

Rates and FX Outlook

Polish Financial Market

April 2012

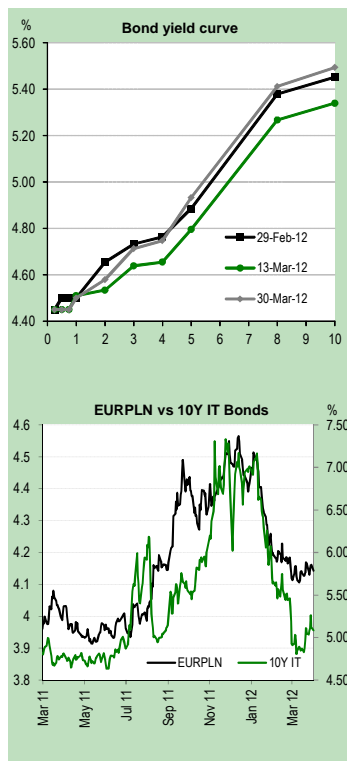


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- **Data published in Poland in recent weeks did not change the overall assessment of economic situation.** Production growth was lower than forecasted, but the positive surprise was recorded in terms of retail sales. We do not change our forecasts (updated a month ago) of GDP growth slightly below 3% with gradual slowdown throughout the year.
- **CPI inflation for February surprised on the upside (4.3%) and there are several other factors, which change the inflation path in the following months.** While previously, one could have expected that CPI inflation would reach the levels close to 3.5% in March-April, now such a scenario seems too optimistic. This is mostly due to supply-side factors such as prices of food (among others, sharp rise in eggs prices due to the EU regulation on protection of laying hens) and fuel (still elevated commodity prices). We still expect CPI inflation to go down to only moderately above 3% at the end of the year due to low demand-side pressure on prices and lagged effect of recent zloty strengthening. However, except the final months of the year, 12M CPI readings will not fall below the upper end of tolerance range around the target of 3.5%.
- **The changed inflation path in 2012 together with still hawkish rhetoric of central bankers led us to change the view on monetary policy this year.** We expect the official NBP rate to remain flat against the previous forecast of some moderate easing in monetary conditions in the second half of 2012. The comments of the MPC suggest that they pay a lot of attention to current inflation rate and this is probably connected with the fact that CPI inflation remains well above the target of 2.5% and the Council feels far from comfortable in such situation. This is even to such an extent that one cannot rule out the possibility that a few members could put a motion to HIKE interest rates soon. We do not think this is necessary and justified by economic conditions, but some of the comments are quite unambiguous. In any case, with all the things said by the MPC and with higher inflation path during the year, it will be hard for them to take a decision to cut rates later during the year even if economic slowdown continues (still, this will be rather moderate slowdown).
- **After latest inflation release the Polish fixed income market finally saw a correction and the yields moved up sharply with the most significant move in the long-end of the curve.** We expect that after this long awaited increase in yields we will see stabilisation in 5-10 year segment in the short-term. On the other hand, short-end may be under pressure due to central bankers' hawkish comments (after April's meeting), which may be offset later during the month by the releases of inflation (fall to below 4%), as well as weak production and wages figures (our forecasts below consensus).
- **After two-months rally, the Polish FX market stabilised in March.** The zloty is trading in the relatively narrow range, but we see a possibility of an upward move to above 4.17-4.18 rather than strengthening to below 4.08. The weakening of the zloty may be more significant against the US dollar if our forecast of downward move of EURUSD materialises. The situation in the euro zone will probably remain the main driver of the Polish currency fluctuations, but we do not see many factors that could continue to support risky assets and therefore our view for a more visible profit taking in April.

This report is based on information available until 2nd April

Short- and Medium-term Strategy

Interest rate market

	Change (bps)		Level end-Mar	Expected trend	
	Last 3M	Last 1M		1M	3M
Reference rate	0	0	4.50	→	→
WIBOR 3M	-5	-2	4.94	→	→
2Y bond yield	-26	-7	4.58	↗	↗
5Y bond yield	-37	5	4.93	→	→
10Y bond yield	-40	4	5.49	→	↗
2/10Y curve slope	-15	11	91	↘	→

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

Rates: our view and risk factors

PLN rates market	<p>Money market: WIBOR rates remain elevated and this is not likely to change soon. FRA rates still show lower path of WIBOR 3M later this year, which might be connected with pricing-in lower spread between market and NBP rates. We see NBP rates flat in 2012 and lower WIBOR in 2H 2012.</p> <p>Short end: Currently, we foresee a gradual increase in 2Y benchmark as the MPC keeps hawkish rhetoric, but CPI inflation, which will be published in April (our forecast at 3.8%) together with weaker economic data (production, wages) could bring some decrease in second half of April.</p> <p>Long end: Correction move in 5Y and 10Y sectors, which we expected, was quite significant (yields increased by 15bps in two weeks, though 4 bp in March as a whole). In April we expect horizontal trend and only sharp risk aversion could lead to testing important levels of 5% for 5Y and 5.60% for 10Y bonds. IRS curve should oscillate around 4.80%.</p> <p>Risk factors to our view: Uncertainty still dominates on the market, also as regards monetary policy prospects. The risk-case scenario of rate hike by the MPC (which we do not assume) would lead to further correction, especially at the short-end. The long-end remains under influence of global moods and any significant shifts in risk appetite may lead to sharp moves in yields.</p>
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FX market

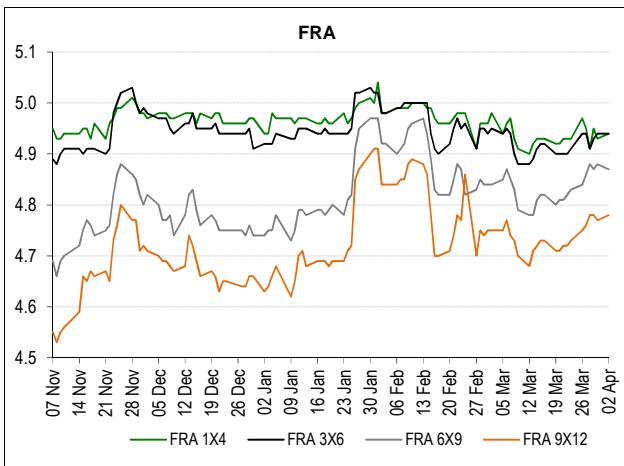
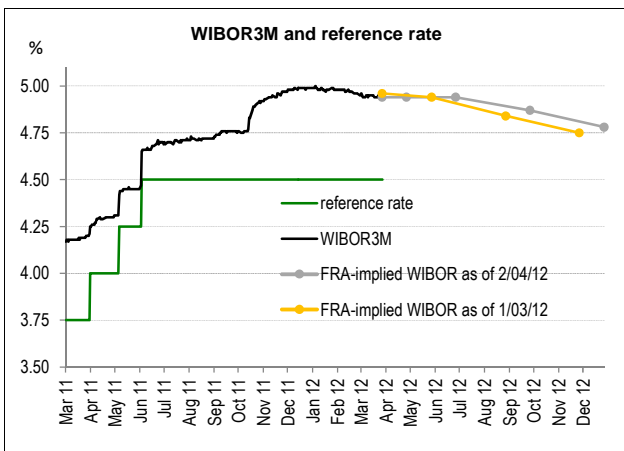
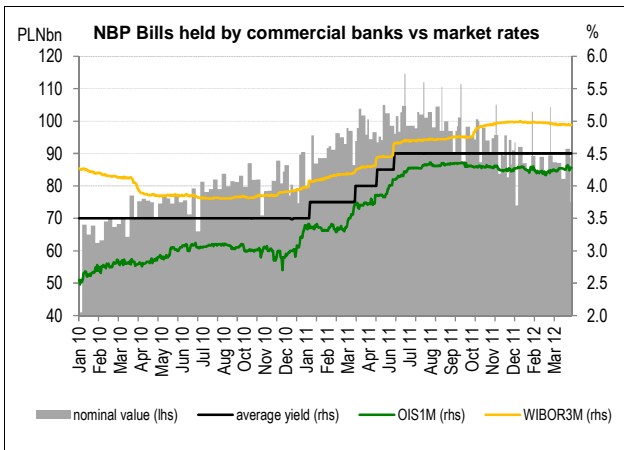
	Change (%)		Level end-Mar	Expected trend	
	Last 3M	Last 1M		1M	3M
EURPLN	-5.8	0.6	4.16	→	↗
USDPLN	-8.7	1.5	3.12	↗	↗↗
CHFPLN	-5.0	0.6	3.45	↘	↘
GBPPLN	-5.7	1.5	4.97	↗	↗
EURUSD	3.2	-0.9	1.33	↘	↘↘

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

FX: our view and risk factors

PLN FX market	<p>EUR: March saw stabilisation of EURPLN after two-months rally. We think that there are a lot of risk factors, which could push rate to test resistance level of 4.17-4.18, and its breaking would open the room to further increase, even above 4.20. Support is still at 4.08.</p> <p>USD: Sovereign debt problems in the euro zone and a possibility of QE3 by Fed as the main drivers. We see more possibility of downward move in EURUSD, which would mean a gradual weakening of the zloty against the US dollar. This trend should be more visible in three-month time.</p> <p>CHF: There is still possibility that the SNB raises EURCHF currency floor from current 1.20 due to lower growth and disinflation, supporting moderate zloty strengthening vs. the Swiss franc.</p> <p>Risk factors to our view: The main risk factor to our view of zloty weakening against the euro and the dollar would be another wave of positive mood in global markets, driven for example by lower worries regarding euro zone's periphery and/or QE3 announcement by Fed.</p>
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Money Market



Expensive month behind. Rates will gradually fall in April

- March was a relatively expensive month, short-term WIBOR rates (with maturity up to 1M) stayed above the reference rate. We noted also significant increase in Polonia rate towards 4.64% (during the month it varied between 4.20-4.64%) and moderate growth of short term OIS rates. We think that it was a consequence of demand during the OMO auctions, which was exceeding the amounts necessary for the balanced liquidity.
- For April the minimum reserve requirement level was set at ca. PLN29bn. Domestic commercial banks started a new reserve period with overbuilt liquidity (over PLN40bn), mainly due to Easter holiday in the first week of April. However, money market rates fell only gradually. It could suggest that despite earlier experience (i.e. falling carry and a cheap month) April could bring short term money cost only slightly below the reference rate.

- Sentiment on the money market was fragile, bringing OIS rates slightly up by 1-5bps on average. The highest increase was noted in case of 1M rate. At the end of March 3M OIS rate was traded around 4.27%. It still reflects quite high availability of money in the banking system.

WIBOR rates continue to fall moderately

- March brought some gradual fall of WIBOR rates by 2bps along the curve, however WIBOR rates between 6M and 1Y have remained flat (near 4.96%). Market reaction to the rhetoric by the NBP Governor (cooling interest rate hikes expectations in coming months) as well as hawkish comments of other MPC members was rather limited.

- FRA market was more volatile, immediately pricing information from the MPC's members. After NBP's Governor statements ("being too late is probably a lesser mistake than increasing interest rates and then having to reverse the move") FRA 1x4 and 3x6 continued downward trend and ended March at lower level (by 3bps and 1bps, respectively) compared with the end of February. On the other hand, Belka's comment and macroeconomic data reduced expectations for monetary easing later this year, which is also our base-case scenario. As a consequence, longer tenors 6x9 and 9x12 increased by 3-4bps. Investors on the FRA market still expect lower path of WIBOR 3M till year-end, though it may be driven by predictions of lower spread between WIBOR and reference rate, rather than pricing-in official rate cuts in the second half of 2012.

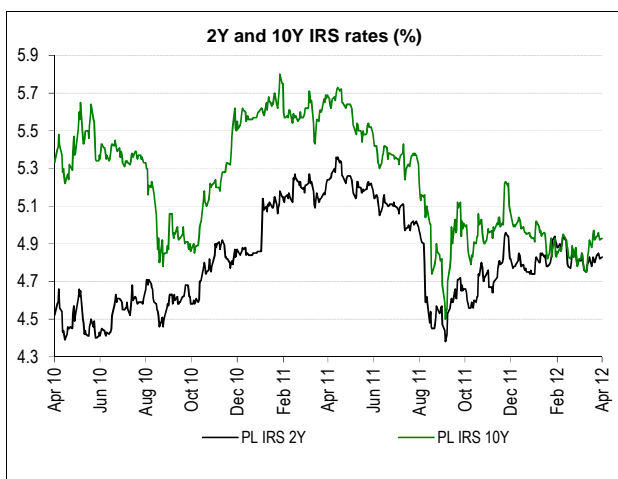
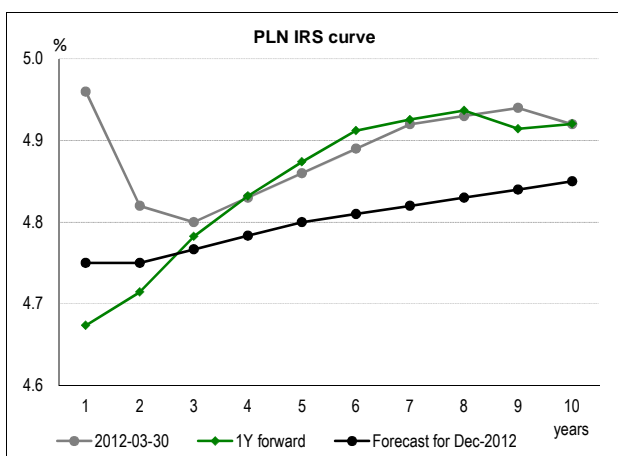
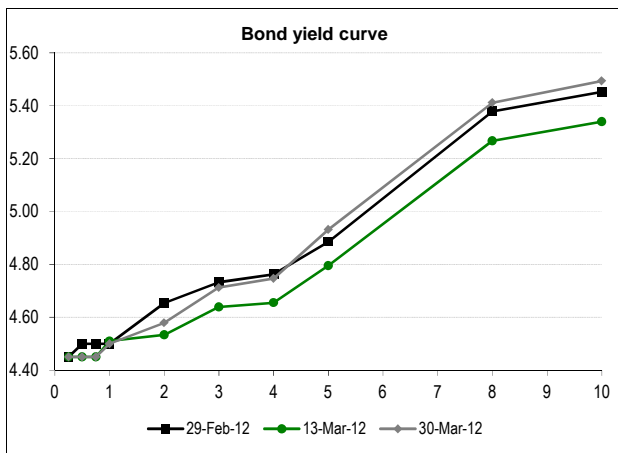
- We expect that WIBOR rates fall in coming months will be rather subdued, with a possibility of more significant move in 2H 2012. We revised upward WIBOR rates forecasts in coming months due to changes in our baseline scenario regarding monetary policy. As mentioned above, currently we assume that the MPC will keep interest rates unchanged till end-2012. We forecast 3M WIBOR to decrease to 4.85% by year-end.

Money market rates (%)

	Reference rate (%)	Polonia (%)	WIBOR (%)				OIS (%)				Spread WIBOR / OIS (bp)			
			1M	3M	6M	12M	1M	3M	6M	12M	1M	3M	6M	12M
End of March	4.50	4.34	4.72	4.94	4.96	4.96	4.28	4.27	4.25	4.25	44	67	71	71
Last 1M change (bp)	0	-17	-2	-2	-2	-2	5	4	2	2	-7	-6	-4	-4
Last 3M change (bp)	0	69	-5	-5	-4	-4	1	-2	-4	-3	-6	-3	0	-1
Last 1Y change (bp)	75	125	81	75	55	39	72	64	42	16	9	11	13	23

Sources: Reuters, BZ WBK

IRS and T-Bond Market



Correction after reaching the lowest level in years

Positive sentiment on the domestic debt market continued till inflation and current account data release in mid-March. During the first part of month benchmark yields hit their minimums at 4.53% for 2Y (lowest level since October 2011), 4.78% for 5Y and 5.34% for 10Y (more or less since October 2010 in both cases). Higher than expected current account gap, which caused the zloty weakening, as well as overall global sentiment deterioration put some pressure on mid- and long-end of the curve. Change in sentiment and profit-taking after strong rally caused significant increase in yields, towards crucial technical resistance levels at 4.95% for 5Y and 5.55% for 10Y. At the same time yield of 2Y benchmark remained relatively stable, oscillating slightly above 4.55%.

However, after comments from the central bank, which limited expectations for rate cuts, yield of 2Y benchmark increased towards 4.60%. Yields of benchmark papers moved up by 4bps on front and by 15bps on mid and long end of the curve compared with recent year-low levels. At the end of March bond market reached some sort of equilibrium and flows balanced, which was supported by the release of issuance plan for 2Q 2012.

IRS market followed moves on the bond market, but the scope of changes was more significant. Mid of the month also brought correction move and rates increased by 7-17bps (with the highest growth in 10Y segment of the curve), while in monthly terms IRS curve moved up by 1-14bps. As a consequence asset swap spread in 10Y sector narrowed by 10bps to slightly below 60bps at the end of March, mainly due to sharp increase in 10Y IRS rate.

We expect yields to remain in horizontal trend

The beginning of April on the domestic debt market is still influenced by favourable Q2 issuance plan. After a relatively light correction (yield curve moved up by 4-5bps in 5-10 sector MoM) we expect yields to oscillate in horizontal channel between 4.55% and 4.65% for 2Y, 4.85-5.00% for 5Y and 5.40-5.50% for 10Y, testing either the upper or the lower band.

We decided to revise our interest rate path for this year, assuming that the MPC will keep official rates unchanged till year-end. As a result we foresee short end of the curve to remain under pressure, mainly due to hawkish rhetoric of the MPC, even at April's meeting. On the other hand, CPI reading for March below 4% (we expect 3.8%), together with some other dovish statistics (e.g. low production) could bring some positive sentiment in the front-end later during the month.

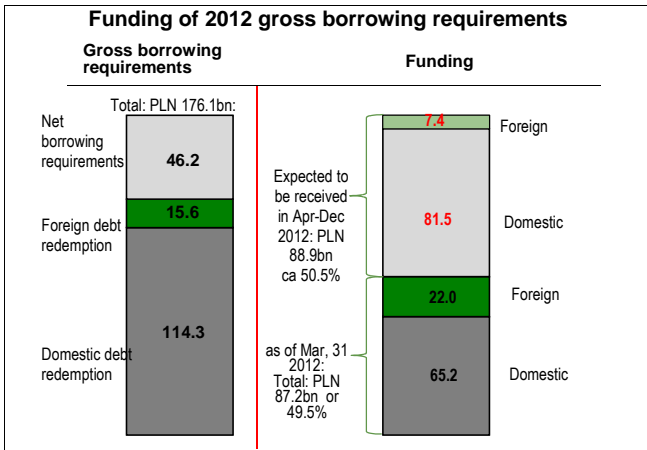
The long-end will remain under influence of global mood. Risk aversion may result in further increase in yield of 10Y benchmark. However, the upward move will be limited given low supply in Q2. Additionally, release of fiscal data for 2011 (decline in the general government deficit) could be also supportive for 10Y.

Bond and IRS market (%)

	T-bills	BONDS			IRS			Spread BONDS / IRS (bp)		
	52-week	2Y	5Y	10Y	2Y	5Y	10Y	2Y	5Y	10Y
End of March	4.50	4.58	4.93	5.49	4.82	4.86	4.92	-24	7	57
Last 1M change (bp)	0	-8	5	4	2	12	14	-10	-7	-10
Last 3M change (bp)	5	-26	-37	-40	8	6	-1	-34	-43	-39
Last 1Y change (bp)	-1	-43	-84	-79	-37	-81	-77	-6	-3	-2

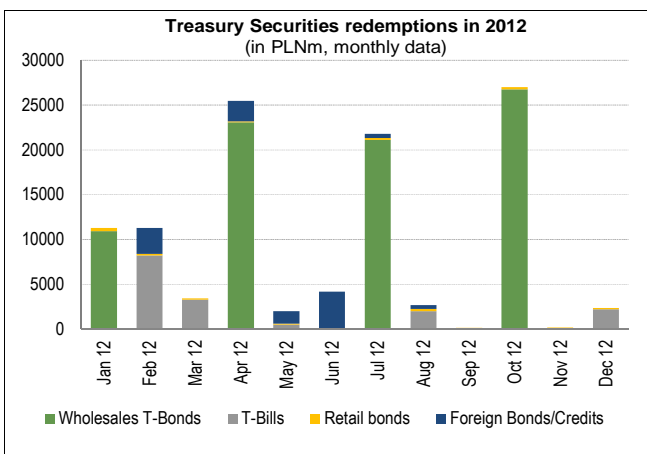
Sources: Reuters, BZ WBK

Treasury Securities Supply Corner



Half of borrowing needs already covered

- As predicted, March saw moderate supply, with the Ministry of Finance selling a total of PLN10.56bn in wholesale bonds. The figure was slightly below amount sold in February, but nearly 2-times higher as compared to the same period of last year. Similarly as in the previous month, the recorded demand was solid and auction yields have continued to decline.
- Overall, in Q1 2012 the MF launched marketable T-bonds on the domestic market worth of PLN39.2bn via both regular and switch tenders (much higher as compared with previous quarter and the same period of 2011). In January-March period the MF has covered 50% of its borrowing needs for 2012. This resulted from this year's issuance on both domestic and foreign markets, but also from the pre-financing in 2011 as well as higher-than-planned financial resources available at the end of 2011.



- In Q1 2012 the MF remained focused on the short-end and mid of the curve. The 2-5Y sector represented nearly 60% of total issuance in January-March period.

- At the end of the first quarter liquidity cushion in PLN and FX-denominated funds amounted to PLN40bn; a part of this sum will be used to redeem debt.

The Q2 2012 issuance plan focuses on short end...

- The issuance plan for Q2 2012 includes wholesale T-bonds worth of PLN13-20bn on four tenders. Additionally, the Ministry will hold one auction in June of up to PLN2.0bn in infrastructural bonds issued by the state-owned BGK.

- T-bonds offer on auctions will be quite diverse (OK/PS/DS/WS/WZ/IZ), strongly depending on market situation and investors' appetite. However, it will concentrate on front end of the curve, with 2Y and 5Y benchmarks supply at PLN11-16bn in Q2, which would represent 80-85% of total issuance in April-June period. On the other hand, the MF limited the supply on long end to one auction in the quarter (in May) to "give investors a respite", as MF's official said.

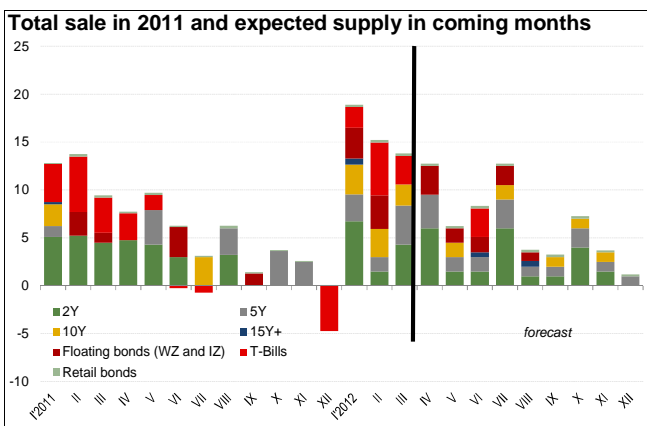
Issuance calendar in April-June period

Date of auction	Settlement date	Bonds / Bills	Expected offer (in PLN bn)
05-Apr	10-Apr	Switch tender	
19-Apr	25-Apr	OK0714 / PS1016	5.0 - 9.0
23-Apr	25-Apr	31-week Bills	1.0 - 3.0
07-May	09-May	Conditional auction of T-bill	
16-May	18-May	OK / PS	2.0 - 3.5
23-May	25-May	DS. / WS / WZ / IZ	2.0 - 4.0
04-Jun	06-Jun	51-week Bills	1.0 - 3.0
14-Jun	18-Jun	Switch tender	
20-Jun	22-Jun	OK / PS	2.0 - 3.5
27-Jun	29-Jun	Infrastructure bonds issued by BGK	up to 2.0

- The Ministry will also hold switching auctions to redeem papers maturing from April to October 2012. In April investors can purchase floating-rate T-bonds WZ0117 and WZ0121 instead of PS0412, OK0712 and OK1012 bought back by MF.

- As predicted, offer of T-bills in Q2 has been reduced significantly to PLN3-6bn. T-bills, with term to maturity of 31-51 weeks, will be auctioned only in April and June.

- In terms of foreign financing, the MF may conduct issues on the core international markets, depending on the market situation. It also sees possibility of additional financing by structured coupon bonds' issuance in the private placement system. Loans from international financial institutions are expected at EUR0.6bn. According to the officials, the possibility of foreign issue cannot be excluded already in April.



...with high supply in April

- As we expected, the T-bonds supply concentrates in April. The MF offers T-bonds 2Y OK0714 and 5Y PS1016 worth of PLN5.0-9.0bn and 31-week T-bills worth of PLN1.0-3.0bn on regular auctions and WZ0117 and WZ0121 on switch tender.

- Switch tender results will determine offer on both regular auctions in April. However, we are sceptical in case of investors' willingness to change fixed-rate bonds into floating ones, especially from non-residents side, who hold 53% of outstanding amount in PS0412 paper. Switch is more probable in case of domestic commercial banks, which hold nearly 30% of their portfolio in WZ series.

- All in all, we expect solid demand on regular auctions (both T-bond and T-bill) in April, supported by high liquidity due to PS0412 redemption and coupon payments.

Sources: Ministry of Finance, BZ WBK

Treasury Securities Supply Corner

Total issuance in 2012 by instruments (in PLNm, nominal terms)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
T-bonds auction	10,820	11,503	10,560	12,500	6,000	4,880	13,000	3,500	3,000	6,000	2,000	1,000	84,763
T-bills auction	2,223	5,778	3,000	3,000		3,000							17,001
Retail bonds	213	248	248	241	241	241	241	241	241	220	200	200	2,773
Foreign bonds/credits	7,979	2,200		2,514					3,265		2,405		18,363
Refinancing and financial resources at the end of 2011	31,600												31,600
Total	52,835	19,729	13,808	18,255	6,241	8,121	13,241	3,741	6,506	6,220	4,605	1,200	154,500
Redemption	11,297	3,981	5,275	23,203	4,855	2,778	25,718	3,127	1,058	27,014	3,924	2,368	114,598
Net inflows	41,537	15,749	8,532	-4,948	1,386	5,342	-12,477	614	5,448	-20,794	681	-1,168	39,902
Rolling over T-bonds	6,309												6,309
Buy-back of T-bills													0
Total	47,846	15,749	8,532	-4,948	1,386	5,342	-12,477	614	5,448	-20,794	681	-1,168	46,210
Coupon payments	1,451			7,211			1,497		1,455	7,413			19,026

Note: Our forecasts – shaded area

Schedule Treasury Securities redemption by instruments (in PLNm)

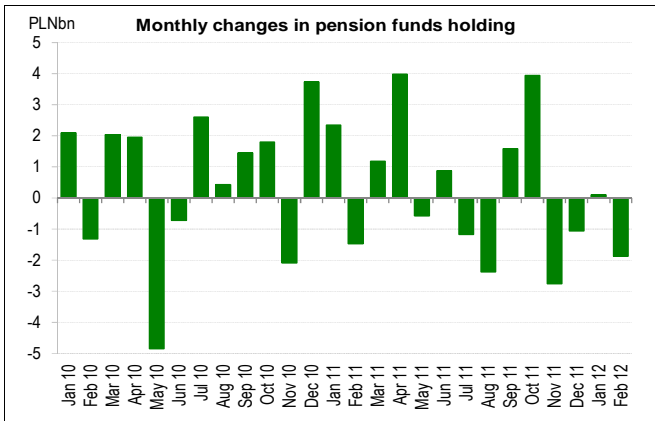
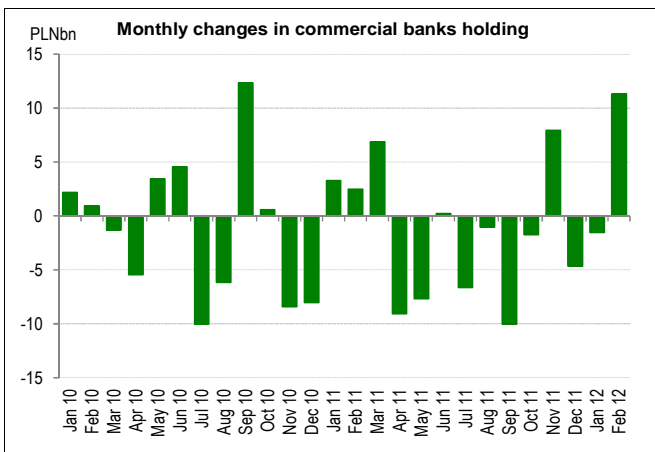
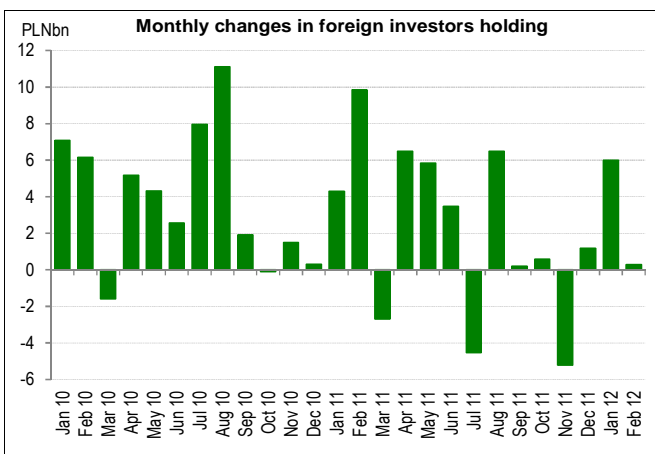
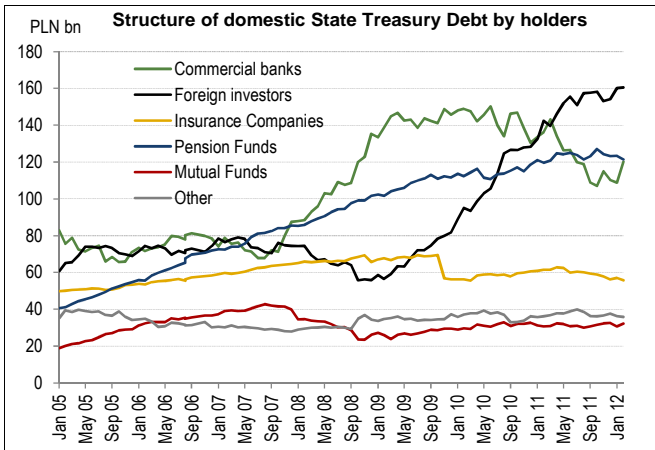
	Bonds	Bills	Retail bonds	Total domestic redemption	Foreign Bonds/Credits	Total redemptions
January	10,946	0	351	11,297	0	11,297
February	0	3,799	182	3,981	0	3,981
March	0	1,997	129	2,125	3,150	5,275
April	23,071	0	132	23,203	0	23,203
May	0	2,223	117	2,339	2,516	4,855
June	0	0	112	112	2,666	2,778
July	21,090	0	218	21,308	4,410	25,718
August	0	1,997	248	2,245	882	3,127
September	0	0	176	176	882	1,058
October	26,749	0	265	27,014	0	27,014
November	0	3,000	208	3,208	716	3,924
December	0	2,223	146	2,368	0	2,368
Total 2012	81,856	12,238	2,283	96,378	15,221	111,598
Total 2013	82,468	3,781	1,698	87,948	14,825	102,773
Total 2014	47,084	0	628	47,712	17,448	65,160
Total 2015	78,880	0	485	79,365	14,329	93,694
Total 2016	48,023	0	91	48,114	16,871	64,985
Total 2017+	175,263	0	3,288	178,551	134,966	313,518

Schedule wholesales bonds redemption by holders (data at the end of February 2012, in PLNm)

	Foreign investors	Domestic banks	Insurance Funds	Pension Funds	Mutual Funds	Individuals	Non-financial sector	Other	Total
Q1 2012	0	0	0	0	0	0	0	0	0
Q2 2012	12,309	4,922	1,941	1,658	300	97	44	1,834	23,105
Q3 2012	8,572	6,262	1,335	2,485	1,030	136	40	1,264	21,125
Q4 2012	10,421	7,132	1,162	3,747	1,516	82	32	2,691	26,783
Total 2012	31,302	18,316	4,438	7,890	2,846	315	116	5,789	71,013
	44%	26%	6%	11%	4%	0%	0%	8%	100%
Total 2013	35,227	12,752	12,575	13,395	3,529	504	104	4,516	82,602
	43%	15%	15%	16%	4%	1%	0%	5%	100%
Total 2014	14,209	9,509	4,930	10,339	4,153	413	143	3,678	47,374
	30%	20%	10%	22%	9%	1%	0%	8%	100%
Total 2015	19,203	24,884	6,956	16,135	4,978	184	719	5,869	78,927
	24%	32%	9%	20%	6%	0%	1%	7%	100%
Total 2016	11,474	8,679	3,720	19,818	4,065	51	507	2,639	50,952
	23%	17%	7%	39%	8%	0%	1%	5%	100%
Total 2017+	48,557	32,644	21,927	52,863	11,292	269	832	7,779	176,161
	28%	19%	12%	30%	6%	0%	0%	4%	100%

Sources: Ministry of Finance, BZ WBK

Treasury Securities Holders



Foreigners passive in February, more active in March

▪ The structure of holdings at the end of February showed that foreign investors were more passive on the Polish debt market, after strong purchasing in previous months. Non-residents upped their holdings in Polish bonds slightly by PLN0.4bn, while downed in T-bills by near PLN0.1bn. At the end of February foreign investors portfolio amounted to PLN160.5bn (up by 0.3bn in monthly terms), which accounted for 30.5% of total debt in marketable and non-marketable (savings) Treasury Securities.

▪ Foreign banks have raised their holding in Polish bonds in February for the second month in a row. At the end of the month their portfolio amounted to ca. PLN22bn (up by PLN1.4bn in monthly terms), the highest level since August 2011. They purchased bonds along the curve up to 10Y, slightly decreasing their holding in sector 15Y+ and floating rate bonds. To sum up, foreign banks increased their share in Polish bonds debt to 13.7% of total non-residents portfolio, up from 12.9% in previous month.

▪ As regards foreign non-bank financial sector, in February it was on the supply side. It decreased its holding in Polish bonds by ca. PLN1.1bn to PLN131.1bn. It accounted for nearly 82% of non-resident portfolio (down from ca. 83% in January, but still well above the level in February 2011 of 70%). Despite some reduction of portfolio, foreign non-bank financial sector remains the main player on the Polish debt market.

▪ Commenting on issuance plan for Q2 2012, Piotr Marczak, the head of Finance Ministry's debt department said that in March foreign investors were more active on the domestic bond market than in February and a more significant foreign capital inflow was observed. It supports our view that non-residents will take opportunities to purchase bonds at lower prices on corrective move in March.

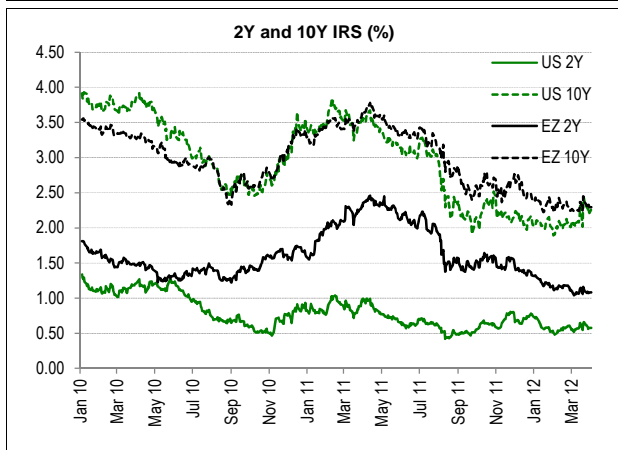
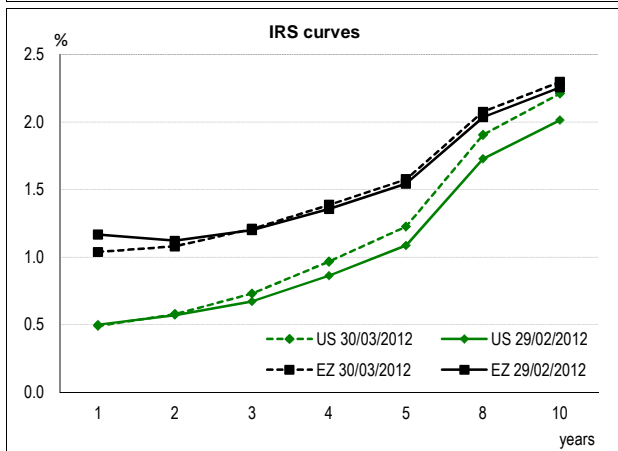
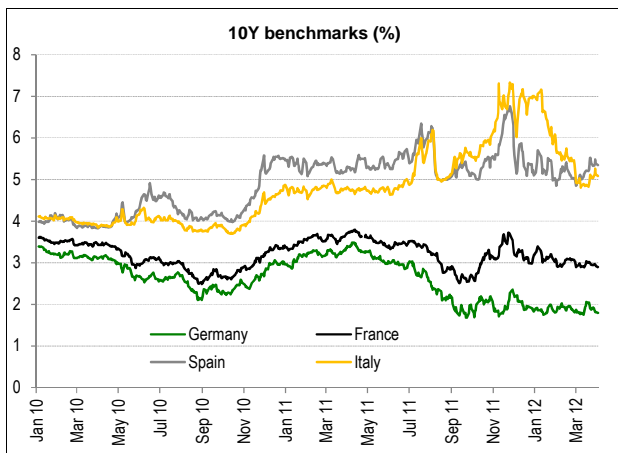
Local banks as the main buyer in February

▪ As expected, in February domestic investors increased their activity on the debt market, though different performance among investor groups was observed. Domestic commercial banks posted PLN11.3bn increase over the month not only due to increase volume in buy-sell back transactions with the Ministry, but also invested a fresh capital. At the end of February Polish banks' holdings amounted to PLN120.1bn (out of which transactions with the MF amounted to PLN7.3bn), reaching the highest level since June 2011. Commercial banks increased their position in bonds by PLN13.3bn, which represents the highest monthly increase ever. They purchased PS series (mainly PS0415 and current 5Y benchmark PS1016) worth of PLN4.5bn, OK series (mainly OK1012 and current 2Y benchmarks OK0114) worth of PLN2.6bn and further increased floating rate bonds holding (by PLN2.3bn mainly by purchasing WZ0117). On the other hand, banks sold T-bills worth ca. PLN2bn, decreasing their share in portfolio to PLN6.7bn.

▪ Investment funds (TFI) were also on the demand side. TFI increased their holding by nearly PLN1.5bn to PLN32.2bn (increasing their portfolio to the level from the end of last year). On the other hand, pension funds (OFE) and insurance companies were on the supply side. OFE holdings declined by PLN1.9bn to PLN121.4bn (lowest level since August 2011). However, pension funds kept their dominant position among local investors on the debt market. We think that domestic investors were also relatively active player on the bond market in March.

Sources: Ministry of Finance, BZ WBK

International Bond Markets



Investors remain more cautious...

- The first part of March brought continuation of upward trend in 10Y sector of Bunds and the US Treasuries. Positive mood for risky assets and peripheries debt came mainly from February's LTRO, but also from better-than-expected macroeconomic data (from the US) as well as the Fed's more optimistic expectations about the economic developments. Yield of 10Y Bund increased to slightly above 2.05% (highest level since end of the 2011), while yield of 10Y Treasuries reached the level of 2.36% (highest since August 2011).
- Sell-off in Bunds and the US Treasuries stopped in mid-March amid renewed concerns over Euro area sovereign risk (mainly about Spain). The end of March brought core bond market strengthening, which trimmed part of losses from the first part of the month. Notwithstanding, in monthly terms the US curve moved up by 4-22bps (the highest increase was observed in 10Y, the lowest in 2Y and as a consequence the US curve steepened), while the German curve was relatively stable.
- The spread between 10Y US Treasuries and 10Y Bund has gradually widened to ca. 35bps from slightly above 10bps at the end of February and 0 at the end of January, which, in fact, is the biggest gap in more than 12 months. On the other hand, the German yield curves slightly flattened.
- The beginning of April might bring low activity on core markets due to Easter break. However, in medium term Bernanke's cautious stance and fiscal concerns on Spain have supported Bunds and the US Treasuries. Forthcoming macro data will be crucial.

... as problems in euro zone's periphery not solved

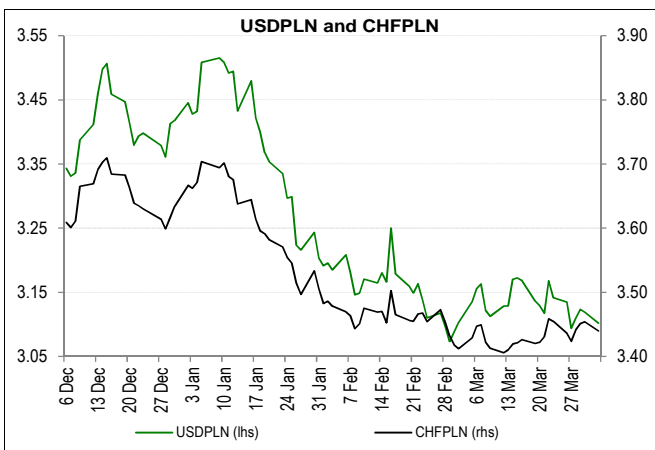
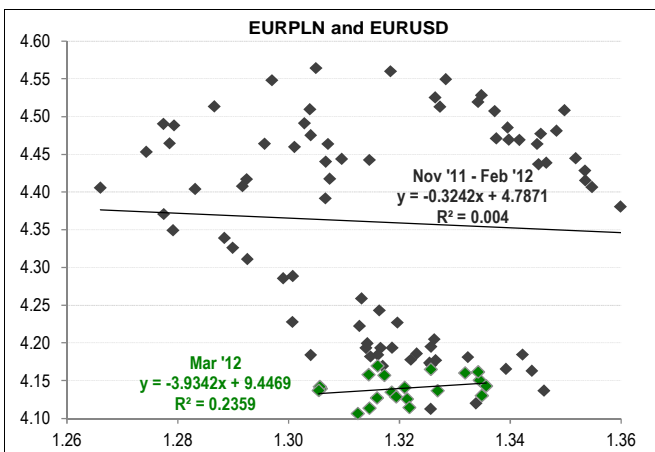
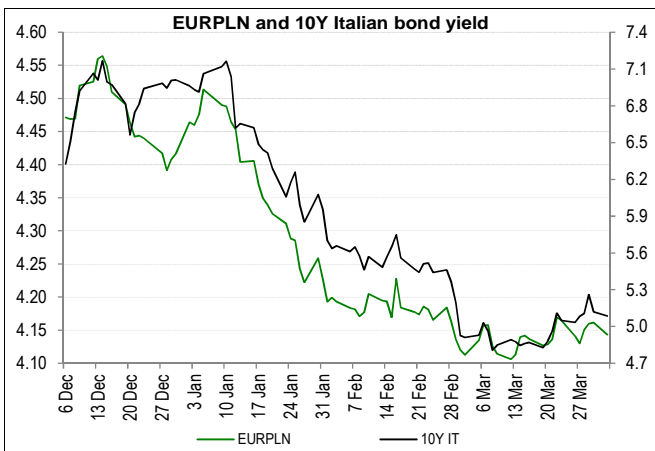
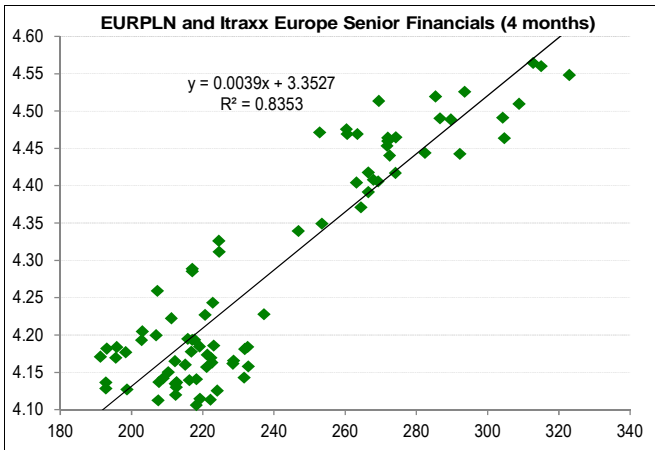
- February's LTRO results positively influence the European sovereign bonds, especially as regards peripheral markets securities. Situation on the Italian government bonds market was a perfect example. Yields on 10Y benchmark fell below 5% for the first time since mid-2011. The decision on the Greek debt reduction and further financial aid also supported peripheral securities. The debt auctions on these markets attracted solid demand, which resulted in decline in risk premium. However, weak European PMI indices and growing concerns about fiscal consolidation in Spain caused profit taking and some increase in yields.
- Uncertainty on peripheries could prolong in coming weeks and it will weigh on the long end of the curves. The supply side also could bring some pressure, especially in case of Italy, which at the end of Q1 covered only 22% of its expected 2012 borrowing requirements (compared with 41% of borrowing needs coverage in Spain).

Euro zone's issuance plans and completion in 2012 (€bn)

	Total redemptions	Deficit	Borrowing needs	Expected bond supply	% of completion (YtD)
Austria	14	8.3	22.3	22.3	33
Belgium	27.9	7	34.9	26	62
Finland	6.3	7.5	13.8	13.8	26
France	101.7	78.7	180.4	178	29
Germany	157	26.6	183.6	170	26
Greece	33.2	16.2	49.4	-	-
Ireland	5.5	13.7	19.2	-	-
Italy	192.2	41.1	233.3	233.3	22
Netherlands	29.7	12.3	42	60	36
Portugal	12.9	17.4	30.3	-	-
Spain	50.1	36.2	86.3	86.3	41
Total	630.5	265.0	895.5	789.7	30

Source: Reuters, BZ WBK

Foreign Exchange Market



Stabilisation of the zloty after two-months rally...

▪ In March the appreciation trend of the zloty observed since the beginning of the year terminated and the domestic currency stabilised. Monthly changes of main FX rates of the Polish currency (EURPLN, USDPLN, CHFPLN) amounted to ca. 1%.

▪ Just as we suggested in March, the market has been pricing-in scenario of less severe economic slowdown in Europe. Therefore, when much weaker than expected data on flash PMI for German and euro zone manufacturing were released, there was some risk aversion on the global market. Also the outlook of weaker growth in China put negative pressure on risky assets. There was also some uncertainty regarding developments in the euro zone and ability of peripheral countries to fulfil their obligations of fiscal consolidation amid weaker growth prospects. The process of debt restructuring in Greece did not trigger any higher volatility.

▪ Despite the fact that there were some periods of turmoil, the risk aversion was not high enough to trigger any more visible depreciation of the domestic currency. Risky assets to some extent were backed by the Fed which presented more positive outlook of the US economy and at the same time left door open for QE3. Additionally, the domestic currency remained mainly under the influence of developments on the peripheries of the euro zone and uncertainty over European debt crisis was not that high (as the market remained supported by two ECB's LTROs). It is worth to notice, that relationship between the EURPLN and the EURUSD rates has increased.

... and is likely to depreciate in April

▪ This month will be rich in important events. Market attention should focus on French presidential elections (as first round will take place in late April) as well as expectations regarding the possible shape of Greek government after parliamentary election (held probably in early May). In late April the Fed holds the meeting and its outlook of the economic performance and investors' assessment of chances for QE3 may trigger some market volatility. As we do not see any factor that could support risky assets but the hopes for more quantitative easing in US, we expect that in April some visible profit taking may be recorded on Polish FX market. Next macro data shall indicate that economic slowdown in Europe is continued and market expectations for less severe deceleration have probably been too optimistic.

▪ Unsolved problems in the euro zone and the uncertainty over situation in Portugal and Spain together with recent cut of short bets on the euro give bigger potential for fall in EURUSD rate. As mentioned above, the relationship between the EURPLN and EURSD has recently increased and consequently, the likely restart of the dollar's appreciation trend versus the euro may affect not only the USDPLN, but also the EURPLN.

▪ In our view, it is getting more likely that amid lower growth and deflation the SNB will decide to increase the floor of the EURCHF to ca. 1.25. That shall have some temporary impact on the EURUSD, but what is more important, it should provide quite visible support for the zloty versus the Swiss franc.

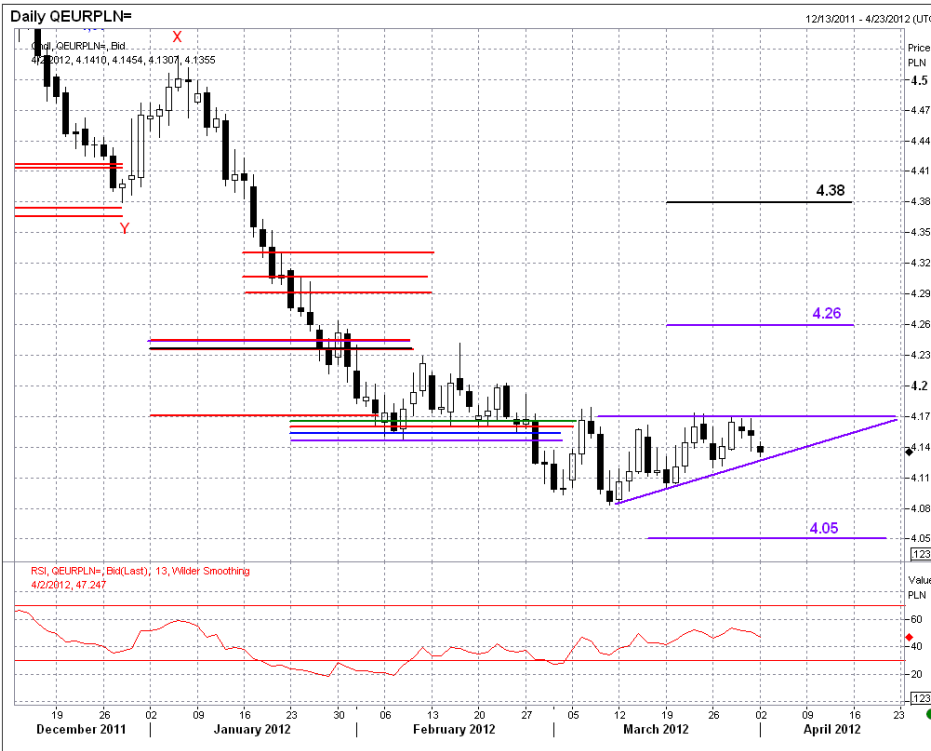
Forint and koruna also flat and likely to depreciate

▪ Over the past month the remaining CEE3 currencies also remained relatively stable. What is important, there were no new negative signals from Hungary that would put negative pressure on the zloty.

▪ Both EURHUF and EURCZK are currently close to vital levels of resistance (ca. 295 and 24.8 respectively). EURPLN also hovers close to important area 4.17-4.18 and it seems that CEE3 currencies may follow the same pattern in coming weeks.

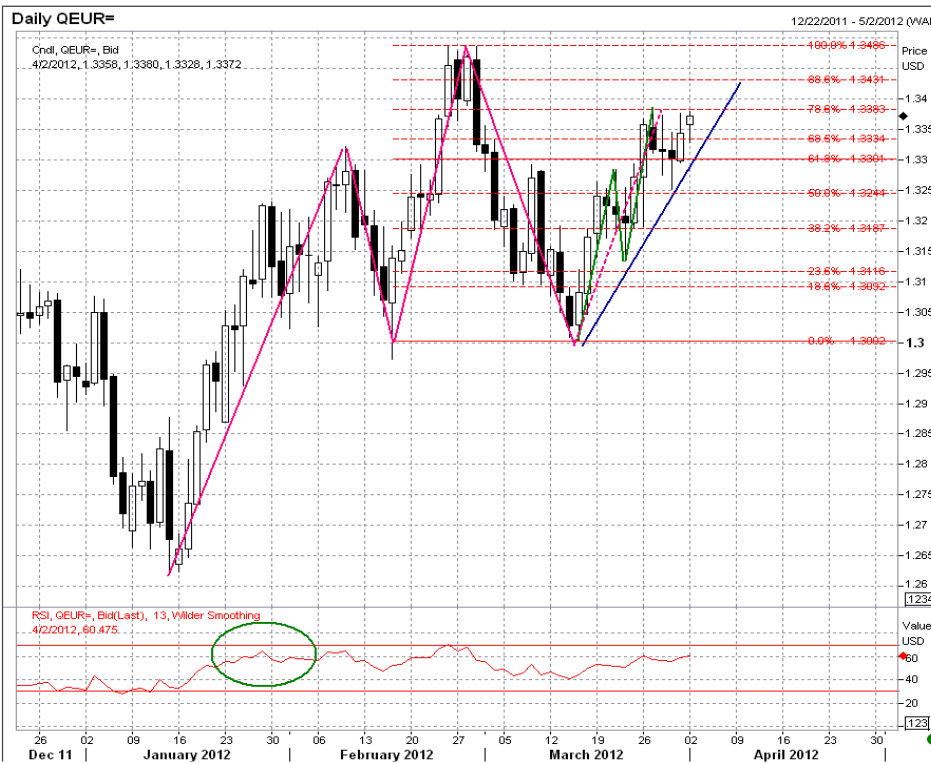
Sources: Reuters, BZ WBK

FX Technical Analysis Corner



EURPLN

- Despite a rebound to 4.17 in early March the EURPLN tested 4.08 (the projection from triangle pattern).
- Since then the exchange rate is staying in next triangle pattern and some bigger move shall take place somewhere before mid-April. The potential scale of move is 4.26 and 4.05, depending on the direction.
- The USDPLN is currently close to local lows (ca. 3.08) and pattern of triangle has also been plotted by the exchange rate.
- Any bigger move on the EURPLN may be related to higher volatility of the EURUSD.
- We find it more likely that zloty will depreciate versus the euro and the EURPLN will be close to 4.20 at the end of the month.



EURUSD

- Lows from mid-February at close to 1.30 prevented further decline of the EURUSD.
- Currently the exchange rate stays in short-term steep upward trend and is close to 78.6% retracement.
- Latest pattern (market green on the chart) fits pretty good Fibon ratios.
- These two factors support lower EURUSD. Still, latest peak at 1.3384 is above maximum from February and it seems that this shoulder is too high and awaiting SHS pattern may be at this time too risky.
- On weekly charts the EURUSD is close to upward band of downward trend observed since Q2 2011 and that indicates that developments in coming days may point direction for next weeks.
- We expect the EURUSD to test again lows at 1.30 in April.

Sources: Reuters, BZ WBK

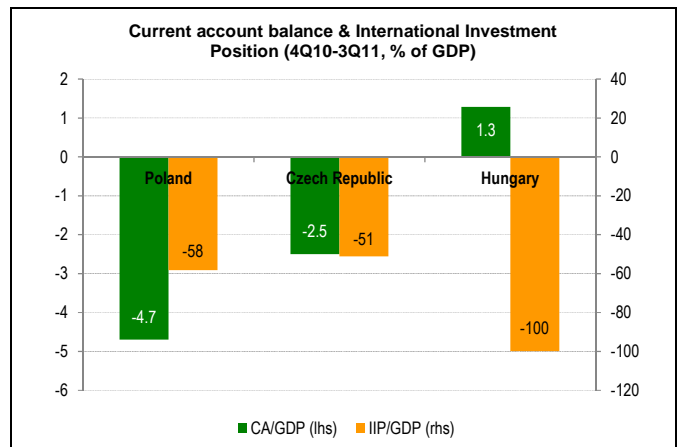
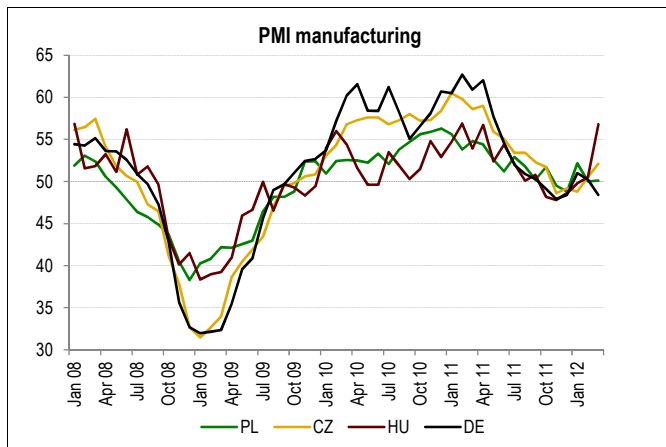
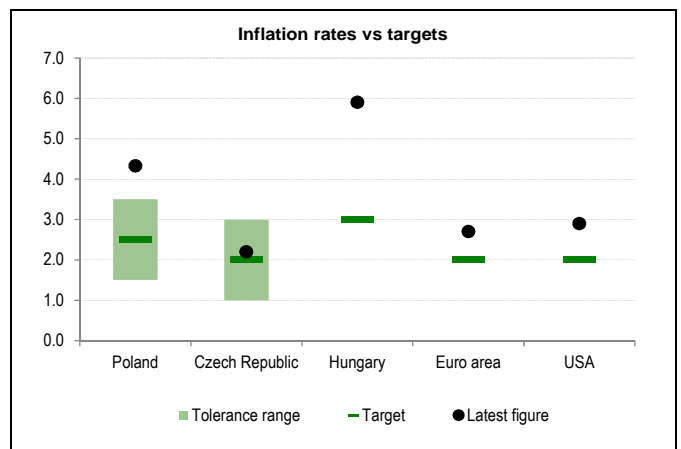
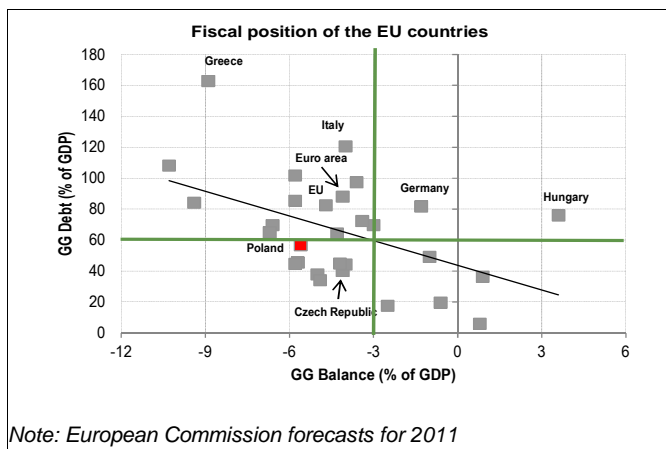
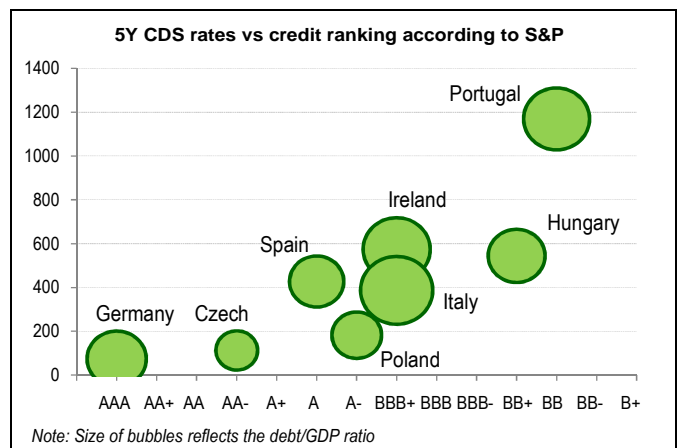
Poland vs other countries - economy

Main macroeconomic indicators (European Commission's forecasts)

	GDP* (%)		Inflation* (HICP, %)		C/A balance (% of GDP)		Fiscal Balance (% of GDP)		Public Debt (% of GDP)	
	2011E	2012F	2011E	2012F	2011E	2012F	2011E	2012F	2011E	2012F
Poland	4.3	2.5	3.9	3.5	-5.0	-4.3	-5.6	-4.0	56.7	57.1
Czech Republic	1.7	0.0	2.1	3.0	-3.6	-3.2	-4.1	-3.8	39.9	41.9
Hungary	1.7	-0.1	3.9	5.1	1.7	3.2	3.6	-2.8	75.9	76.5
EU	1.5	0.0	3.1	2.3	-0.3	0.0	-4.7	-3.9	82.5	84.9
Euro area	1.4	-0.3	2.7	2.1	-0.1	0.0	-4.1	-3.4	88.0	90.4
Germany	3.0	0.6	2.5	1.9	5.1	4.4	-1.3	-1.0	81.7	81.2

Note: * European commission interim forecast – February 2012

	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+	negative	Ba1	negative	BB+	negative
Germany	AAA	stable	Aaa	stable	AAA	stable
France	AA+	negative	Aaa	negative	AAA	negative
UK	AAA	stable	Aaa	negative	AAA	negative
Greece	SD	---	C	---	B-	stable
Ireland	BBB+	negative	Ba1	negative	BBB+	negative
Italy	BBB+	negative	A3	negative	A-	negative
Portugal	BB	negative	Ba3	negative	BB+	negative
Spain	A	negative	A3	negative	A	negative

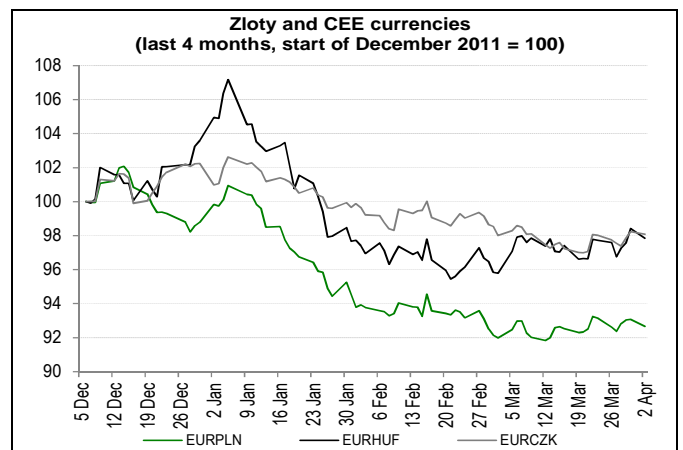
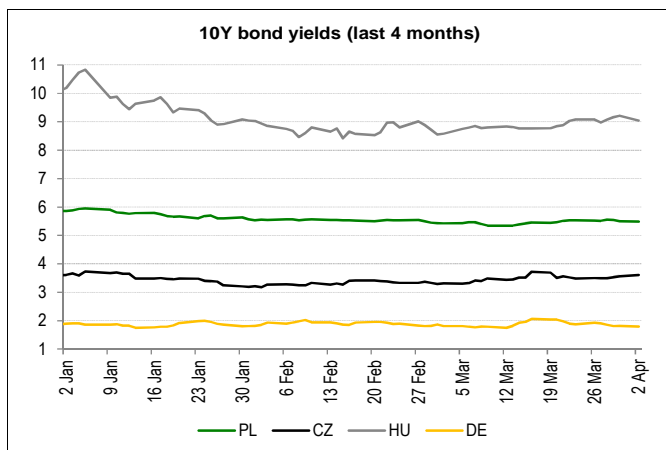
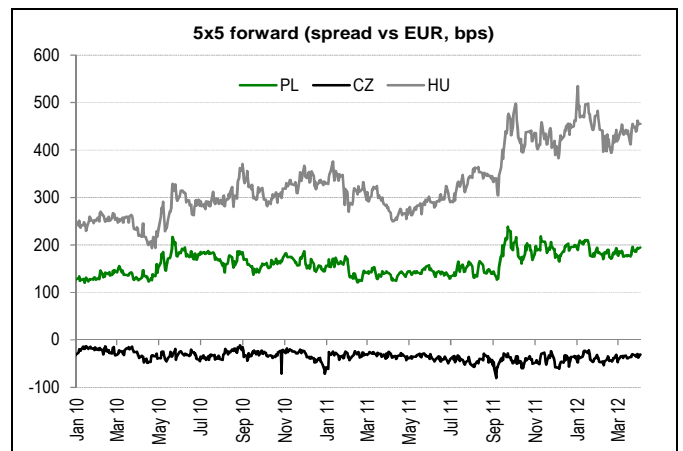
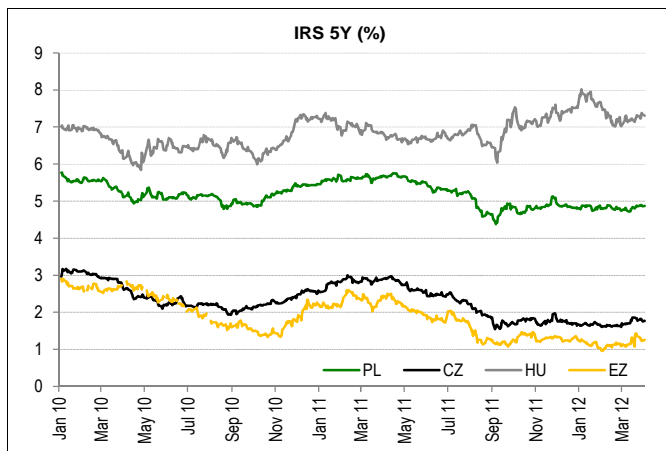
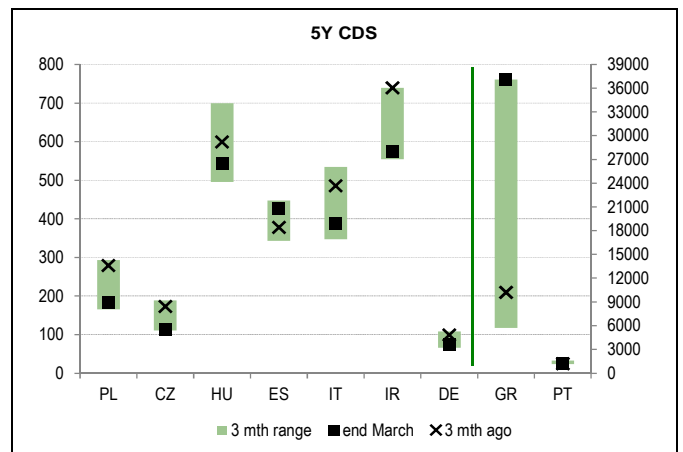
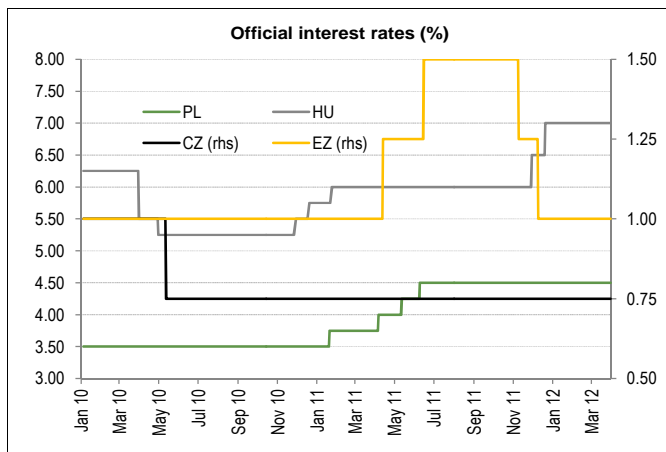


Source: stat offices, central banks, Reuters. BZ WBK, EC

Poland vs other countries - market

Main market indicators (%)

	Reference rate (%)		3M market rate (%)		10Y yields (%)		10Y Spread vs Bund (bps)		CDS 5Y	
	2011	2012F	2011	end of March	2011	end of March	2011	end of March	2011	end of March
Poland	4.50	4.50	4.99	4.94	5.88	5.50	405	368	279	182
Czech Republic	0.75	0.75	0.78	0.85	3.59	3.56	176	174	173	113
Hungary	7.00	7.00	7.24	7.25	9.90	9.21	807	739	599	544
Euro area	1.00	1.00	1.36	0.78						
Germany					1.83	1.82			99	75



Source: stat offices, central banks, Reuters. BZ WBK, EC

Central Bank Watch

		Last	2011	2012F	Expected changes (bps)			Risks
					1M	3M	6M	
Euro	Forecast	1.00	1.00	1.00	0	0	0	The ECB meeting will be relatively uneventful. We see no policy change and rhetoric very much in line with last month.
	Market implied »				0	0	0	
UK	Forecast	0.50	0.50	0.50	0	0	0	No policy changes are anticipated also this month.
	Market implied »				-3	-9	-11	
US	Forecast	0-0.25	0-0.25	0.25	0	0	0	Fed's governor Ben Bernanke expressed its caution about the improvement in the US labour market. Rates on hold
	Market implied »				0	0	0	
Poland	Forecast	4.50	4.50	4.50	0	0	0	The MPC will keep interest rates unchanged, but we do not rule out that a motion for interest rate hike will be voted.
	Market implied »				-1	0	-6	
Czech	Forecast	0.75	0.75	0.75	0	0	0	The Czech central bank predicted that market interest rate will be stable in the near future, which is also our baseline scenario.
	Market implied »				39	36	34	
Hungary	Forecast	7.00	7.00	7.00	0	0	0	The central bank will probably refrain from cutting interest rate (highest level in the EU) because of a delay in obtaining an the IMF loan.
	Market implied »				5	14	1	

Note: Market implied expectations show implied changes in 3M market rates based on FRA rates

Economic Calendar and Events

Date	Event:	Note:
4-Apr	PL MPC Meeting – interest rate decision	Our forecast and market consensus: no change in rates. The MPC could vote a rate hike motion
	EZ ECB Meeting – interest rate decision	Our forecast and market consensus: 1.00%.
	SP Auction of 3Y, 5Y and 10Y bonds	Offer: €2.5-3.5bn
	GE Auction of 5Y bonds	Offer: €4bn
5-Apr	PL Switch auction	-
	FR Auction of 5Y, 10Y, 15Y & 30Y bonds	Offer: €7.0-8.5bn
11-Apr	GE Auction of a new 10Y bonds	Offer: €5bn
12-Apr	IT Auction of 3Y & long-end bonds	Offer: €5.5-7.5bn
13-Apr	PL CPI for March	Our forecast: 3.8%YoY vs market consensus at 3.9%YoY.
18-Apr	PL Employment and wages for March	Weak data, especially in case of wages growth. We are well below market consensus
	GE Auction of 2Y bonds	Offer: €5bn
19-Apr	PL Industrial output for March	We predict significant weakening of growth
	PL Auction of 2Y and 5Y bonds	Offer: PLN5.0-9.0bn
	SP Auction of 5Y & 10Y bonds	Offer: €3.5-4.5bn
	FR Auction of 2/3Y & 5Y bonds	Offer: €7.0-8.0bn
20-Apr	PL Core inflation measures for March	Net core inflation (exc. food & energy prices) to decrease slightly below NBP's target
22-Apr	FR Presidential election in France	
23-Apr	PL Auction of 31-week T-bills	Offer: PLN1.0-3.0bn
24-Apr	HU NBH Meeting – interest rate decision	Our forecast: 7.00%
25-Apr	GE Auction of 30Y bonds	Offer: €3bn
26-Apr	PL Minutes of the April MPC's meeting	-
3-May	EZ ECB Meeting – interest rate decision	Our forecast and market consensus: 1.00%
	CZ CNB Meeting – interest rate decision	Our forecast: 0.75%
9-May	PL MPC Meeting – interest rate decision	Our forecast: the MPC will remain on hold

Source: stat offices, central banks, Reuters, BZ WBK

Economic and market forecasts

Poland		2009	2010	2011	2012	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12
GDP	PLNbn	1,343.4	1,415.4	1,522.7	1,621.5	349.3	369.3	375.1	428.9	372.8	392.8	401.5	454.4
GDP	%YoY	1.6	3.9	4.3	2.7	4.5	4.3	4.2	4.3	3.3	2.6	2.4	2.4
Domestic demand	%YoY	-1.1	4.6	3.8	1.2	4.4	4.3	3.2	3.3	2.6	0.7	0.8	0.9
Private consumption	%YoY	2.1	3.2	3.1	1.9	3.7	3.6	3.0	2.0	2.2	1.7	1.8	2.0
Fixed investments	%YoY	-1.2	-0.2	8.5	5.2	5.9	6.9	8.5	10.3	9.5	7.0	5.0	3.0
Unemployment rate ^a	%	12.1	12.4	12.5	13.5	13.3	11.9	11.8	12.5	13.5	12.7	12.7	13.5
Current account balance	EURm	-12,152	-16,493	-15,917	-11,473	-3,135	-3,359	-4,459	-4,964	-3,657	-1,630	-2,665	-3,522
Current account balance	% GDP	-3.9	-4.7	-4.3	-3.0	-4.8	-4.9	-4.6	-4.3	-4.5	-4.0	-3.5	-3.0
General government balance	% GDP	-7.3	-7.9	-5.5	-3.4	-	-	-	-	-	-	-	-
CPI	%YoY	3.5	2.6	4.3	3.9	3.8	4.6	4.1	4.6	4.1	3.9	4.2	3.5
CPI ^a	%YoY	3.5	3.1	4.6	3.1	4.3	4.2	3.9	4.6	3.8	4.1	4.3	3.1
CPI excluding food and energy prices	%YoY	2.7	1.6	2.4	2.3	1.7	2.3	2.6	3.0	2.5	2.2	2.3	2.3
EUR/PLN	PLN	4.33	3.99	4.12	4.24	3.94	3.96	4.15	4.42	4.23	4.22	4.31	4.21
USD/PLN	PLN	3.11	3.02	2.96	3.34	2.88	2.75	2.94	3.28	3.23	3.27	3.44	3.44
CHF/PLN	PLN	2.87	2.90	3.34	3.30	3.06	3.16	3.56	3.60	3.50	3.35	3.25	3.08
GBP/PLN	PLN	4.86	4.66	4.75	5.13	4.62	4.48	4.73	5.16	5.07	5.08	5.20	5.19
Reference rate ^a	%	3.50	3.50	4.50	4.50	3.75	4.50	4.50	4.50	4.50	4.50	4.50	4.50
WIBOR 3M	%	4.42	3.94	4.54	4.91	4.10	4.43	4.72	4.91	4.97	4.93	4.89	4.85
Yield on 52-week T-bills	%	4.54	3.96	4.51	4.45	4.37	4.62	4.54	4.50	4.50	4.45	4.44	4.42
Yield on 2-year T-bonds	%	5.17	4.72	4.81	4.63	5.01	4.97	4.54	4.71	4.66	4.63	4.62	4.58
Yield on 5-year T-bonds	%	5.65	5.31	5.44	4.97	5.79	5.60	5.17	5.19	5.02	4.94	4.98	4.93
Yield on 10-year T-bonds	%	6.11	5.74	5.98	5.55	6.27	6.03	5.77	5.83	5.58	5.53	5.58	5.50

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

This analysis is based on information available until 2nd April 2012 and has been prepared by:

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