9X12	6X12
03/12/09	4.23%	4.24%	4.36%	4.58%	4.55%
04/12/09	4.23%	4.23%	4.37%	4.56%	4.54%
07/12/09	4.20%	4.24%	4.38%	4.58%	4.54%
08/12/09	4.21%	4.23%	4.36%	4.58%	4.50%
09/12/09	4.24%	4.22%	4.38%	4.58%	4.55%

**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
03/12/09	4.38%	4.17%	4.91%	4.88%	5.56%	5.62%	5.59%	6.15%
04/12/09	6.59%	4.17%	4.91%	4.90%	5.56%	5.63%	5.60%	6.17%
07/12/09	4.38%	4.17%	4.92%	4.88%	5.57%	5.64%	5.60%	6.19%
08/12/09	4.38%	4.17%	4.93%	4.89%	5.57%	5.64%	5.61%	6.22%
09/12/09	4.38%	4.17%	4.95%	4.93%	5.60%	5.71%	5.63%	6.26%

**PRIMARY MARKET RATES**

## Last Primary Market Rates

	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	09/10/26	10/10/26	95.905	4.22%	500	1758	431
OK0712	09/12/02	12/07/25	87.692	5.10%	5000	5472	1440
PS0414	09/12/02	15/04/25	98.691	5.78%	5000	5614	3629
DS1017	09/04/08	19/10/25	94.460	6.22%	2500	4846	1820

**FX VOLATILITY**

date	USD/PLN 0-delta stradle				25-delta RR		25-delta FLY	
	1M	3M	6M	1Y	1M	1Y	1M	1Y
03/12/09	19.00	19.25	19.25	19.75	3.25	4.50	0.80	0.85
04/12/09	19.00	19.25	19.25	19.75	3.25	4.50	0.80	0.85
07/12/09	19.00	19.25	19.25	19.75	3.25	4.50	0.80	0.85
08/12/09	19.00	19.25	19.25	19.75	3.25	4.50	0.80	0.85
09/12/09	19.70	19.25	19.25	19.75	3.25	4.50	0.80	0.85

**PLN SPOT PERFORMANCE**

## PLN spot performance

date	USD/PLN	EUR/PLN	bias
03/12/09	2.7093	4.0954	-19.71%
04/12/09	2.7166	4.0946	-20.01%
07/12/09	2.7479	4.0660	-19.68%
08/12/09	2.7435	4.0725	-19.77%
09/12/09	2.7966	4.1266	-19.03%

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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