



## POLAND WEEKLY REVIEW

### MACROECONOMICS AND FINANCIAL MARKETS

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#### PREVIEW: The week of October 1<sup>st</sup> 2010 to October 7<sup>th</sup> 2010

Indicator	Date of release	Pe-riod	BRE forecast	Consen-sus	Last	Comment
PMI Index	Oct 1	Sep	52.8	53.0	53.8	Lately we observe a consolidation on this indicator with a tendency to mean-revert after spikes.
FinMin's inflation forecast	Oct 1	Sep	2.4-2.5%	2.3%	2.0%	The main risk is stemming from food prices, especially prices of wheat and vegetables. Core inflation likely to retreat towards 1.1% y/y.

## In Focus / Macroeconomics

### Rates on hold

After the very long meeting (the decision was announced at 3.20 PM...1.5h later than usual) the MPC left the rates unchanged at the yesterday's meeting, matching market expectations. We will never know whether this fact is relevant (reflecting the lively discussion) or stems simply from technical reasons.

The statements seems softer than the last one (followed by more hawkish "Minutes"). It seems the hawks were spooked by a reversion of inflation expectations...Turning to details, the assessment of Polish economy state was somewhat less upbeat. Parallel to solid growth of industrial output, the statement mentions soft credit growth along with worse business activity indicators (concerning consumers and enterprises as well). The lines regarding discussion on inflation were also softened. MPC members acknowledged limited inflationary pressures, and the discussion regarding the future was lead along the lines of only possible inflationary pressures (not simply inflationary pressures, as written in August statement). We did not find any link to the zloty exchange rate what makes us think it is the not relevant issue right now.

Although the statement does not indicate there was any motion regarding rate hikes, we cannot exclude such a possibility (we will know as soon as "Minutes" are published). However, Wednesday's meeting reduces chances for leading and more aggressive rate hike. The incoming data should support chances for somewhat higher rates this year, along with the risk that there is a serious communication problem between MPC and the market (is the difference between the statement and the ensuing "Minutes" likely to be happen again?). There is growing possibility that the current MPC behaves alike the previous body (dependence on current data, bias towards supporting the real sphere) and rate hikes will take place in the environment of much higher inflation (headline and the core).

### MID-TERM FORECATS

Indicator	2007	2008	2009	2010	2011
GDP y/y (%)	6.5	4.8	1.7	3.6	4.2
Inflation rate (% , average)	2.4	4.3	3.5	2.8	3.5
Current account (% of GDP, average)	-4.5	-5.3	-1.6	-1.8	-2.9
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	<b>3.75↓</b>	4.50

Indicator	2009		2010			
	Q3	Q4	Q1	Q2	Q3	Q4
GDP y/y (%)	1.7	3.1	3.0	3.5	4.0	4.1
Inflation rate (% , average)	3.5	3.3	3.0	2.1	2.6	2.8
NBP repo rate (end-of-quarter)	3.50	3.50	3.50	3.5	3.5	<b>3.75↓</b>

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

## Fixed Income

### Long meeting without any outcome.

The main issue that dominated the last week trading mood became a quite surprising failure. As the market was speculating on a preemptive 50BP rate hike, the longer than ever this year lasting RPP meeting turned out not to give any satisfaction to both traders and analysts. The very mysterious discussion had its finish at nearly 5.20 pm without any change in monetary policy. The market disappointment and slightly dovish conference moved the yield curve about 10bp down in a short end and about 5-7bp in the longer-end sector (3x6S FRA down to 4.12 from 4.22 and both 5Y and 10Y down to 4.87 from 4.92).

It's quite hard to estimate whether the market would be too eager again to reenter the paying positions in a short-end before the October's meeting but it couldn't be ruled out definitely. It would be really dependent on how much risk was likely to be taken off the short FRAs in a meantime. At the same time the market would be more willing to enter the steepeners again after losing confidence to the possible scope or of a rate hikes this year, especially when the curve became too flat on September's 50BP rate hike (2Y5Y down to 24 points and 5Y10Y even 2 points negative). The outrageous state deficit debt at over 8% of GDP might definitely help in

making decision.

**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	10/4/2010	-	3.918%	9/27/2010
2Y T-bond OK1012	10/6/2010	-	4.672%	9/1/2010
5Y T-bond PS0415	10/13/2010	-	5.431%	9/6/2010
10Y T-bond DS1020	10/20/2010	-	5.456%	9/15/2010
20Y T-bond WS0429	10/20/2010	-	6.170%	9/15/2010

**Money Market**

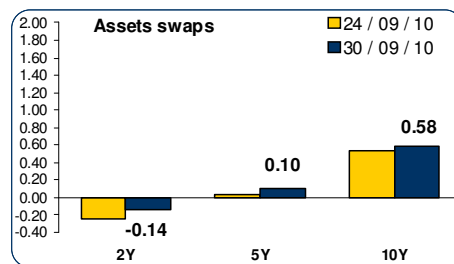
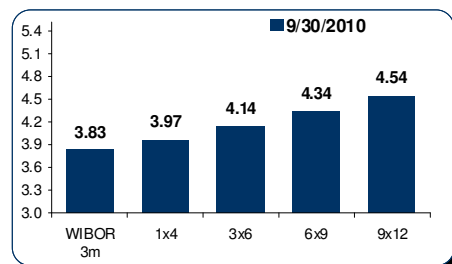
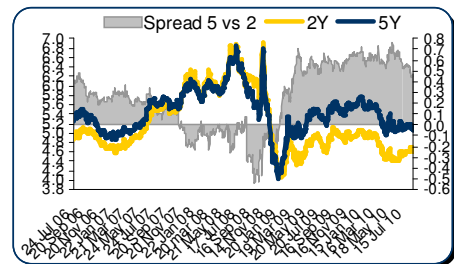
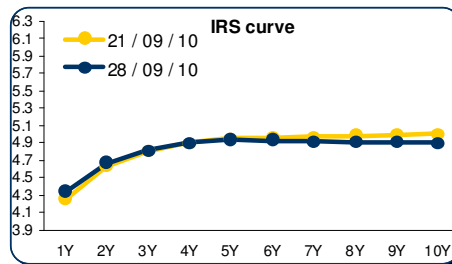
*Very cheap end of the reserve*

*The MPC did not surprise the market*

Very cheap end of the reserve requirement settlement period with the deposit in the central bank reaching PLN 10 billion. Starting from today's situation will get back to normal (at least for some time), and the cost of carry will be seen nearby 3%.

The highlight of the week was the MPC meeting. Although the great majority of the market was not expecting the hike, some players were, betting on it as the risk reward trade-off was highly asymmetric in case of the change. The probability of this scenario was growing parallel to the delay in the decision announcement. So were the IR derivatives prices. Ultimately the majority was right, and the MM curve dropped 5-10 bps discounting consensus for the hike, which now is 25 bps in October. This scenario has no value though.

**FIXED INCOME & MONEY MARKET CHARTS**



**Foreign Exchange**

*Zloty weaker*

Zloty has extended losses. Three week's series of higher bottoms (3.93, 3.9450, 3.96) traded hand in hand with higher tops (3.9650, 3.9830, 3.9950) has been forming into short-term uptrend channel. What was behind this week's top (3.9950) and overall weaker Zloty? Higher yields of European debt and lack of September's PLN rate hike simply has translated into market story: close and wait for better levels to reenter. Correlation with usual benchmarks (DJI, EURJPY, EURUSD) still calculates low values, while with CE3 region is closer to 1.0.

*Volatility curve untouched*

Slightly weaker PLN and low realized volatility - this is present implied vols environment. Such combination has not affected run, ATM has been traded at same levels: 1M at 10.4, 3M at 11.0, 1Y at 12.05. Smile (3M 25D RR) and currency spread (USDPLN vs EURPLN) has also stayed at

same levels, respectively 3.0 and 6.75%. We add another low value to low values weekly realized series: 6%, 5%, 6%, 6.8% and 6.9% for this week.

**Short-term forecasts:**

SPOT

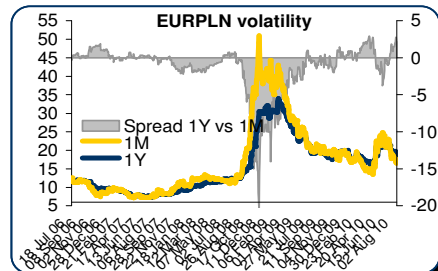
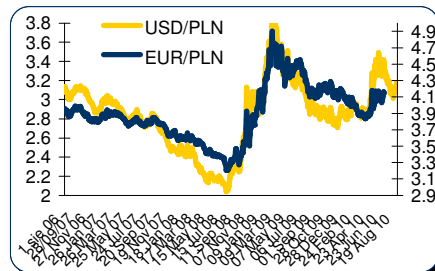
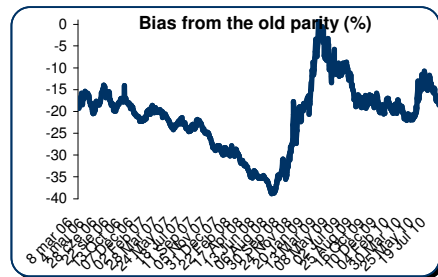
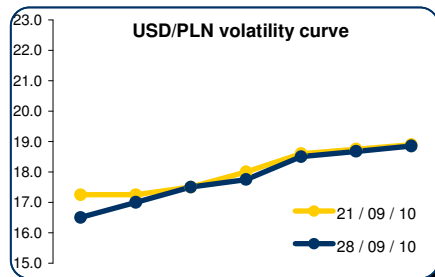
Main supports / resistances:  
 EUR/PLN: 3.9000 / 4.0500  
 USD/PLN: 2.9800. / 3.1500

Low dynamics of upward move has not changed our medium term view. Minor resistance is at 3.9970/4.000, stronger one at 4.03/05 and the support at 3.90 seems a good place to stop any PLN appreciation (at least short term).

OPTIONS

Despite weaker PLN and higher implied vols, realized volatility is on our side. We maintain our view the gamma is poised to go down.

**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
24/09/10	3.53%	3.83%	3.95%	3.93%	4.20%	4.15%
27/09/10	3.69%	3.83%	3.83%	3.94%	4.20%	6.59%
28/09/10	3.70%	3.83%	3.83%	6.49%	4.16%	4.15%
29/09/10	3.70%	3.83%	3.93%	3.94%	4.15%	4.16%
30/09/10	3.69%	3.83%	3.93%	3.94%	4.15%	4.16%

**FRA MARKET RATES**

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

date	1X4	3X6	6X9	9X12	6X12
	24/09/10	3.90%	4.09%	4.33%	4.52%
27/09/10	3.90%	4.14%	4.31%	4.51%	4.49%
28/09/10	3.99%	4.19%	4.38%	4.58%	4.53%
29/09/10	3.98%	4.22%	4.41%	4.62%	4.55%
30/09/10	3.98%	4.22%	4.42%	4.63%	4.59%

**FIXED INCOME MARKET RATES**

## Fixed Income Market Rates (Closing mid-market levels)

date	1Y		2Y		5Y		10Y	
	WIBOR	TB	IRS	OK0112	IRS	PS0511	IRS	DS1017
24/09/10	4.15%	3.98%	4.68%	4.43%	4.93%	4.96%	4.91%	5.44%
27/09/10	6.59%	3.97%	4.68%	4.44%	4.94%	4.96%	4.93%	5.45%
28/09/10	4.15%	3.98%	4.66%	4.45%	4.93%	4.95%	4.90%	5.44%
29/09/10	4.16%	3.96%	4.59%	4.45%	4.85%	4.95%	4.86%	5.44%
30/09/10	4.16%	3.96%	4.59%	4.45%	4.85%	4.95%	4.86%	5.44%

**PRIMARY MARKET RATES**

## Last Primary Market Rates

	au. date	maturity	avg price	avg yield	supply	demand	sold
52W TB	10/09/27	11/09/27	96.189	3.92%	600	1150	580
OK1012	10/09/01	12/10/24	90.670	4.67%	4000	6603	4000
PS0415	10/08/08	15/04/25	101.123	5.21%	3000	7500	3000
DS1019	10/06/16	19/04/25	95.807	5.79%	3000	2965	2430

**FX VOLATILITY**

date	USD/PLN 0-delta straddle				25-delta RR		25-delta FLY	
	1M	3M	6M	1Y	1M	1Y	1M	1Y
24/09/10	17.00	18.00	18.50	18.75	3.75	5.05	0.75	0.90
27/09/10	16.75	17.75	18.40	18.75	3.75	5.05	0.75	0.90
28/09/10	17.00	17.75	18.50	18.85	3.55	5.05	0.75	0.90
29/09/10	16.75	17.50	18.40	18.75	3.50	4.90	0.75	0.90
30/09/10	17.00	17.75	18.50	18.85	3.50	4.90	0.75	0.90

**PLN SPOT PERFORMANCE**

## PLN spot performance

date	USD/PLN	EUR/PLN	bias
24/09/10	2.9704	3.9747	-18.21%
27/09/10	2.9425	3.9582	-18.23%
28/09/10	2.9645	3.9773	-18.72%
29/09/10	2.9227	3.9710	-18.99%
30/09/10	2.9250	3.9870	-18.81%

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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