RATES AND FX OUTLOOK

POLISH FINANCIAL MARKET

January 2014

Bank Zachodni WBK
Grupa Santander

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Summary

- Recent macroeconomic data showed that recovery in developed markets strengthens. This is visible also in Poland. The data released over the last month of 2013 suggested that the rebound gained steam in 4Q 2013 (we expect GDP growth above 2.5%) and the pace of economic growth is going to accelerate further in 2014. Domestic economic data for December, which will be published later this month, should confirm the improving macro outlook despite weaker December's PMI reading (our forecast of industrial output, construction and retail sales are well above market consensus). We are estimating that CPI inflation increased modestly (to 0.8%YoY in December, above consensus as well), but stayed well below the NBP's target. The upcoming months should bring further gradual recovery, and the headline CPI should be closer to the target at the end of the year (near 2%YoY).
- The first meeting of the Polish Monetary Policy Council in 2014 will be quite uneventful as the Council stated that it would leave interest rates on hold until the end of 1H14. Meetings of the ECB and the Czech National Bank are going to be quite boring as well (we do not expect any changes in official rates and statements). The NBH and FOMC meetings should be more interesting. So far, recent data have not suggested that the Fed may diverge from the tapering path indicated at its December's meeting. Therefore, investors will focus on December's non-farm payroll data, which in our opinion should remain strong and will justify Fed's tapering decision. As regards the NBH, the board might consider additional monetary easing due to low inflation path.
- Investors' mood on the debt market in December was quite positive. Market reaction to the FOMC's decision to reduce the QE3 program was very limited, suggesting that investors were better prepared to such an action than in May 2013. However, the year 2014 shows a modest correction, which already started in the last days of 2013. While the front end of curves have remained well anchored due to low inflationary pressure and strong central bank's forward guidance, the mid and long end of curves should stay under pressure of news about changes in OFEs' portfolios before transfer and global mood. We believe that recent yields increase should attract foreign investors' demand, while demand from OFE is more uncertain, but if it appears it will be a supportive factor for the debt market in the short run. In the medium term we expect yields/rates to increase gradually.
- As expected, the zloty firmed quite visibly against the main currencies in December. The beginning of the new year started with some profit-taking. We foresee the zloty to appreciate gradually in coming months (towards 4.12 per euro at the end of 1Q), as it will be supported by improving condition of Poland's economy and stable monetary policy outlook.

Short- and Medium-term Strategy: Interest rate market

	Change (bp)		Level	Expected trend	
	Last 3M	Last 1M	end-December	1M	3M
Reference rate	0	0	**2.50**	→	→
WIBOR 3M	4	6	**2.71**	→	→
2Y bond yield	-3	18	**3.00**	→	→
5Y bond yield	-23	-13	**3.61**	↗	↗
10Y bond yield	-15	-19	**4.32**	↗	↗↗
2/10Y curve slope	-12	-37	**132**	↗	↗↗

Note: Single arrow down/up indicates at least 5bp expected move down/up, double arrow means at least 15bp move

PLN Rates Market: our view and risk factors

Money market: WIBOR rates (mainly 3M) moderately increased at the turn of the year. We expect WIBOR rates to remain roughly stable in coming months as long as inflation pressure is low and the MPC sticks to its forward guidance, assuming stable rates (at least) till 1H 2014.

Short end: 2Y bond is well anchored near 3% amid low CPI inflation and strong MPC's declaration to keep rates unchanged at least until mid-2014. We see CPI inflation and economic activity data above consensus. However, positive mood should be supported by demand from foreign investors. The recent MF's data showed some demand for short-term coupon papers from non-residents (PS and DS. series).

Long end: Mid and long end of curves strengthened in December despite the unexpected Fed's announcement about start of the QE3 tapering. The market situation will strongly depend on foreign investors' demand. We believe that recent yields increase should be attractive for investors, notwithstanding we expect gradual increase on monthly basis, in particular in 10Y sectors. In the medium term the expected rise in core yields will result in a more significant increase in yields/rates of 10Y securities. Consequently, curves should remain steeper.

Risk factors to our view: Investors' mood is fragile. If our scenario, assuming limited OFE's demand for government bonds, does not materialise, yields may decrease at the front of the curve. Other risk factors are central banks' decisions, in particular of the Fed. Increasing risk that the pace of QE3 tapering will increase more significantly in coming months might add not only volatility on the market, but also put negative pressure on core yields and consequently, domestic bond market (especially in 10Y sector).

Short- and Medium-term Strategy: FX market

	Change (%)		Level	Expected trend	
	Last 3M	Last 1M	end-December	1M	3M
EURPLN	-1.6	-1.3	**4.15**	→	→
USDPLN	-3.5	-2.4	**3.01**	→	→
CHFPLN	-2.0	-0.8	**3.38**	→	↘
GBPPLN	-1.2	-1.0	**4.98**	→	↘
EURUSD	2.0	1.1	**1.38**	→	→

Note: Single arrow down/up indicates at least 1.5% expected move down/up, double arrow means at least 5% move

PLN FX Market: our view and risk factors

EUR: The beginning of 2014 was not favourable for the zloty, but profit-taking after December's strengthening was not significant. In coming months the zloty should benefit from recovery of Poland's economy and improving balance of payments data (narrowing CA deficit in % of GDP terms). Our baseline scenario assumes the EURPLN to decline gradually towards 4.12 at the end of 1Q 2014.

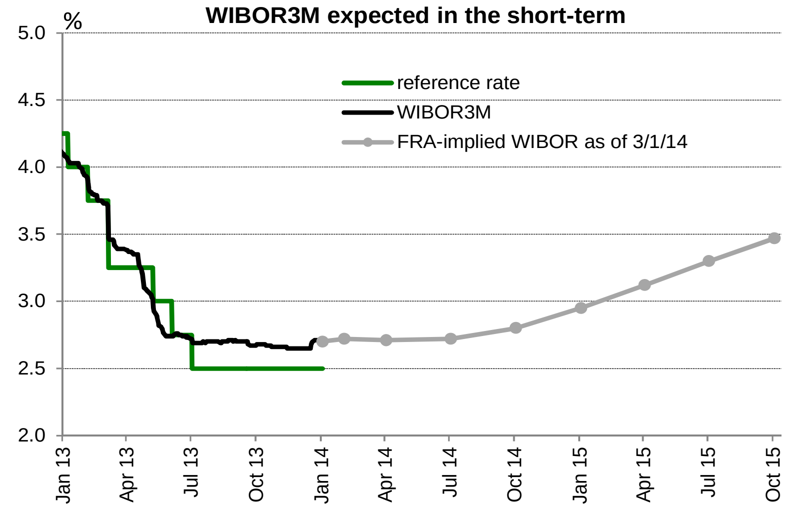
USD: We foresee EURUSD to remain relatively stable in coming months. Despite the Fed's decision to start QE3 tapering at its December meeting the US dollar strengthening was limited due to better prospects of the euro zone economic outlook (supported by a quite impressive rebound in the euro zone peripheries) and stable monetary policy of the ECB. Therefore, we do not expect significant changes in EURUSD, which should support the relatively stable outlook for the USDPLN.

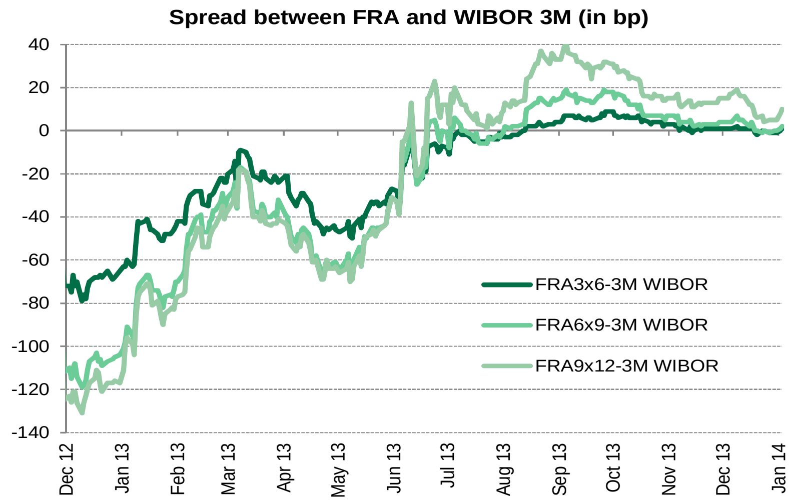
CHF: Our baseline scenario assumes EURCHF to increase gradually in coming months (towards 1.25 at the end of 1Q 2014) due to the improvement in euro zone risk, as shown by the narrowing peripheral spreads to Bunds. Consequently, it should support our expectations of zloty appreciation against the CHF in 3M horizon.

Risk factors to our view: The risk factors for the zloty have remained unchanged. Negative pressure on the domestic currency may come from the main central banks' decisions, in particular of the Fed if the pace of QE3 tapering speeds up. Situation in other CEE3 might also add some volatility on the zloty market.

Domestic Money Market: Under influence of forward guidance

- The last days of December brought some increase in WIBOR rates, in particular of 3M, which climbed above 2.70%. This was partly due to the year-end effect. Historically, the turn of the year brings increase in WIBOR rates (up to 6M). Consequently, spread between WIBOR 3M and the reference rate widened above 20bp, the highest level since September.
- As we already mentioned before, FRA rates were more sensitive to released macro data. The lower-than-expected November's CPI reading resulted in rates decline across the board. The increase of WIBOR accompanied by some decline of FRA resulted in a visible reduction in interest rate hikes expectations. FRA9x12-3M WIBOR spread declined to 5bp, down from 15bp at the end of November (or even 40bp in early September), while FRA6x9-3M WIBOR spread reached 0bp vs. nearly 20bp in early September.
- Money market rates have remained under influence of the MPC's declaration of leaving interest rates unchanged till mid-2014. Current market expectations are below our forecast (we expect the first rate hike in September). We expect WIBOR rates to remain more or less stable in coming months as long as inflation outlook is fairly benign and economic growth is moderate.

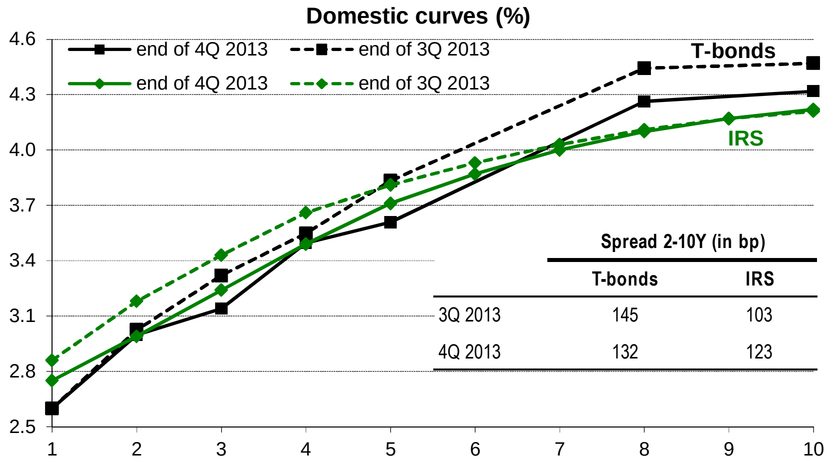




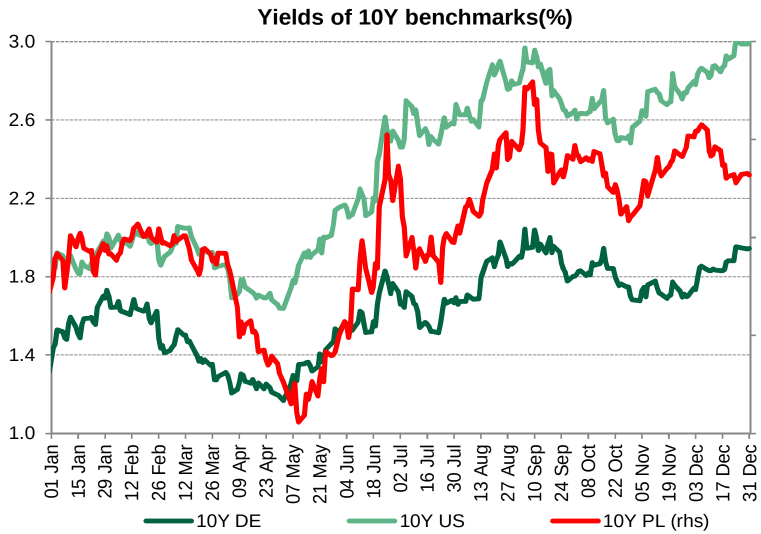
Sources: Reuters, BZ WBK

Domestic IRS and T-Bond Market: OFE and global mood should set the direction

- December brought a strengthening of Polish bond and IRS markets. Despite Fed's decision the PLN curves declined. The strongest buying interest was visible at the long end of the curve, causing a further flattening of curves (2-10Y spread narrowing) after reaching their historical maximums (near 170bp for bonds and near 130bp for IRS). What is more, yield spread between Polish 10Y Bond and its German counterpart narrowed significantly (below 240bp at year-end, the lowest level since late October).
- Volatility on the markets remained high at the beginning of the new year. Supply side dominated due to uncertainty about pension funds' activity on the debt market this month (a possibility of buying to reach a required limit). However, recent yields increase (in particular on mid and long end of curve) should attract non-residents' interest or other domestic investors (particularly banks). The front end of curves should remain well anchored due to the softer-than-expected inflation pressure.
- In the upcoming months, the global sentiment will be the most important factor due to increased role of non-residents after the overhaul of the pension system. Therefore, uncertainty about the pace of further reduction in QE3 program by Fed might put negative pressure on the Polish bonds, particularly on the long-end.



Spread 2-10Y (in bp)	T-bonds	IRS
3Q 2013	145	103
4Q 2013	132	123

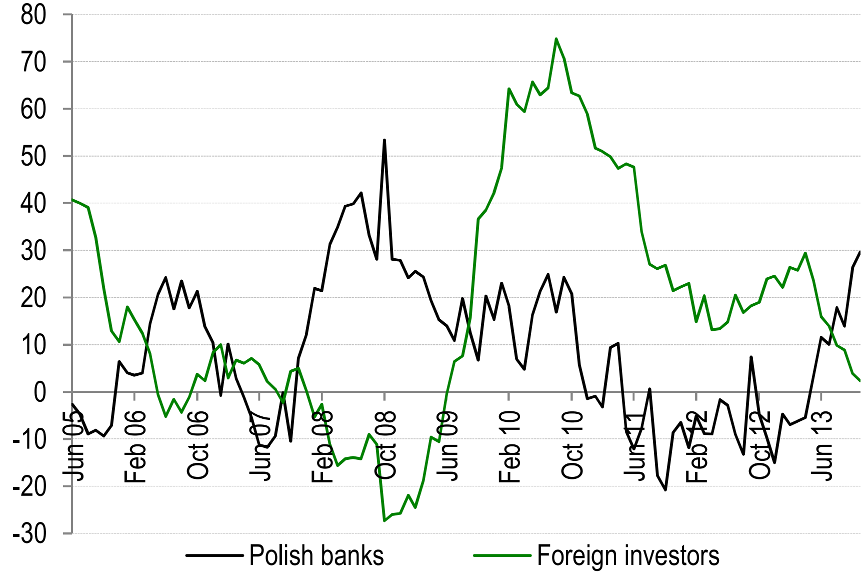


Sources: Reuters, CB, BZ WBK

Demand Corner: Foreigners still on the selling side

- November was the 2nd month in a row when foreign investors were reducing their holdings of PLN-denominated marketable debt. This time, they sold bonds of nominal value PLN1.5bn and their portfolio was worth PLN192.1bn, the lowest amount since December 2012. Within this group, non-financial institutions and non-bank financial sector contributed most to this reduction (by PLN1.1bn and PLN1.5bn, respectively), while foreign banks bought bonds worth nearly PLN1.1bn. Overall, foreign investors sold mainly new 2Y benchmark (PLN1.3bn of OK0116), while there was a net buying of coupon-bonds (DS and PS series) maturing till 2018 (ca. PLN400m).
- Private pension funds increased their holdings for the 8th month in a row amid preparations for transferring government bonds to the public pension system.
- It is also worth to mention that holdings of Polish banks posted the most considerable increase since June 2013 – by PLN7.8bn.
- Due to changes described above, the share of debt held by domestic investors rose above 67%, to the highest level since May 2012.

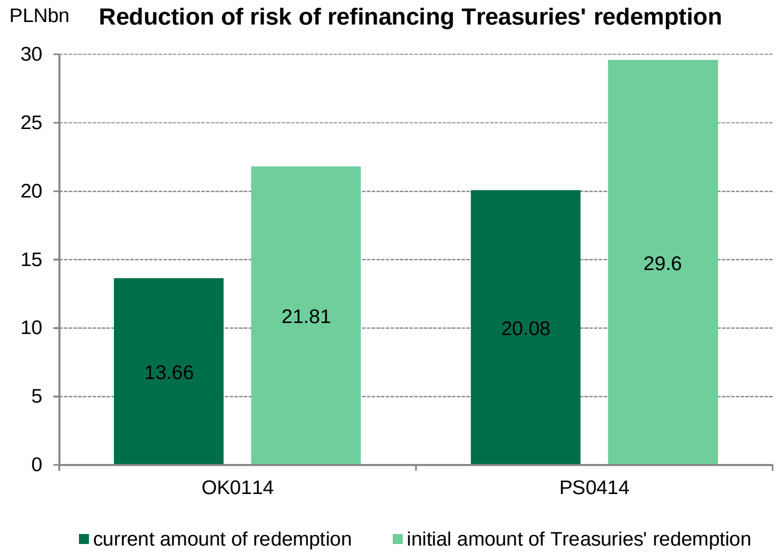
Annual percentage change of Polish marketable, PLN bonds holdings



Sources: MF, BZ WBK

Supply Corner: Strong start of 2014

- Poland's Ministry of Finance has started the new year well-secured. At the end of 2013 the Ministry financed over 25% of the 2014 borrowing needs thanks to pre-financing process. Due to both bond swap and buy-back the Ministry reduced refinancing risk connected with T-bonds' redemptions in 2014 (see chart).
- There are two auctions scheduled on the domestic market this month. Offer amounts to PLN8-16bn in total and includes not only new and current benchmarks, but also off-the-run instruments. High supply on the domestic market in January is in line with expectations, taking into account inflows from redemptions and interest payments worth PLN15.2bn in total.
- In January-March, the Ministry will offer T-bonds on the domestic market worth PLN25-35bn (5-6 auctions) and plans only one switch tender (March), depending on market situation. As regards foreign financing the Ministry assumes credit worth €0.5-0.6bn from IFIs and issues of bond denominated in EUR or USD. All in all, the Ministry wants to secure 50-60% of borrowing needs at the end of 1Q 2014, making plans to cover borrowing needs in 100% at the end of July feasible.



Auctions schedule for January 2014

Auction date	Settlement date	T-bonds	Expected supply
9 Jan 2014	13 Jan 2014	PS0718 / WZ0124	PLN3.0-5.0bn
23 Jan 2014	27 Jan 2014	OK0716* / WZ0119 / off-the-run T-bonds	PLN5.0-10.0bn

** only if not offered on 9th January, 2014*

Sources: MF, BZ WBK

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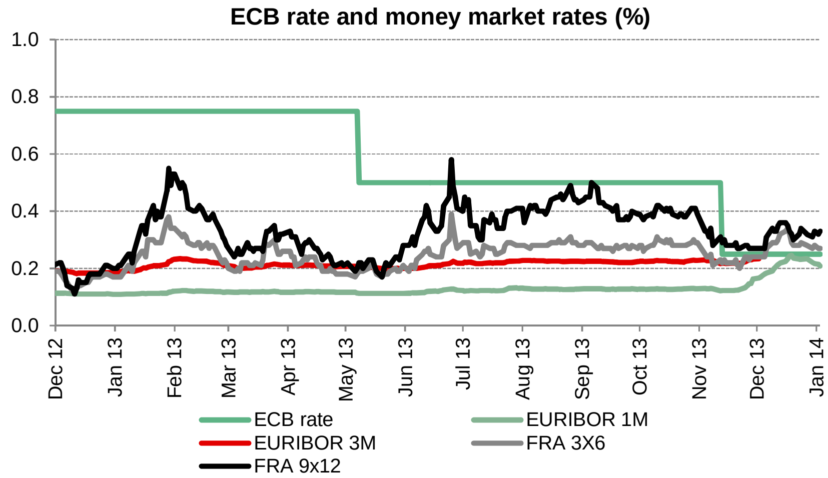
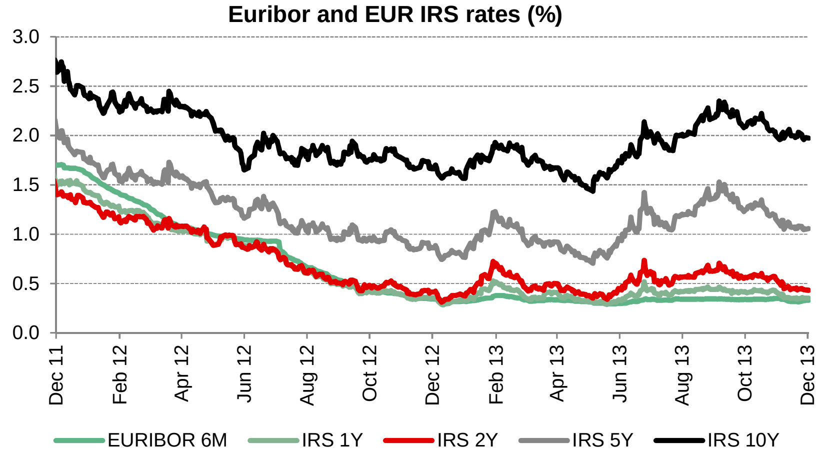
International Money Market and IRS: Muted upward trend in rates

- The December's FOMC decision to reduce QE3 program by $10bn starting from January plus the better macro data, suggesting that the recovery has strengthened not only in the US, but also in the euro zone, triggered a further increase in money market and IRS rates. Muted upward trend in EURIBOR is also supported by repayment LTRO borrowings by euro area banks (over €400bn repaid so far). On the other hand low CPI inflation (far away from the ECB's target) and still dovish ECB's rhetoric limit rates growth.
- At the same time, euro zone IRS and US IRS shifted up by 10-30bp and by 5-20bp, respectively.
- The euro area economic recovery implies reduced pressure on the ECB at the meeting this week. However, we believe that the ECB will uphold its dovish rhetoric, which together with forward guidance (assuming further actions if necessary) should help to keep EURIBOR rates under control.
- January's FOMC meeting may be more interesting. However, we do not expect the Fed to diverge from the tapering path presented at its December's meeting. Notwithstanding, as long as the Fed keeps strong forward guidance, ensuring low rates for some time, growth of LIBOR rates should be limited.

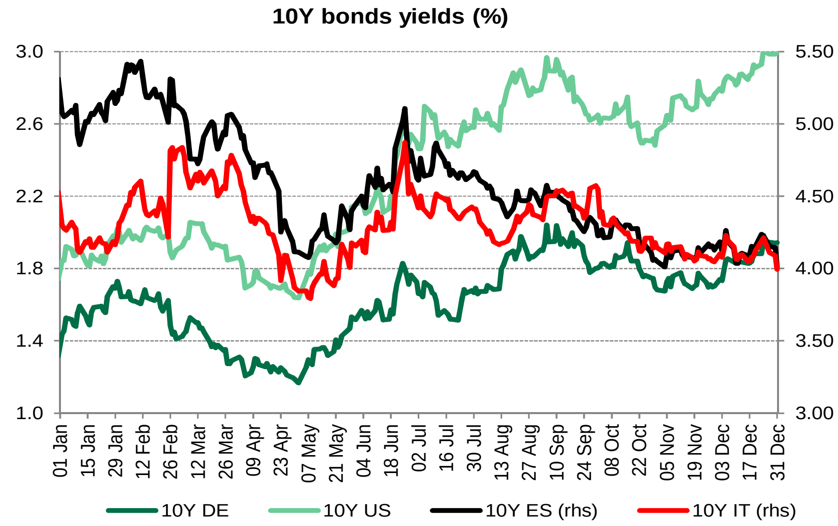


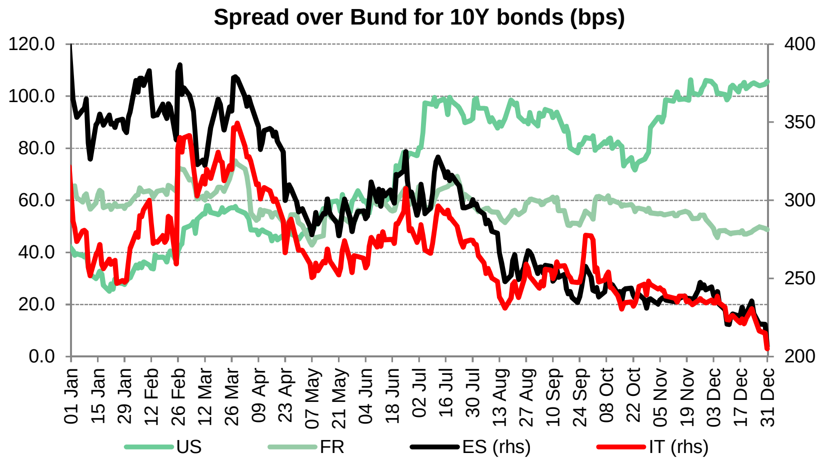


Sources: Thomson Reuters, ECB, Fed, BZ WBK

International Bond Market: Stronger fundamentals of the euro peripherals support bonds

- The FOMC decided to gradually start reducing the pace of its quantitative easing (by $10bn per month from January 2014). In contrast with what happened over the summer the market was relatively well prepared for a such decision. The U.S. Treasury yield increases were moderate (6-10bp in 5-10Y segment of the curve after announcing). However, the better-than-expected macro data releases temporarily pushed yield of 10Y USD slightly above 3%, and 10Y Bunds near 2%.
- Market sentiment has continued to be positive for the euro peripherals debt as released macro data show further strengthening in their fundamentals. Consequently, spread over Bunds in 10Y sector narrowed significantly. What is more the start of the new year was favourable for peripheral bonds due to better than expected December's PMI readings. It resulted in decrease of yields below 4% for both Italian and Spanish 10Y benchmarks (first time since 4Q 2010).
- We expect core bond yields to continue to edge higher, but the pace of yield increases should be muted as both Fed and the ECB maintain their forward guidance, ensuring low rates for some time (at least until 2015 or longer). As a consequence yield curves should remain steep (short-term rates will remain firmly anchored by central banks' guidance). As regards peripheral countries yields might continue gradual decline due to further strengthening of economic fundamentals.



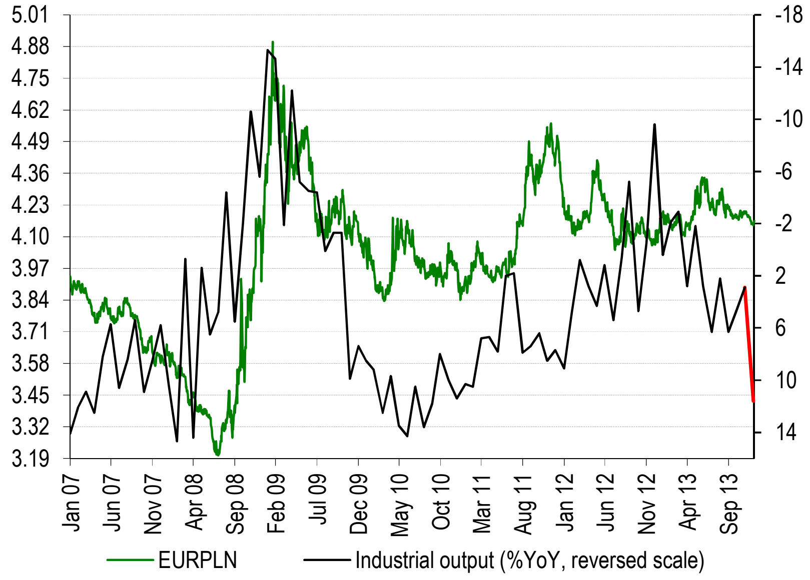


Sources: Thomson Reuters, BZ WBK

Foreign Exchange Market: Polish data may help the zloty

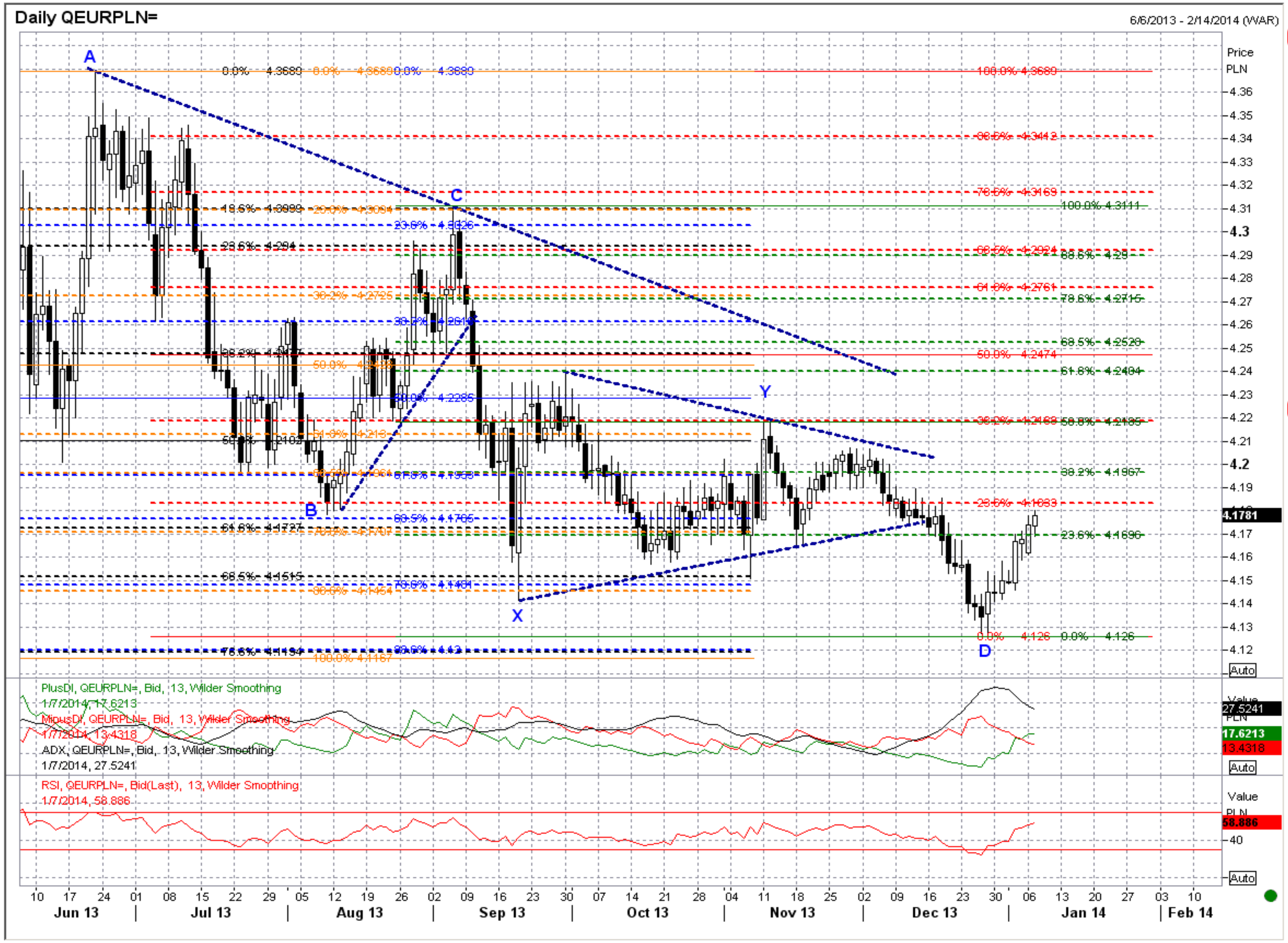
- Last month we said that the range trading of EURPLN is narrowing gradually and some stronger move may be soon observed. During the year-end period the zloty gained quite visibly versus the euro due to rising stock prices and activity of the Polish state-owned BGK bank. EURPLN declined temporarily below local low at c.4.14 established in mid-September, but in early 2014 it rebounded back to nearly 4.17.
- According to Bloomberg, the zloty was the 4th best performing emerging market currency vs. the euro and the dollar in 2013. Still, after the depreciation seen at the beginning of the new year, the zloty is underperforming LatAm currencies, Turkish lira or Russian rouble, which are doing better vs. the euro and the dollar.
- This correction might have been to some extent driven by the weaker than expected data on manufacturing PMI for Poland, that dropped surprisingly in December. However, our forecasts for retail sales, industrial output and CPI are above market consensus and should be enough to confirm that the economic revival in Poland is on track and support the zloty.
- We forecast average EURPLN at around 4.15 in January, but move towards 4.18 in first half of the month brings an upward risk to this forecast.

EURPLN and Polish industrial output



Sources: BZ WBK, Reuters, CSO

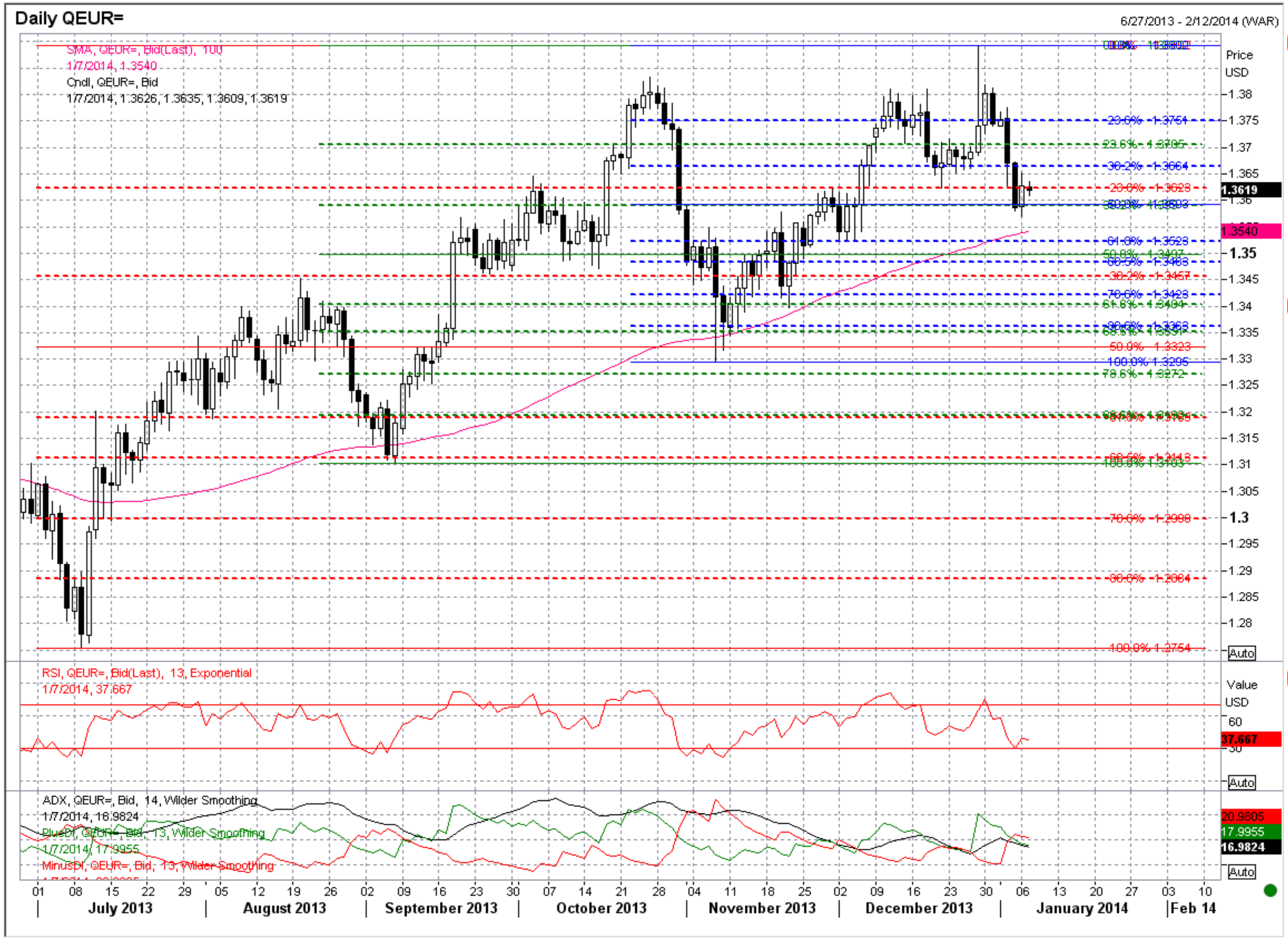
FX Technical Analysis Corner: Room for increase?



- EURPLN has finally left the narrowing range trading. The exchange rate tested the strong support at c.4.14 consisting of a several Fibonacci retracements, but did not manage to stay below for longer.
- A few circumstances suggest that some upward move may be continued: AB/CD~1 and CX/YD~2. Additionally, RSI gave a clear buy signal for the first time since August 2012 (it proved very correct then). First strong resistance is at 4.22.

Sources: BZ WBK, Reuters

FX Technical Analysis Corner: Close to first support



- EURUSD managed to break c.1.363 at the second attempt. However, even two attempts were not enough to break the peak at c.1.383.
- The downward move paused recently at support consisting of two Fibo retracement levels. The exchange rate stays above 100-day MA and it is too early to announce termination of the upward trend.
- Next support is at 1.35, resistance at 1.383.

Sources: Reuters, BZ WBK

Macroeconomic Forecasts

Poland		2011	2012	2013	2014	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14
GDP	PLNbn	1,523.2	1,595.2	1,632.0	1,702.4	377.9	395.7	404.3	454.1	391.8	412.9	422.1	475.6
GDP	%YoY	4.5	1.9	1.5	3.1	0.5	0.8	1.9	2.6	2.7	3.2	3.3	3.3
Domestic demand	%YoY	3.6	-0.2	-0.2	2.2	-0.9	-1.7	0.5	0.9	1.0	1.9	2.3	3.4
Private consumption	%YoY	2.6	0.8	0.7	1.8	0.0	0.2	1.0	1.5	1.5	1.7	2.0	2.2
Fixed investments	%YoY	8.5	-0.8	-0.5	3.7	-2.1	-3.2	0.6	1.0	1.0	2.0	3.0	6.0
Unemployment rate [a]	%	12.5	13.4	13.6	12.8	14.3	13.2	13.0	13.6	13.8	13.0	12.6	12.8
Current account balance	EURm	-18,519	-14,191	-5,119	-833	-2,313	486	-2,072	-1,220	-209	1,053	-412	-1,265
Current account balance	% GDP	-5.0	-3.7	-1.3	-0.2	-3.1	-2.3	-1.9	-1.3	-0.8	-0.6	-0.2	-0.2
General government balance	% GDP	-5.0	-3.9	-4.4	-3.6	-	-	-	-	-	-	-	-
CPI	%YoY	4.3	3.7	0.9	1.4	1.3	0.5	1.1	0.8	1.0	1.4	1.2	1.9
CPI [a]	%YoY	4.6	2.4	0.8	2.0	1.0	0.2	1.0	0.8	1.1	1.6	1.5	2.0
CPI excluding food and energy prices	%YoY	2.4	2.2	1.2	1.8	1.2	1.0	1.4	1.3	1.7	1.8	1.6	2.0

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates; [a] at the end of period * without changes in pension system

Interest Rate and FX Forecasts

Poland		2011	2012	2013	2014	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14
Reference rate [a]	%	4.50	4.25	2.50	3.00	3.25	2.75	2.50	2.50	2.50	2.50	2.75	3.00
WIBOR 3M	%	4.54	4.91	3.02	2.88	3.77	2.96	2.70	2.66	2.70	2.73	2.92	3.17
Yield on 2-year T-bonds	%	4.81	4.30	2.98	3.26	3.29	2.77	2.98	2.88	2.99	3.10	3.35	3.58
Yield on 5-year T-bonds	%	5.44	4.53	3.46	3.84	3.49	3.09	3.63	3.64	3.69	3.73	3.92	4.03
Yield on 10-year T-bonds	%	5.98	5.02	4.04	4.64	3.95	3.58	4.26	4.36	4.45	4.58	4.70	4.82
2-year IRS	%	4.98	4.52	3.10	3.44	3.43	2.81	3.14	3.04	3.11	3.28	3.58	3.80
5-year IRS	%	5.24	4.47	3.51	3.95	3.52	3.08	3.76	3.68	3.72	3.82	4.05	4.22
10-year IRS	%	5.33	4.56	3.86	4.46	3.76	3.41	4.13	4.14	4.22	4.37	4.53	4.70
EUR/PLN	PLN	4.12	4.19	4.20	4.06	4.16	4.20	4.25	4.19	4.14	4.08	4.04	3.99
USD/PLN	PLN	2.96	3.26	3.16	2.96	3.15	3.22	3.21	3.08	3.02	3.00	2.95	2.87
CHF/PLN	PLN	3.34	3.47	3.41	3.23	3.38	3.41	3.44	3.40	3.34	3.26	3.21	3.11
GBP/PLN	PLN	4.75	5.16	4.94	4.85	4.88	4.94	4.97	4.98	4.90	4.83	4.84	4.84

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates; [a] at the end of period

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Economic Calendar and Events

Date		Event:	Note:
8-Jan	**PL**	**MPC Meeting – interest rate decision**	**We expect the MPC to keep interest rates unchanged**
9-Jan	**PL**	**Bond auction of PS0718 and WZ0124**	**Offer: PLN3.0-5.0bn**
	EZ	ECB Meeting – interest rate decision	-
	SP	Bond auction	-
15-Jan	**PL**	**CPI for December**	**Our forecast: 0.8%YoY**
	DE	Auction of 5Y benchmark	Offer: €5bn
16-Jan	**PL**	**Core inflation for December**	**We predict core CPI after excluding food and energy prices at 1.3%YoY**
20-Jan	**PL**	**Employment and wages for December**	**We expect employment to increase by 0.3%YoY and wages growth at 2.7%YoY**
21-Jan	**PL**	**Industrial output and PPI for December**	**Our forecast of industrial output is 11.6%YoY. We predict PPI at -1%YoY**
	HU	MPC Meeting – interest rate decision	-
22-Jan	DE	Auction of 2Y benchmark	Offer: €4bn
23-Jan	**PL**	**Bond auction**	**Offer: PLN5.0-10.0bn**
TBA	**PL**	**Retail sales for December**	**Our forecast is 7.3%YoY**
29-Jan	US	FOMC Meeting – interest rate decision	-
	DE	Auction of 10Y benchmark	Offer: €5bn
5-Feb	**PL**	**MPC Meeting – interest rate decision**	**We expect the MPC to keep interest rates unchanged**
6-Feb	EZ	ECB Meeting – interest rate decision	-

Annex

1. Domestic markets performance
2. Polish bonds: supply recap
3. Polish bonds: demand recap
4. Euro zone bonds: supply recap
5. Poland vs other countries
6. OFE overhaul
7. Central bank watch

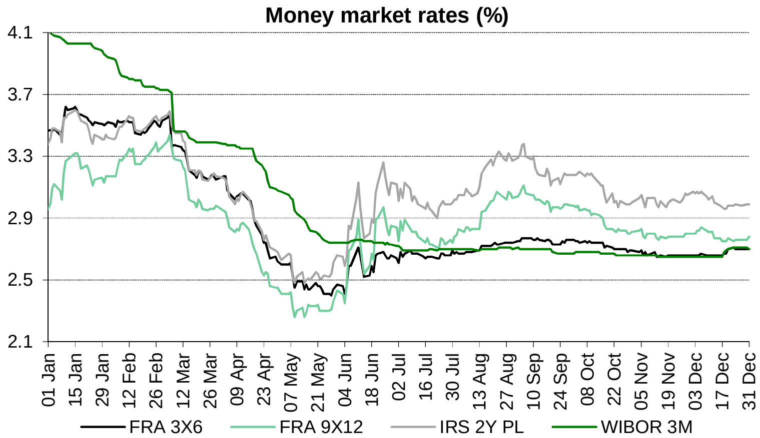
1. Domestic markets performance

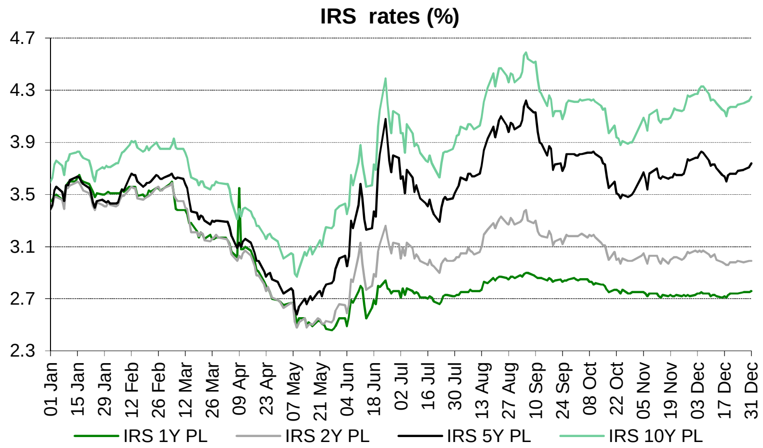
Money market rates (%)

	Reference rate (%)	Polonia (%)	WIBOR (%) 1M	WIBOR (%) 3M	WIBOR (%) 6M	WIBOR (%) 12M	OIS (%) 1M	OIS (%) 3M	OIS (%) 6M	OIS (%) 12M	FRA (%) 1x4	FRA (%) 3x6	FRA (%) 6x9	FRA (%) 9x12
End of December	**2.50**	**2.40**	**2.61**	**2.71**	**2.72**	**2.75**	**2.38**	**2.38**	**2.40**	**2.48**	**2.70**	**2.70**	**2.71**	**2.76**
Last 1M change (bp)	0	-26	1	5	2	0	-3	-1	-1	-2	3	1	-2	-5
Last 3M change (bp)	0	2	2	4	1	0	2	-3	-2	-8	-2	-6	-14	-22
Last 1Y change (bp)	-175	-134	-160	-140	-136	-123	-165	-145	-98	-70	-116	-76	-36	-18

Bond and IRS market (%)

	BONDS 2Y	BONDS 5Y	BONDS 10Y	IRS 2Y	IRS 5Y	IRS 10Y	Spread BONDS / IRS (bp) 2Y	Spread BONDS / IRS (bp) 5Y	Spread BONDS / IRS (bp) 10Y
End of December	**3.00**	**3.61**	**4.32**	**2.99**	**3.71**	**4.22**	**1**	**-10**	**10**
Last 1M change (bp)	17	11	15	-1	19	29	18	-8	-14
Last 3M change (bp)	-3	-23	-15	-19	-10	1	16	-13	-16
Last 1Y change (bp)	-8	41	60	-37	35	65	29	6	-5





Sources: Reuters, BZ WBK

2. Polish bonds: supply recap

Total issuance in 2014 by instruments (in PLNm, nominal terms)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
T-bonds auction	15,000	7,000	7,000	13,000	10,000	5,000	5,000	5,000	5,000	5,000	3,000	2300	82,300
T-bills auction													0
Retail bonds	150	170	190	170	170	170	170	180	170	175	185	176	2,076
Foreign bonds/credits	5,374	4,100	5100				5450			3200			23,224
Prefinancing and financial resources at the end of 2013	25,000												25,000
Total	**45,524**	**11,270**	**12,290**	**13,170**	**10,170**	**5,170**	**10,620**	**5,180**	**5,170**	**8,375**	**3,185**	**2476**	**132,600**
Redemption	16,497	5,613	2,230	20,147	116	60	11,612	1,793	2,514	83	816	91	61,571
Net inflows	**29,027**	**5,657**	**10,060**	**-6,977**	**10,054**	**5,110**	**-992**	**3,387**	**2,656**	**8,292**	**2,369**	**2,385**	**71,029**
Rolling over T-bonds													**0**
Buy-back of T-bills/ FX-denominated bonds													**0**
Total	**29,027**	**5,657**	**10,060**	**-6,977**	**10,054**	**5,110**	**-992**	**3,387**	**2,656**	**8,292**	**2,369**	**2,385**	**71,029**
Coupon payments from domestic debt	*1,546*			*6,917*			*1,552*		*1,497*	*9,062*			*20,575*

Note: Our forecasts – shaded area

Sources: MF, BZ WBK

2. Polish bonds: supply recap (cont.)

Schedule Treasury Securities redemption by instruments (in PLNm)

	Bonds	Bills	Retail bonds	Total domestic redemption	Foreign Bonds/Credits	Total redemptions
January	13,660		155	**13,815**	2,681	**16,497**
February			171	**171**	5,442	**5,613**
March			117	**117**	2,113	**2,230**
April	20,080		66	**20,147**		**20,147**
May			116	**116**		**116**
June			60	**60**		**60**
July	10,287		89	**10,376**	1,236	**11,612**
August			198	**198**	1,594	**1,793**
September			76	**76**	2,438	**2,514**
October			83	**83**		**83**
November			171	**171**	645	**816**
December			91	**91**		**91**
Total 2014	44,027		1,395	**45,422**	16,149	**61,571**
Total 2015	90,137		1,357	**91,494**	15,993	**107,487**
Total 2016	87,720		927	**88,647**	17,396	**106,043**
Total 2017	71,444		795	**72,239**	12,566	**84,805**
Total 2018	80,994		849	**81,843**	14,396	**96,239**
Total 2019+	185,558		3,136	**188,694**	135,784	**324,478**

Sources: MF, BZ WBK

2. Polish bonds: supply recap (cont.)

Schedule wholesale bonds redemption by holders (data at the end of November 2013, in PLNm)

	Foreign investors	Domestic banks	Insurance Funds	Pension Funds	Mutual Funds	Individuals	Non-financial sector	Other	Total
Q1 2014	8,503	5,489	2,274	612	727	108	16	2,023	19,753
Q2 2014	11,892	4,980	3,184	2,859	828	86	72	2,127	26,028
Q3 2014	5,512	2,452	932	263	835	139	12	239	10,385
Q4 2014	0	0	0	0	0	58	7	13	77
Total 2014	**25,907**	**12,921**	**6,390**	**3,734**	**2,390**	**392**	**106**	**4,402**	**56,242**
	46%	**23%**	**11%**	**7%**	**4%**	**1%**	**0%**	**8%**	**100%**
Total 2015	35,291	26,178	8,131	7,540	7,475	221	275	5,096	90,208
	39%	29%	9%	8%	8%	0%	0%	6%	100%
Total 2016	29,034	14,695	6,649	23,122	10,181	76	401	4,963	89,119
	33%	16%	7%	26%	11%	0%	0%	6%	100%
Total 2017	24,380	12,070	5,492	17,394	8,361	48	136	3,564	71,444
	34%	17%	8%	24%	12%	0%	0%	5%	100%
Total 2018	14,137	22,744	2,860	29,359	7,741	73	157	3,922	80,994
	17%	28%	4%	36%	10%	0%	0%	5%	100%
Total 2019+	63,321	29,916	22,624	47,091	14,849	183	260	8,695	186,939
	34%	16%	12%	25%	8%	0%	0%	5%	100%

Sources: MF, BZ WBK

3. Polish bonds: demand recap

Holders of marketable PLN bonds

	Nominal value (PLN, bn)				Nominal value (PLN, bn)			% change in November			Share in TOTAL (%) in November
	End Nov'13	End Oct'13	End Jun'13	End Dec 2012	End 3Q 2012	End 2Q 2012	End 1Q 2012	MoM	3-mth	YoY	
Domestic investors	391.4	380.6	369.4	337.5	341.8	352.9	361.4	2.84	2.03	15.16	67.1 (0.8pp)
Commercial banks	118.5	110.7	113.9	87.8	102.0	102.1	110.9	7.02	6.67	29.64	20.3 (1.0pp)
Insurance companies	52.1	51.5	53.1	52.8	54.7	57.0	54.3	1.33	-4.08	-3.67	8.9 (-0.1pp)
Pension funds	128.2	126.5	117.7	117.4	116.7	120.3	120.7	1.38	6.04	7.48	22.0
Mutual funds	51.0	49.6	46.5	41.7	32.5	33.0	31.3	2.90	4.20	31.49	8.7 (0.1pp)
Others	41.5	42.4	38.3	37.8	35.9	40.5	44.3	-2.0	7.3	14.6	7.1 (-0.3pp)
Foreign investors*	192.1	193.6	201.8	189.9	184.2	174.0	163.2	-0.79	-2.93	2.33	32.9 (-0.8pp)
Banks	28.2	27.2	32.3	28.4	27.8	22.6	24.3	3.91	-1.23	1.40	4.8 (0.1pp)
Non-bank fin. sector	156.2	157.7	160.1	153.1	147.5	143.1	131.7	-0.97	-2.12	3.14	26.8 (-0.7pp)
Non-financial sector	4.3	5.4	5.3	5.2	5.6	5.2	4.4	-19.74	-25.15	-16.65	0.7 (-0.2pp)
TOTAL	583.5	574.2	571.2	527.4	526.0	526.9	524.7	1.61	4.65	10.60	100

**Total for Foreign investors does not match sum of values presented for sub-categories due to omission of irrelevantly small group of investors.* *Sources: MF, BZ WBK*

4. Euro zone bonds: supply recap

Euro zone's issuance plans and completion in 2014 (€ bn)

	Total redemptions	Deficit	Borrowing needs	Expected bond supply	% of completion (YtD*)
Austria	23.4	4.3	27.7	24.7	-
Belgium	21.8	9.8	31.6	30.0	-
Finland	6.9	4.8	11.7	11.7	-
France	105.0	70.2	175.2	174.0	-
Germany	144.0	-	144	144.0	-
Greece	*16.8*	*5.6*	-	-	-
Ireland	6.9	7.7	14.6	14.6	-
Italy	187.8	27.6	235.4	235.4	-
Netherlands	32.0	15.9	47.9	45.9	-
Portugal	11.4	7.4	18.8	7.2	-
Spain	68.2	36.7	141.3	141.3	-
Total	**624.2**	**189.9**	848.2	**828.8**	**-**

Sources: Eurostat, BZ WBK

**/ YtD (year calendar) data for 2014*

5. Poland vs other countries

Main macroeconomic indicators (European Commission's forecasts)

	GDP (%)		Inflation (HICP, %)		C/A balance (% of GDP)		Fiscal Balance (% of GDP)		Public Debt (% of GDP)	
	2013F	2014E	2013F	2014E	2013F	2014E	2013F	2014E	2013F	2014E
Poland	**1.3**	**2.5**	**1.0**	**2.0**	**-1.5**	**-1.3**	**-4.8**	**4.6**	**58.2**	**51.0**
Czech Republic	-1.0	1.8	1.4	0.5	-1.6	-1.1	-2.9	-3.0	49.0	50.6
Hungary	0.7	1.8	2.1	2.2	3.0	2.7	-2.9	-3.0	80.7	79.9
EU	0.0	1.4	1.7	1.6	1.6	1.7	-3.5	-2.7	89.7	90.2
Euro area	-0.4	1.1	1.5	1.5	2.7	2.9	-3.1	-2.5	95.5	95.9
Germany	0.5	1.7	1.7	1.7	7.0	6.6	0.0	0.1	79.6	77.1

Main market indicators (%)

	Reference rate (%)		3M market rate (%)		10Y yields (%)		10Y Spread vs Bund (bp)		CDS 5Y	
	2012	2013	2012	end of Dec	2012	end of Dec	2012	end of Dec	2012	end of Dec
Poland	**4.25**	**2.50**	**4.11**	**2.71**	**3.72**	**4.32**	**241**	**238**	**80**	**79**
Czech Republic	0.05	0.05	0.18	0.05	1.86	2.53	54	58	63	60
Hungary	5.75	3.00	5.75	2.99	6.23	5.71	492	377	269	256
Euro area	0.75	0.25	0.19	0.29						
Germany					1.32	1.94			39	26

Sources: EC – Autum 2013, stat offices, central banks, Reuters, BZ WBK

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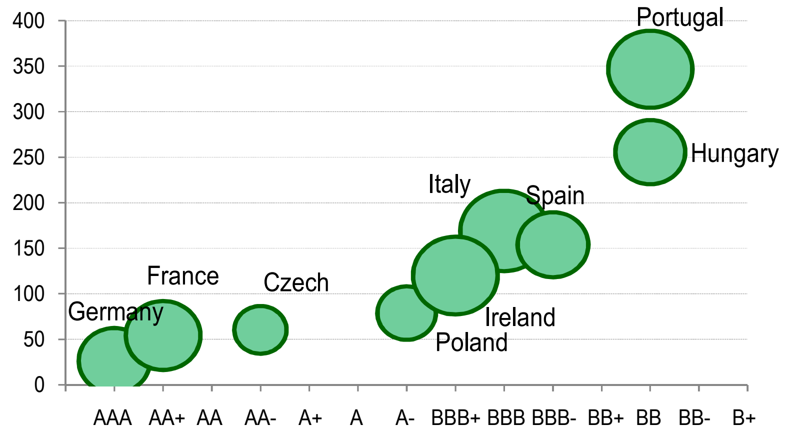
Grupa Santander

5. Poland vs other countries (cont.)

Sovereign ratings

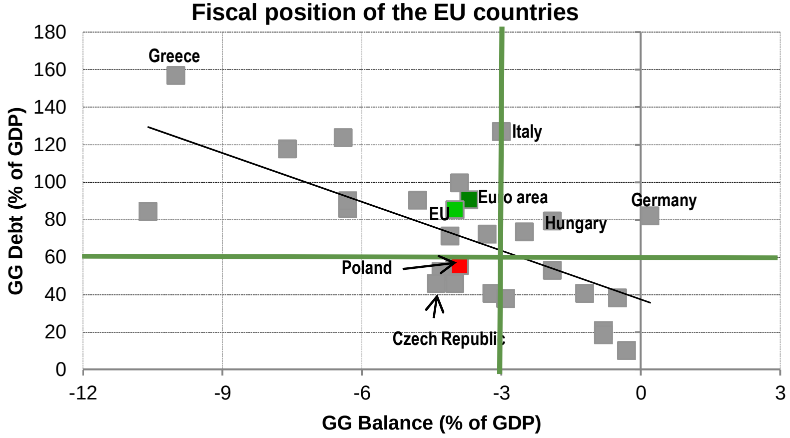
	S&P		Moody's		Fitch	
	rating	outlook	rating	outlook	rating	outlook
Poland	A-	stable	A2	stable	A-	stable
Czech	AA-	stable	A1	stable	A+	stable
Hungary	BB	stable	Ba1	negative	BB+	stable
Germany	AAA	stable	Aaa	negative	AAA	stable
France	AA	stable	Aa1	negative	AA+	negative
UK	AAA	negative	Aa1	negative	AA+	stable
Greece	B-	stable	Caa3	stable	B-	stable
Ireland	BBB+	positive	Ba1	negative	BBB+	stable
Italy	BBB	negative	Baa2	negative	BBB+	negative
Portugal	BB	negative	Ba3	stable	BB+	negative
Spain	BBB-	stable	Baa3	stable	BBB	stable

5Y CDS rates vs credit ranking according to S&P

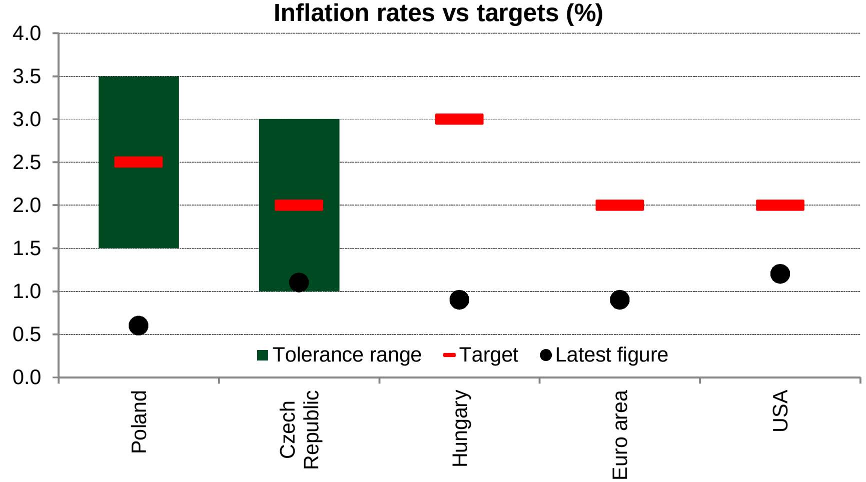


Note: Size of bubbles reflects the debt/GDP ratio

Fiscal position of the EU countries



Inflation rates vs targets (%)



Source: rating agencies, Reuters, BZ WBK, EC

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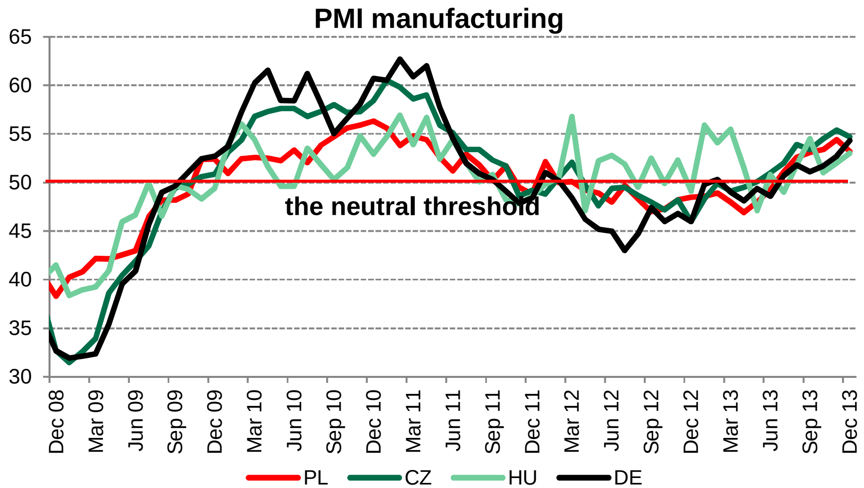
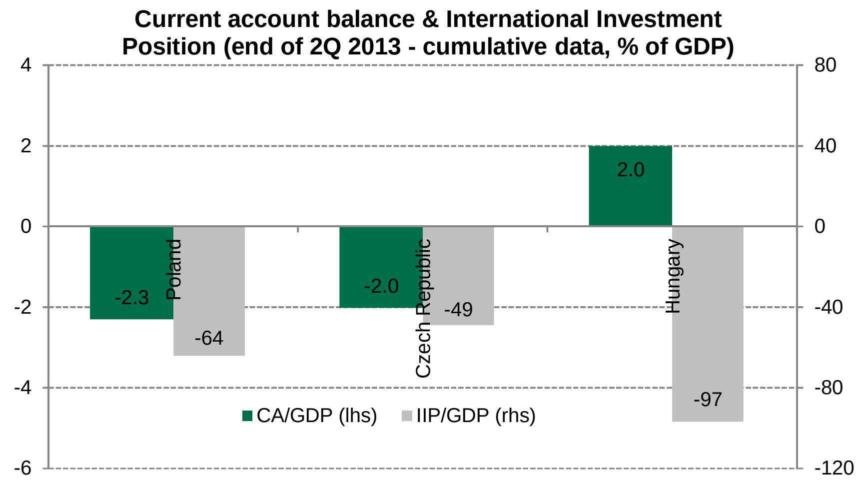
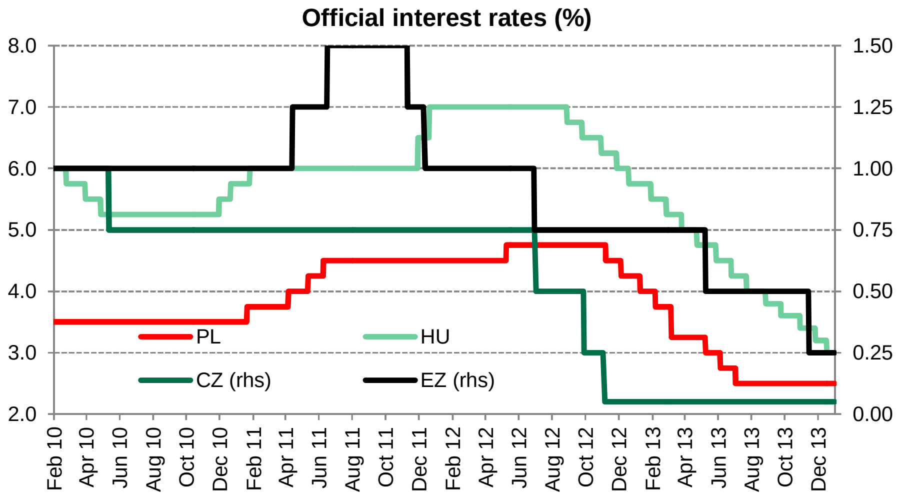
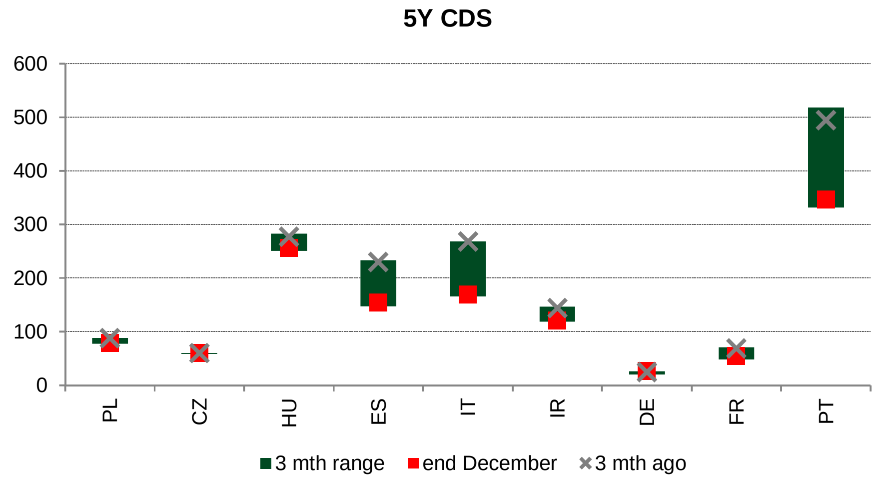
5. Poland vs other countries (cont.)









Source: Markit, Eurostat, central banks, Reuters, BZ WBK, EC

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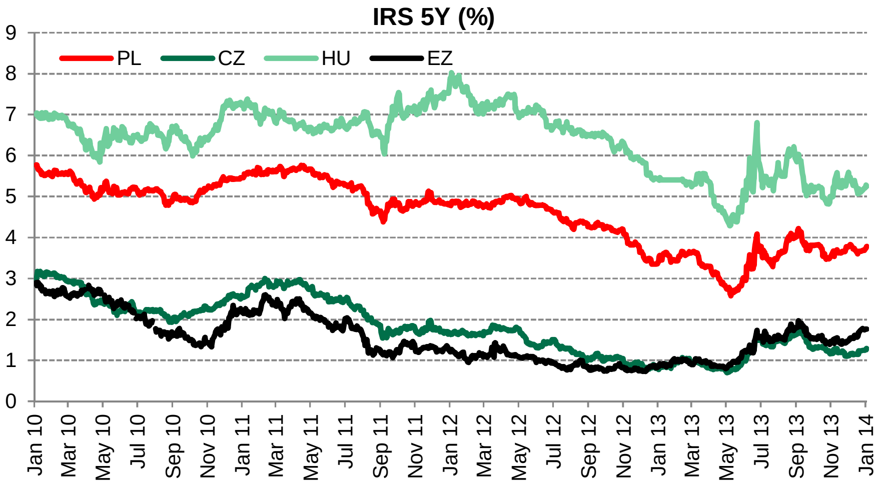
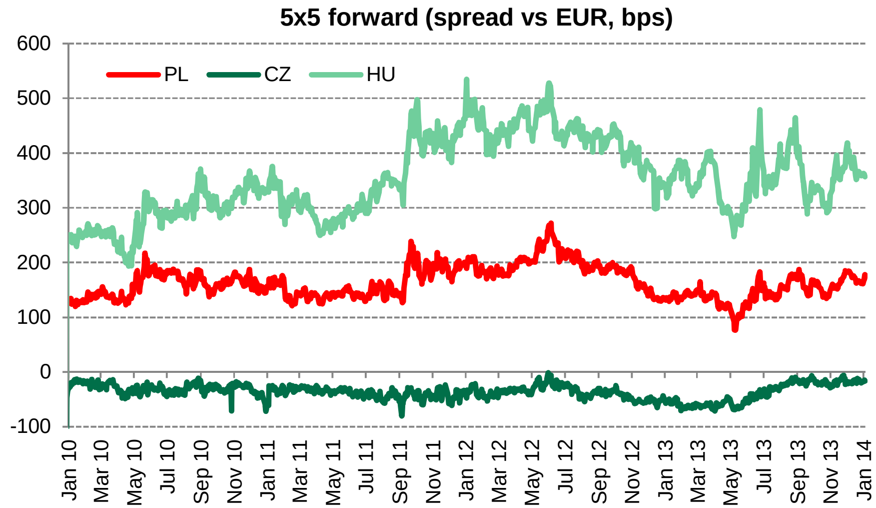
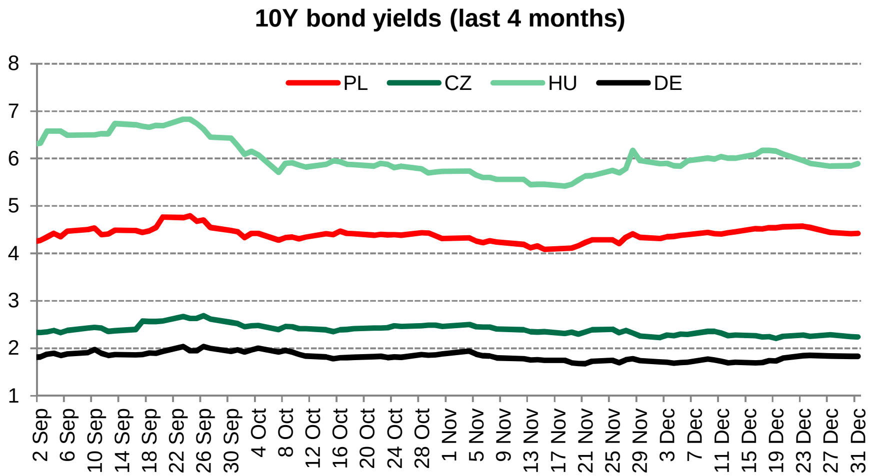
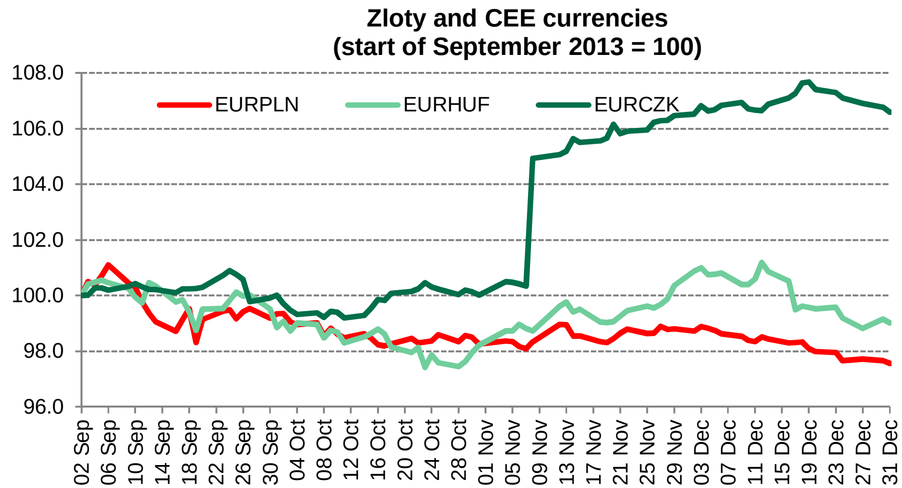
5. Poland vs other countries (cont.)









Source: Reuters, BZ WBK

6. OFE overhaul

Structure of OFE's investment portfolios (end-November 2013)

Fund	Assets (PLNbn)	Asset allocation (%)							
		Bonds*	change MoM (pp)	Equities	change MoM (pp)	Deposits	change MoM (pp)	Other	change MoM (pp)
ING	73.7	44.7%	-0.6	44.8%	0.2	6.3%	0.5	4.2%	-0.1
Aviva	68.3	47.2%	-0.1	43.2%	0.3	6.3%	0.2	3.3%	-0.4
PZU	41.0	46.8%	0.2	44.8%	0.4	3.4%	0.0	5.0%	-0.6
Amplico	24.4	48.7%	1.4	45.2%	0.5	2.0%	-4.7	4.1%	2.8
AXA	19.1	50.0%	0.0	40.5%	0.6	4.4%	-0.5	5.1%	-0.1
Generali	15.3	51.9%	0.6	41.0%	0.2	3.5%	-0.2	3.6%	-0.6
Nordea	13.8	50.0%	0.0	42.5%	0.6	1.4%	-0.5	6.1%	-0.1
PKO BP	13.5	51.2%	0.1	43.4%	0.2	3.9%	-0.4	1.4%	0.1
AEGON	12.9	43.6%	0.7	42.6%	0.2	8.6%	1.4	5.2%	-2.3
Allianz	9.3	48.0%	0.3	42.7%	0.3	1.8%	-1.0	7.5%	0.5
Pocztylion	5.8	49.4%	2.6	44.3%	0.8	2.5%	-4.4	3.8%	1.0
Pekao	4.6	48.2%	0.5	44.5%	-0.6	4.1%	0.3	3.3%	-0.2
Warta	4.1	50.7%	0.1	43.2%	0.8	3.2%	-1.4	2.9%	0.5
Total	**305.8**	**47.4%**	**0.1**	**43.7%**	**0.3**	**4.8%**	**-0.4**	**4.2%**	**-0.1**

* State treasuries, road bonds and state-guaranteed bonds

Source: BZ WBK Brokerage

Bank Zachodni WBK
Grupa Santander

6. OFE overhaul (cont.)

OFE's holding - the biggest nominal value plus current 2Y, 5Y and 10Y benchmarks (end-November 2013)

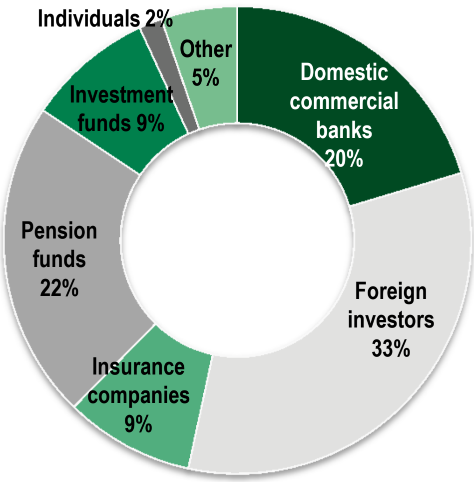
	OK0116	IZ0816	PS1016	WZ0117	PS0417	WZ0118	PS0418	PS0718	DS1019	DS1020	WZ0121	DS1021	IZ0823	DS1023
Nominal value held by OFE (PLNm)	3,163	8,577	6495	8,475	5,415	8,924	12,982	7,452	7,176	5,573	6,564	5,138	10,315	3,794
Share held by OFE in series outstanding	12%	55%	28%	34%	27%	33%	40%	35%	28%	24%	24%	24%	71%	16%
Share held by foreign investors in series outstanding	28%	33%	24%	20%	34%	3%	25%	25%	41%	46%	16%	42%	14%	37%
Share held by biggest holder	**32%**	**17%**	15.0%	**16%**	12%	15%	2%	2%	12%	7%	**15.0%**	13%	8%	2%
Share held by biggest foreign holder	**32%**	3%	4%	**16%**	5%	2%	2%	2%	2%	3%	**15.0%**	3%	2%	1%
Without OFE sector														
Share held by foreign investors in series outstanding	32%	**73%**	**34%**	31%	**46%**	4%	41%	38%	**56%**	**61%**	22%	**55%**	**50%**	44%
Share held by biggest holder	**36%***	6%	6%	**25%**	7%	4%	4%	3%	3%	3%	**20%**	4%	6%	1%
Share held by biggest foreign holder	**36%***	6%	6%	**25%**	7%	4%	4%	3%	3%	3%	**20%**	4%	6%	1%

Source: MF, Bloomberg, BZ WBK.   OK0116, PS0718 and DS1023 are 2Y, 5Y and 10Y benchmarks added for comparison
**percentage for individual holders exceeds share for total foreign investors group because last individual holding data is available for September, when the amount held by foreigners was clearly larger than at the end of November*

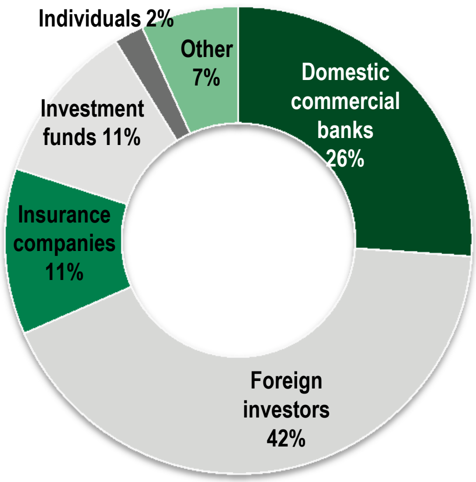
6. OFE overhaul (cont.)

Pension funds' T-bonds portfolio (in PLN m, end-November)

	OK	PS	DS	WS	WZ & IZ	Total
2013						
2014	875.3	2,858.8				3,734.1
2015	431.2	1,916.1	1,998.0		3,195.2	7,540.4
2016	3,163.3	11,381.7			8,577.1	23,122.1
2017		5,415.0	3,504.7		8,474.5	17,394.3
2018		20,434.6			8,924.0	29,358.6
2019			7,175.6		1,185.2	8,360.8
2020			5,572.9			5,572.9
2021			5,138.2		6,564.2	11,702.5
2022				1,408.5		1,408.5
2023			3,794.4		10,315.6	14,110.0
2024+				2,020.4	3,860.3	5,880.7
Total	4,469.7	42,006.2	27,183.8	3,428.9	51,096.2	128,184.9



Change of bond holders' shares without OFE sector (data at the end of November)



Sources: MF, BZ WBK

7. Central bank watch

		Last	2013	2014F	Expected changes (bp) 1M	3M	6M	Risks/Events
Euro zone	Forecast	0.25	0.25	0.25				We do not expect any significant changes in the ECB's monetary policy this month. We think that the ECB might focus more on the improvement in the economic outlook, in particular on the peripheries.
	Market implied »				-1	-1	0	
UK	Forecast	0.50	0.50	0.75				In general, macroeconomic situation will not change significantly in comparison with the previous meeting. Therefore, we expect the BoE to keep official rates unchanged in January. Further improvement in UK economy might allow the BoE to hike rates in 4Q 2014.
	Market implied »				1	5	14	
US	Forecast	0-0.25	0-0.25	0.25				Unexpectedly, FOMC at its December's meeting announced a slowdown of asset purchases from $85bn to $75bn per month starting in January. This was due to better than expected labour market data. What is more Fed strengthened its forward guidance (official rates will remain close to zero for other two years) to keep short rates from rising sharply.
	Market implied »				1	3	7	
Poland	Forecast	2.50	2.50	3.00				As the MPC stated that it would leave interest rates on hold until the end of 1H14, monetary policy will be quite uneventful in the next two quarters. A new member will join the Council this month, but this will not change the general monetary policy outlook. We foresee the Council to keep interest rates unchanged and dovish rhetoric.
	Market implied »				-1	-1	0	
Czech Republic	Forecast	0.05	0.05	0.05				We foresee also uneventful meeting in the Czech Republic. However, central bank will closely watch CPI inflation, which might decline near to 0% at the beginning of this year. Further FX intervention is still very likely this year if needed.
	Market implied »				31	28	28	
Hungary	Forecast	3.00	3.00	3.00				In line with expectations the NBH cut rates in December, trimming the official rate to 3%. Further cuts are still possible this year due to subdued CPI inflation path. But we foresee NBH to keep official rates unchanged this year.
	Market implied »				-2	-17	-12	

This analysis is based on information available until 3rd January 2014 and has been prepared by:

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