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Polish data to watch: September 26 to September 30

Publication	Date	Period	BRE	Consensus	Prior
C/A balance (EUR bn)	29.09	Q2			-3.4
NBP inflation expectations (%)	30.09	Sep			4.2

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Last yield (%)	Prev auction
52-week T-Bills	10/3/2011	600	4.578	5/30/2011
2Y T-bond OK0114	10/12/2011	3000	4.469	8/10/2011
5Y T-bond PS0416	10/19/2011	3000	5.256	8/10/2011
10Y T-bond DS1021	10/19/2011	3000	5.803	7/21/2011
20Y T-bond WS0429	9/22/2011	250	6.246	1/12/2011

Macroeconomic forecasts

Wskaźnik	2008	2009	2010	2011 F	2012 F
GDP y/y (%)	4.8	1.7	3.8	3.8	3.2
CPI Inflation y/y (average %)	4.3	3.5	2.8	4.3	3.1
Current account (%GDP)	-5.3	-1.6	-4.5	-4.9	-4.3
Unemployment rate (end of period %)	9.5	11.9	12.3	11.9	11.5
Repo rate (end of period %)	5.00	3.5	3.5	4.5	4

	2010 Q3	2010 Q4	2011 Q1	2011 Q2	2011 Q3 F	2011 Q4 F
GDP y/y (%)	4.2	4.5	4.4	4.3	3.7	3.7
CPI Inflation y/y (average %)	2.6	2.9	3.7	4.2	4.2	4.2
Repo rate (end of period %)	3.5	3.5	4	4.5	4.5	4.5

F - forecast

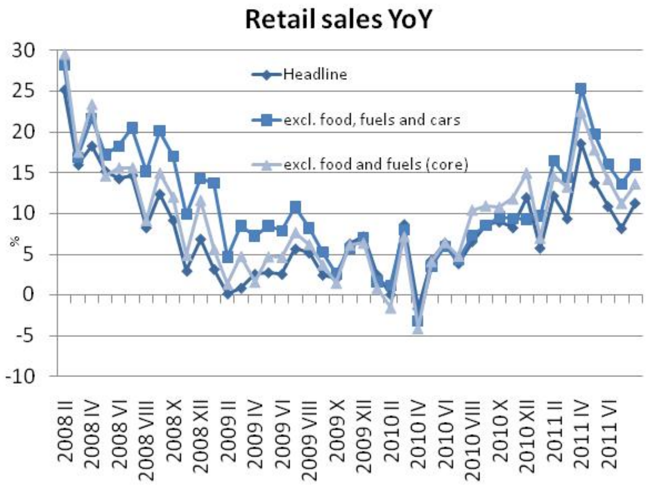
Economics

Industrial production surprised positively, so did retail sales

Industrial production growth increased to 8.1% in August from 1.8% in July; in seasonally adjusted terms output increased by 5.4% against 4.6% in July. Manufacturing still seems to be driven by export sections (two-digit growth): metal processing, electrical equipment, furniture. This contrasts with continously decelerating German economy. As we do not believe in decoupling hypothesis (the correlation between Polish and German exports is stubbornly strong) and construction output was also on weaker side (so the hypothesis of very robust investment also does not seem to be fully sensible), we would like to treat industrial output reading as an odd one out in falling trend. Such a reasoning finds confirmation also in the latest data on producer prices.

Producer prices accelerated in August to 6.6% from 5.9% in previous month (this time there was no backward-looking correction). On monthly basis the growth rate of manufacturing prices accelerated to 0.5%. Although we usually do not elaborate on the raw forecasts from models we use, this time it is worth to note that 0.5% was even lower reading than the lower ranger of model forecasts (0.6-1.1%). Why is it important? Becasuse in times of rapid PLN depreciation the models used to understate the actual growth of producer prices, and this time was the other way round. That is why we think that other factors may have gained on importance: competition among enterprises on shallow local market (and this would confirm the situation in real sphere is actually worse than posted by raw data) and wider margins of exporterts (generated by weaker PLN) which may have been partially shared with local buyers.

Retails sales in August also surprised positively: 11.3% y/y against 8.2% in July. However, we are far from giving ”all clear” signal. We would rather stress that better data is a correction of previous 3 months of consecutive drops (in the history of retail sales there was no single series of 4 consecutive drops on annual basis). Going into more dailed analysis, food sales rose by 4.4% y/y (-0.1% m/m, slightly over seasonal pattern), there was a significant rise of fuel sales (+17.1% YoY - seemingly the reduction of price generated the desired, positive volume effect) and car sales (+4.2% y/y); unexpectedly ”others” category shot up after recent drops, rising by 6.5% m/m. Expected corrections happened in clothing/footwear sales and radio/furniture/household appliances (respectively 9.1% MoM and 1.2% MoM). Stripping categoies with „odd” and unexpeted growth (car sales, fuels, ”other”) we end up around 6%. Therefore we sustain our forecast that private consumption will slow down during forthcoming months because of negative sentiment connected with indebtedness in euro area, uncertainty in labor market (see recent weak data) and still lethal CHFPLN and EURPLN exchange rate.

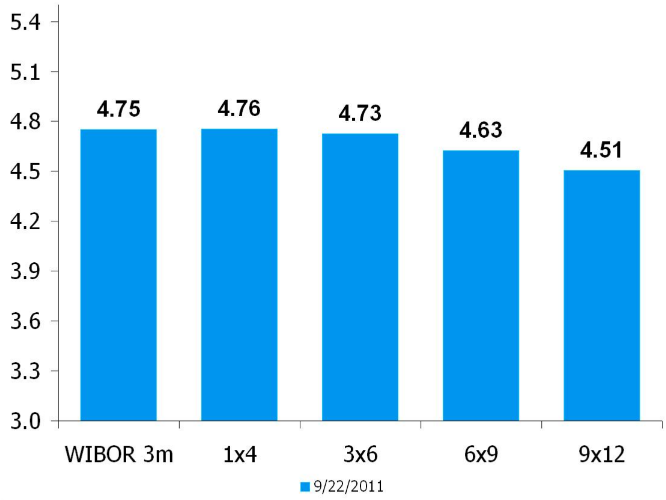


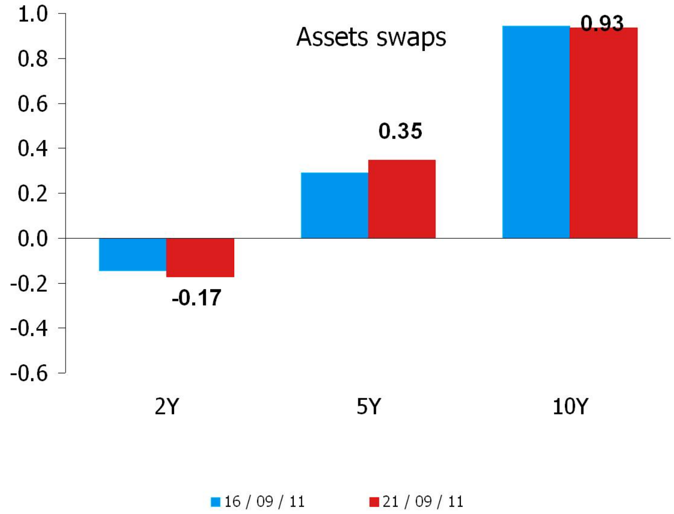
Recently published „Minutes” from September MPC meeting confirm that although MPC is far from admitting there is a slowdown in the Polish economy, it is the reasoning they are unlikely to follow in the future given the mentioned uncertainties and risks for real sphere. Therefore recent bunch of ”better” data may be a good breather for MPC, which does not want to act fast in order to support the zloty, but nothing more. Altough we think that the data are going to turn into worse in coming months (real sphere), weaker zloty and elevaten inflation are also going to keep MPC in check. Window of opportunity for cuts will open at the start of the year should base effects will be sufficient to bring inflation at least somewhat down, and end-year MF/BGK actions aimed at supporting the zloty prove succesfull; by then also the weaker GDP data will be at MPCs disposal and we think that it would ultimately tip the scale.

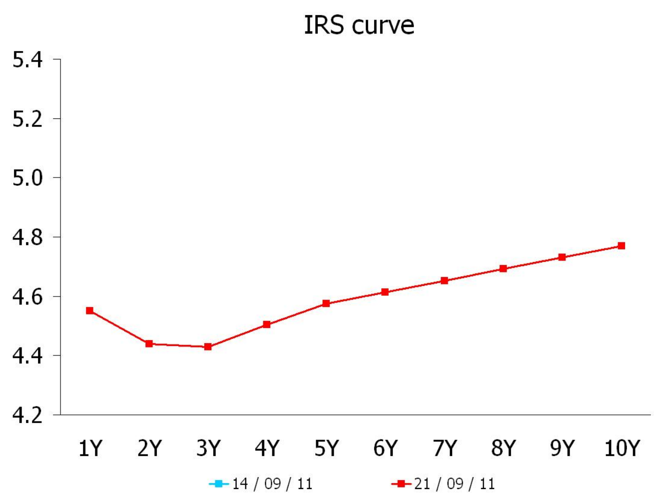
Fixed income

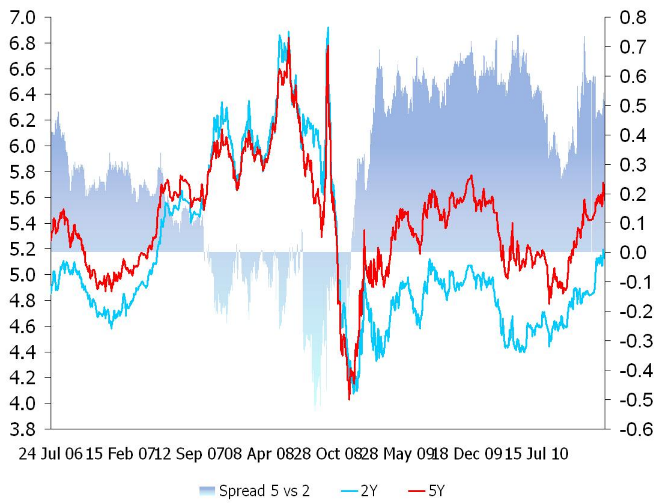
Opening followed by further sell-off...

Almost each day last week looked the same - weak opening followed by further sell-off, with long end suffering the most. Front end of the curve moved up by some 15bp, 5y and 10y 25bp. Also bonds in 5y+ sector lost 25-30bp. Steepening of the curve also caused 5y5y spread over Euro to widen to 245bp, level not observed since 2006. All macro data published this week surprised on the upside - CPI at 4.3% y/y versus 4.1% expected industrial output 8.1% vs. 3.8%, retail sales 11.3% vs. 8.9%. Comments from MPC members were all in quite hawkish tone, reiterating that economy doesn't show clear signals of slowing down, yet inflation remains elevated, therefore definitely not a situation that would justify any policy easing in the nearest future. As market had been very optimistic about rate cuts, some repricing happened. Now rates are seen flat till end of year with some chances for a cut in the first half on 2012 (3x6 FRA trades just few bp below spot Wibor, 9x12 20bp lower). Also 1y1y forward doesn't price in much easing in the upcoming cycle. From that perspective current levels start to look attractive to receive - even with recent PLN weakness rate hikes are definitely out of the question, and leading indicators suggest that macroeconomic outlook will deteriorate in the near future. Nevertheless there is much more value in the long end that there is in the front. Negative global sentiment that puts pressure on zloty and POLGBs will finally start to fade and some bull flattening move should start from current levels.







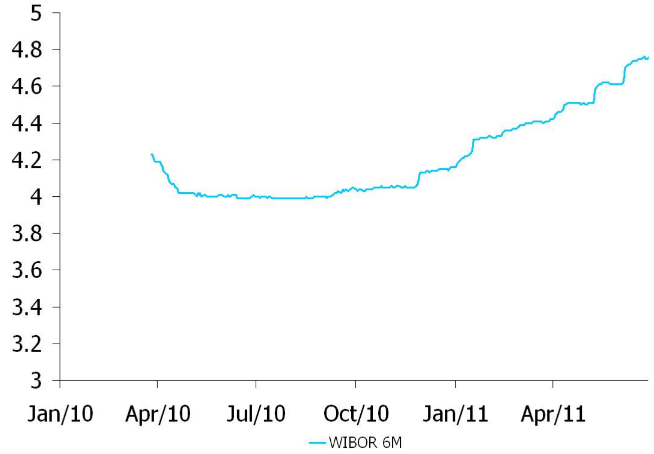


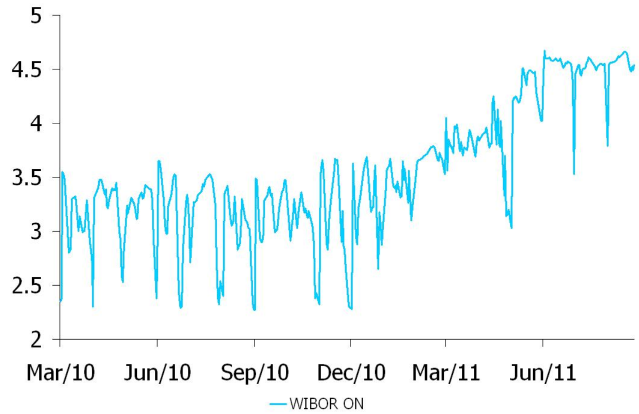
Money market

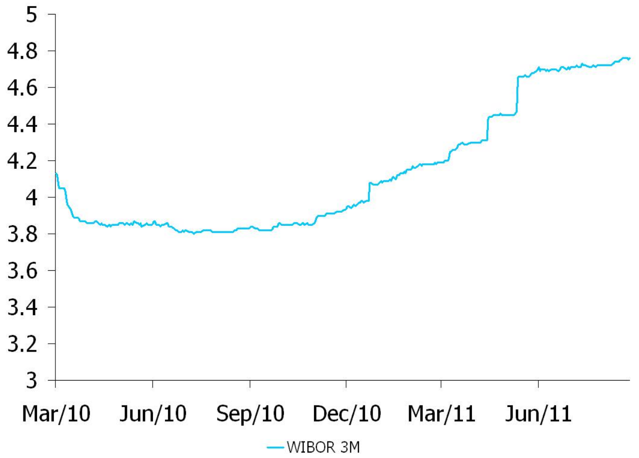
Very probable cheap cost of carry next week

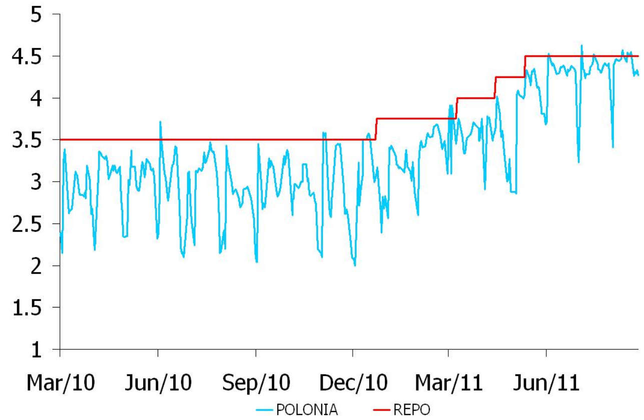
Low intake of the money bills today (pln 98 bln vs 104) should again put downward pressure on the cost of carry. After additional OMO this Tuesday odds were quite even, however now the probability of the cheap end of the reserve has grown radically.

Bearish sentiment caused mainly by the global factors, with the Fed policy in highlights. However, local data also supported the march north. Higher PPI (6.6 vs 6.4%), much higher industrial output (8.1 vs 3.8%), higher core CPI (rise to 2.7 from 2.4%), and last but not least much higher retail sales 11.3 vs 8.5% expected. All this is unquestionable argument for hawks not to be in a rush with any rates cuts. First probable term for the easing is now 1Q 2012, therefore rates had to adjust after some expectations even for 4Q this year.





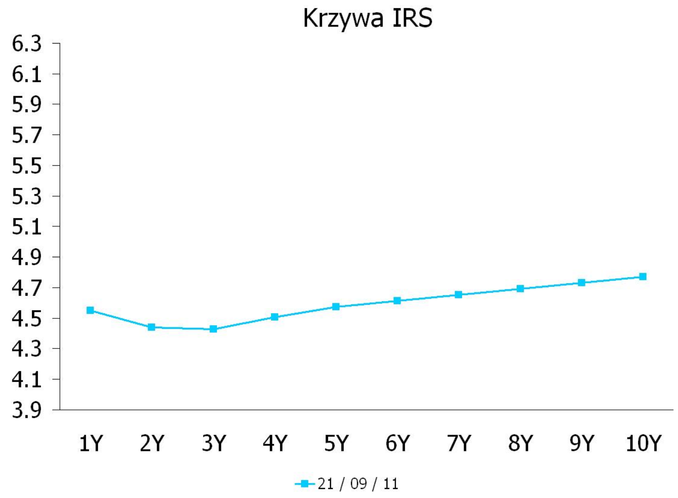




Forex

Zloty above 4,50 Massive position liquidation in CEE3 space (and not only there) took EUR/PLN to 4.5370 high (last seen in 2009). The violent move that took a series of stop losses on its way. This is the knee jerk reaction to the global turbulences (very serious to be admitted), but the Polish fundamentals in contrast are still looking quite positive. The EUR/PLN above 4.60 is a potential threat to government debt to GDP ratio, so we expect that government make take same actions if Zloty losses further.

The 1m EUR/PLN ATM paid at 17.75%, 3 months EURPLN ATM paid 16% and 1 year traded around 14.75%. The currency spread (the difference between USD/PLN and USD/PLN) reached 10%, and the risk reversals and flies moved higher as well. The liquidity is really poor and spreads are terribly wide...

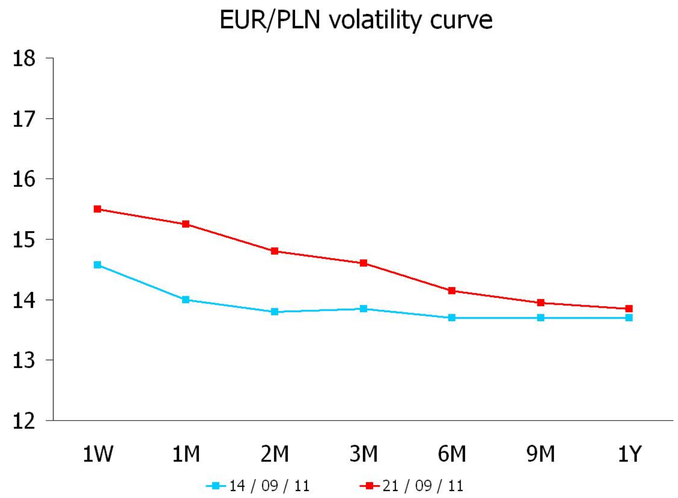


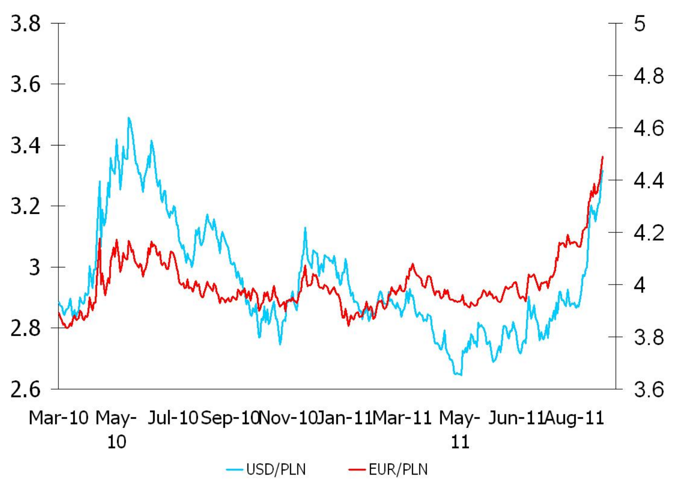
Short-term forecasts

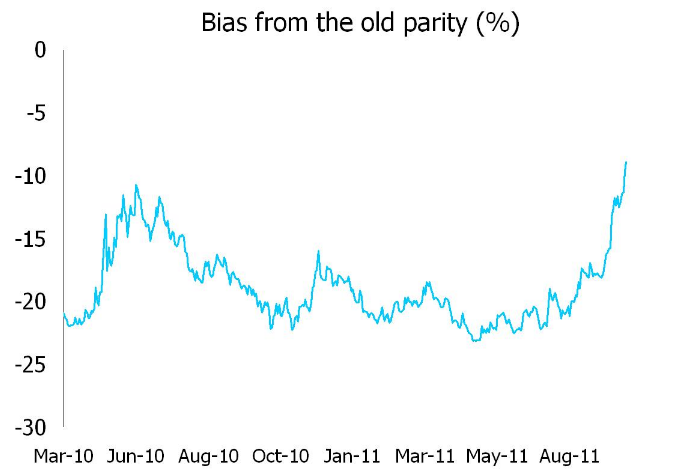
Main supports and resisances
EUR/PLN: 4.4000 / 4.5500
USD/PLN: 3.1500 / 3.4000

Spot. Current market conditions are for the brave souls and locally based dealers. We still try to play the wide range now 4,40/4,55 but the higher we go, the more our bias switches to PLN longs. The PLN fundamentals are encouraging, and the government should be more and more active in protecting the PLN as the year end approaches.

Derivatives. We sold the spikes in EURPLN vol curve, and that is the first time we have done it this year. We are far from saying the current madness is over, it is simply, fully reflected in current volatility levels. We stick to ATM and would not advice to go short in the upside strikes.







Market prices update

Money market rates (mid close)								FRA rates (mid close)				
Date	FXSW 3M	WIBOR 3M	FXSW 6M	WIBOR 6M	FXSW 1Y	WIBOR 1Y	1x4	3x6	6x9	9x12	12x15	6x12
9/15/2011	4.65	4.75	4.85	4.76	4.90	4.78	4.71	4.70	4.55	4.42	4.31	4.58
9/16/2011	4.64	4.76	4.74	4.76	4.78	6.59	4.71	4.68	4.56	4.43	4.38	4.62
9/19/2011	4.62	4.76	4.74	6.49	4.79	4.79	4.73	4.68	4.55	4.41	4.33	4.60
9/20/2011	4.64	4.76	4.72	4.75	4.76	4.78	4.73	4.68	4.54	4.40	4.33	4.59
9/21/2011	4.63	4.76	4.74	4.75	4.78	4.79	4.74	4.71	4.58	4.47	4.40	4.67

Last primary market rates							
Paper	Au. date	Maturity	Avg. price	Avg. yield	Supply	Demand	Sold
52W TB	1/31/2011	1/31/2012	95.84	4.35	2000	2968	1961
OK0113	4/13/2011	1/26/2013	89.16	5.16	5500	7385	4758
PS0416	1/5/2011	4/25/2016	97.08	5.64	6500	2795	1140
DS1020	1/12/2011	4/25/2019	93.02	6.21	2250	4252	2250

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0113	5Y IRS	PS0416	10Y IRS	DS1019
9/15/2011	4.780	4.570	4.601	4.409	4.756	5.050	4.926	5.848
9/16/2011	6.590	4.530	4.586	4.440	4.751	5.042	4.926	5.870
9/19/2011	4.790	4.530	4.656	4.472	4.851	5.117	5.041	5.964
9/20/2011	4.780	4.570	4.575	4.454	4.745	5.080	4.920	5.889
9/21/2011	4.790	4.570	4.635	4.463	4.820	5.168	5.015	5.950

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY	
Date	1M	3M	6M	1Y	1M	1Y	1M	1Y
9/15/2011	13.55	13.40	13.25	13.15	13.15	4.36	0.59	0.79
9/16/2011	13.55	13.40	13.25	13.15	13.15	4.36	0.59	0.79
9/19/2011	14.50	14.00	13.70	13.55	13.55	4.36	0.59	0.78
9/20/2011	14.40	13.85	13.50	13.40	13.40	4.51	0.59	0.78
9/21/2011	15.25	14.60	14.15	13.85	13.85	4.84	0.57	0.76

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
9/15/2011	4.3871	3.1858	3.6361	4.1527	1.5245	0.1786
9/16/2011	4.3462	3.1506	3.6017	4.1058	1.5169	0.1771
9/19/2011	4.3513	3.1867	3.6076	4.1482	1.5059	0.1775
9/20/2011	4.3811	3.2067	3.6323	4.1890	1.5037	0.1780
9/21/2011	4.3925	3.2123	3.5944	4.2056	1.5115	0.1765

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