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Comment on the upcoming data and forecasts

This week brings the PMI data for June and MPC decision. After an unexpected rise in industrial production and higher business cycle indicators, we should in fact expect higher PMI readings. Though, amid global uncertainty, as reflected i.a. in falling, strongly correlated PMI (and Ifo) indices in Germany and systematic employment decreases, we do not see any room for de-correlation of the Polish and German indicators, and we expect the optimism to be reflected in the lack of substantial deterioration. On Wednesday, we expect the MPC to remain on hold. With lower path of inflation projection, the communicate should become slightly more dovish.

Polish data to watch: July 2nd to July 6th

Publication	Date	Period	BRE	Consensus	Prior
PMI	2.07.	June	48.5	48.6	48.9
NBP interest rate decision	4.07.	July	4.75	4.75	4.75

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 OK0714	7/19/2012	7500	4.759	4/19/2012
5Y T-bond PS0417	7/19/2012	4800	4.784	6/20/2012
10Y T-bond DS1021	7/11/2012	4000	5.349	5/10/2012
20Y T-bond WS0429	7/11/2012	4000	5.563	5/10/2012

Macroeconomic forecasts

Wskaźnik	2009	2010	2011	2012 F	2013 F
GDP y/y (%)	1.7	3.8	4.3	2.5	2.1
CPI Inflation y/y (average %)	3.5	2.8	4.2	3.6	3.2
Current account (%GDP)	-1.6	-4.5	-4.9	-3.6	-1.5
Unemployment rate (end of period %)	12.1	12.4	12.5	13.6	12.4
Repo rate (end of period %)	3.5	3.5	4.5	4.8	4.25

	2011 Q3	2011 Q4	2012 Q1	2012 Q2 F	2012 Q3 F	2012 Q4 F
GDP y/y (%)	4.2	4.3	3.5	3.0	2.3	1.1
CPI Inflation y/y (average %)	4.1	4.6	3.9	4.2	4.3	3.3
Repo rate (end of period %)	4.50	4.50	4.50	4.75	4.75	4.75

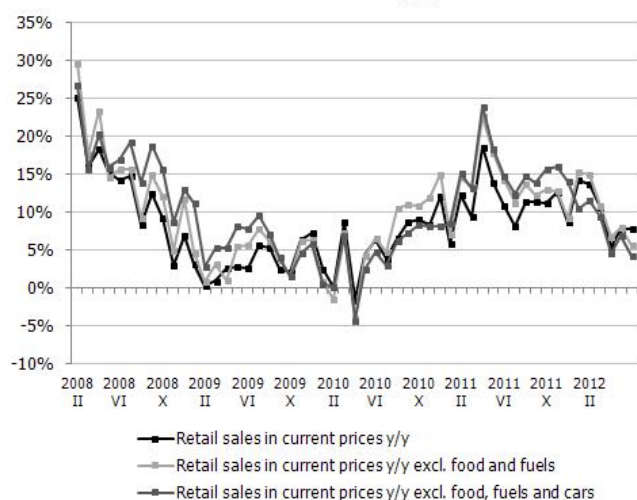
F - forecast

Economics

Retail sales – higher dynamics due to one-offs

Retail sales grew in May by 7.7% in annual terms (after 5.5% in the previous month). The core growth rate - i.e. after the exclusion of food, fuels and cars - amounted to 6.9% y/y against 4.5% in April. Growth rates of similar size occurred in all core categories (see Graph below).

Retail sales y/y



The highest contributions to growth rate came from fuels (3.2% m/m), food (5.8% y/y, out of which 2pp. was added by the low base effect of 2011) and the category of furniture, radio, TV and household appliances (6.2% m/m). On top of that, the category others (over 20% of the entire retail sales value) grew as much as 6.8% m/m, which was the greatest (and unfortunately hardly predictable) surprise. On monthly basis, the most sizeable decreases were recorded in clothing and footwear (-5.1% m/m) other retail sales in non-specialised stores (-3.1% m/m). The distribution of increases and decreases already points to a forward-looking impact of EURO2012 on consumer behaviour in May - purchasing of TV appliances at the cost of clothing and footwear. The media also point to the decreasing interest in shopping centers, as confirmed by earlier than usual sales of summer collections motivated with the football tournament by clothing producers. As a consequence, in June we should expect further deviations from seasonal patterns that distort the underlying trends of the real economy. This, however, does not affect our baseline scenario as regards weaker consumption in 2012 that builds upon solid, fundamental factors (i.a. weakening labour market) and indicators that exhibit long-run correlation with individual consumption (expected financial situation of households or savings rate at a record low).

MPC to cut rates when growth slows to 2%

Data neutral for the market (or maybe just discouraging for the fans of aggressive rate-cut play). Also neutral for the MPC, while the downward trend of retail sales dynamics seems to be more significant. The present expectations of rate cut result above

all from the global context (ultra-low interest rate environment, expected quantitative easing in USA and the euro area, but also business cycle deterioration in the emerging markets, decreases in fuel and food prices, and hence prospects for lower inflation and room for rate cuts). In spite of that, the MPC rhetoric is becoming more dovish (and the probability of hikes tends towards zero). In q3 and q4, we shall witness a significant slowdown of GDP. The fall of GDP dynamics below 2% y/y and a remarkable drop in inflation (no earlier than October, yet) should pave the way towards rate cuts. They are possible at the turn of the year, because 1) the issue of credibility after the recent hike reduce the chance of quick and emotional cuts, 2) MPC must not only expect, but also eye-witness lower inflation readings. We should bear in mind that MPC is not dogmatically hawkish and that, as soon as the risk of non-fulfilling the inflation mandate decreases significantly, the MPC... will cut the rates.

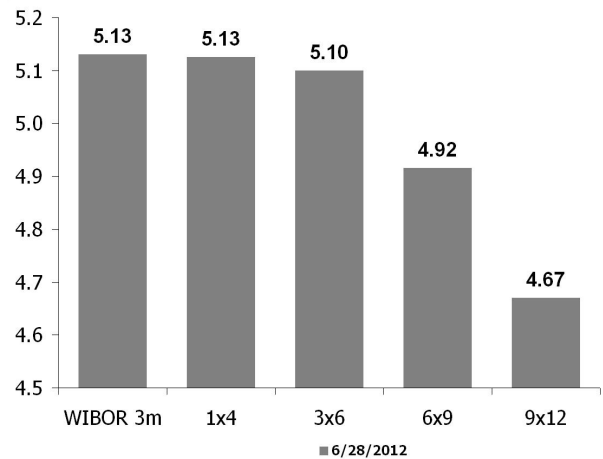
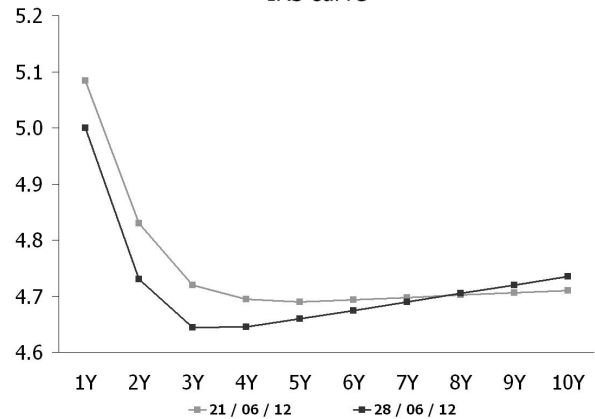


Fixed income

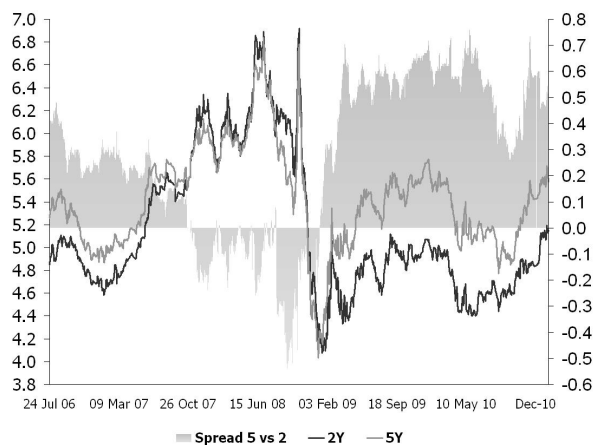
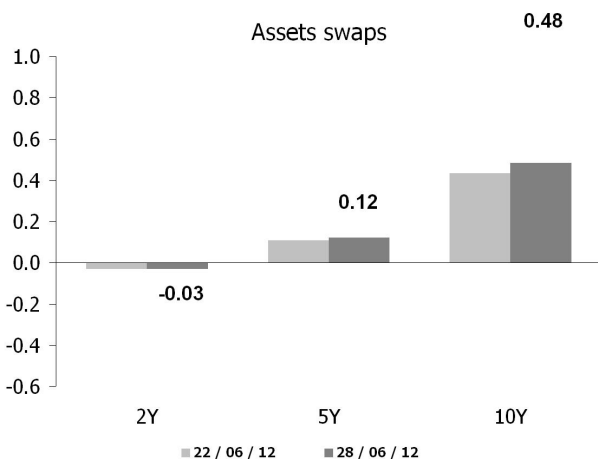
Run for lower rates

The speculation for another rate hike in Poland has definitely vanished. Though the market analysts expect higher June macro data to be released in July, nobody really believes the MPC would be more eager to force more tightening policy in the future. The global call for lower rates towards stimulating eurozone economy and widely anticipating slowdown in Poland within the next months are likely to result in interest rates cuts period. Both the pace and the scope of an easing period would be determined by and correlated with the pace and scale of a slowdown. As we look at the yield curve, we could easily observe the FRA contracts maturing at the end of this year pricing the risk of 25bp interest rate cut and another 50bp in the first half of the next that corresponds with what we expect to happen. No matter what the market has already priced, we still recognize a huge value in 9x12s-12x15s range as we believe the major easing will take place in the first half of 2013 with another 75bp to obtain. Carefully watching the next months economy status we tend to receive rates on tops anyway.

IRS curve



Assets swaps



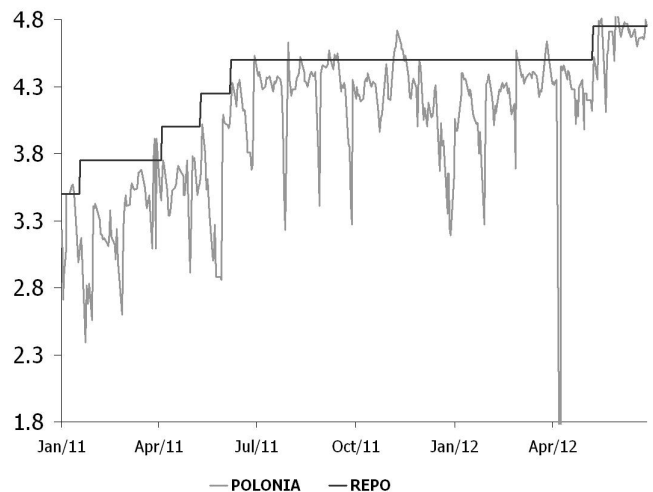
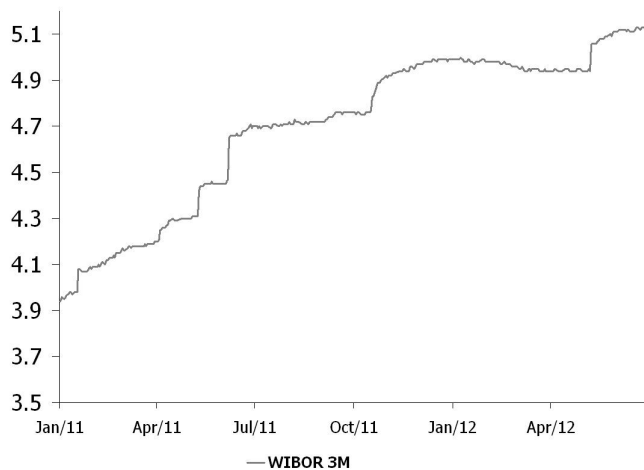
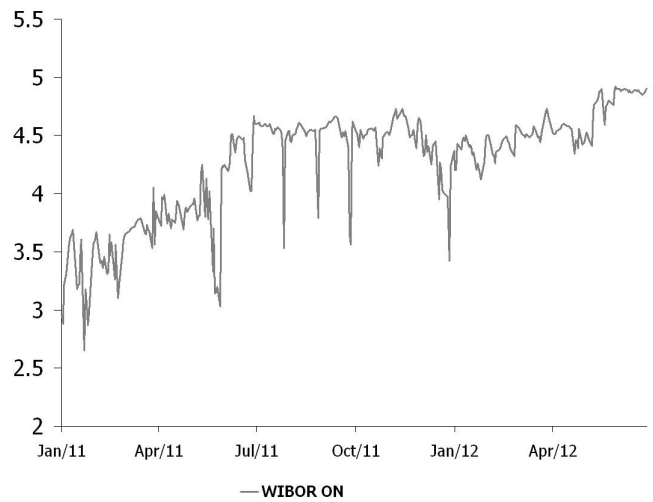
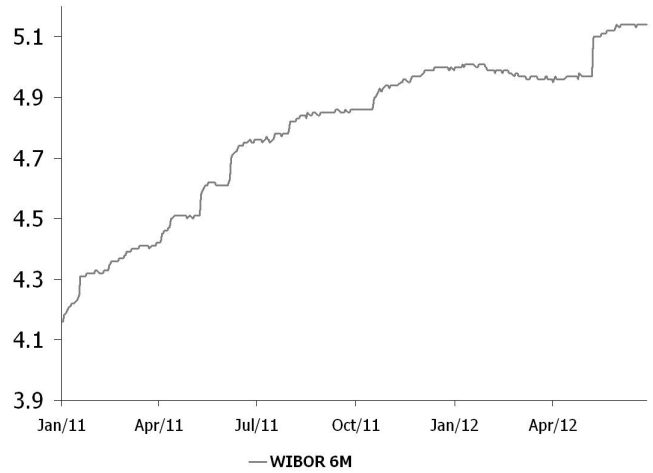


Money market

Another expensive end of reserve period

As we head to the end of another month, cash still stays very high. We wrote in the previous „weekly” about 5 pips spread with reference rate and today it’s even less. One month average polonia vs reference rate spread came down to 3 bp. The most important question is if this trend is going to be extended into next months. We can imagine that this measure goes flat or slightly negative but not more than -7. Polish banks are buying every week around 95 bio NBP bills at 4.82, if overnight goes higher there will be no point in doing so anymore.

The price action last week lowered the end of the curve. 1 year OIS is 4.47 and 9 months 4.53; the rest rather unchanged. That completed our view on a spread between 6 months and 1 year. Now we are more or less in line with what the FRAs are showing about future rate changes.





Forex

Range served. In the first three days of the last week, the EURPLN held pretty well – most of the activity took place in the vicinity of 4.25. With the beginning of the EU Summit, a flood of fresh comments from various prominent officials gave a kick to the market and put some pressure on EURPLN. But finally it was not enough to bring significant levels on the upside within reach - 4.30 remained a strong resistance, and should hold in the coming days.

Vols softer. Most of the last week, EURPLN was traded in the narrow range 4.24/4.26 and realized volatility has fallen. So there is nothing strange that the ATM's Volatility and the skew were hammered hard. The fresh optimism is winning. The 1-month moved down from 11.9% to 10.3% (13% percent of nominal value!), 6-month from 12.0% to 10.9% (9 percent of nominal value!), 1 year is now 11.45% versus 12.2% last week. 1 year 25d risk reversals dropped from 4.5% to 4.1%, 3m 25d RR is now 3.0% versus 3.4% last week.

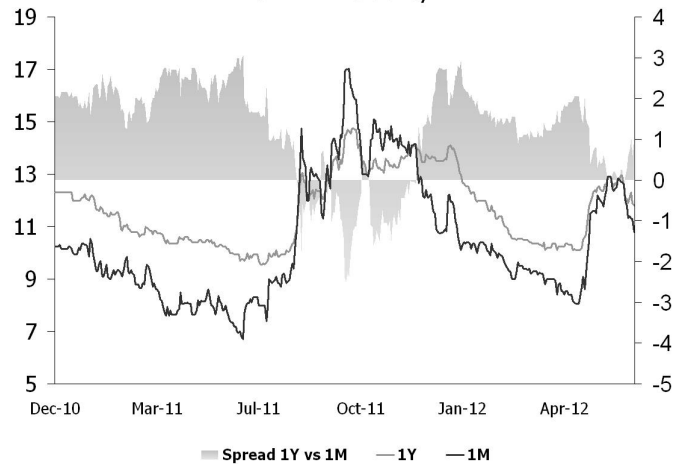
Short-term forecasts.

Main supports and resistances
EUR/PLN: 4.2000 / 4.3000
USD/PLN: 3.3000 / 3.4500

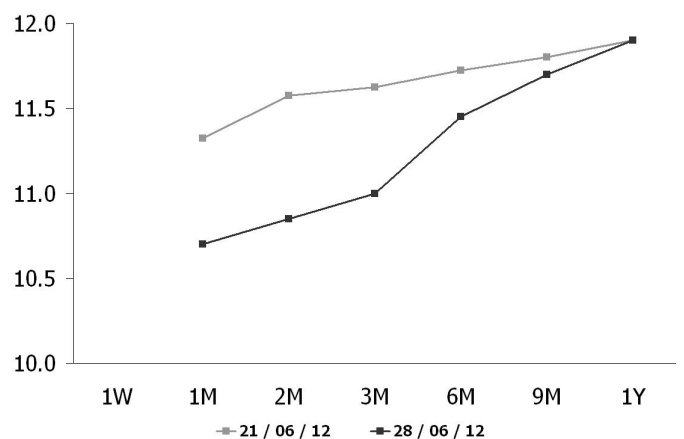
Spot. After the EU Summit, we have positive tone in the market. But we are not really convinced the crisis is over. In our opinion the range simply moved down a little and it's 4.20/4.30 now. Consequently, we are better bids in 4.23 region with 4.20 s/l and hope for move to 4.30.

Derivatives. As we have experienced a very healthy supply of Vega, the market is currently consolidating the move. The Vega, skew and currency spread is still better offered around the curve. The eurozone debt problems are not resolved so we wouldn't venture to open short position in vega. Volatilities are now in the mid of the last year's range, so still sidelined at the moment.

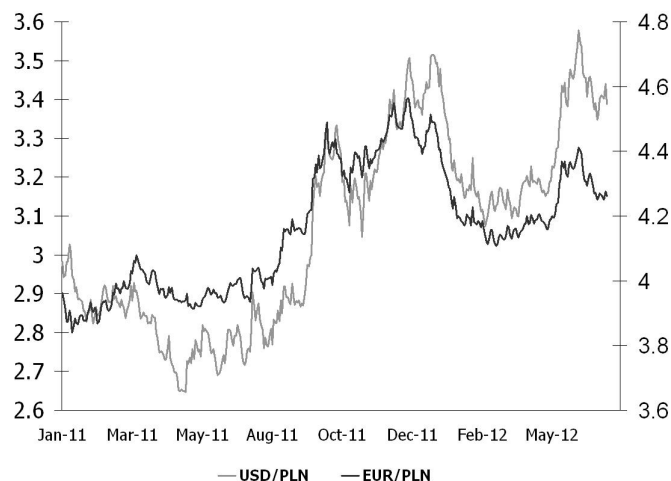
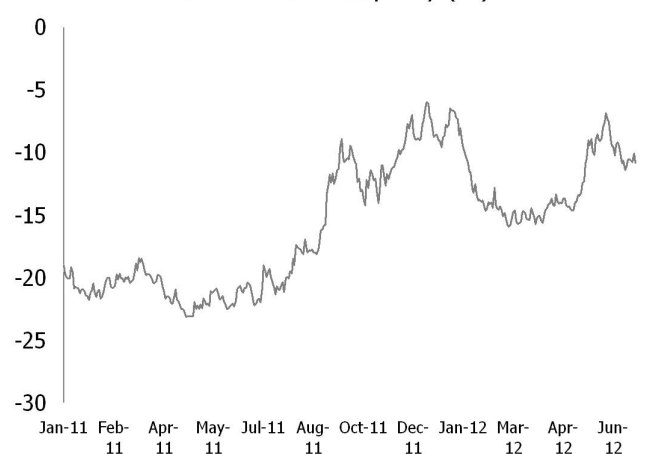
EURPLN volatility



EUR/PLN volatility curve



Bias from the old parity (%)





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
6/22/2012	4.91	5.13	5.02	6.49	5.16	6.59	5.13	5.11	4.93	4.70	4.52	4.91
6/25/2012	5.06	5.12	5.06	5.04	5.07	5.04	5.11	5.08	4.88	4.65	4.42	4.87
6/26/2012	4.93	5.13	4.94	5.04	5.08	5.05	5.14	5.09	4.87	4.67	4.41	4.86
6/27/2012	5.00	5.13	5.15	5.04	5.08	5.05	5.12	5.09	4.88	4.66	4.47	4.88
6/28/2012	4.93	5.13	4.94	5.04	5.08	5.05	5.13	5.10	4.92	4.67	4.43	4.89

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
6/22/2012	6.590	4.813	4.750	4.723	4.680	4.787	4.715	5.149
6/25/2012	5.040	4.813	4.722	4.710	4.660	4.760	4.720	5.159
6/26/2012	5.050	4.813	4.700	4.661	4.650	4.767	4.738	5.177
6/27/2012	5.050	4.813	4.723	4.705	4.650	4.782	4.745	5.200
6/28/2012	5.050	4.813	4.730	4.701	4.660	4.782	4.735	5.217

EUR/PLN 0-delta stradle					25-delta RR		25-delta FLY
Date	1M	3M	6M	1Y	1M	1Y	1Y
6/22/2012	11.40	11.85	12.05	12.15	12.15	4.50	1.03
6/25/2012	11.30	11.70	12.15	12.30	12.30	4.50	1.03
6/26/2012	11.30	11.48	11.58	11.90	11.90	3.94	0.70
6/27/2012	10.80	11.13	11.43	11.80	11.80	3.76	0.66
6/28/2012	10.70	11.00	11.45	11.90	11.90	4.00	1.03

PLN Spot performance						
Date	EURPLN	USDPLN	CHFPLN	JPYPLN	HUFPLN	CZKPLN
6/22/2012	4.2710	3.4025	3.5564	4.2348	1.4866	0.1659
6/25/2012	4.2645	3.4105	3.5511	4.2592	1.4831	0.1656
6/26/2012	4.2580	3.4088	3.5463	4.2967	1.4845	0.1646
6/27/2012	4.2500	3.4015	3.5387	4.2750	1.4869	0.1637
6/28/2012	4.2760	3.4408	3.5605	4.3391	1.4863	0.1654

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