



POLAND WEEKLY REVIEW

MACROECONOMICS AND FINANCIAL MARKETS

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PREVIEW: The week of April 9th 2010 to April 15th 2010

Indicator	Date of release	Pe-riod	BRE forecast	Consensus	Last	Comment
C/A balance EUR	Apr 13	Feb	+229mln	-237mln	-710mln	Trade balance near zero (very positive developments in industrial output and wholesale trade). Significant inflow from UE (EUR 1.5bn in current transfers).
M3 Supply y/y	Apr 14	Mar	4.9%	5.0%	5.1%	In trend.
CPI inflation y/y	Apr 15	Mar	2.6%	2.6%	2.9%	Food prices +0.7% m/m, fuels +2.7% m/m. Inflation falling on base effects from 2009. Core inflation at 2.0% (vs 2.2% in previous month).

In Focus / Macroeconomics

2009 NBP profit. Further highlights on arguments within MPC.

Conflict within MPC escalated recently so much that rate-setter Bratkowski declared he will submit his resignation if the government reaches agreement with NBP board, discrediting thereby all resolutions taken by sovereign MPC. Bratkowski stresses that such a solution would be against the law and would violate the constitutional MPC independence. Although Rzonca has recently tried to ease the mounting tension a bit, suggesting there was no violation yet, as NBP board has still some time to execute MPC resolution, Kazmierczak (staying side by side with NBP board) puts the conflict on a knife edge claiming the whole story may find its end in the constitutional court. So far we look forward to a solution (or a hint for the one) on April 12, but regardless of the outcome, the whole mess bears at least two important implications: first connected with fiscal issues and the second with the conduct of monetary policy.

Although the ongoing arguments does not explicitly involve government, MPC members more or less bluntly suggest they are not indifferent to 2010 budget issues (with Winiecki at the fore). That is why, the whole story attracts financial markets' attention to budget issues (with naturally arising question: is it really so bad the PLN 4bn make such a difference to compromise central bank independence?).

The second implication stems from a very interesting observation made in an article by former MPC member Czekaj. He claims that "it is unlikely that the ongoing transformation of doves into hawks and vice versa results from fundamental change of economic views...". Rather we should perceive it through "the willingness of those MPC members to meet expectations of their political promoters". Such a state of affairs naturally shovels the problems of current monetary policy into the background – what apparently must have been seen during the last conference during which, apart from the statement, all (to be honest quite emotional) speeches of MPC members were concentrated on the NBP's profits. It raises concerns whether the MPC would be able to act promptly on rising inflationary pressures (former two MPCs tracked the momentum of prices in quite timely manner).

In such circumstances we expect the period of low interest rates to be prolonged (the view will be given additional support by the falling inflation). However, we should be aware of risk of pricing in the behind-of-the-curve scenario in which MPC will have to implement more painful and time-dense hikes in, say, 2011. Such a scenario may result in FRA curve steepening and rising FRA spreads. Will the conflict affect EURPLN stability? Rather not. Investors are ignoring the political risk in Poland and do not perceive the conflict within NBP as a risk for the whole financial system. Polish assets are still popular and the underlying flows are gradually appreciating PLN.

MID-TERM FORECATS

Indicator	2007	2008	2009	2010	2011
GDP y/y (%)	6.5	4.8	1.7	3+	4.5
Inflation rate (% , average)	2.4	4.3	3.5	2.3	2.9
Current account (% of GDP, average)	-4.5	-5.3	-1.6↓	-2.7↓	-3.7
Unemployment rate (end-of-year)	11.4	9.5	11.9	12.1	10.9
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	3.1	2.6-2.8	3.3
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

Last week we had quite interesting week on the FI market. Despite "holiday season" market was pretty active and we had seen important levels on the IRS curve. 2y IRS traded at this year's low, touching 4.50 level pricing less than 75bp tightening in the cycle. 5y followed and they traded at

Not really "holiday season"

5.11 as the low. Curve has steepened in 5y10y sector to 25 bp. In our opinion the most significant events were impressive move down in 3M Wibor rates (currently standing at 4.00 down some 30bp from the beginning of the year and 15bp in one month time) and the 2y bond auction (which for the first time in a while showed that demand at this yield levels is starting to be fragile). Slide in 3M triggered some stops in pay positions especially in the 1y1y IRS. Compression in this part of the curve made FRA spread look very cheap, 50bp tightening in 2011 is least one can expect, given even very modest recovery scenario. Investors were keen to pay 2y IRS at around 4.50-55 level. Fuel to the fire as added by rather unsuccessful 2y bond auction (new benchmark OK1012) and then next day we saw sharp move in the yields up. We have to admit that we have taken negative stance towards the market. In our opinion rates are low, risk profile is not favorable. The only good news that can come from the econ side is falling CPI, but that is already known by the market. We may get some dovish comments from MPC members, but the more dovish the MPC, the more behind the curve they will fall giving rise to steeper FRA curve. There are some risk concerning bonds, especially at current yields. We are waiting for stabilization in 3M Wibor rate, but somehow we get a feeling it will be falling not for very much longer. Plus the closer 3M Wibor to NBP repo rate the more reaction we will have when MPC will decide to move.

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	4/12/2010	-	3.929%	4/1/2010
2Y T-bond OK0712	5/5/2010	-	4.541%	4/7/2010
5Y T-bond PS0415	4/21/2010	-	5.736%	12/2/2009
10Y T-bond DS1019	4/14/2010	-	6.103%	2/19/2010
20Y T-bond WS0429	6/16/2010	-	6.170%	9/23/2009

Money Market

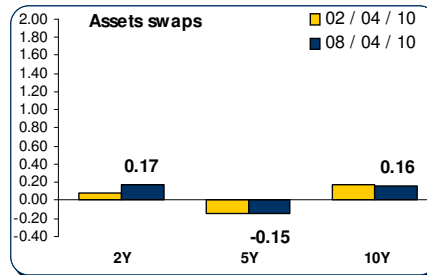
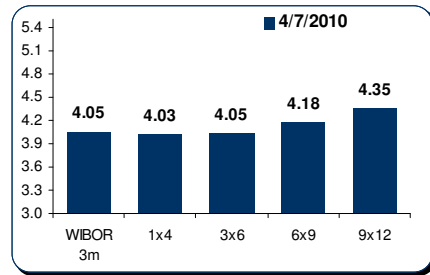
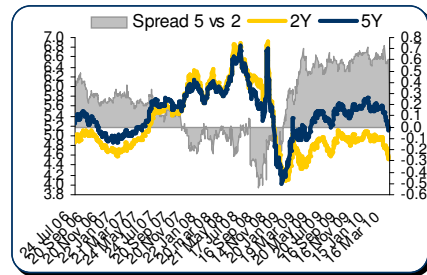
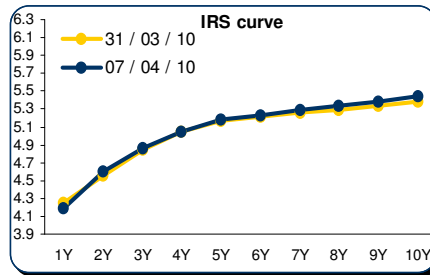
Cheap start of the reserve

Market bought only PLN 70 bn (74 billion was on the offer) of the money bills just before the Easters, creating a PLN 3 billion surplus of the cash in the system. It was enough to keep the ON rates well below 3%. If tomorrow they do the same, we will face a really cheap April.

Strong zloty helps the bulls

Stronger zloty again pushed the yield curves down, and as of now this is the main factor that prevents us from unavoidable correction movement. If it stays like this till the real economy figures release (expectations are quite bullish), the correction will be fatherly postponed. On the other hand the main threat is escalating conflict within the MPC body and the budget deficit issue.

FIXED INCOME & MONEY MARKET CHARTS



Foreign Exchange

Zloty stronger

In the last week polish Zloty has been boxed in extremely tight range, 3.8220-3.8620 for EUR/PLN. We have seen good both-side interest in zloty: the flows into Poland as we have broken the important support at 3.8550 and the interest to lock in profit at that level. Taking into account the global factors (Greece), the zloty is performing really well and we expect that trend to continue even if we cannot exclude the short-term correction to 3.8800 or even 3.9300.

Implied volatility keeps on declining

The historic volatility hit the lowest levels this year. Its partially due to Easter holidays, but the effect was disastrous for short term vols. As an effect the implied volatility curve has become even more steep (spread 1 year versus 1 month has reached 2,5%) as the short term options (gamma) were the most offered on the market. Today (Thursday) the EUR/PLN run is higher due to Greece story but we believe it will be short lived, unless the historic volatility picks up significantly.

Short-term forecasts

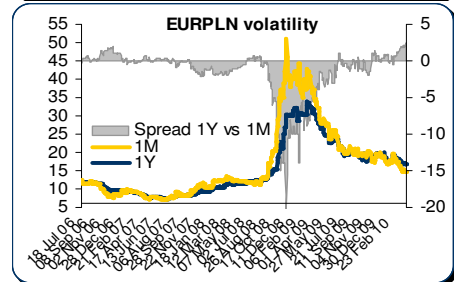
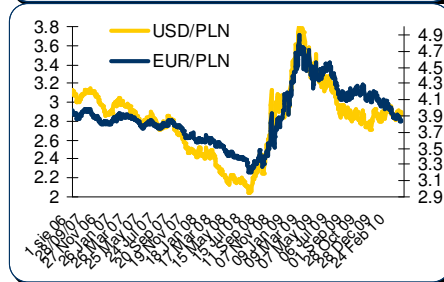
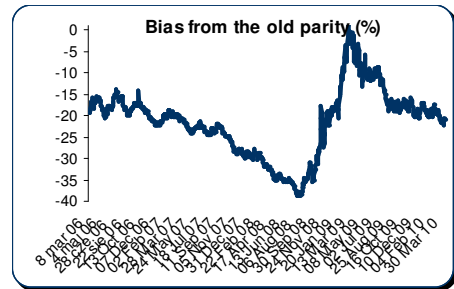
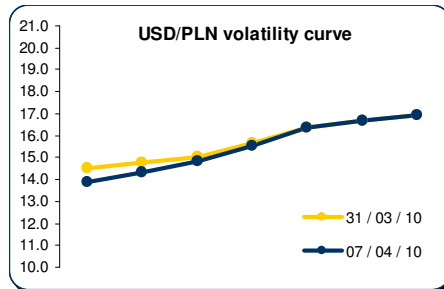
SPOT
 Main supports / resistances:
 EUR/PLN: 3.8000 / 9.9500
 USD/PLN: 2.8000 / 3.9500

IPOs and SPOs scheduled for May and June plus recently published information from Eureco that they had already had hedged their FX exposure (already sold zloty) is strongly supporting Zloty. In case of correction important levels are 3.8800, 3.9300 and then 3.9500.

OPTIONS

The volatility is at historical lows. That is why we may see lower ERU/PLN Vega. The most preferable tenors are from 2 months to 6 months.

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
30/03/10	4.03%	4.12%	4.10%	4.13%	4.30%	4.34%
31/03/10	4.01%	4.10%	4.13%	4.11%	4.33%	6.59%
01/04/10	3.96%	4.05%	4.06%	6.49%	4.23%	4.28%
06/04/10	3.96%	4.05%	4.09%	4.09%	4.28%	4.28%
07/04/10	3.96%	4.05%	4.09%	4.09%	4.28%	4.28%

FRA MARKET RATES

FRA Market Rates (Closing mid-market levels)

date	1X4	3X6	6X9	9X12	6X12
30/03/10	4.14%	4.17%	4.24%	4.47%	4.42%
31/03/10	4.12%	4.15%	4.22%	4.46%	4.39%
01/04/10	4.10%	4.15%	4.22%	4.35%	4.34%
06/04/10	4.05%	4.06%	4.15%	4.31%	4.29%
07/04/10	4.04%	4.06%	4.11%	4.28%	4.26%

FIXED INCOME MARKET RATES

Fixed Income Market Rates (Closing mid-market levels)

date	1Y		2Y		5Y		10Y	
	WIBOR	TB	IRS	OK0709	IRS	PS0511	IRS	DS101
30/03/10	4.34%	3.85%	4.63%	4.41%	5.21%	5.05%	5.42%	5.51%
31/03/10	6.59%	3.78%	4.56%	4.38%	5.17%	5.00%	5.38%	5.52%
01/04/10	4.28%	3.84%	4.53%	4.30%	5.11%	4.97%	5.34%	5.52%
06/04/10	4.28%	3.87%	4.57%	4.32%	5.15%	4.99%	5.40%	5.56%
07/04/10	4.28%	3.87%	4.60%	4.36%	5.18%	5.03%	5.44%	5.60%

PRIMARY MARKET RATES

Last Primary Market Rates

	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	10/03/29	11/03/29	96.179	3.93%	1000	2637	1000
OK0712	10/04/07	12/07/25	89.301	4.54%	3000	6726	2999
PS0415	09/12/02	15/04/25	98.691	5.78%	5000	5614	3629
DS1019	10/02/19	19/04/25	95.629	6.10%	2000	5570	2000

FX VOLATILITY

date	USD/PLN 0-delta stradle				25-delta RR		25-delta FLY	
	1M	3M	6M	1Y	1M	1Y	1M	1Y
30/03/10	14.50	15.65	16.35	16.95	2.25	3.75	0.50	0.80
31/03/10	14.50	15.65	16.35	16.95	2.25	3.75	0.50	0.80
01/04/10	14.30	15.55	16.35	16.95	2.25	3.75	0.50	0.80
06/04/10	14.00	15.30	16.20	16.95	2.25	3.75	0.50	0.80
07/04/10	14.10	15.20	15.90	16.95	2.25	3.75	0.50	0.80

PLN SPOT PERFORMANCE

PLN spot performance

date	USD/PLN	EUR/PLN	bias
30/03/10	2.8748	3.8765	-22.11%
31/03/10	2.8720	3.8622	-21.83%
01/04/10	2.8506	3.8467	-21.17%
06/04/10	2.8618	3.8356	-20.95%
07/04/10	2.8675	3.8378	-20.99%

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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