Bureau of Economic Analysis
(research)

Ernest Pytlarczyk, PhD, CFA
chief economist
tel. +48 22 829 01 66
ernest.pytlarczyk@brebank.pl

Marcin Mazurek, PhD
senior analyst
tel. +48 22 829 01 83
marcin.mazurek@brebank.pl

Paulina Ziembinska
analyst
tel. +48 22 829 02 56
paulina.ziembinska@brebank.pl

Artur Pługa
analyst
tel. +48 22 526 70 34
artur.pluska@brebank.pl

Financial Markets Department
(business contacts)

Lukasz Barwicki
head of trading
tel. +48 22 829 01 93
lukasz.barwicki@brebank.pl

Inga Gaszkowska-Gebska
institutional sales
tel. +48 22 829 01 67
inga.gaszkowska-gebska@brebank.pl

Bartlomiej Malocha, CFA
money market
tel. +48 22 829 01 77
bartlomiej.malocha@brebank.pl

Jaroslaw Stolarczyk
structured products
tel. +48 22 829 01 67
jaroslaw.stolarczyk@brebank.pl

Marcin Turkiewicz
fx market
tel. +48 22 829 01 67
marcin.turkiewicz@brebank.pl

Reuters pages:
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SWIFT:
BREXPLPW

BRE Bank S.A.
18 Senatorska St.
00-950 Warszawa
P. O. BOX 728
tel. +48 22 829 00 00
fax. +48 22 829 00 33
http://www.brebank.pl

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Comment on the upcoming data and forecasts

MPC is set to leave interest rates unchanged in March. Simultaneous release of inflation projection should show high inflation in 2012 and its decrease towards NBP's inflation target in 2014. GDP growth forecasts will not be highly optimistic as model includes forecasts for euro area growth from the beginning of the year. However, for MPC the greatest problem is currently statistically missed inflation mandate. In the horizon of 1-2 months, when inflation comes back to NBP's inflation target band (expected in March and April) we can count on more dovish comments from some MPC members. As for now, MPC will maintain „wait and see" stance.

Polish data to watch: March 5 to March 9

Publication	Date	Period	BRE	Consensus	Prior
MPC decision (%)	7.03.	Mar	4.5	4.5	4.5

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Last yield (%)	Prev auction
52 Week T-bills	3/26/2012	2000	4.480	2/29/2012
2Y T-bond OK0114	3/14/2012	5500	4.688	2/9/2012
5Y T-bond PS1016	3/14/2012	5500	5.020	2/9/2012
10Y T-bond DS1021	3/21/2012	3000	5.511	2/1/2012
20Y T-bond WS0429	3/21/2012	3000		2/16/2011

Macroeconomic forecasts

Wskaźnik	2008	2009	2010	2011	2012 F
GDP y/y (%)	5.1	1.6	3.9	4.3	2.8
CPI Inflation y/y (average %)	4.3	3.5	2.8	4.3	3.6
Current account (%GDP)	-5.3	-1.6	-4.5	-4.9	-3.6
Unemployment rate (end of period %)	9.5	12.1	12.4	12.5	13.6
Repo rate (end of period %)	5.0	3.5	3.5	4.5	4.0

	2011 Q1	2011 Q2	2011 Q3	2011 Q4	2012 Q1 F	2012 Q2 F
GDP y/y (%)	4.5	4.3	4.2	4.3	3.8	3.5
CPI Inflation y/y (average %)	3.7	4.2	4.1	4.6	4.1	3.7
Repo rate (end of period %)	4.0	4.5	4.5	4.5	4.5	4.5

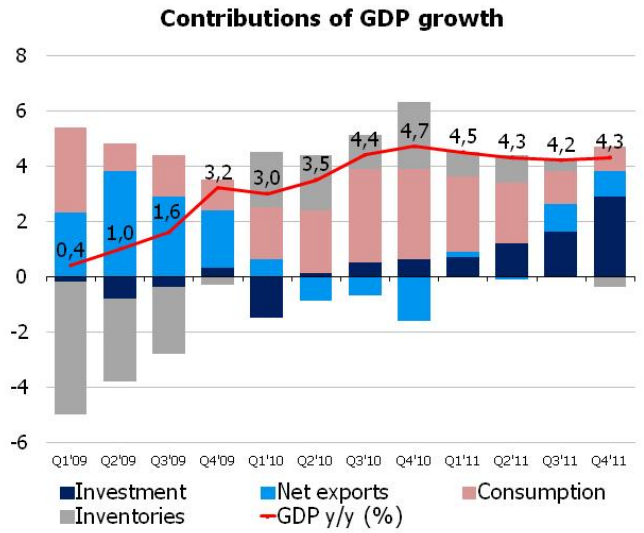
F - forecast

Economics

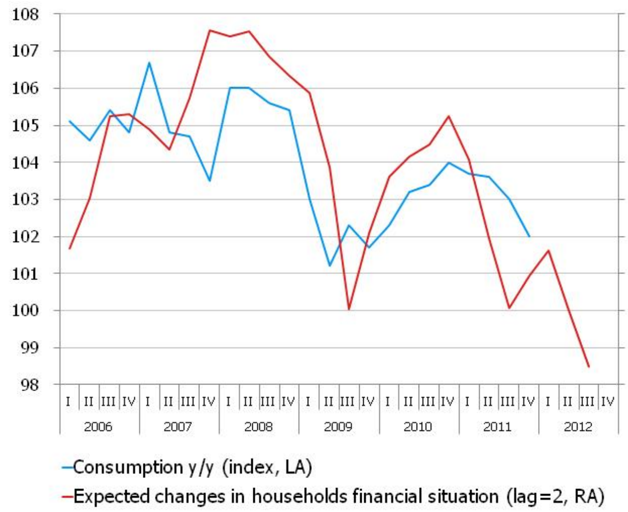
Decent GDP growth but poised to decline

According to the fresh data, GDP growth came out at 4.3% in Q4 2011, better than expected 4.2%. Looking at seasonally adjusted sequential growth, there is also nothing to be ashamed of: 1.1% QoQ positions itself perfectly within the recent trend. The composition of GDP growth does not indicate a further acceleration, though. In our opinion growth rate has locally topped in Q4 and there are only lower numbers to come, although without sharp deceleration.

Turning to details, consumption growth amounted to 2.0% (vs 3.0% in the previous quarter), fixed business investment accelerated to 10.3% (vs 8.5%). Once again fiscal consolidation drove public consumption downwards, this time 0.8% off the Q4 2010. The highest boost to GDP growth was given by investment (+2.9pp.). Private consumption was clearly inferior but still on the black (+1.0pp.). Net exports added +0.9pp. which was partially shaved off by negative inventory formation (-0.4pp.).



Turning more to economic analysis, it has to be noted that investment growth owes more and more to private fixed capital formation, however we still cannot tell precisely how many machinery orders can be tied to new investment and how many units simple substitute for obsolete ones. Given the current uncertainty and the cloudier state of employment (often going hand in hand with new investment) we think the latter is the case. Therefore as soon as infrastructure investment gives in (in H2), replacement investment will not be high enough to sustain double digit investment growth. Therefore we look for overall deceleration of investment aggregate towards 4% in H2. As for consumption, the current state and the deceleration itself shows that simple Keynesian consumption function is detached from reality. It is far better to look beyond wage growth. Therefore we checked the relevance of consumer expectations (regarding the current and expected balance sheet of a household; such a view incorporates a multitude of factors, beyond current income growth) for the evolution of private consumption. The results are presented on the graph - although the current growth rate of consumption is relatively low, there is in our opinion still more downward adjustment in the pipeline.



Before we see a meaningful GDP growth deceleration, we will probably have to deal with quite decent growth in Q1. Such a view is hinted by relatively high potential of investment activity to surprise (at the start of the year infrastructure investment and private replacement investment „work" together), and possibility of a relatively high share of net exports, not only reflecting usual anti-cyclical behavior of this aggregate but also positive response of exports to earlier PLN depreciation and deceleration of imports driven by lower consumption. To corroborate this view one can look at recent PMI readings, but not necessarily only on the headline but primarily on the composition. We see that current decent output readings stem mainly from realizing past orders, whereas new orders index is only slowly drifting higher (not necessarily in the pace able to sustain current production levels). Therefore even if Q1 may still be quite decent in terms of GDP growth (still close to 4%, but this time rather below the figure), next quarters are set to be slower. All in all we expect GDP growth in 2012 close to 3% level.

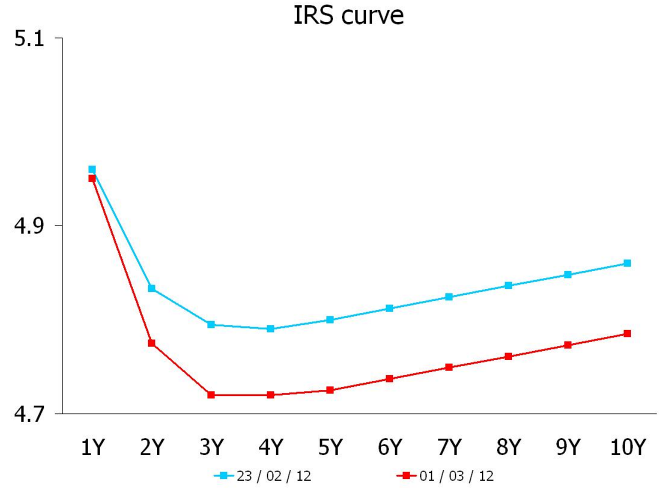
The data are neutral for MPC. Relatively high growth is still a base case scenario for majority of MPC members. So even high readings should not exert much additional pressure on the Committee. The real game changer for now is inflation. Falling CPI growth will keep in check any more hawkish rhetoric giving room for stable rates for some months or even some easing in H2 2012.

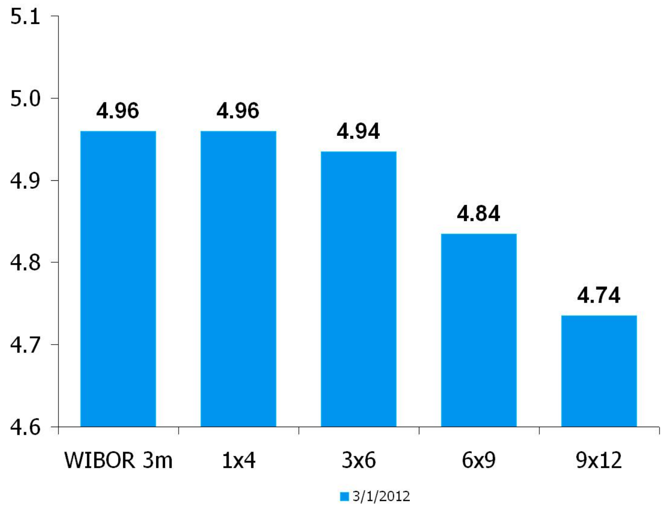
Fixed income

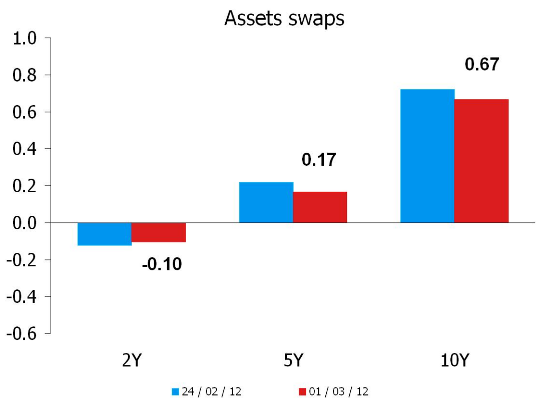
Nothing new

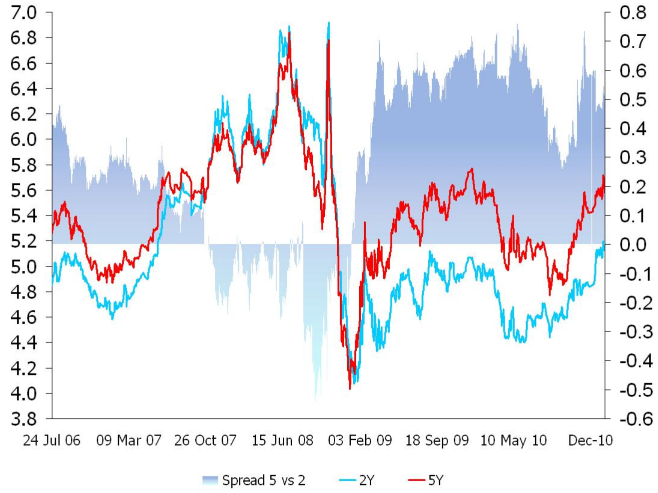
Last week didn't bring any significant changes to the overall picture of the polish FI market. Rates very slowly drifting lower, closing the week some 3bp below previous week's close. Demand for PolGBs in 5y+ sector remains constant. Bond yields fell by ca. 10bp and asset-swap spreads narrowed even further. Economic data releases last week were quite neutral from rates perspective, also comments from MPC members were held in the same tone as before - rate hikes more likely than cuts; it needs probably more time and more data before that changes. Everything we wrote last week remains valid - MPC will try to stay hawkish as long as possible, keeping front end rates at elevated levels, bonds will remain well bid, considering they're still cheap in ASW terms, the FinMin managed to finance over 42% of this year needs and is willing to limit issuance after April.

Next week the new inflation projection will be published along with MPC decision - comments from the Council will definitely be more important that the document itself, especially after previous surprising reading. Nevertheless what we'll be concentrating on more is the next data and, moreover, impact of yearly basket revision. Should the latter be 0.2-0.3pp., which isn't unlikely, we'd find ourselves in quite a new environment, with CPI at 3.8-3.9%. Probably that won't be enough for a major change on the yield curve, but that would be another important argument against rate hikes. The market probably would need few more before it finally realizes what's happening here, but any tops in 2y IRS are a receiving opportunity already.







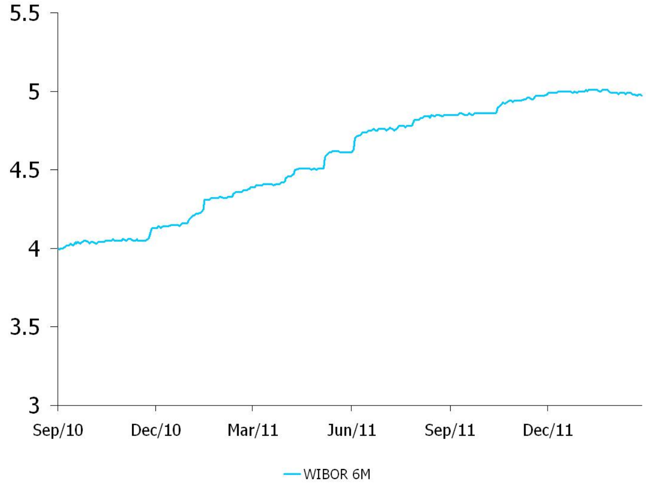


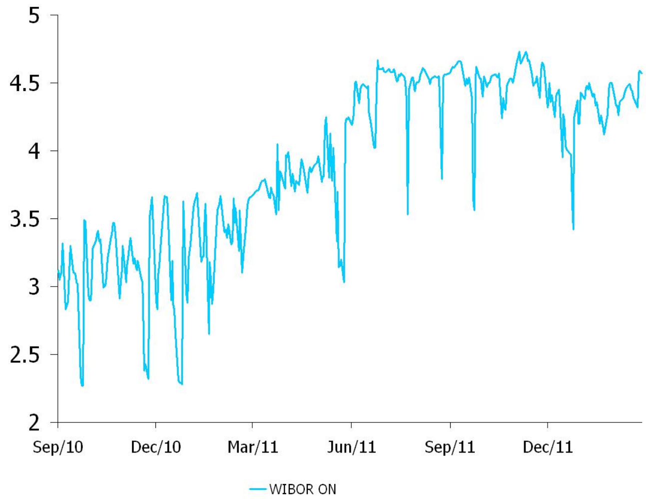
Money market

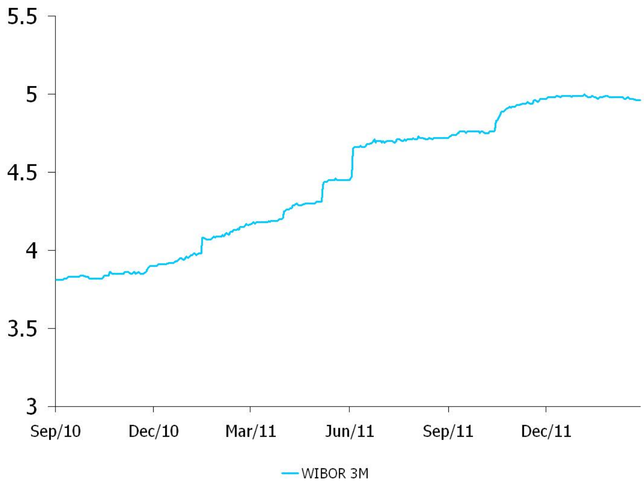
Expensive end of the month

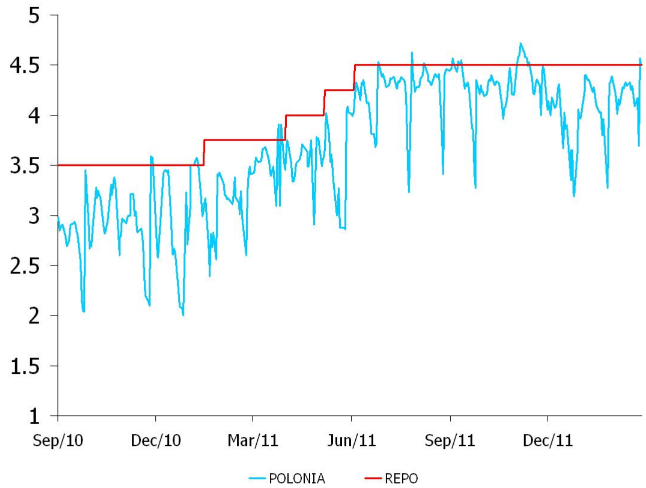
We finally got through end of the month which was suprisingly expensive in terms of cost of carry. As a result average 30 day POLONIA rose around 17 pips to 4.25, levels seen before December. Question is wheather this is set to persist through the next months. If it does we can see some upside repricing on the whole curve (2-3 pips). Although almost nothing is happening on the OIS market which follows no significant changes in market feelings about next MPC action.

On Monday we had t-bills auction. Demand was quite hudge, yield fell to 4.48% and the market bought PLN 2.2 bn. We will have only one auction in March, so looks like MinFin is in good shape, and the t-bills will stay expensive.





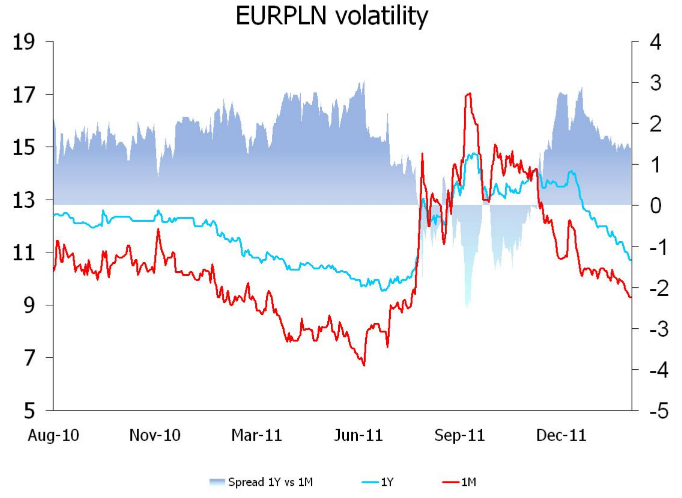




Forex

Zloty soars After a decent consolidation phase EUR/PLN finally broke the 4.15 strong support line on the fresh wave of optimism fueled by a successful ECB LTRO, and on trade recommendation published by the one of the biggest investment house which see target for EUR/PLN at 4.0400. We think some fresh money has joined the trend. The low so far was 4.0960... The correlation between EUR/USD and the Zloty is weakening! The PLN is still "risk on" currency but is the EUR/USD rate still a proxy for risk??

Volatility lower The sell off continues, the mid backend suffered most. 1 month EUR/PLN atm is 9.0% vs 9.2% last week (small change) but 6m atm 10.0 % (0.4 % lower) and 1Y atm 10.5 (0.4% lower) is much more impressive. The risk reversals are 0.2% lower and currency spread (difference between USD/PLN vs EUR/PLN) is stable at 7.25%.

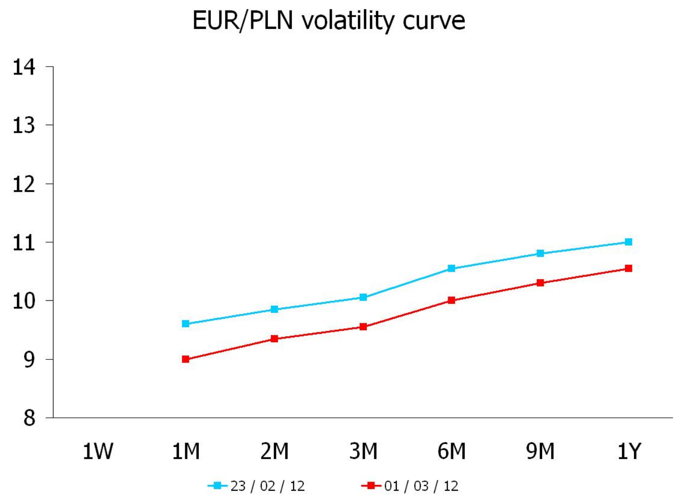


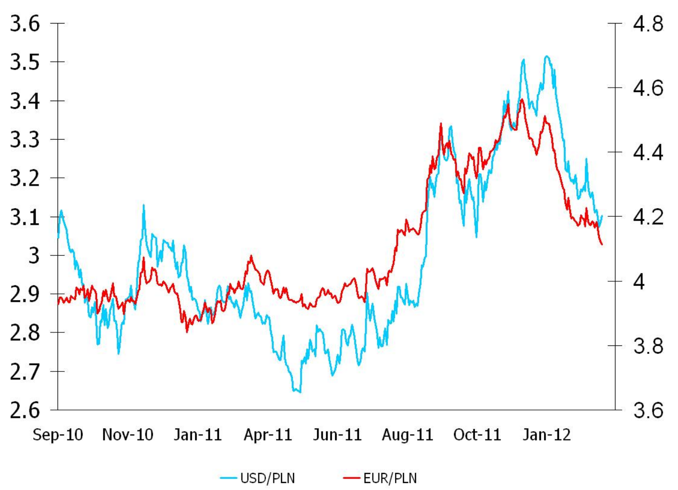
Short-term forecasts.

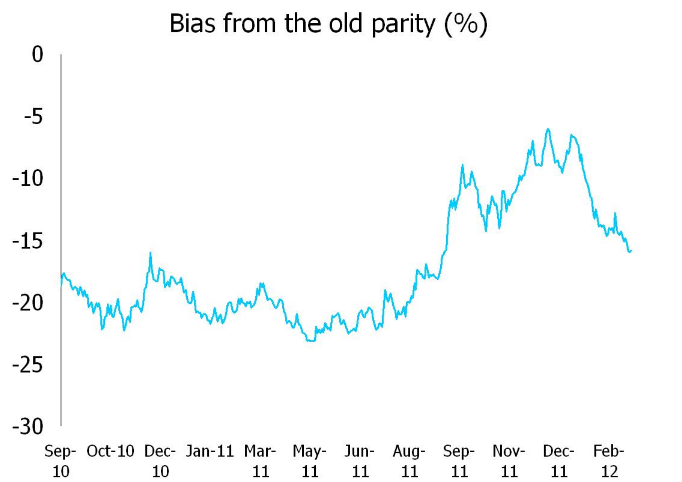
Main supports and resisances
EUR/PLN: 4.0400 / 4.1800
USD/PLN: 3.0000 / 3.2500

Spot. The positive sentiment still supports the risky assets, hawkish MPC rhetoric also improves prospects for PLN. We would like to sell EURPLN at 4.1350/4.1450 with 4.1800 stop loss with target 4.02/4.04.

Derivatives The correlation stronger Zloty-lower implied volatility curve is still valid. The sell off in the middle and back-end is quite impressive. The last year range for 1 year EURPLN atm was 9.25% - 14.0%, so we still have same potential...







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
2/24/2012	4.61	4.97	4.64	6.49	4.64	6.59	4.97	4.97	4.87	4.77	4.67	4.89
2/27/2012	4.58	4.96	4.78	4.88	4.83	4.88	4.95	4.95	4.87	4.77	4.68	4.92
2/28/2012	4.59	4.96	4.62	4.88	4.62	4.88	4.97	4.95	4.85	4.74	4.64	4.87
2/29/2012	4.58	4.96	4.80	4.88	4.62	4.88	4.96	4.95	4.84	4.73	4.61	4.86
3/1/2012	4.75	4.96	4.77	4.88	4.77	4.88	4.96	4.94	4.84	4.74	4.61	4.87

Last primary market rates							
Paper	Au. date	Maturity	Avg. price	Avg. yield	Supply	Demand	Sold
52W TB	5/30/2011	5/30/2012	95.57	4.58	600	2667	505
OK0114	8/10/2011	1/25/2013	89.58	4.58	5000	4934	1889
PS1016	10/19/2011	10/25/2016	98.44	5.11	3600	11200	3638
DS1021	7/21/2011	10/25/2021	99.53	5.80	3000	5608	3000

Fixed income market rates (closing mid-market levels)								
Date	1Y WIBOR	1Y T-bill	2Y IRS	OK0113	5Y IRS	PS0416	10Y IRS	DS1019
2/24/2012	6.590	4.450	4.795	4.672	4.760	4.977	4.815	5.536
2/27/2012	4.880	4.510	4.810	4.679	4.750	4.990	4.830	5.543
2/28/2012	4.880	4.450	4.810	4.680	4.740	4.945	4.800	5.517
2/29/2012	4.880	4.500	4.775	4.675	4.740	4.904	4.780	5.468
3/1/2012	4.880	95.992	4.775	4.671	4.725	4.891	4.785	5.452

EUR/PLN 0-delta stradle						25-delta RR			25-delta FLY
Date	1M	3M	6M	1Y		1M	1Y		1Y
2/24/2012	9.50	10.05	10.55	11.00		11.00	3.47		0.75
2/27/2012	9.40	9.95	10.45	10.90		10.90	3.47		0.75
2/28/2012	9.30	9.80	10.20	10.70		10.70	3.50		0.66
2/29/2012	9.30	9.75	10.15	10.70		10.70	3.50		0.71
3/1/2012	9.00	9.55	10.00	10.55		10.55	3.50		0.71

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
2/24/2012	4.1654	3.1103	3.4543	3.8610	1.4423	0.1666
2/27/2012	4.1845	3.1176	3.4730	3.8661	1.4320	0.1668
2/28/2012	4.1630	3.0977	3.4535	3.8367	1.4336	0.1663
2/29/2012	4.1365	3.0730	3.4318	3.8133	1.4274	0.1661
3/1/2012	4.1198	3.0887	3.4178	3.8074	1.4310	0.1656

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