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Table of contents

Economics	page 2
• PMI - again under 50	
Fixed income	page 3
• Hike or not, it's still a receive	
Money market	page 4
• Cost of carry not an issue at the moment	
• Front end rally an opportunity to buy.	
FX market	page 5
• Range is intact	
• Consolidating at lows	

Comment on the upcoming data and forecasts

On Wednesday MPC is to announce interest rate decision. Hawkish message delivered in the April's statement and "Minutes" met with some softer comments thereafter, influenced by weaker industrial output. In these circumstances, to-date declared hawk Kazmierczak expressed doubts whether interest rate hike is warranted because of intensifying threats to Polish real sphere. Hausner spoke in similar vein, and also the others. Therefore everything will be decided during the upcoming meeting, no strings attached yet. Having said that we stress that inflation is unlikely to fall below 4% mark before Autumn and MPC reads signals from the real economy still ambiguously. Recent (more or less unchanged or only slightly tweaked) diagnosis of ECB does not change much, therefore we still believe the chances for a hike are prevailing.

Polish data to watch: May 7 to May 11

Publication	Date	Period	BRE	Consensus	Prior
MPC rate decision	09.05	May	4.8	4.5	4.5

Treasury bonds and bills auctions

Paper	Next auction	Last Offer	Last yield (%)	Prev auction
52 Week T-bills	-	3000	4.470	3/26/2012
2Y T-bond OK0114	6/20/2012	7500	4.759	4/19/2012
5Y T-bond PS1016	6/20/2012	7500	5.004	4/19/2012
10Y T-bond DS1021	5/23/2012	2500	5.478	3/21/2012
20Y T-bond WS0429	5/23/2012	3600		1/12/2011

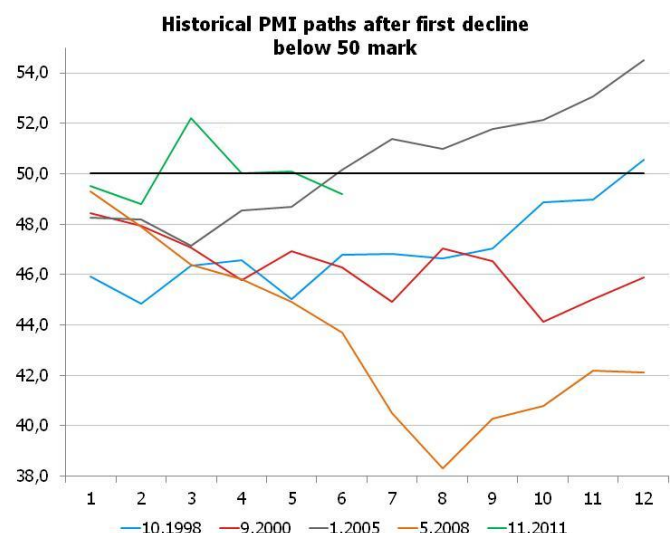
Macroeconomic forecasts

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	4.1	
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	4.75	
	2011 Q1	2011 Q2	2011 Q3	2011 Q4	2012 Q1	2012 Q2 F
GDP y/y (%)	4.5	4.3	4.2	4.3	3,6(F)	2.8
CPI Inflation y/y (average %)	3.7	4.2	4.1	4.6	3.9	4.2
Repo rate (end of period %)	4.0	4.5	4.5	4.5	4.5	4.75
F - forecast						

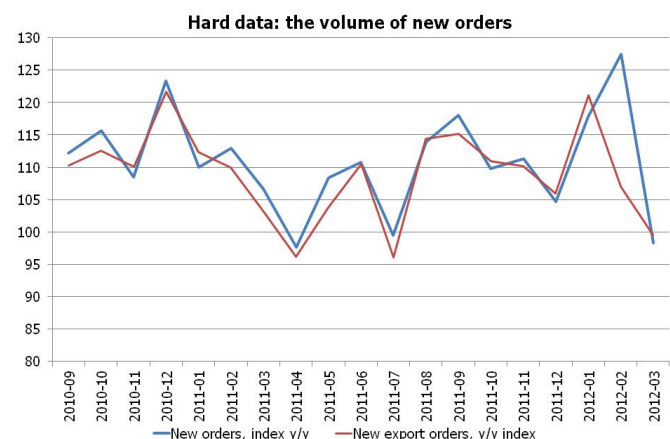
Economics

PMI - again under 50

PMI went again under 50pts barrier in April reaching 49.2pts. (it is the second lowest reading in this cycle, after December's 48.8pts). The fall is consistent with the behavior of other business tendency indicators, including PMI for the German economy. However, the scale of decrease is lower in Poland, especially after taking into account that recent euro zone PMI diverged substantially (downwards) even from the flash readings which is a rare phenomenon.



The decrease of the index is pulled by the collapse of new business volume (the steepest since June 2009) applying both to domestic and export orders. The same tendencies can be spotted in the hard data (see the graph). Output estimates drifted lower again, falling almost to 50pts. The backlog of orders eased and employment index recorded a minor rise (we do not treat this as a sign of stabilization as other employment indicators suggest there is more weakness ahead, although not so pronounced as in 2009). As for nominal indices, input prices decelerated to 7-month minimum but output prices were still able to show modest growth (the slowest since September 2011).



lower gear. GDP decelerated at the beginning of the year, possibly towards 3.4-3.6% range. As for the MPC, it is highly unlikely that one weaker report is going to shock them as: 1) they have been already supplied with the positive, comprehensive NBP report of business activity (which they claim very reliable), 2) they used to expect some sort of a slowdown. What is more, it is inflation that bothers MPC much and the perspective of failing to deliver price stability for too long. Since Draghi did not explicitly announce the rate cut at the upcoming June meeting and did not change ECB's official stance with regard to the real sphere (recent soft readings added only to uncertainty but still the bank expects economy to gradually expand, supported by record low interest rates), it should not interfere with MPC's own, still quite optimistic, diagnosis. Moreover, although ECB's balance of risks for inflation shifted to neutral, it stays on the upside in the short-term. As inflation is unlikely to settle below 4% before Autumn and inflation expectations stay elevated, we sustain our view that rate hike is the most possible outcome of May's meeting, the more so it has been actually announced by governor Belka.

All in all, latest PMI reading confirms the economy is shifting



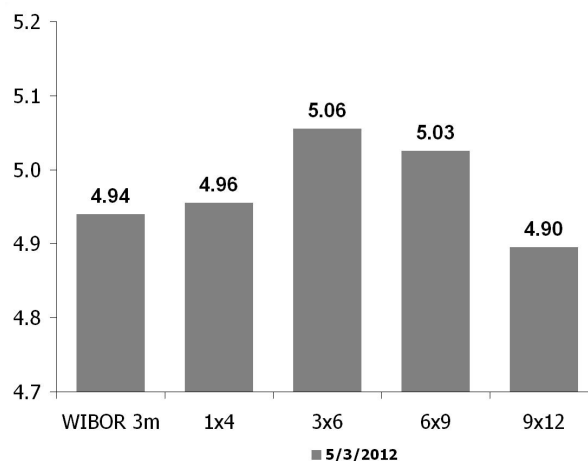
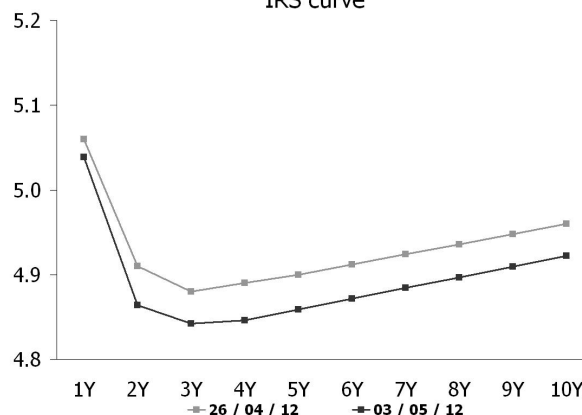
Fixed income

Hike or not, it's still a receive.

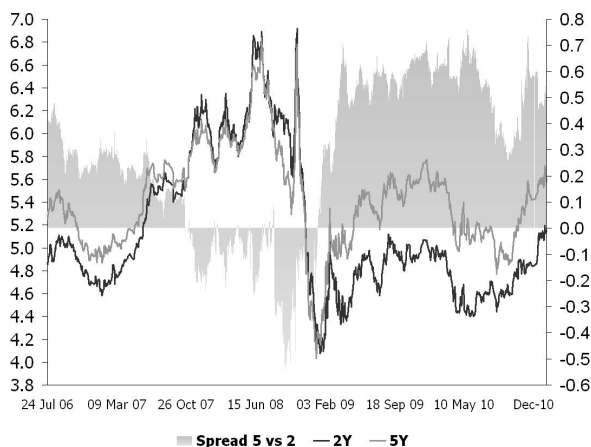
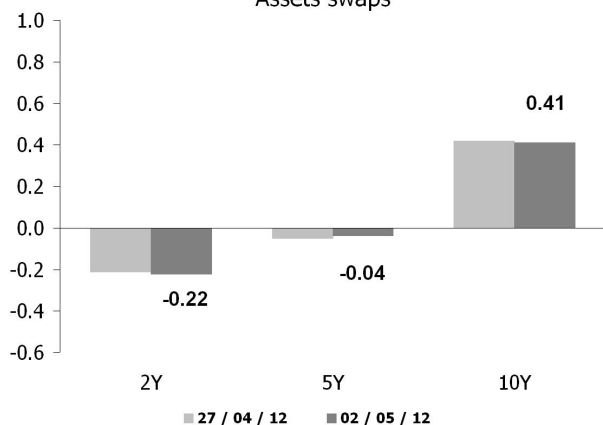
With two holidays this week and therefore absence of most players, market was relatively quiet with limited turnover. Nevertheless there's been some volatility of prices. On Monday we've observed some upward pressure on rates, which moved some 2bp compared to Friday's close. Later on there were some surprisingly dovish comments from MPC Kaźmierczak (a declared hawk recently), who claimed to be still hesitating if he should support a rate hike in May, as he clearly sees slowdown risks ahead of Polish economy.

From that perspective - when even alleged hawks start to give up, the idea of a rate hike sounds really surreal. Having announced such a move, the Council will have quite a difficult choice - either withdraw from this move which would hit their credibility one more time and likely cause another repricing of rates path, or actually hike. The latter would have been even more tricky, as justifying just one move would be difficult so there would have to be some suggestion that another move is likely to happen... From rates perspective the first option would lead to repricing of all tightening and going back to putting bets on when easing starts. The latter, on the other hand, would push very front end of the curve higher but that would also enhance and bring forward rate cut expectations. In both scenarios curve from 1y1y to 5y is a receive and bonds are an attractive buy.

IRS curve



Assets swaps





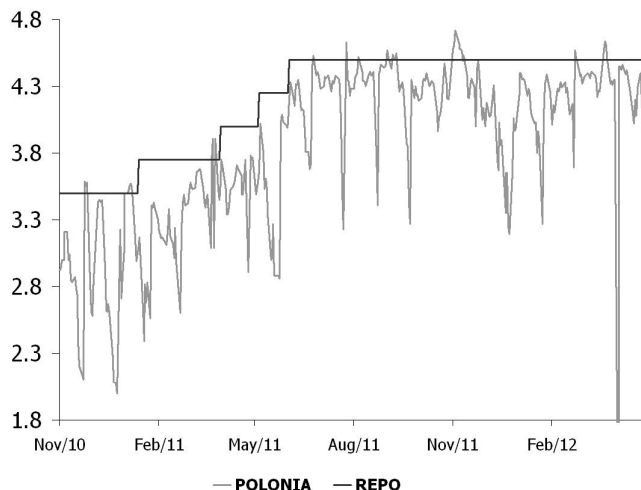
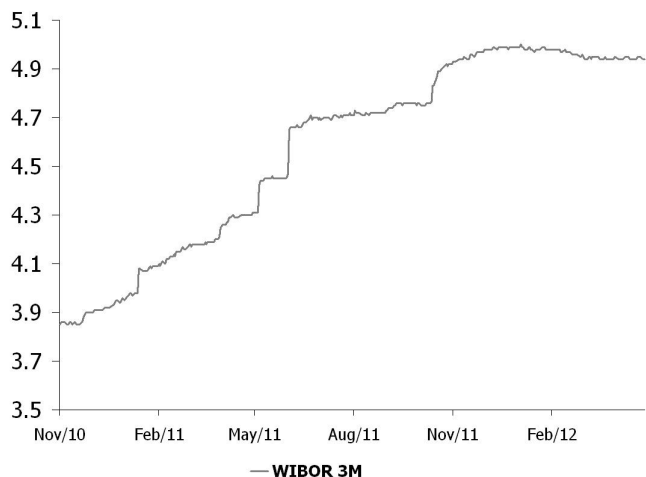
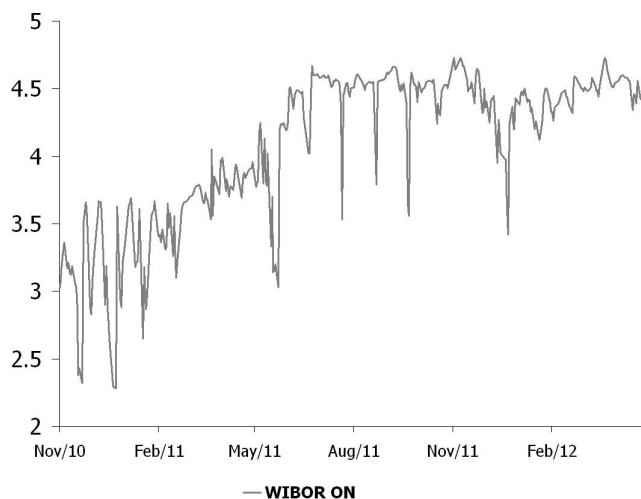
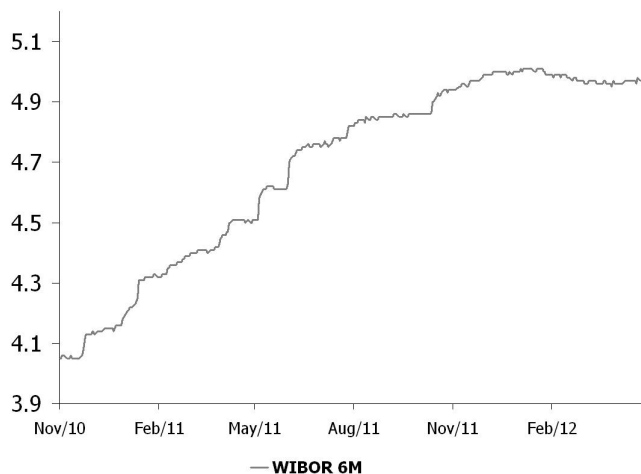
Money market

Cost of carry not an issue at the moment. Front end rally an opportunity to buy.

Cost of carry not an issue this or next week, cash surplus of around 2 billion pln should sustain current levels of the shortest rates, which are slightly above 4%. Today's OMO was underbid by 5 billion pln (85.4 vs 90.5 billion pln), however it should not have any significant impact.

Week with two holidays is always an excuse for lower turnover and interest, however we could see some front end rally. We think it is a good opportunity to open a pay position before next week's MPC meeting. The probability of hike is too high to be ignored, moreover the MPC can start talking about the cycle no matter how it sounds to the market participants. Therefore we strongly recommend hedging the event of hike and/or the more restrictive comment after the decision. The higher CPI reading for April will also be supportive for this strategy.

Be square or pay till the CPI reading.





Forex

Range is intact It was very short week - Tuesday and Thursday were a public holiday in Poland and market activity on Zloty was subdued. On Tuesday EURPLN gapped lower as positive US data prompted a rally across markets and the thin liquidity in the Zloty prompted a quick 200 pip dump to 4.1470. Later sentiment on market has changed. The biggest move came on Thursday after the poor US ISM figures and EURPLN jumped to 4.18 and now it is oscillating around this level.

Consolidating at lows The EUR/PLN holds the 4.1600/4.2200 range for one more week so realized volatility is at it's the lowest levels during last year and implied volatilities follows them. Albeit the latter are at their some kind of support now and the positive differences between implied and realized volatilities for tenors 1W - 6M is expanding. 1M implied is 7.9 mid against 7.0 realized, 6M implied is 9.7mid against 9.3 realized, 1Y implied is 10.15 mid against 10.75 realized. The risk reversals and flies are also being sold.

Short-term forecasts.

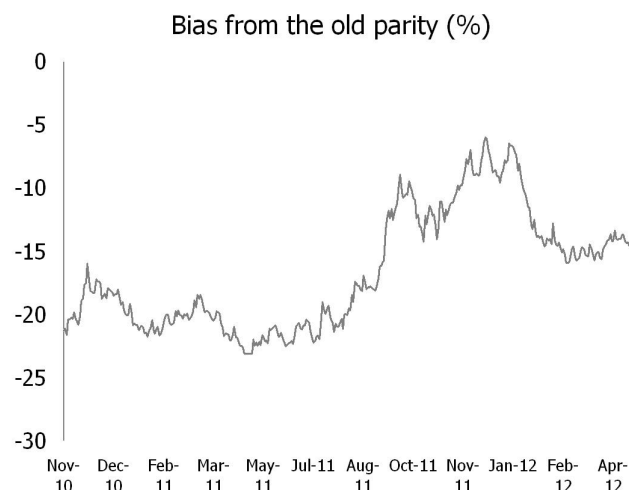
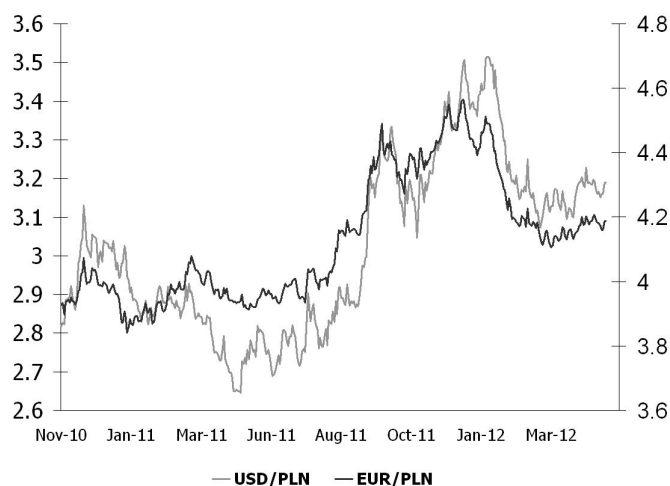
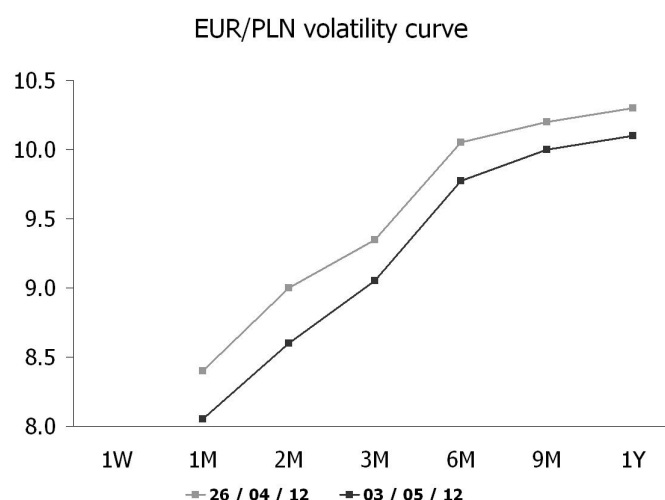
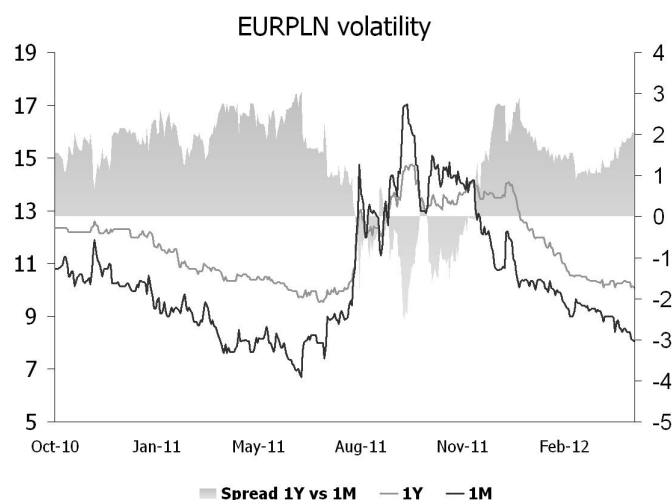
Main supports and resistances

EUR/PLN: 4.1200 / 4.2200

USD/PLN: 3.1000 / 3.2500

Spot. EUR/PLN 4.17 is still the main anchor with movements around this anchor determined by external factors (NFP, the approaching European elections). Because of the failure to break above the 4.21 zone we think that another move down is possible. But taking to account many uncertainty because of external factors we prefer to stay on the sidelines at this moment.

Derivatives As week before we are square in EUR/PLN Vega/Gamma, the Theta/gamma ratio was not that attractive any more with such a low implied volatilities. On USD/PLN, we still believe it is a good value to be short long end, and eventually install the hedge for short gamma by purchase a mid curve strike. It's makes even more sense, as the curve is really steep, and being long mid curve and short backend, gamma neutral, is still Theta positive.





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
4/25/2012	4.64	4.94	4.85	4.87	4.69	4.88	5.02	5.06	5.06	4.97	4.73	5.08
4/28/2012	4.58	4.95	4.64	6.49	4.65	6.59	5.04	5.07	5.07	4.97	4.81	5.09
4/29/2012	4.58	4.95	4.64	6.49	4.65	6.59	5.04	5.07	5.07	4.97	4.81	5.09
4/30/2012	4.73	4.95	4.63	4.87	4.78	4.88	5.03	5.08	5.07	4.97	4.83	5.09
5/2/2012	4.58	4.94	4.75	4.87	4.98	4.87	5.01	5.07	5.01	4.91	4.71	5.02
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				
4/25/2012	4.880	4.590	4.910	4.625	4.900	4.887	4.960	5.408				
4/28/2012	6.590	4.670	4.920	4.708	4.930	4.880	4.980	5.400				
4/29/2012	6.590	4.670	4.920	4.708	4.930	4.880	4.980	5.400				
4/30/2012	4.880	4.630	4.940	4.704	4.925	4.878	4.985	5.406				
5/2/2012	4.870	4.610	4.864	4.641	4.859	4.822	4.922	5.333				
EUR/PLN 0-delta stradle						25-delta RR		25-delta FLY				
Date	1M	3M	6M	1Y		1M	1Y		1Y			
4/25/2012	8.40	9.35	10.05	10.30		10.30	3.47		0.42			
4/28/2012	8.40	9.35	10.05	10.30		10.30	3.47		0.42			
4/29/2012	8.40	9.35	10.05	10.30		10.30	3.47		0.42			
4/30/2012	8.15	8.90	9.50	10.10		10.10	3.46		0.63			
5/2/2012	8.05	9.05	9.78	10.10		10.10	3.49		0.63			
PLN Spot performance												
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN						
4/25/2012	4.1870	3.1675	3.4841	3.9018	1.4332	0.1681						
4/28/2012	4.1820	3.1666	3.4820	3.9295	1.4540	0.1686						
4/29/2012	4.1820	3.1666	3.4820	3.9295	1.4540	0.1686						
4/30/2012	4.1721	3.1509	3.4731	3.9313	1.4591	0.1683						
5/2/2012	4.1600	3.1593	3.4625	3.9346	1.4653	0.1670						

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