



# RATES AND FX OUTLOOK

## POLISH FINANCIAL MARKET

July 2014



Bank Zachodni WBK

 Grupa Santander

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# Summary

- ❶ **Market expectations for interest rate cuts in Poland received strong support in the last month.** Although Polish GDP growth accelerated more than expected in 1Q14, a set of below-forecast data releases for May strengthened investors' concern that the pace of economic recovery may be abating. Moreover, the CPI rate was lower than expected again, falling to 0.2%YoY in May, and it now seems very likely that inflation will be below zero in July and possibly also in August. Subdued inflation and worries about the momentum of the economic recovery convinced the Monetary Policy Council (MPC) to ease its tone in June. The Council did not rule out interest rate cuts in future, signalling a possible change in its communication framework in July, after receiving updated inflation and GDP projections from the central bank.
- ❷ The MPC meeting in July will be very important. **While one of the Council members suggested that an interest rate cut may be discussed, we think such a decision is quite unlikely so soon after the MPC reiterated that rates should remain on hold until the end of 3Q14. However, the National Bank of Poland (NBP) president and other MPC members argued recently that the forward guidance framework is no longer useful in current circumstances and we would not rule out the central bank dropping this formula from its statement in July.** The financial markets may interpret such a move as increasing the probability of a rate cut in September (the MPC does not hold a decision-making meeting in August), unless it is neutralised by some other changes in the statement. We think the decision on monetary easing will depend heavily on economic data released in the next two months. If our forecasts of robust economic growth and strong domestic demand are confirmed by then, rate cuts would be both unnecessary and unlikely.
- ❸ The Polish fixed income market has rallied in recent weeks, fuelled by ECB policy easing and market expectations of interest rate cuts in Poland. A correction caused by the 'tape scandal' (the leak of secret recordings of top officials, including the NBP President Marek Belka) proved to be short-lived and not very strong. **We think that yields may drop slightly further in the coming weeks, supported by dovish MPC rhetoric, very low inflation and the limited supply of debt. However, we are probably approaching the bottom.** We are expecting an upward trend in yields and IRS after the summer, once it becomes clear that further monetary easing in Poland is unlikely.
- ❹ After breaking out of a narrowing trading range, the EURPLN rate fell to a one-year low at the start of June and then retreated due to worries about a possible economic slowdown, increasing expectations of interest rate cuts and the 'tape scandal'. **We still believe the zloty will appreciate in the medium run, supported by a growing economy, a stable external balance and the interest rate disparity between Poland and core markets.** In the near term, the currency may be negatively affected by higher geopolitical risk (Ukraine, Iraq).

# Short- and Medium-term Strategy: Interest Rate Market

	Change (bp)		Level	Expected trend	
	Last 3M	Last 1M	end-June	1M	3M
Reference rate	0	0	2.50	→	→
3M WIBOR	-3	-4	2.68	→	→
2Y bond yield	-51	-23	2.48	↘	↗
5Y bond yield	-74	-25	3.01	↘	↗↗
10Y bond yield	-79	-24	3.43	→	↗↗
2/10Y curve slope	-28	0	95	→	↗

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

## PLN rates: our view and risk factors

**Money market:** Money market rates may drop further, in our view, as the MPC is likely to abandon its forward guidance framework at the next meeting in July, reinforcing the markets' belief that an interest rate cut is possible after the summer. While any decline in WIBOR rates will be probably very small, the FRA market should react more strongly.

**Short end:** We think yields may decline slightly more after the MPC meeting, supported by dovish MPC rhetoric, very low inflation and the limited supply of debt. However, we are probably approaching the bottom. We predict that most of monthly economic data releases in the coming month will be above consensus.

**Long end:** A slight downward move in yields is still possible, but likely to be less than at the short end. First of all, bond supply this month will be concentrated mainly in the long tenors. Secondly, we expect an upward move of long-term bond yields in the core Euro zone markets, which would also put some pressure on Polish debt.

**Risks to our view:** If the MPC does not abandon its forward guidance in July and repeats its pledge to keep rates on hold until the end of 3Q14, it will be a jug of cold water for the market, which would send yields higher across the curve. On the other hand, a rate cut in July (very unlikely in our view), would drive a much stronger fall in yields and would trigger speculation of more monetary easing to come.

# Short- and Medium-term Strategy: FX Market

	Change (%)		Level	Expected Trend	
	Last 3M	Last 1M	End-June	1M	3M
EURPLN	-0.2	0.5	4.16	→	↘
USDPLN	0.4	0.1	3.05	→	↘
CHFPLN	-0.2	0.6	3.41	→	↘
GBPPLN	2.8	1.9	5.19	→	↘
EURUSD	-0.7	0.3	1.37	→	→

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

## PLN FX Market: Our view and risk factors

**EUR:** While the risk of an early election in Poland has diminished since the government won a confidence vote, the weaker macro data and hopes for interest rate cuts, plus high geopolitical risk (Ukraine, Iraq) are weighing on the zloty. We still think the EURPLN rate should gradually decline in the coming months, supported by economic growth, the small external imbalance and the interest rate disparity between Poland and core markets.

**USD:** The Fed continues to taper QE3 but the outlook for rates staying lower for a considerable period of time may prevent a USD rally. We expect the EURUSD to move slowly higher, as the euro still has the support of corporate demand and the external surplus, while the introduction of the ECB's QE may not be imminent. Thus, the USDPLN may decrease faster than the EURPLN.

**CHF:** EURCHF should appreciate gradually if the Euro zone and global risk environments continue to improve and more portfolio flows shift away from the CHF. Therefore, the CHFPLN, after fluctuating near current levels in the near term, is also likely to decrease faster than the EURPLN in the coming months.

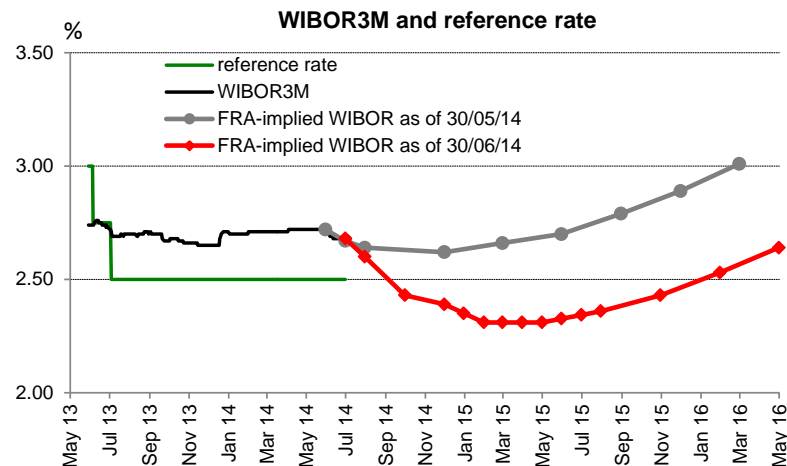
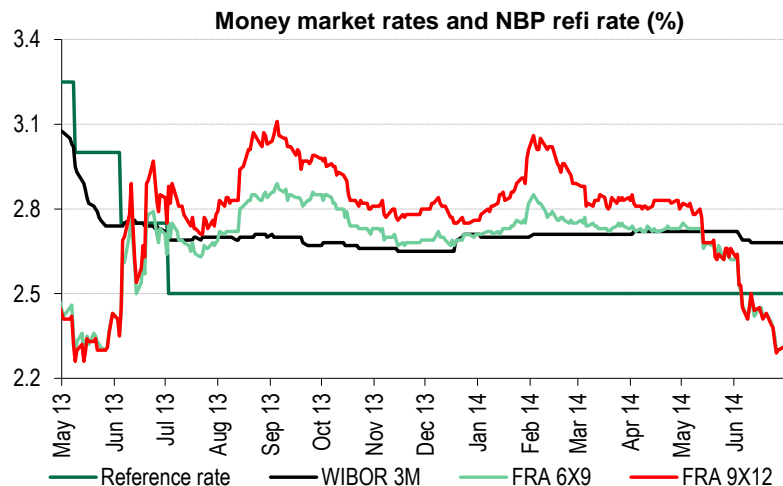
**Risks to our view:** The geopolitical situation remains tense and an escalation of conflict may have a negative impact on emerging market (EM) currencies. Much weaker-than-expected Polish economic data and faster or deeper rate cuts could also be negative for the zloty.

# Domestic Money Market: Strong Belief in a Rate Cut This Year

▶ Much lower-than-expected inflation, some disappointing economic data and a change in the MPC's bias, when it did not rule out a rate cut in the foreseeable future, have strongly impacted the market's expectations about monetary policy in Poland. As a result, WIBOR rates declined gradually by 1-6bp across the curve. FRAs dropped more: In monthly term rates fell by 20-40bp, with the highest drop for the longer tenors. Currently, the FRA market is pricing-in a rate cut of 25bp in three months' time and another one by the end of 4Q14. Moreover, an interest rate hike is no longer being discounted by rates with maturities up to two years.

▶ The MPC meeting in July will be crucial for the money market's expectations. In our opinion, the Council will keep interest rates unchanged, but it may drop the forward guidance, keeping the door open to further easing if needed. Money market rates may drop again, as the market will be speculating about an interest rate cut in September.

▶ In the medium term, we still assume there will be a gradual increase in WIBOR and FRA rates, as we think that monetary easing will not materialise until data show that economic growth remains robust, while inflation is likely to accelerate.



Source: Reuters, BZ WBK

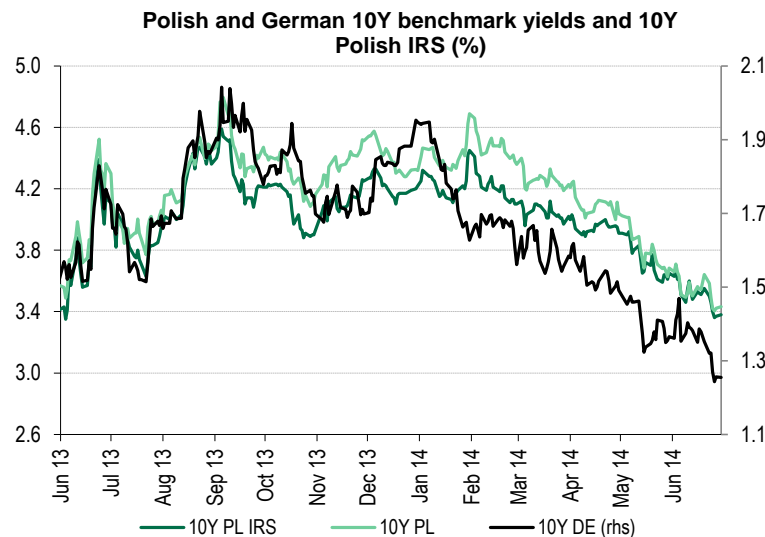
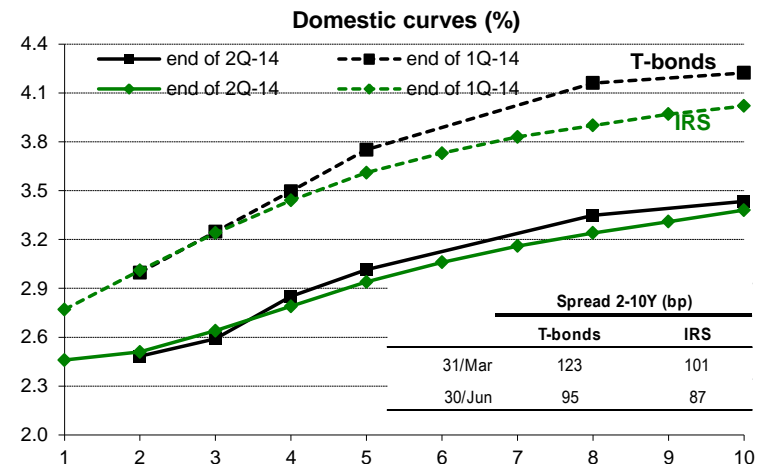
# Domestic IRS and the T-Bond Market: The Rally May Be Running Out of Steam

The domestic debt market has strengthened significantly in recent weeks, supported by low inflation, which spurs speculation about the risk of deflation, and by the dovish stance of the MPC fuelling expectations of a rate cut. A correction in the second half of the month, due to the ‘tape affair’ and worries about a snap election, proved neither strong nor long-lasting. The government won a vote of confidence in parliament and this quickly brought bond yields and IRS rates down to their lowest levels in a year. Domestic bonds were also underpinned by strengthening bonds in core markets.

A bullish flattener developed in both T-bond and IRS markets as the long end of the curves benefited the most. The 2-10Y spread narrowed slightly to 94bp for T-bonds and to 87bp for IRS.

If the MPC abandons forward guidance at its July meeting, it would probably strengthen the idea that an interest rate cut in September is very likely and would send yields lower. We expect a sharper decline at the short end of the curve, while the fall in long-term domestic yields may be limited by gradually rising bond yields in core debt markets.

However, in general we think that the scope for further strengthening of Polish debt is diminishing and yields are approaching the bottom. The trend may reverse after the summer, when it becomes clear that further monetary easing in Poland is unlikely.



Source: Reuters, BZ WBK.

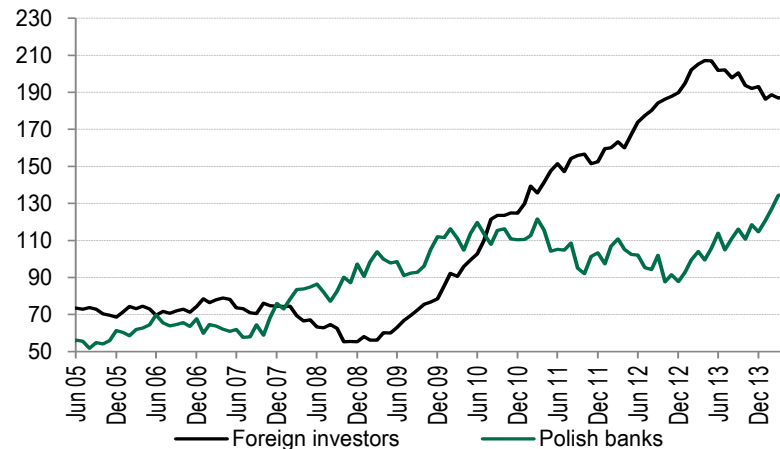
# Demand Corner: Foreign Investors Continue to Purchase Polish T-bonds

In May non-residents increased their holdings of Poland's marketable T-bonds by cPLN2bn to PLN189.6bn, maintaining their share at slightly above 40% of total PLN-denominated marketable debt. It was the third month in a row in which non-residents increased their portfolios. Demand was mainly concentrated on medium- and long-term T-bonds, maturing in 2019-23 (in monthly terms, holdings of these instruments increased by cPLN3bn in total). According to the Finance Ministry, there was clear foreign demand in June, with visibly more intense inflows than in May.

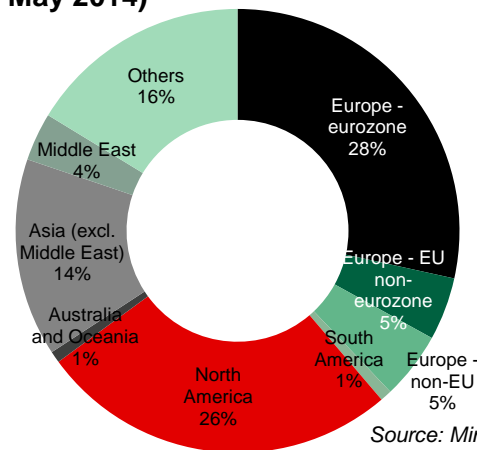
Non-resident institutional holdings were dominated by investment funds (with 42% of the total foreign portfolio at the end of May). However, in May central banks, mainly from the Middle East, increased their portfolio of Polish T-bonds by PLN2.9bn. The geographical breakdown shows investors from Asia, North America and the Middle East increased their holdings (by cPLN2.5bn in total), while Euro zone investors' holdings declined by PLN0.9bn.

Commercial banks are currently the biggest domestic players in the T-bond market. They increased their portfolios by cPLN4.5bn to nearly PLN140bn in May, the highest level ever recorded.

**Nominal holdings of Polish bonds by foreign investors and domestic banks (PLN bn)**



**Geographical structure of non-resident T-bond holdings (end of May 2014)**



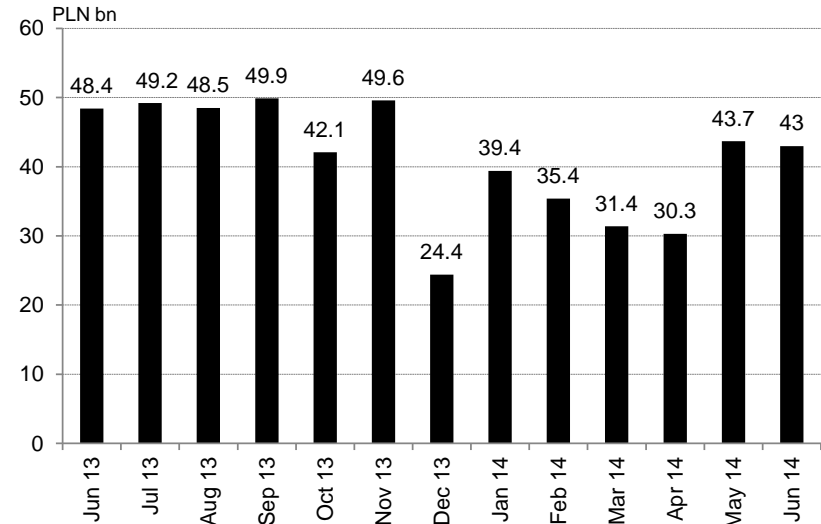
Source: Ministry of Finance, BZ WBK.



# Supply Corner: Pause in August

- ▶ The Polish Finance Ministry sold PLN11.1bn of T-bonds via both standard and switch tenders in June. As a result, it has already financed c90% of this year's borrowing requirement target. The ministry has maintained the reserve of zloty and foreign currency funds of some PLN43bn. What is more, it has started the pre-financing process for 2015 with a switch tender (in June it bought back T-bonds maturing in 2015 (i.e. WZ0115) worth PLN5.3bn).
- ▶ The Finance Ministry has said it plans to issue T-bonds worth PLN10-15bn in 3Q14, in three auctions, two of which will be held in July and one in September. In July the offer at standard auctions will amount to PLN3-9bn. The prospect of it redeeming OK0714 and making interest payments worth cPLN10.4bn in total according to its own estimates should support demand on the primary market.
- ▶ As regards foreign financing in 3Q14, the Ministry expects €0.7-0.8bn from international financial institutions and may consider issuing debt on foreign markets, depending on market conditions.
- ▶ This means the 2014 gross borrowing requirements should be 100% covered at the end of July.

## Liquid reserves held by the Ministry of Finance at end of month



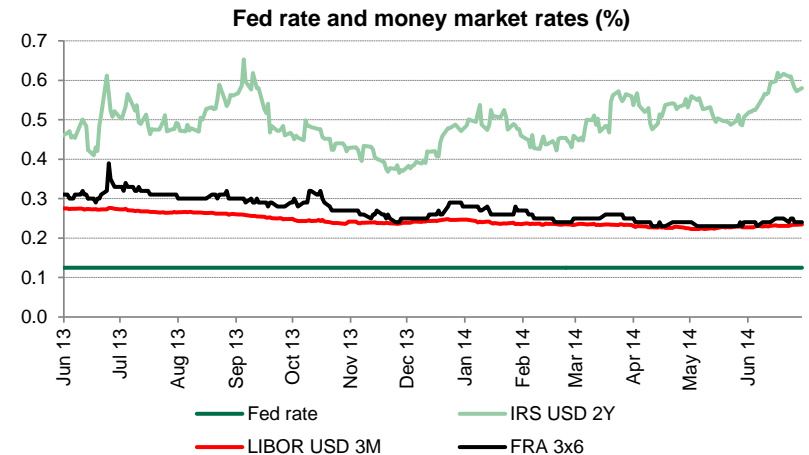
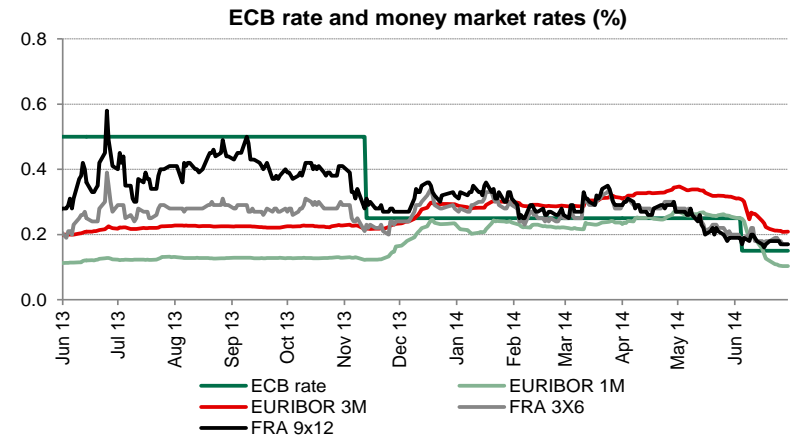
## Auction schedule for July 2014

Auction date	Settlement date	T-bonds	Expected supply
3 Jul 2014	7 Jul 2014	DS0725 / WS0428	PLN1.0-3.0bn
23 Jul 2014	25 Jul 2014	the choice depends on market conditions	PLN2.0-6.0bn

Source: Ministry of Finance, BZ WBK.

# International Money Market and IRS: Less Eventful Central Bank Meetings

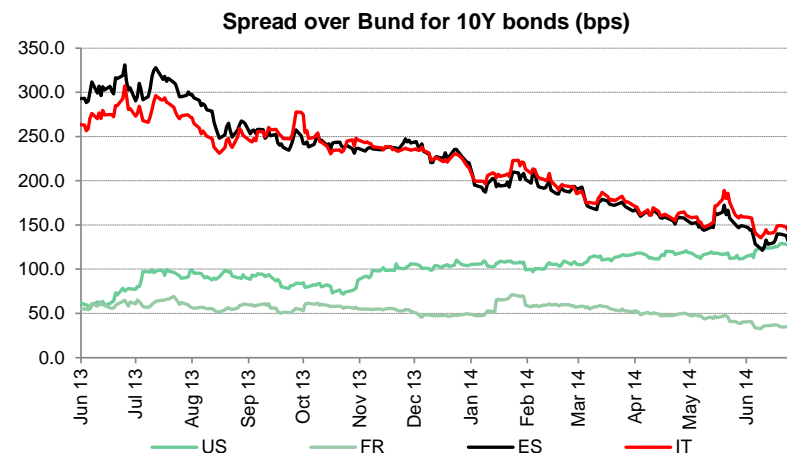
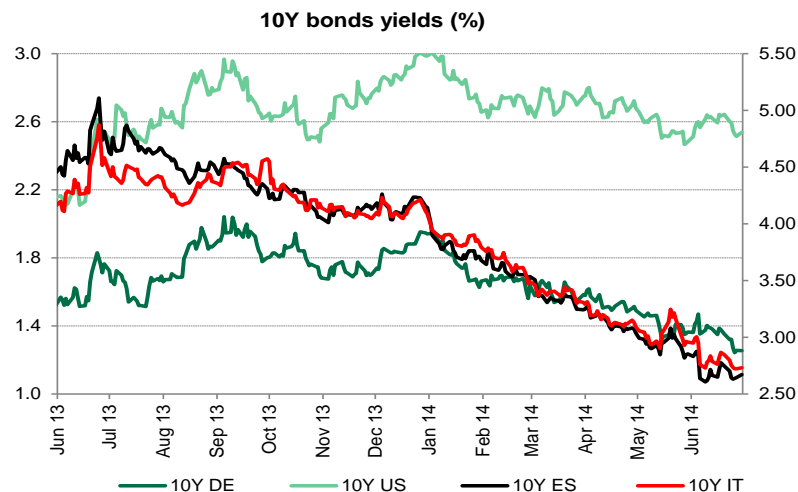
- EUR rates fell significantly after the June ECB meeting at which the bank decided to ease monetary policy, trimming official rates by 10bp, turning the deposit rate negative and introducing a series of non-standard measures. This improved market sentiment significantly and both EURIBOR and IRS fell by 5-15bp. The EUR 5Y IRS is now trading at an all-time low.
- The story is different on the other side of the Atlantic where an improving labour market and a gradual increase in inflation could cause the Fed to hike rates sooner rather than later. In monthly terms, LIBOR USD rates were more or less stable, while USD IRS increased gradually (by 3-7bp).
- Central bank meetings still take centre stage. However, the ECB's should be less eventful as the bank will now evaluate the effect of the series of easing measures presented in June. The ECB remains committed to increasing monetary easing further, if needed, which may put downward pressure on the front end of the curves in the coming months. In the US, we expect a further reduction of the FOMC's QE program in the next few months. The Fed might focus on the early communication of its exit strategy over the next few meetings. Therefore we do not rule out some upward pressure, in particular on USD IRS rates.



Source: Reuters, ECB, Fed, BZ WBK.

# International Bond Market: Higher US Rates May Put Upward Pressure on Long-term European Bonds

- ▶ The European T-bond market has continued to rally due to the ECB's decision to introduce conventional and non-conventional measures in June, combined with anaemic growth and low inflation readings. Consequently, German bond yields are close to all time lows, with the 10Y benchmark near 1.25%. Interestingly, the 10Y Spanish bond yield fell below the US Treasury equivalent, with the Italian benchmark only slightly above. At the same time, the spread between peripheral debt and bunds narrowed considerably to the lowest levels since 2010.
- ▶ US Treasuries weakened quite significantly in early June, due to the improvement in the economy and the rise in the CPI, but increasing geopolitical tensions (Ukraine, Iraq) drove yields lower again, to 2.50% for the 10Y benchmark (the lowest in four weeks). The decline in bund yields was even bigger and the spread between 10Y US Treasuries and Bunds widened to nearly 126bp in June (from 112bp at the end of May).
- ▶ In our opinion, neither the ECB nor the FOMC meeting in July will bring significant changes to monetary policy as the banks delivered signals in June. We believe that a further improvement in the US economy should cause Treasuries yields to return to an upward trend. Higher US rates would put upside pressure on EUR yields, particularly longer-dated ones, in the medium term.

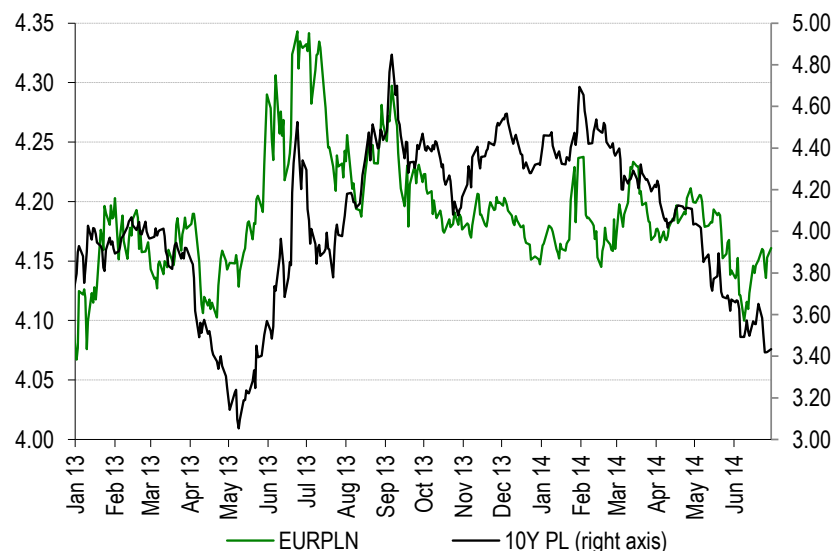


Source: Reuters, BZ WBK.

# Foreign Exchange Market: Zloty Weakens Temporarily

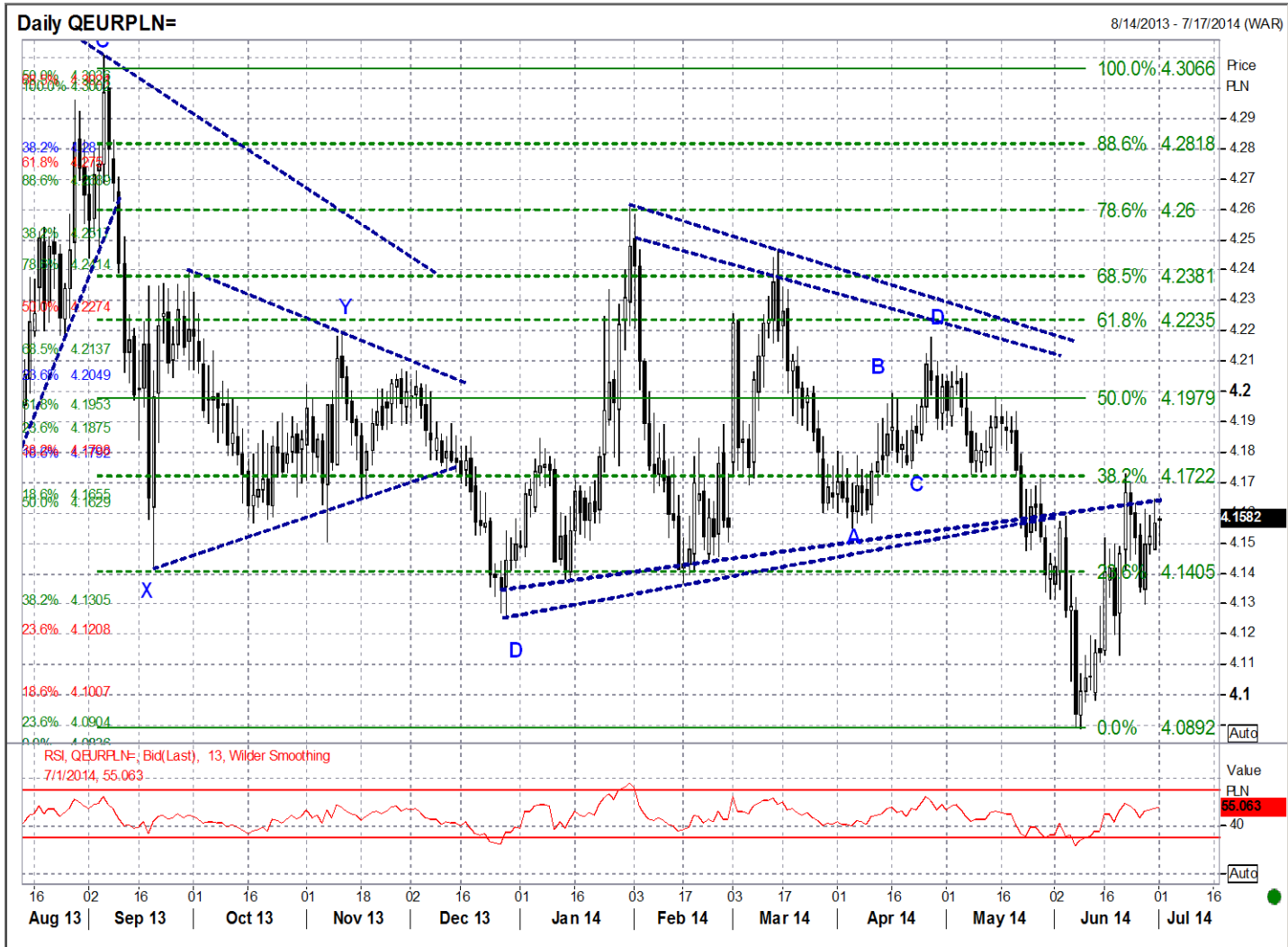
- At the end of May/beginning of June, the EURPLN broke the lower boundary of the narrowing trading range and dropped to 4.09, its lowest since April 2013. However, since then, the zloty has weakened, due to worries about a possible economic slowdown and growing expectations of interest rate cuts, among other things. The currency was also hit by the ‘tape scandal’, which involved leaked recordings of controversial conversations between top politicians, including the NBP governor. This threatened to disrupt the government and prompted speculation about an early election.
- Even though the political uncertainty disappeared quite quickly after the government won a vote of confidence, the currency failed to recover all the lost ground. It seems that weaker macro data and increasing expectations of lower interest rates are weighing on the zloty and the conflicts in Ukraine and Iraq are also having some impact.
- We still believe that, in the medium term, the zloty will be supported by a continuation of robust economic growth, a low external imbalance and the wide interest rate disparity between Poland and the core European markets.

EURPLN and Polish 10Y benchmark yield



Source: Reuters, BZ WBK

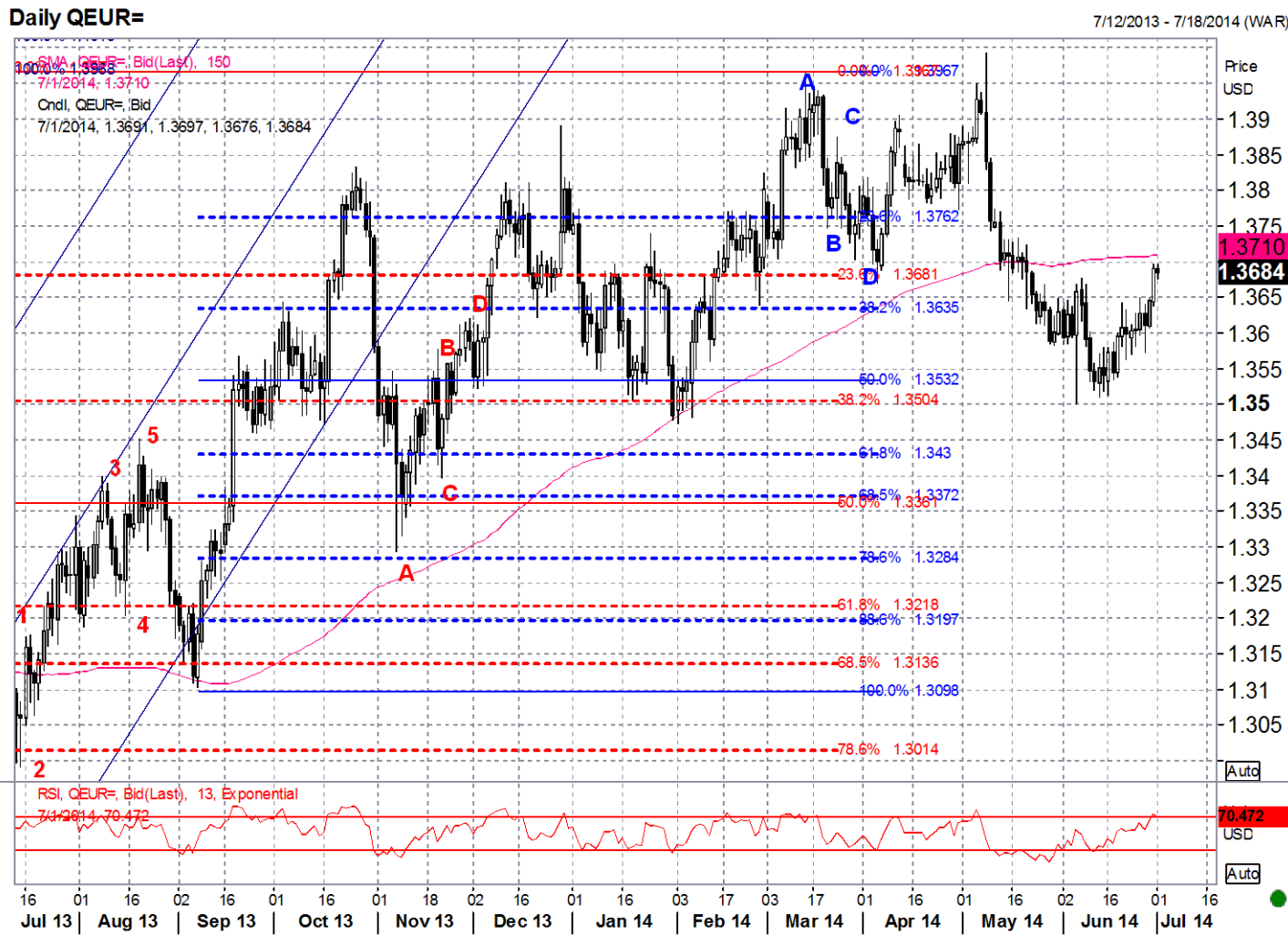
# FX Technical Analysis Corner: EURPLN in a Wide Range



- ▶ In line with our expectations, the EURPLN declined temporarily to 4.09, supported by the ECB's action in June. The downward trend effectively stopped at this level.
- ▶ The EURPLN marked a new high of 4.17, which seems a strong resistance level.
- ▶ The first support level is at 4.14 (23.6% retracement) and breaking this would open the door to a further decline.

Source: Reuters, BZ WBK

# FX Technical Analysis Corner: Will the EURUSD Break 1.371?



- As we mentioned in June's report, the EURUSD fell to its strong support point of 1.35. This level effectively stopped a further decline.
- Mixed data from the US economy and more dovish comments from Fed officials pushed the EURUSD towards 1.37.
- Currently the rate is slightly below the 150-session moving average (near 1.371). Breaking this level would open the door to a rise to towards 1.40, with short-term resistance near 1.376.

Source: Reuters, BZ WBK.

# Macroeconomic Forecasts

Poland		2011	2012	2013	2014E	1Q13	2Q13	3Q13	4Q13	1Q14E	2Q14E	3Q14E	4Q14E
GDP	PLNbn	1,528.1	1,596.4	1,635.7	1,703.5	378.4	396.3	405.6	455.5	397.4	413.8	419.5	472.7
GDP	%YoY	4.5	2.0	1.6	3.5	0.4	0.8	2.0	2.7	3.4	3.3	3.6	3.6
Domestic demand	%YoY	3.6	-0.1	0.0	3.6	-1.0	-1.6	0.6	1.8	3.0	3.7	3.5	3.9
Private consumption	%YoY	2.6	1.3	0.8	2.8	0.0	0.1	1.0	2.1	2.6	2.8	3.0	3.0
Fixed investment	%YoY	8.5	-1.6	-0.2	6.2	-2.4	-3.3	0.5	2.0	10.7	2.0	6.0	7.0
Unemployment rate <sup>a</sup>	%	12.5	13.4	13.4	12.2	14.3	13.2	13.0	13.4	13.5	12.1	11.8	12.2
Current account balance	EURm	-18,519	-14,191	-5,328	-2,379	-2,313	486	-2,086	-1,415	-766	1,980	-1,165	-2,428
Current account balance	% GDP	-5.0	-3.7	-1.4	-0.6	-3.1	-2.3	-1.9	-1.4	-1.0	-0.6	-0.3	-0.6
General government balance	% GDP	-5.1	-3.9	-4.3	5.7	-	-	-	-	-	-	-	-
CPI	%YoY	4.3	3.7	0.9	0.3	1.3	0.5	1.1	0.7	0.6	0.3	-0.1	0.5
CPI <sup>a</sup>	%YoY	4.6	2.4	0.7	0.6	1.0	0.2	1.0	0.7	0.7	0.3	0.1	0.6
CPI excluding food and energy prices	%YoY	2.4	2.2	1.2	0.7	1.2	1.0	1.4	1.2	0.8	0.8	0.6	0.8

Source: CSO, NBP, Finance Ministry, BZ WBK estimates.

<sup>a</sup> at the end of the period

\* without changes in the pension system

# Interest Rate and FX Forecasts

Poland		2011	2012	2013	2014E	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14E	3Q14E	4Q14E
Reference rate <sup>a</sup>	%	4.50	4.25	2.50	2.50	3.25	2.75	2.50	2.50	2.50	2.50	2.50	2.50
WIBOR 3M	%	4.54	4.91	3.02	2.69	3.77	2.96	2.70	2.66	2.71	2.71	2.65	2.68
Yield on 2-year T-bonds	%	4.81	4.30	2.98	2.73	3.29	2.77	2.98	2.88	3.01	2.76	2.49	2.67
Yield on 5-year T-bonds	%	5.44	4.53	3.46	3.34	3.49	3.09	3.63	3.64	3.71	3.35	3.03	3.28
Yield on 10-year T-bonds	%	5.98	5.02	4.04	3.85	3.95	3.58	4.26	4.36	4.38	3.82	3.47	3.73
2-year IRS	%	4.98	4.52	3.10	2.86	3.43	2.81	3.14	3.04	3.07	2.82	2.64	2.90
5-year IRS	%	5.24	4.47	3.51	3.40	3.52	3.08	3.76	3.68	3.70	3.31	3.12	3.47
10-year IRS	%	5.33	4.56	3.86	3.69	3.76	3.41	4.13	4.14	4.16	3.73	3.33	3.53
EUR/PLN	PLN	4.12	4.19	4.20	4.12	4.16	4.20	4.25	4.19	4.19	4.17	4.12	4.03
USD/PLN	PLN	2.96	3.26	3.16	3.00	3.15	3.22	3.21	3.08	3.06	3.04	3.00	2.90
CHF/PLN	PLN	3.34	3.47	3.41	3.36	3.38	3.41	3.44	3.40	3.42	3.42	3.35	3.23
GBP/PLN	PLN	4.75	5.16	4.94	5.06	4.88	4.94	4.97	4.98	5.06	5.11	5.11	4.97

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates; <sup>a</sup> at the end of period



# Economic Calendar and Events

Date		Event:	Note:
2-Jul	PL	<b>MPC Meeting – interest rate decision</b>	<b>Official rates on hold, the MPC may consider abandoning its forward guidance</b>
3-Jul	EZ	ECB Meeting – interest rate decision	–
	PL	<b>Auction of DS0725 / WS0428</b>	<b>Offer: PLN1.0-3.0bn</b>
8-Jul	EZ	Ecofin meeting	–
15-Jul	PL	<b>CPI for June</b>	<b>Our forecast: 0.3%YoY, slightly above the market consensus of 0.2%YoY</b>
16-Jul	PL	<b>CPI excluding food and energy prices for June</b>	<b>Our forecast of 0.9%YoY is slightly above market consensus of 0.8%YoY</b>
	PL	<b>Employment and wages for June</b>	<b>We expect employment to increase by 0.7%YoY and wages to grow 4.9% YoY. Our forecast for wage growth is above market consensus of 4.6%</b>
17-Jul	PL	<b>Industrial output and PPI for June</b>	<b>Our forecast of industrial output is 4.4%YoY (above market consensus of 3.5%YoY). We predict PPI at -2%YoY</b>
	EZ	Ecofin meeting	–
22-Jul	HU	NBH meeting - interest rate decision	We expect a rate cut of 10bp
23-Jul	PL	<b>The choice of T-bonds depends on market conditions</b>	<b>Offer: PLN2.0-6.0bn</b>
TBA	PL	<b>Retail sales for June</b>	<b>Our forecast is 3.8% YoY vs market consensus of 4.2%YoY</b>
29-30-Jul	US	FOMC meeting – interest rate decision	–
31-Jul	CZ	CNB meeting - interest rate decision	–
7-Aug	EZ	ECB Meeting – interest rate decision	–

Source: CB, CSO, Finance Ministry

# Annexe

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1. Domestic Market Performance
2. Polish Bonds: Supply Recap
3. Polish Bonds: Demand Recap
4. Euro Zone Bonds: Supply Recap
5. Poland vs Other Countries
6. Central Bank Watch

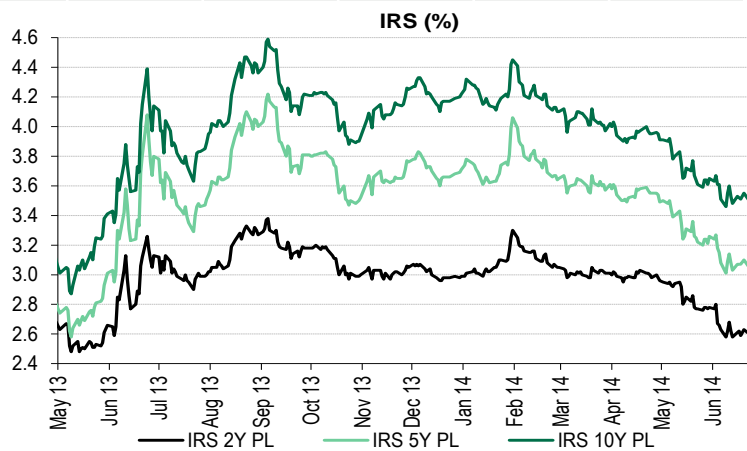
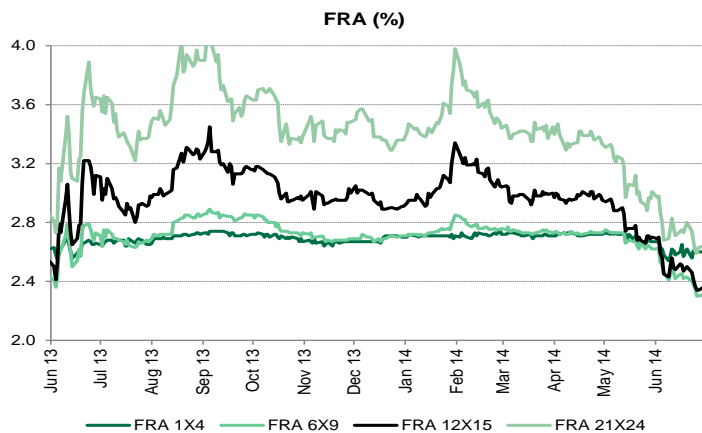
# 1. Domestic Market Performance

## Money market rates (%)

	Reference	Polonia	WIBOR (%)				OIS (%)				FRA (%)			
	rate (%)	(%)	1M	3M	6M	12M	1M	3M	6M	12M	1x4	3x6	6x9	9x12
End of June	2.50	2.51	2.61	2.68	2.69	2.74	2.41	2.33	2.23	2.18	2.60	2.43	2.31	2.31
Last 1M change (bp)	0	5	-1	-4	-5	-6	-2	-9	-17	-22	-7	-21	-31	-35
Last 3M change (bp)	0	9	0	-3	-5	-5	-2	-10	-20	-30	-11	-28	-42	-53
Last 1Y change (bp)	-25	12	-14	-4	-2	3	-9	-17	-32	-37	-5	-21	-40	-53

## Bond and IRS market (%)

	BONDS			IRS			Spread BONDS / IRS (bp)		
	2Y	5Y	10Y	2Y	5Y	10Y	2Y	5Y	10Y
End of June	2.48	3.01	3.43	2.51	2.94	3.38	-3	7	5
Last 1M change (bp)	-23	-25	-24	-27	-32	-27	4	7	3
Last 3M change (bp)	-51	-74	-79	-50	-67	-64	-1	-7	-15
Last 1Y change (bp)	-50	-66	-86	-61	-84	-73	11	18	-13



Source: Reuters, BZ WBK

## 2. Polish Bonds: Supply Recap

### Total issuance in 2014 by instruments (in PLN mn, nominal terms)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
<b>T-bonds auction</b>	18,143	8,821	6,573	17,503	5,694	4,990	9,000		5,000	5,000	3,000	2300	86,024
<b>T-bills auction</b>													0
<b>Retail bonds</b>	256	475	190	170	170	170	170	180	170	175	185	176	2,487
<b>Foreign bonds/credits</b>	16,724	1,150					5450			3200			26,524
<b>Prefinancing and financial resources at the end of 2013</b>	25,000												25,000
<b>Total</b>	<b>60,123</b>	<b>10,445</b>	<b>6,763</b>	<b>17,673</b>	<b>5,864</b>	<b>5,160</b>	<b>14,620</b>	<b>180</b>	<b>5,170</b>	<b>8,375</b>	<b>3,185</b>	<b>2476</b>	<b>140,034</b>
<b>Redemption</b>	16,497	5,613	2,230	16,035	116	60	9,470	1,793	2,796	83	816	91	55,599
<b>Net inflows</b>	<b>43,626</b>	<b>4,832</b>	<b>4,533</b>	<b>1,638</b>	<b>5,749</b>	<b>5,100</b>	<b>5,150</b>	<b>-1,613</b>	<b>2,374</b>	<b>8,292</b>	<b>2,369</b>	<b>2,385</b>	<b>84,435</b>
<b>Rolling over T-bonds</b>			4,807			6,117							10,924
<b>Buy-back of T-bills/ FX-denominated bonds</b>													0
<b>Total</b>	<b>43,626</b>	<b>4,832</b>	<b>9,340</b>	<b>1,638</b>	<b>5,749</b>	<b>11,216</b>	<b>5,150</b>	<b>-1,613</b>	<b>2,374</b>	<b>8,292</b>	<b>2,369</b>	<b>2,385</b>	<b>95,359</b>
<b>Coupon payments from domestic debt</b>	1,546			5,596			1,327		1,298	7,507			17,275

Note: our forecasts = shaded area

Source: MF, BZ WBK

## 2. Polish Bonds: Supply Recap (cont.)

Schedule of Treasury securities redemption by instruments (in PLN m)

	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	15,968		66	16,035		16,035
May			116	116		116
June			60	60		60
July	8,145		89	8,234	1,236	9,470
August			198	198	1,594	1,793
September			359	359	2,438	2,796
October			83	83		83
November			171	171	645	816
December			91	91		91
<b>Total 2014</b>	<b>37,773</b>		<b>1,677</b>	<b>39,450</b>	<b>16,149</b>	<b>55,599</b>
<b>Total 2015</b>	<b>78,037</b>		<b>1,710</b>	<b>79,747</b>	<b>14,789</b>	<b>94,536</b>
<b>Total 2016</b>	<b>84,347</b>		<b>1,273</b>	<b>85,621</b>	<b>17,262</b>	<b>102,882</b>
<b>Total 2017</b>	<b>58,543</b>		<b>917</b>	<b>59,460</b>	<b>12,566</b>	<b>72,026</b>
<b>Total 2018</b>	<b>66,671</b>		<b>911</b>	<b>67,582</b>	<b>14,396</b>	<b>81,978</b>
<b>Total 2019+</b>	<b>148,099</b>		<b>3,233</b>	<b>151,332</b>	<b>135,784</b>	<b>287,116</b>

Source: MF, BZ WBK

## 2. Polish Bonds: Supply Recap (cont.)

Scheduled wholesale bond redemption by holders (data at the end of May 2014, in PLN mn)

	Foreign investors	Domestic banks	Insurance Funds	Pension Funds	Mutual Funds	Individuals	Non-financial sector	Other	Total
Q1 2014	0	0	0	0	0	0	0	0	0
Q2 2014	0	0	0	0	0	0	0	0	0
Q3 2014	4,942	1,914	1,500	14	465	131	10	120	9,096
Q4 2014	0	0	0	0	0	57	7	13	77
<b>Total 2014</b>	<b>4,942</b>	<b>1,914</b>	<b>1,500</b>	<b>14</b>	<b>465</b>	<b>187</b>	<b>16</b>	<b>133</b>	<b>9,173</b>
	54%	21%	16%	0%	5%	2%	0%	1%	100%
<b>Total 2015</b>	30,612	31,587	8,316	532	5,959	240	284	5,894	83,425
	37%	38%	10%	1%	7%	0%	0%	7%	100%
<b>Total 2016</b>	40,953	17,711	7,793	798	10,998	119	406	6,627	85,406
	48%	21%	9%	1%	13%	0%	0%	8%	100%
<b>Total 2017</b>	23,444	16,576	6,093	627	7,846	54	172	3,732	58,543
	40%	28%	10%	1%	13%	0%	0%	6%	100%
<b>Total 2018</b>	16,376	31,702	3,838	383	9,488	68	171	4,290	66,317
	25%	48%	6%	1%	14%	0%	0%	6%	100%
<b>Total 2019+</b>	72,625	37,920	24,887	972	10,847	215	276	8,187	155,929
	47%	24%	16%	1%	7%	0%	0%	5%	100%

Source: MF, BZ WBK

## 3. Polish Bonds: Demand Recap

### Holders of marketable PLN bonds

	Nominal value (PLN bn)				Nominal value (PLN bn)			% change in April			Share in TOTAL (%) in May
	End May'14	End Apr'14	End Dec'13	End Sep'13	End 1Q 2014	End 4Q 2013	End 3Q 2013	MoM	3-mth	YoY	
<b>Domestic investors</b>	282.4	278.7	381.2	377.3	277.9	381.2	377.3	1.32	3.09	-21.32	59.8
<b>Commercial banks</b>	139.9	135.4	114.7	116.2	134.3	114.7	116.2	3.32	10.27	32.23	29.6 (0.6pp)
<b>Insurance companies</b>	52.7	53.2	52.0	52.8	52.9	52.0	52.8	-1.08	0.12	1.26	11.2 (-0.3pp)
<b>Pension funds</b>	3.3	3.5	125.8	122.7	3.5	125.8	122.7	-5.33	25.16	-97.14	0.7
<b>Mutual funds</b>	46.2	46.0	46.7	46.1	45.8	46.7	46.1	0.42	1.30	1.09	9.8 (-0.1pp)
<b>Others</b>	40.2	40.5	42.0	39.5	41.4	42.0	39.5	-2.2	-0.3	9.4	8.5 (-0.2pp)
<b>Foreign investors*</b>	189.7	187.6	193.2	200.6	186.9	193.2	200.6	1.07	-3.24	-8.95	40.2
<b>Banks</b>	30.5	30.5	29.1	32.1	30.5	29.1	32.1	5.72	4.85	-18.10	6.5
<b>Non-bank fin. sector</b>	150.6	150.6	156.0	159.7	150.6	156.0	159.7	-1.21	-3.45	-5.26	31.9 (0.4pp)
<b>Non-financial sector</b>	4.5	4.5	4.7	5.2	4.5	4.7	5.2	7.53	-5.22	-17.35	0.9
<b>TOTAL</b>	472.0	466.3	574.3	577.9	464.8	574.3	577.9	1.22	4.90	-16.59	100

\*Total for foreign investors does not match sum of values presented for sub-categories due to omission of irrelevantly small group of investors.

Source: MF, BZ WBK

## 4. Euro Zone Bonds: Supply Recap

### Euro zone planned and completed issuance in 2014 (€ bn)

	Total redemptions	Deficit	Borrowing needs	Expected bond supply	% of completion (YtD*)
Austria	23.4	4.3	27.7	24.7	49
Belgium	21.8	9.8	31.6	30.0	73
Finland	6.9	4.8	11.7	11.7	55
France	105.0	70.2	175.2	174.0	70
Germany	144.0	-	144	144.0	52
Greece	16.8	5.6	-	-	-
Ireland	6.9	7.7	14.6	14.6	65
Italy	187.8	27.6	235.4	235.4	71
Netherlands	32.0	15.9	47.9	45.9	71
Portugal	11.4	7.4	18.8	7.2	61
Spain	68.2	36.7	141.3	141.3	65
<b>Total</b>	<b>624.2</b>	<b>189.9</b>	<b>848.2</b>	<b>828.8</b>	<b>65</b>

\*/ YTD (year calendar) data for 2014

Source: Eurostat, BZ WBK.



## 5. Poland vs. Other Countries

### Main macroeconomic indicators (European Commission forecasts)

	GDP (%)		Inflation (HICP, %)		C/A balance (% of GDP)		Fiscal balance (% of GDP)		Public debt (% of GDP)	
	2013	2014	2013	2014	2013	2014	2013	2014	2013	2014
<b>Poland</b>	1.6	3.2	0.8	1.1	-1.6	-1.7	-4.3	5.7	57.0	49.2
<b>Czech Republic</b>	-0.9	2.0	1.4	0.8	-1.2	-0.4	-1.5	-1.9	46.0	44.4
<b>Hungary</b>	1.1	2.3	1.7	1.0	3.1	3.0	-2.2	-2.9	79.2	80.3
<b>EU</b>	0.1	1.6	1.5	1.0	1.6	1.8	-3.0	-2.5	88.9	89.5
<b>Euro area</b>	-0.4	1.2	1.3	0.8	2.6	2.9	-3.3	-2.6	95.0	96.0
<b>Germany</b>	0.4	1.8	1.6	1.1	7.4	7.3	0.0	0.0	78.4	76.0

### Main market indicators (%)

	Reference rate (%)		3M market rate (%)		10Y yields (%)		10Y Spread vs Bund (bp)		CDS 5Y	
	2013	end of June	2013	end of June	2013	end of June	2013	end of June	2013	end of June
<b>Poland</b>	2.50	2.50	2.71	2.68	4.32	3.43	238	218	79	57
<b>Czech Republic</b>	0.05	0.05	0.05	0.04	2.53	1.47	58	21	60	45
<b>Hungary</b>	3.00	2.30	2.99	2.34	5.71	4.48	377	323	256	162
<b>Euro area</b>	0.25	0.15	0.29	0.21						
<b>Germany</b>					1.94	1.26			26	21

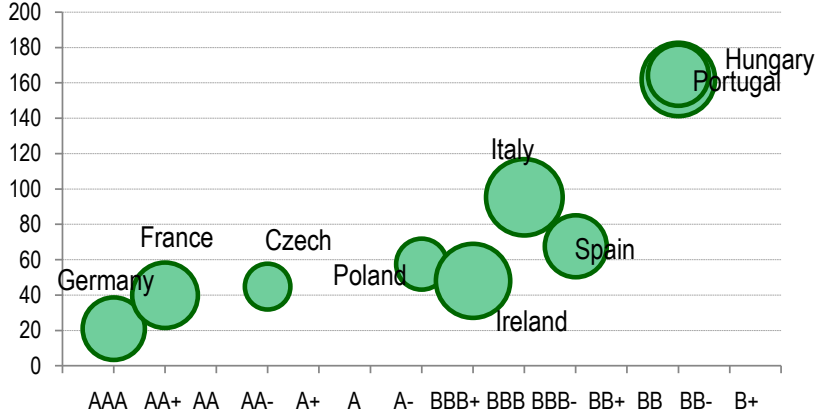
Source: EC – Spring 2014, stat offices, central banks, Reuters, BZ WBK.

# 5. Poland vs Other Countries (cont.)

**Sovereign ratings**

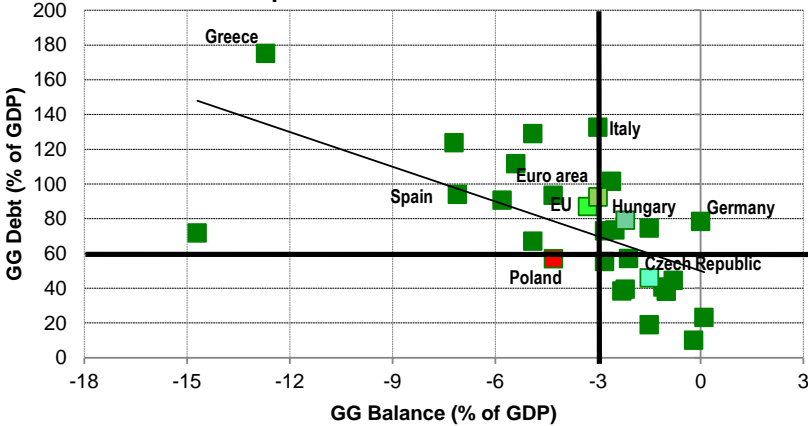
	S&P		Moody's		Fitch	
	rating	outlook	rating	outlook	rating	outlook
Poland	A-	stable	A2	stable	A-	stable
Czech	AA-	stable	A1	stable	A+	stable
Hungary	BB	stable	Ba1	negative	BB+	stable
Germany	AAA	stable	Aaa	negative	AAA	stable
France	AA	stable	Aa1	negative	AA+	negative
UK	AAA	negative	Aa1	negative	AA+	stable
Greece	B-	stable	Caa3	stable	B	stable
Ireland	BBB+	positive	Baa3	positive	BBB+	stable
Italy	BBB	negative	Baa2	stable	BBB+	negative
Portugal	BB	stable	Ba2	positive	BB+	negative
Spain	BBB	stable	Baa3	stable	BBB	stable

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



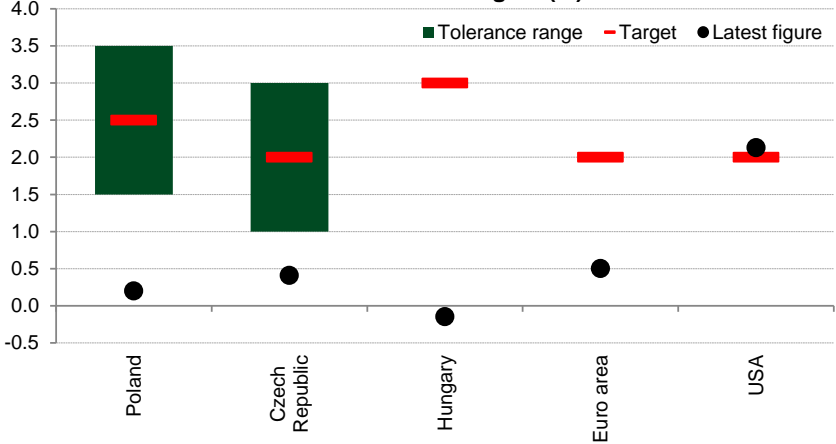
Note: Size of bubbles reflects the debt/GDP ratio

**Fiscal position of the EU countries**

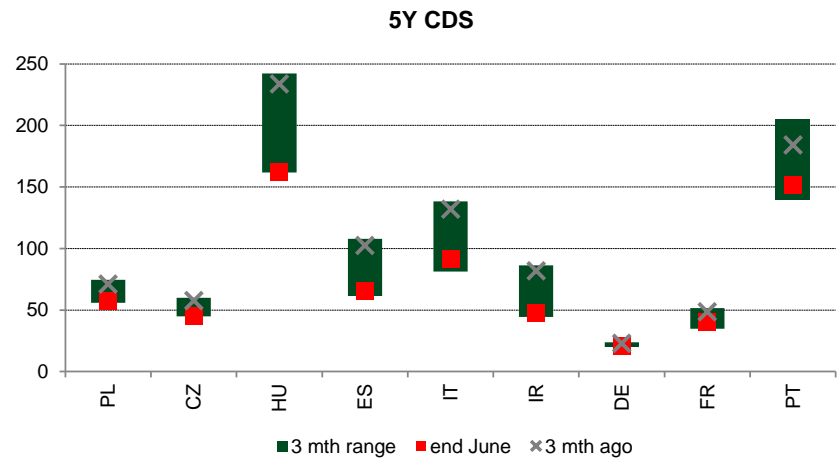
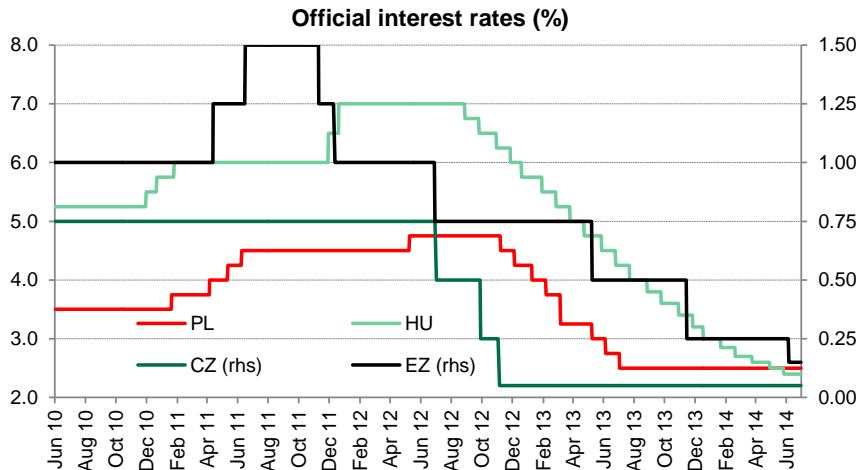
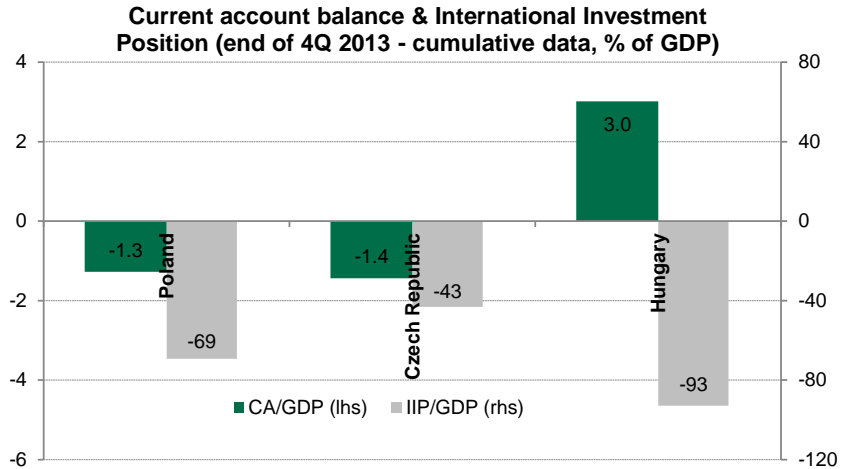
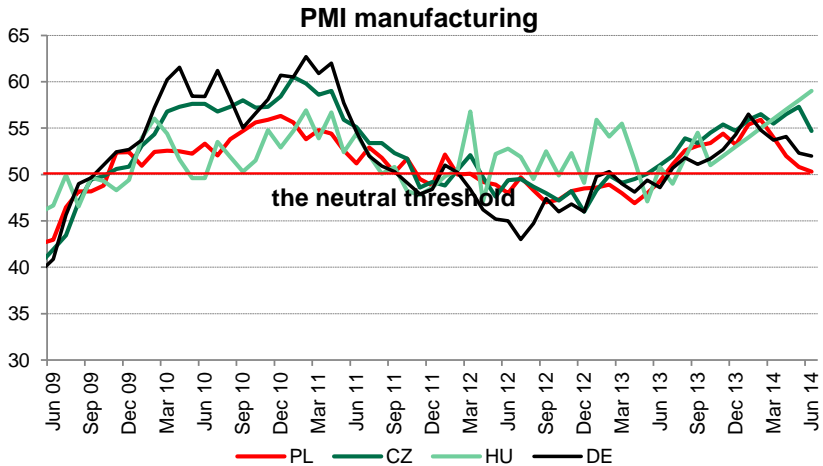


Source: rating agencies, Reuters, EC, BZ WBK

**Inflation rates vs targets (%)**

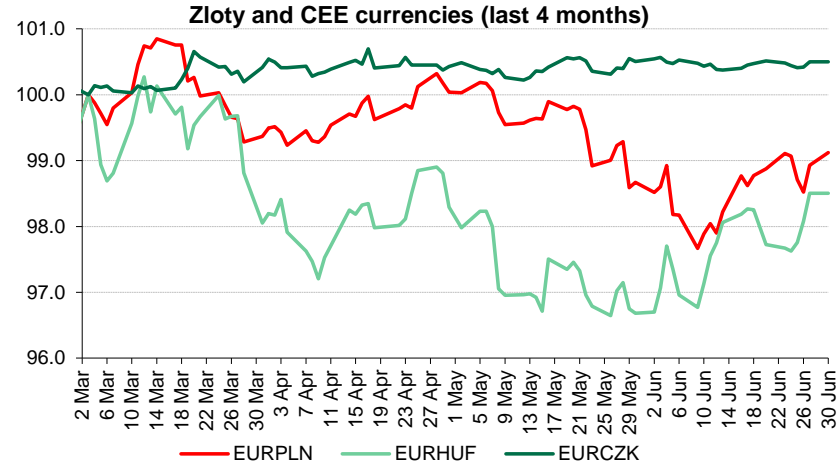
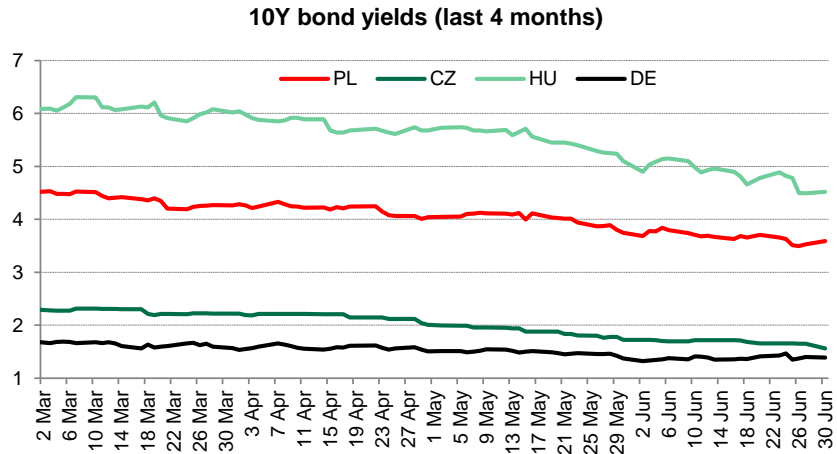
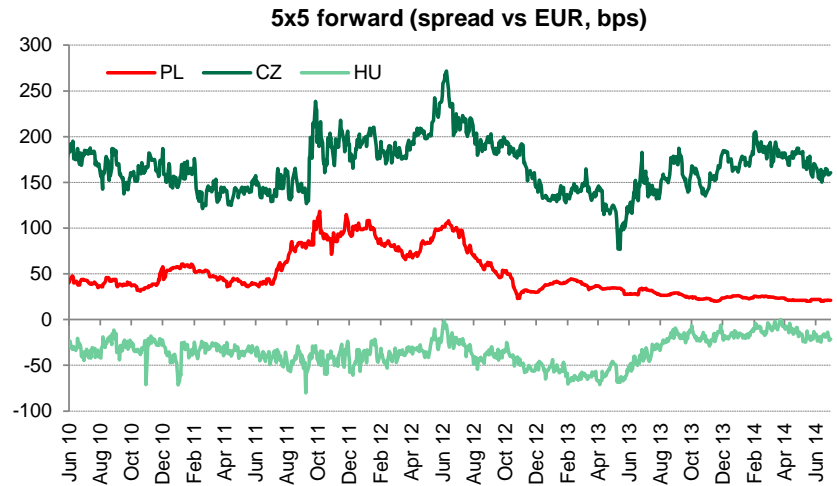
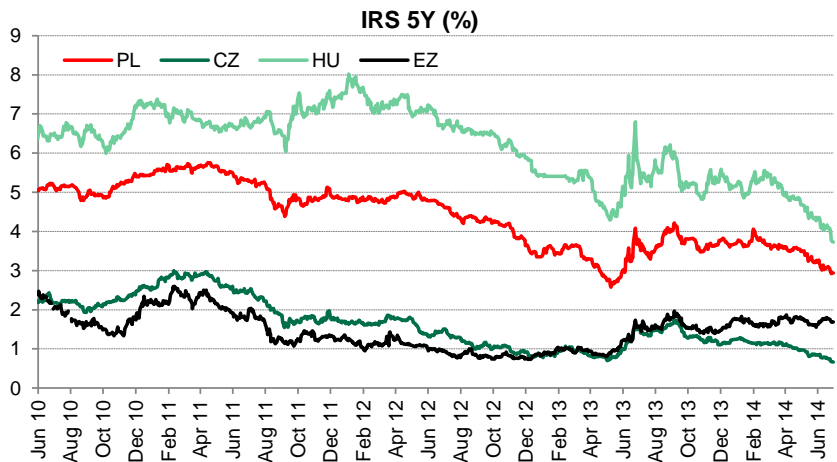


# 5. Poland vs Other Countries (cont.)



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

# 5. Poland vs Other Countries (cont.)



Source: Reuters, BZ WBK

## 6. Central Bank Watch

		Last	2013	2014	Expected changes (bp)			Comments
					1M	3M	6M	
<b>Euro zone</b>	Forecast	0.15	0.25	0.15				The ECB meeting in July is unlikely to bring any significant changes in monetary policy as the bank took action in June. The ECB may provide more details of the TLTROs and even on the ABS programme .
	Market implied »				-3	-2	-5	
<b>UK</b>	Forecast	0.50	0.50	0.75				We expect the BoE to keep interest rates unchanged, but the Council has made clear that it is getting closer to the point where official rates will need to be raised.
	Market implied »				3	13	35	
<b>US</b>	Forecast	0-.25	0-.25	0.25				FOMC meetings in July are unlikely to bring any significant changes to monetary policy. We expect the FOMC to focus on the early communication of its exit strategy over the next few meetings. We uphold our view that the Fed is unlikely to hike rates before 2H15.
	Market implied »				15	23	33	
<b>Poland</b>	Forecast	2.50	2.50	2.50				This month's MPC meeting will be very important. In our opinion, the Council will keep rates unchanged, but it may drop the forward guidance, keeping door open to further monetary easing if needed.
	Market implied »				-8	-25	-37	
<b>Czech Republic</b>	Forecast	0.05	0.05	0.05				The CNB decided to keep interest rates flat (with the key two-week repo rate at 0.05%) and confirmed its current commitment to keep the EURCZK above, but close to, 27. However, the CNB decided to postpone the end of its FX intervention until 2Q15 instead of the previously discussed 1Q15.
	Market implied »				29	30	25	
<b>Hungary</b>	Forecast	2.30	3.00	2.00				The NBH has continued its easing cycle, trimming official rates by 10bp in June. Cautious rate cuts may continue in the coming months. Due to the very low CPI, we decided to change our monetary policy forecast and now expect the bottom of the cycle to be 2%.
	Market implied »				-6	-6	-6	

Source: Reuters, BZ WBK

This analysis is based on information available through June 30, 2014 and has been prepared by:

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### EXPLANATION OF THE RECOMMENDATION SYSTEM

DIRECTIONAL RECOMMENDATIONS IN BONDS		DIRECTIONAL RECOMMENDATIONS IN SWAPS	
	Definition		Definition
<b>Long / Buy</b>	Buy the bond for an expected average return of at least 10bp in 3 months (decline in the yield rate), assuming a directional risk.	<b>Long / Receive fixed rate</b>	Enter a swap receiving the fixed rate for an expected average return of at least 10bp in 3 months (decline in the swap rate), assuming a directional risk.
<b>Short / Sell</b>	Sell the bond for an expected average return of at least 10bp in 3 months (increase in the yield rate), assuming a directional risk.	<b>Short / Pay fixed rate</b>	Enter a swap paying the fixed rate for an expected average return of at least 10bp in 3 months (increase in the swap rate), assuming a directional risk.
RELATIVE VALUE RECOMMENDATIONS			
	Definition		
<b>Long a spread / Play steepeners</b>	Enter a long position in a given instrument vs a short position in another instrument (with a longer maturity for steepeners) for an expected average return of at least 5bp in 3 months (increase in the spread between both rates).		
<b>Short a spread / Play flatteners</b>	Enter a long position in given an instrument vs a short position in other instrument (with a shorter maturity for flatteners) for an expected average return of at least 5bp in 3 months (decline in the spread between both rates).		
FX RECOMMENDATIONS			
	Definition		
<b>Long / Buy</b>	Appreciation of a given currency with an expected return of at least 5% in 3 months.		
<b>Short / Sell</b>	Depreciation of a given currency with an expected return of at least 5% in 3 months.		

NOTE: Given the recent volatility seen in the financial markets, the recommendation definitions are only indicative until further notice.

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