



RATES AND FX OUTLOOK

POLISH FINANCIAL MARKET

August 2014



Bank Zachodni WBK

 Grupa Santander

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Summary

- ❶ The most recent monthly economic data for Poland have clearly disappointed, suggesting that economic growth has slowed. In our view, GDP growth in 2Q14E was indeed lower than in the first quarter, but still above 3%. However, the first monthly data for 3Q14 will be more important, indicating whether the economy is decelerating further or not. **It is true that the recent extension of economic and financial sanctions against Russia by the EU and US generates additional risk for the economic recovery in Europe and in Poland, but we still believe that after a temporary soft patch in 2Q-3Q14, Poland will start growing faster again, with GDP expanding by 3.3% in 2014E and 3.7% in 2015E.**
- ❷ The Monetary Policy Council (MPC) has dropped the forward guidance in July but maintained the view that interest rate cuts are not likely. The next decision-making meeting of the MPC is scheduled for the start of September, when the Council will know not only the GDP data for 2Q14 but also the first monthly figures from the third quarter. **Though the last two weeks brought a 10bp increase in the FRA curve, the FRA 6X9 at c2.35 is still below the reference rate (2.5%) and 3M WIBOR (2.67%). We think that a scenario of rate cuts is possible only if the next data show strong disappointments again. This is not what we predict (though the risk of such a scenario has increased after a very weak PMI reading), but on the other hand we also think that the data releases will not be strong enough to substantially reduce investors' hopes for monetary easing.**
- ❸ The strong rally in the Polish fixed income market has pushed the yields of 2Y bonds in July to a new all-time low, while yields of 5Y-10Y bonds slid to their lowest level since May 2013. However, stronger data from the US and not so dovish FOMC rhetoric triggered a sharp correction in core and emerging debt. **In our opinion, the lack of a clear rebound in this month's domestic economic data releases, a drop in inflation to below zero, plus worries about the potential impact of escalating tension between Russia and Western Europe, may keep short-term yields of Polish bonds near recent lows in coming weeks. We expect the 5-10Y segment to recover after recent losses, though it might be still under the pressure of higher global risk aversion amid expectations for faster rate hikes in the US.** Nevertheless, we think that a more significant correction in the Polish fixed income market is possible in September, after the MPC keeps main interest rates unchanged.
- ❹ The zloty had been extremely stable from mid-June until the last days of July, despite strengthening internal (worries about economic slowdown) and external (geopolitical tensions) risk factors. The geopolitical risks together with the combination of a mix of lower GDP growth / risk of lower rates in Poland and higher GDP / higher risk of rate hikes in the US will continue to weigh on sentiment against the Polish currency. However, **we expect the EURPLN to be rather flat on a 1M horizon and we still expect the zloty to appreciate towards the year-end, supported by a growing economy, low external imbalances and high interest rate disparity.**

Short- and Medium-term Strategy: Interest Rate Market

	Change (bp)		Level	Expected trend	
	Last 3M	Last 1M	end-July	1M	3M
Reference rate	0	0	2.50	→	→
3M WIBOR	-5	-1	2.67	→	→
2Y bond yield	-42	-2	2.46	↘	→
5Y bond yield	-60	-8	2.93	↘	↗
10Y bond yield	-62	-2	3.41	↘	↗
2/10Y curve slope	-20	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: At the turn of July-August, FRA rates increased considerably due to the sell-off on IRS and T-bond markets. Consequently, investors scaled back their expectations of interest rate cuts later this year. In our opinion this development was only short-lived and we expect money market rates to return to a downward trend as macro data due for release in August will not be strong enough to reduce expectations of further monetary easing.

Short end: After declining through July (2Y benchmark reached its lowest level in history), the turn of July-August brought a significant sell-off, but front ends of curves lost less than other instruments. Interest rate cut expectations should anchor the short end of curves near current levels in the short run, but a lack of monetary easing later this year due to a rebound in macro data may bring a more significant upward move in 4Q14E.

Long end: The mid and long end of curves lost the most during a strong sell-off at the turn of July-August. After sharp yield/rates increase we do not exclude a rebound as macro data releases in August will not be very strong and high real yields will increase the attractiveness of these instruments. However, strengthening will be limited in the medium term as the long end of curves remain more vulnerable to external factors, in particular to expectations of rate hikes in the US, which may put again upward pressure on yields/rates.

Risks to our view: A stronger than predicted deterioration in the Polish economic outlook may result in monetary easing as early as September. Consequently, yields/rates would fall sharply, especially at the front end.

Short- and Medium-term Strategy: FX Market

	Change (%)		Level	Expected Trend	
	Last 3M	Last 1M	End-July	1M	3M
EURPLN	-0.8	0.1	4.16	→	↘
USDPLN	2.1	2.0	3.11	→	↘↘
CHFPLN	-0.9	0.0	3.41	↘	↘
GBPPLN	2.5	1.1	5.24	→	↘
EURUSD	-2.9	-1.9	1.34	→	↗

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: The Euro weakened against the US dollar due to renewed expectations of earlier rate hikes in the US after better macro data and the less dovish tone of July's FOMC statement. However, in the medium term we still foresee the EURUSD returning to an upward trend, supported by an external surplus and corporate demand. While in the short run the EURPLN may be volatile around the top limit of a consolidation channel between 4.12 and 4.17, in the medium term we still foresee the zloty strengthening against the euro, supported by the ECB and the Polish MPC's hesitation to cut rates.

USD: In the short run volatility on the USDPLN should remain strong as a further improvement in the USA macro data will generate pressure on the EURUSD's decline. In the short run we expect the USDPLN to stay at high levels (above 3.10), but in the medium term we expect the exchange rate to shift downwards quite considerably as the EURUSD resumes a downward trend.

CHF: The SNB remains committed to its EUR/CHF floor and levels in the 1.20-30 range still imply a strong CHF, with insufficient upward pressure on prices. Accordingly, we expect the CHFPLN to continue its gradual decline in the short and medium terms as the zloty continues strengthening against the euro.

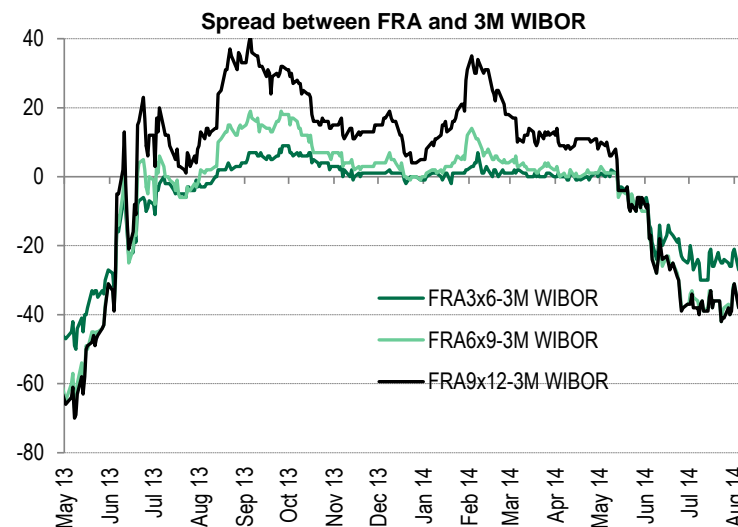
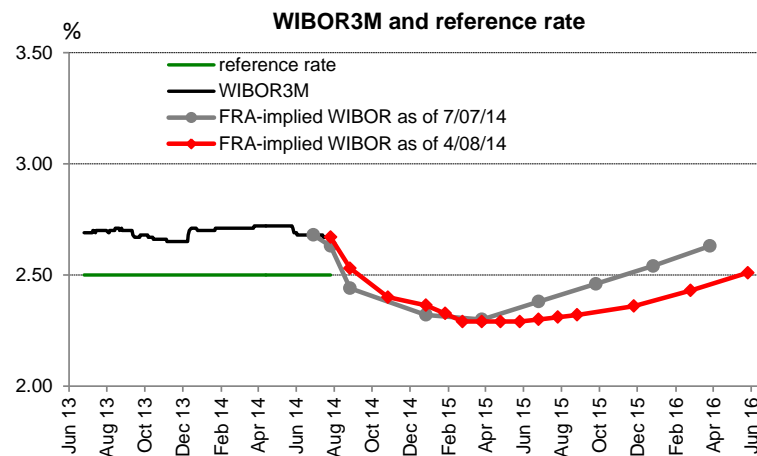
Risks to our view: The mix of lower GDP growth / risk of lower rates in Poland and higher GDP / higher risk of rate hikes in the US does not favour the Polish currency. The materialisation of monetary easing in Poland in 3 months' time may result in a significant zloty weakening.

Domestic Money Market: Repricing rate cut expectations after debt market sell-off

WIBOR rates were more or less stable in July (rates declined by only 1bp in monthly terms) despite disappointing domestic macro data, which significantly strengthened interest rate cut expectations for later this year. At the same time, FRA rates quickly adjusted to weak macro data, pricing-in a rate cut of 25bp in 3 months' time and an 85% chance of another 25bp cut in 6 months.

The sharp correction of the domestic debt market at the turn of July-August caused an increase in FRAs across the board (by 5-20bp in just three days), scaling back expectations for a WIBOR 3M decline in upcoming months (from 42bp after retail sales data to 31bp in 6-9 months). Notwithstanding, investors do not expect any rate hikes in a two-year period.

This month, investors will only focus on macro data as there is no MPC meeting in August. A lower than market consensus reading of 2Q GDP growth should again strengthen expectations of monetary easing later this year, especially as macro data readings in August will not be strong enough to dispel concerns about the state of the Polish economy in the coming months. Therefore, we expect FRA rates to resume a downward trend in upcoming weeks. As regards WIBORs we do not expect any significant changes in 3 months' time.



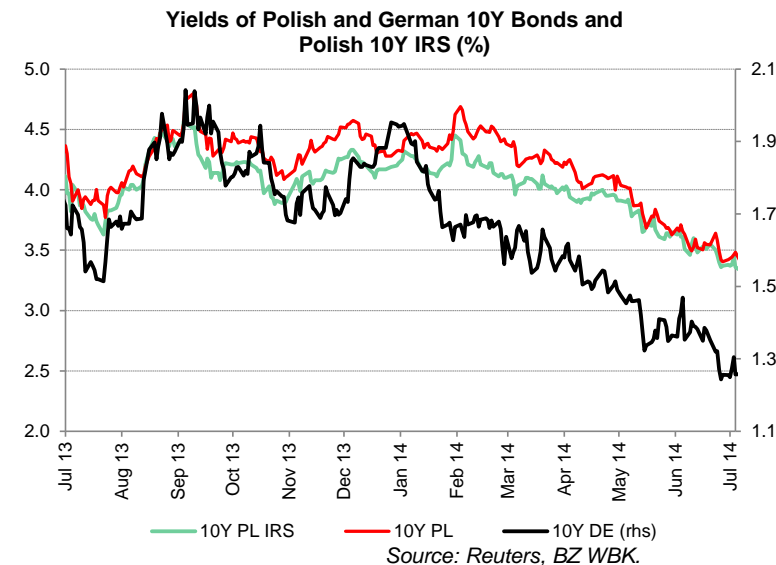
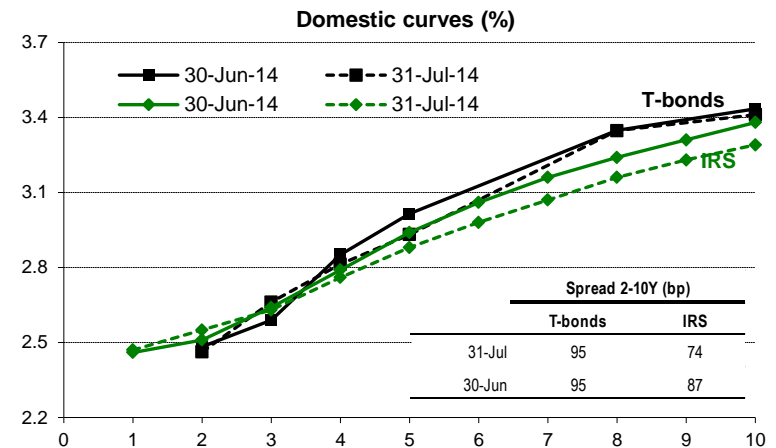
Source: Reuters, BZ WBK

Domestic IRS and the T-Bond Market: Gradual rebound possible after strong sell-off

In July, the domestic interest rate market has continued to gain due to the core bonds rally (the yield on the 10Y Bund reached a new record low) and weak domestic macro data (industrial output, retail sales), which fuelled expectations for monetary easing in Poland later this year. The turn of July and August brought a deeper correction as compared to the previous ones. As a result, IRS rates increased by 5-25bp, while yields on T-bonds increased by 10-33bp in just 3 days. This was due to the Argentina default and Russian sanctions which increased fears about economic growth in the EU and rate hike speculations in the US. What is more, both curves shifted to bear steepening as the long ends lost the most.

Macro data releases in August will not be strong enough to reduce expectations of monetary easing this year, and should anchor front ends of curves near current levels this month. However, a lack of monetary easing in September and a gradual rebound in hard macro data may result in a more significant correction.

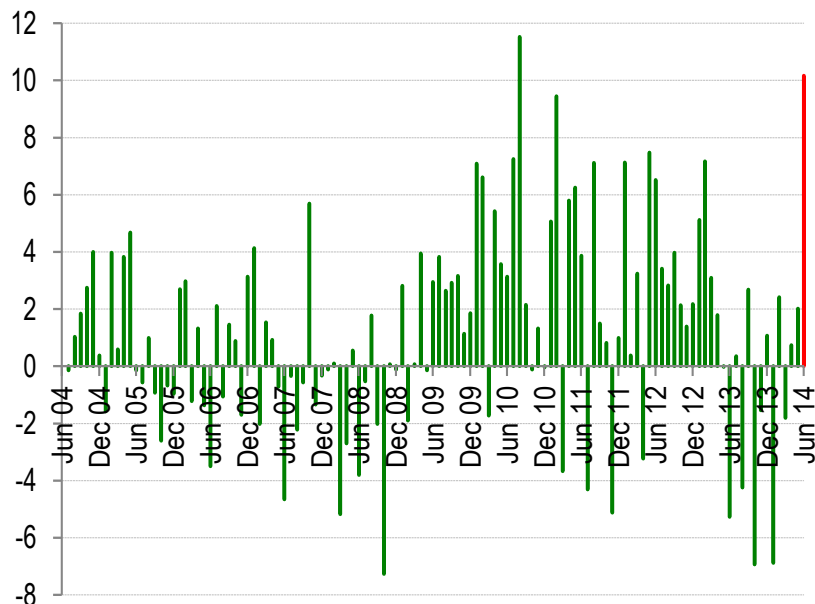
Longer tenors, in particular 10Y sectors will be under the influence of external factors. This month we expect some rebound in yields/rates after abrupt growth at the turn of the July-August. However, a further improvement in macro data in the US may again strengthen expectations for faster interest rate hikes in the US, and put pressure on the long end of curves. Therefore, investors will closely watch minutes from July's Fed meeting (published August, 20) and the Jackson Hole economic policy symposium (late August), looking for confirmation for their expectations on rate hikes in the US.



Demand Corner: Strong accumulation of bonds by foreigners

- In June nonresidents purchased Polish marketable, zloty-denominated bonds for a nominal value of PLN10.2bn. This was the biggest monthly inflow since August 2010. The foreign investors' portfolio is now close to PLN200bn, its highest since September 2013.
- In June, nonresidents focused on the PS and DS series. The biggest purchases were recorded in the case of PS0719 (nearly PLN2bn) and PS0718 (nearly PLN1.5bn). The biggest purchases within a group of nonresidents were made by investment funds and banks. Given the geographical criteria, bonds worth PLN3.4bn were bought by investors from the euro zone. In the whole second quarter, nonresidents purchased debt worth nearly PLN13bn, the most aggressive buying since 1Q13 when bonds for PLN15bn were bought. In 1H14 nonresidents purchased bonds worth PLN6.6bn.
- Domestic investors reduced their holdings by nearly PLN5.2bn in June and PLN4.5bn of this amount was due to domestic commercial banks selling (first outflow after 5 consecutive months of buying). Banks sold bonds from both the mid and long end of the curve – mainly WZ0115 (over PLN5bn) and PS0718 (nearly PLN1.5bn). Over the whole of 1H14, Polish banks bought bonds worth PLN20.7bn.

Monthly change of Polish marketable bonds held by foreign investors

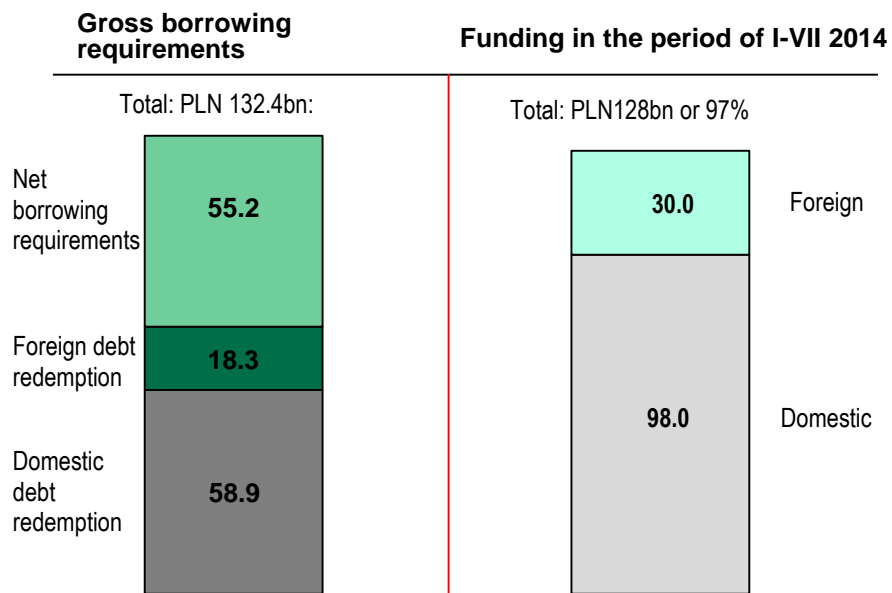


Source: Ministry of Finance, BZ WBK.

Supply Corner: Pause in August

- In July the Ministry of Finance successfully launched T-bonds worth PLN8.4bn in total (or 56% of total issuance plan for 3Q14). The demand recorded at the last auction amounted to PLN20bn and was 4 times higher than the maximum level of supply. As a consequence, the Ministry sold T-bonds at prices well above secondary market levels.
- Given the favourable results of the T-bonds sale, the Ministry of Finance has covered nearly 100% of the planned 2014 gross borrowing requirements. The YtD ratio at the end of July is well ahead of the 83% average seen over the previous four years.
- This should pave the way for calmer supply activity in the remainder of the year. Poland's Ministry of Finance has confirmed a pause in the issuance plan in August as mentioned in the report for the issuance plan for 3Q14, giving market players a breather. The Ministry will return to the primary market with a standard T-bond auction in September. What is more, next month the Ministry may continue the 2015 pre-financing process via a switch auction, offering to repurchase T-bonds maturing in January and April 2015.

Gross borrowing requirements in 2014



Source: Ministry of Finance, BZ WBK.

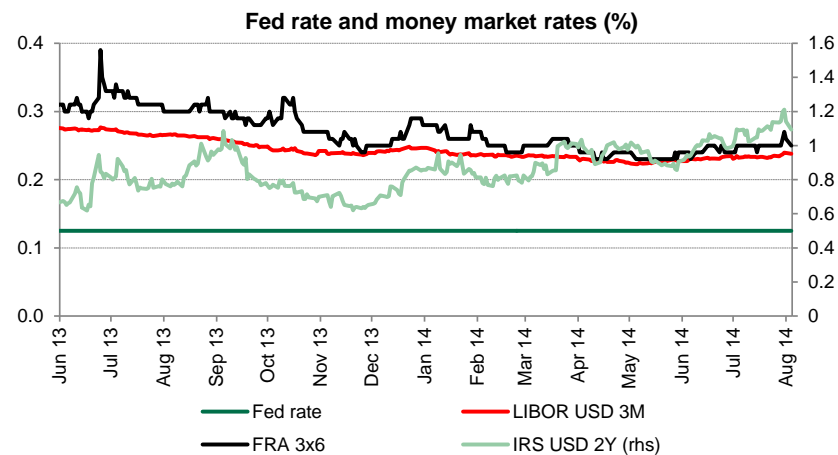
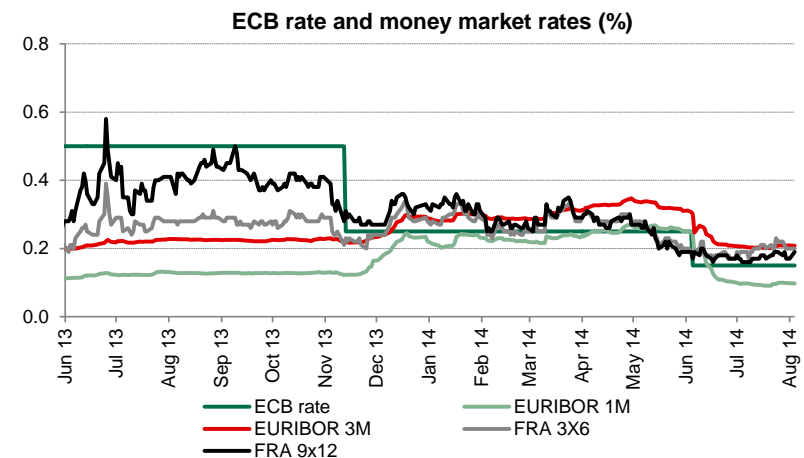
International Money Market and IRS: USD rates under upward pressure

In July EUR money market rates have remained more or less stable as the ECB keeps a dovish tone and macro data confirm moderate economic growth in euro zone. At the same time, USD money market rates (mainly as regards longer tenors) increased quite considerably, in particular at the turn of July-August. This came from renewed expectations of earlier rate hikes by the Fed after the less dovish rhetoric of July's FOMC statements.

Both EUR and USD IRS increased quite significantly (by up to 8bp for EUR IRS and by 5-15bp for USD IRS) at the turn of July-August after a strong performance through July. However, slightly weaker than expected non-farm payrolls (in particular slower growth of earnings) effectively stopped the upward move.

This month investors should focus on the ECB and macro data. We are expecting no important changes in monetary policy stance, given its already dovish bias. The ECB should hold off on major decisions until the effects of the TLTRO, scheduled for September, are known, especially given the recent more optimistic information about economic and loan activity in Europe. Consequently, both EUR money market and IRS rates should maintain a sideways trend ahead of new macro projection releases in September.

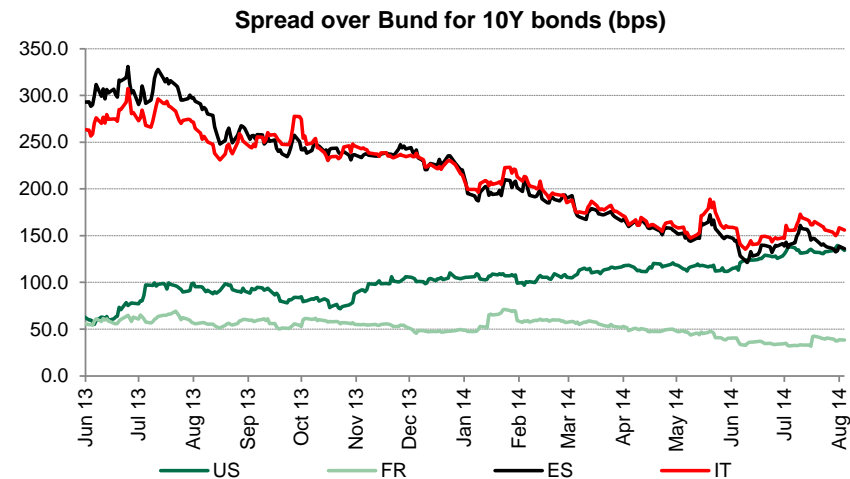
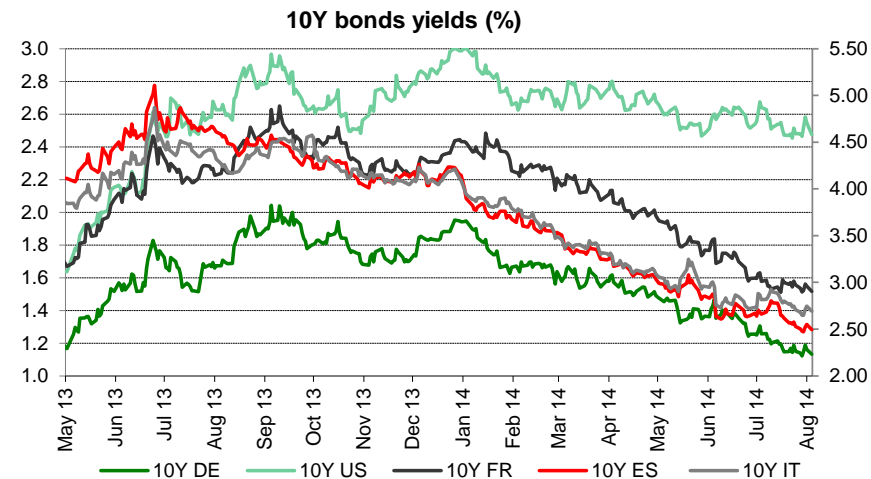
After recent surprises in US data, sentiment should strongly depend on further statistics from the US economy, influencing expectations about the timing of the first rate hike. While changes in USD money market rates should be small, IRS rates may show more significant growth.



Source: Reuters, ECB, Fed, BZ WBK.

International Bond Market: Geopolitical tensions should support safe haven assets

- Government bonds have continued to rally globally through July, with the German 10Y Bund yield falling to a new record low (1.12%). However, yields shifted up at the end of the month as the US GDP release for 2Q painted a much brighter picture of H1 than previously anticipated and FOMC's rhetoric was less dovish than expected. The correction was only short-lived as weak earnings data in the US supported the view that tightening is still a long way off.
- Following a very strong performance through July on peripheral markets, the fixed income markets corrected back in the last two days of July. Consequently, peripheral debt weakened slightly and the spread to Bunds widened slightly.
- In the short run we foresee core markets (Bunds, US Treasuries) remaining strong (with yields near current levels) as geopolitical tensions (Russia-Ukraine conflict, Gaza) shift capital towards safe haven assets. The August ECB meeting should be rather neutral for the market as it will not bring any new information about planned QE. We think that the ECB will want to assess the effects of the June easing package and that can be done at the earliest at the end of the year. However, further improvement in economic activity in the US may put pressure on the long end of curves, which would result in a bear steepening.

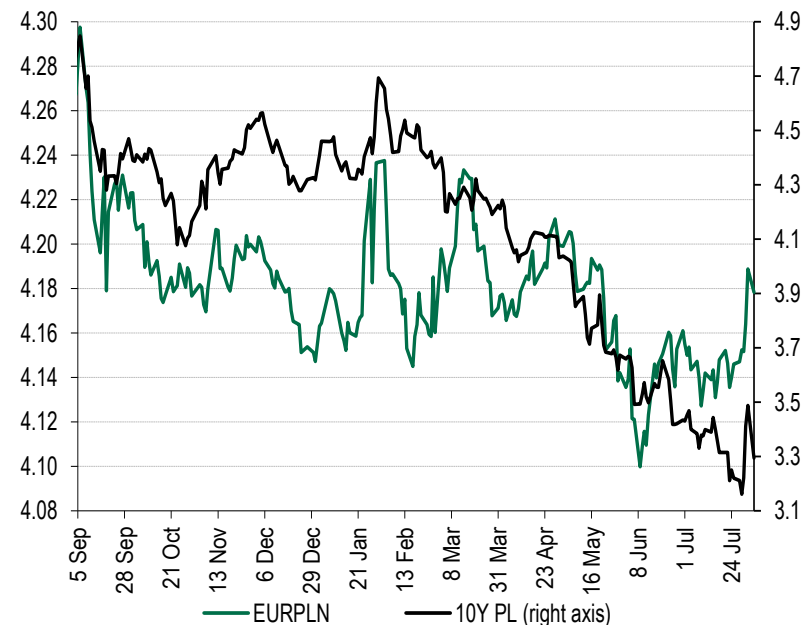


Source: Reuters, BZ WBK.

Foreign Exchange Market: Significant weakening of the zloty

- ▶ In July the zloty was the 8th weakest EM currency vs. the euro and the dollar. The pressure originated from the ongoing tensions in Eastern Europe and the Middle East, poor economic data and the very low CPI in Poland as well as from a significant weakening of Polish bonds. The latter was initiated mainly by mounting expectations that the Fed will start hiking rates sooner than mid-2015. At the same time, the chances of rate cuts in Poland this year have increased. Thus, the zloty might have also been under pressure from the risk that the US-PL interest rate disparity will widen.
- ▶ This suggests that economic activity data may be crucial for the zloty in the short run. In general, monthly and quarterly data should, in our view, confirm that the economy is not heading for a major slowdown, but July's weak PMI has strengthened concerns over the pace of the recovery. We still expect the zloty to appreciate in the medium term, but we see upward risk to our current EURPLN projection due to risks regarding the pace of GDP growth and a prolongation of the Russia-Ukraine crisis. Also, recent weeks have shown that an increased chance of rate cuts in Poland supports the debt market and the capital inflow into bonds supports the zloty.

EURPLN and yield of Polish 10Y benchmark



Source: Bloomberg, BZ WBK

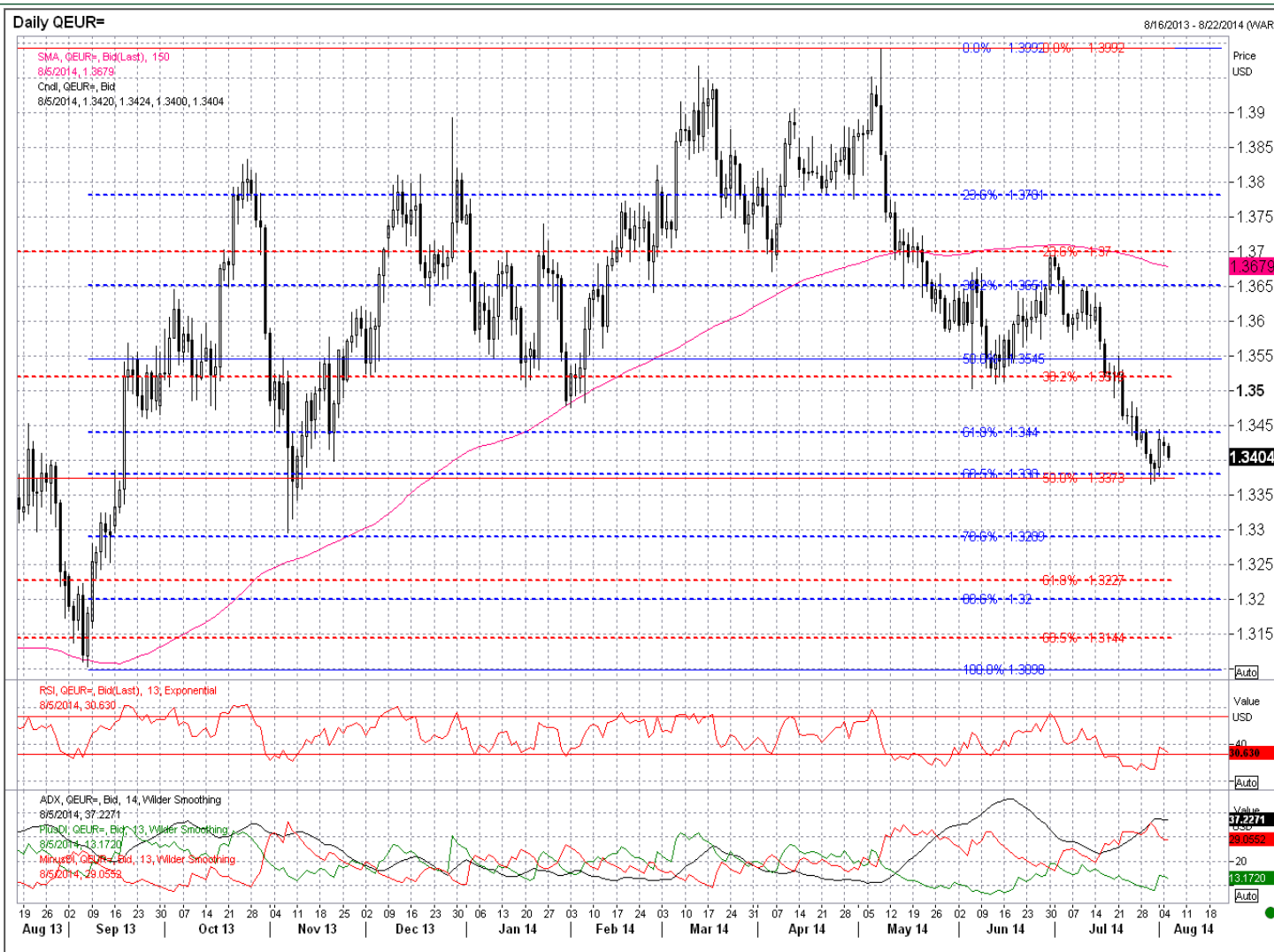
FX Technical Analysis Corner: Room for higher EURPLN?



- ▶ After several weeks of stabilization, the Shark 32 formation (consisting of three bars, each one within the range of the previous one) appeared on the EURPLN weekly chart.
- ▶ EURPLN broke the peak of the first bar at 4.17 and this indicates the exchange rate may rise further. Additionally, the ADX oscillator on the daily chart is gradually rebounding from the local low level suggesting the upward trend is gaining strength. Next resistance levels at 4.20 and 4.23.

Source: Reuters, BZ WBK

FX Technical Analysis Corner: Pause in the EURUSD fall?



- ▶ The EURUSD did not manage to break the 150-day moving average running at around 1.37 and plunged to c1.336. It failed to break the support at c1.337 consisting of the two Fibonacci retracement levels.
- ▶ ADX indicates that the downward trend is already quite strong, so there is an increasing chance that it may halt/reverse soon.
- ▶ Next important support at 1.33, first resistance at 1.35.

Source: Reuters, BZ WBK.

Macroeconomic Forecasts

Poland		2012	2013	2014E	2015E	1Q13	2Q13	3Q13	4Q13	1Q14E	2Q14E	3Q14E	4Q14E
GDP	PLNbn	1,596.4	1,635.7	1,698.5	1,790.6	378.4	396.3	405.6	455.5	397.4	412.2	416.9	472.0
GDP	%YoY	2.0	1.6	3.3	3.7	0.4	0.8	2.0	2.7	3.4	3.1	3.0	3.5
Domestic demand	%YoY	-0.1	0.0	3.6	4.4	-1.0	-1.6	0.6	1.8	3.0	4.0	3.5	3.9
Private consumption	%YoY	1.3	0.8	2.8	3.0	0.0	0.1	1.0	2.1	2.6	2.7	2.9	2.9
Fixed investment	%YoY	-1.6	-0.2	6.2	7.9	-2.4	-3.3	0.5	2.0	10.7	2.0	6.0	7.0
Unemployment rate ^a	%	13.4	13.4	12.3	11.1	14.3	13.2	13.0	13.4	13.5	12.0	11.9	12.3
Current account balance	EURm	-14,191	-5,328	-3,776	-5,037	-2,313	486	-2,086	-1,415	-766	1,064	-1,643	-2,431
Current account balance	% GDP	-3.7	-1.4	-0.9	-1.1	-3.1	-2.3	-1.9	-1.4	-1.0	-0.8	-0.7	-0.9
General government balance	% GDP	-3.9	-4.3	5.7	-2.5	-	-	-	-	-	-	-	-
CPI	%YoY	3.7	0.9	0.3	1.6	1.3	0.5	1.1	0.7	0.6	0.3	-0.2	0.4
CPI ^a	%YoY	2.4	0.7	0.5	2.3	1.0	0.2	1.0	0.7	0.7	0.3	0.0	0.5
CPI excluding food and energy prices	%YoY	2.2	1.2	0.7	1.6	1.2	1.0	1.4	1.2	0.8	0.8	0.4	0.6

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

^a at the end of the period

* without changes in the pension system

Interest Rate and FX Forecasts

Poland		2012	2013	2014E	2015E	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14E	3Q14E	4Q14E
Reference rate ^a	%	4.25	2.50	2.50	3.00	3.25	2.75	2.50	2.50	2.50	2.50	2.50	2.50
WIBOR 3M	%	4.91	3.02	2.69	2.89	3.77	2.96	2.70	2.66	2.71	2.71	2.66	2.68
Yield on 2-year T-bonds	%	4.30	2.98	2.67	3.16	3.29	2.77	2.98	2.88	3.01	2.76	2.40	2.50
Yield on 5-year T-bonds	%	4.53	3.46	3.25	3.83	3.49	3.09	3.63	3.64	3.71	3.35	2.83	3.08
Yield on 10-year T-bonds	%	5.02	4.04	3.79	4.41	3.95	3.58	4.26	4.36	4.38	3.82	3.38	3.58
2-year IRS	%	4.52	3.10	2.78	3.40	3.43	2.81	3.14	3.04	3.07	2.82	2.51	2.73
5-year IRS	%	4.47	3.51	3.29	4.05	3.52	3.08	3.76	3.68	3.70	3.31	2.87	3.27
10-year IRS	%	4.56	3.86	3.63	4.18	3.76	3.41	4.13	4.14	4.16	3.73	3.26	3.38
EUR/PLN	PLN	4.19	4.20	4.13	3.95	4.16	4.20	4.25	4.19	4.19	4.17	4.13	4.03
USD/PLN	PLN	3.26	3.16	3.01	2.75	3.15	3.22	3.21	3.08	3.06	3.04	3.05	2.90
CHF/PLN	PLN	3.47	3.41	3.36	2.97	3.38	3.41	3.44	3.40	3.42	3.42	3.37	3.23
GBP/PLN	PLN	5.16	4.94	5.11	4.84	4.88	4.94	4.97	4.98	5.06	5.11	5.20	5.06

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates;

^a at the end of period

Economic Calendar and Events

Date		Event:	Note:
7-Aug	EZ	ECB Meeting – interest rate decision	–
13-Aug	PL	CPI for July	Our forecast: -0.2%YoY is in line with market expectations
14-Aug	PL	Flash GDP (2Q 2014)	We predict GDP growth at 3.1%, slightly below market consensus at 3.2%
	PL	CPI for July	Our forecast: 0.2%YoY, well below the market consensus of 0.4%YoY
	EZ	Flash GDP (2Q 2014)	-
	DE	Flash GDP (2Q 2014)	-
19-Aug	PL	Employment and wages for July	We expect employment to increase by 0.8%YoY and wages to grow 4.0% YoY. Our forecast for wage growth is above market consensus of 3.8%
20-Aug	PL	Industrial output and PPI for July	Our forecast of industrial output is 2.9%YoY (above market consensus of 2.0%YoY). We predict PPI at -1.8%YoY
	US	Minutes from July's FOMC meeting	–
21-Aug	PL	Minutes from July's MPC meeting	-
26-Aug	HU	NBH meeting - interest rate decision	-
TBA	PL	Retail sales for July	Our forecast is 1.6% YoY is slightly below market consensus of 1.9%YoY
28-Aug	US	Preliminary GDP (2Q 2014)	–
30-Aug	PL	GDP (Q2 2014) with structure breakdown	–
1-Sep	PL	PMI manufacturing for August	-
	EZ	PMI manufacturing for August	-
3-Sep	PL	MPC Meeting – interest rate decision	
4-Sep	EZ	ECB Meeting – interest rate decision	–

Source: CB, Markit, CSO, Finance Ministry

Annexe

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

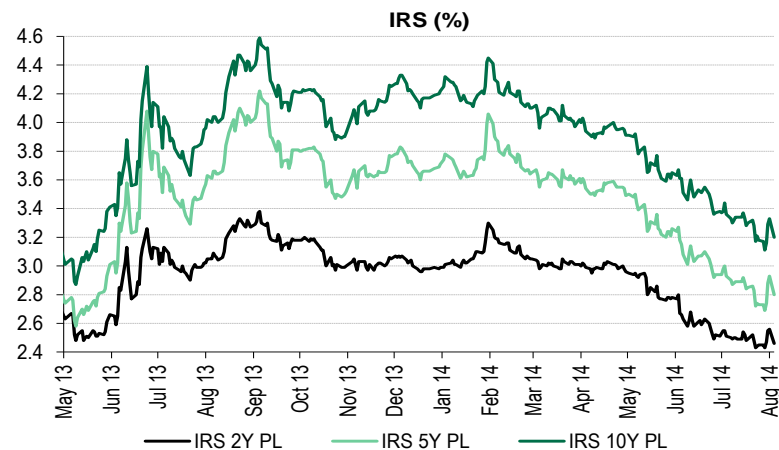
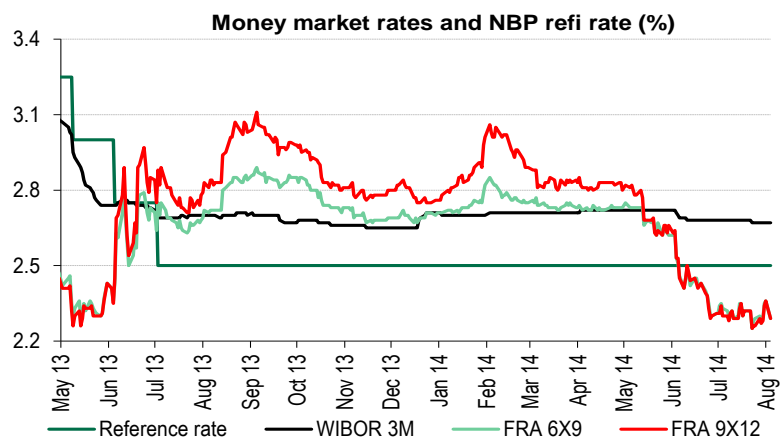
1. Domestic Market Performance

Money market rates (%)

	Reference	Polonia	WIBOR (%)				OIS (%)				FRA (%)			
	rate (%)	(%)	1M	3M	6M	12M	1M	3M	6M	12M	1x4	3x6	6x9	9x12
End of July	2.50	2.51	2.60	2.67	2.69	2.73	2.47	2.38	2.30	2.23	2.63	2.45	2.35	2.34
Last 1M change (bp)	0	-2	-1	-1	0	-1	6	5	7	5	3	2	4	3
Last 3M change (bp)	0	1	-2	-5	-5	-6	7	-7	-16	-27	-9	-27	-38	-46
Last 1Y change (bp)	0	4	-3	-3	-2	-1	6	-5	-13	-21	-2	-22	-33	-44

Bond and IRS market (%)

	BONDS			IRS			Spread BONDS / IRS (bp)		
	2Y	5Y	10Y	2Y	5Y	10Y	2Y	5Y	10Y
End of July	2.46	2.93	3.41	2.55	2.88	3.29	-9	5	12
Last 1M change (bp)	-2	-8	-2	4	-6	-9	-6	-2	7
Last 3M change (bp)	-42	-60	-62	-41	-61	-62	-1	1	0
Last 1Y change (bp)	-32	-47	-66	-47	-66	-66	15	19	0



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
T-bonds auction	18,143	8,821	6,573	17,503	5,694	4,990	8,418		5,000	5,000	3,000	2300	85,442
T-bills auction													0
Retail bonds	256	475	190	170	170	170	170	180	170	175	185	176	2,487
Foreign bonds/credits	16,724	1,150								3200			21,074
Prefinancing and financial resources at the end of 2013	25,000												25,000
Total	60,123	10,445	6,763	17,673	5,864	5,160	8,588	180	5,170	8,375	3,185	2476	134,002
Redemption	16,497	5,613	2,230	16,035	116	60	9,470	1,793	2,796	83	816	91	55,599
Net inflows	43,626	4,832	4,533	1,638	5,749	5,100	-882	-1,613	2,374	8,292	2,369	2,385	78,403
Rolling over T-bonds			4,807				6,117						10,924
Buy-back of T-bills/ FX-denominated bonds													0
Total	43,626	4,832	9,340	1,638	5,749	11,216	-882	-1,613	2,374	8,292	2,369	2,385	89,327
Coupon payments from domestic debt	1,546			5,596			2,775		1,298	7,910			19,125

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
Total 2014	37,773		1,677	39,450	16,149	55,599
Total 2015	78,037		1,710	79,747	14,789	94,536
Total 2016	84,347		1,273	85,621	17,262	102,882
Total 2017	58,543		917	59,460	12,566	72,026
Total 2018	66,317		911	67,228	14,396	81,624
Total 2019+	179,098		3,233	182,332	135,784	318,116

Source: MF, BZ WBK

2. Polish Bonds: Supply Recap (cont.)

Scheduled wholesale bond redemption by holders (data at the end of June 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	5,012	1,000	1,532	14	455	129	10	90	8,243
Q4 2014	0	0	0	0	0	56	7	14	77
Total 2014	5,012	1,000	1,532	14	455	185	16	104	8,319
	60%	12%	18%	0%	5%	2%	0%	1%	100%
Total 2015	30,508	25,030	8,626	522	6,017	237	301	6,831	78,071
	39%	32%	11%	1%	8%	0%	0%	9%	100%
Total 2016	42,741	18,106	7,982	724	9,600	106	404	5,744	85,406
	50%	21%	9%	1%	11%	0%	0%	7%	100%
Total 2017	24,269	15,978	6,179	610	7,291	56	188	3,971	58,543
	41%	27%	11%	1%	12%	0%	0%	7%	100%
Total 2018	18,160	31,067	3,524	385	8,700	70	171	4,239	66,317
	27%	47%	5%	1%	13%	0%	0%	6%	100%
Total 2019+	79,116	44,199	25,302	1,021	12,699	212	336	8,256	171,141
	46%	26%	15%	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 June			Share in TOTAL (%) in June
	End Jun'14	End May'14	End Apr'14	End 1Q 2014	End 4Q 2013	End 3Q 2013	MoM	3-mth	YoY	
Domestic investors	277.2	282.4	278.7	277.9	381.2	377.3	-1.84	2.63	-24.97	58.1 (-1.7pp)
Commercial banks	135.4	139.9	135.4	134.3	114.7	116.2	-3.24	0.83	18.86	28.4 (-1.3pp)
Insurance companies	53.1	52.7	53.2	52.9	52.0	52.8	0.89	0.44	0.09	11.1
Pension funds	3.3	3.3	3.5	3.5	125.8	122.7	-1.79	-6.33	-97.21	0.7
Mutual funds	44.8	46.2	46.0	45.8	46.7	46.1	-3.18	-2.33	-3.73	9.4 (-0.4pp)
Others	40.6	40.2	40.5	41.4	42.0	39.5	1.0	-1.8	6.1	8.5
Foreign investors*	199.8	189.7	187.6	186.9	193.2	200.6	5.36	6.91	-0.97	41.9 (1.7pp)
Banks	12.6	10.5	11.9	30.5	29.1	32.1	20.63	n.a.	n.a.	2.6 (0.4pp)
Central banks	18.0	17.3	14.4	150.6	156.0	159.7	4.21	n.a.	n.a.	3.8 (0.1pp)
Public institutions	0.7	0.7	0.7	n.a.	n.a.	n.a.	3.81	n.a.	n.a.	0.2
Insurance companies	9.5	9.4	9.1	n.a.	n.a.	n.a.	1.70	n.a.	n.a.	2.0
Pension funds	12.3	12.2	11.9	n.a.	n.a.	n.a.	1.08	n.a.	n.a.	2.6
Mutual funds	83.4	80.2	79.1	n.a.	n.a.	n.a.	3.97	n.a.	n.a.	17.5 (0.5pp)
Hedge funds	0.1	0.1	0.1	n.a.	n.a.	n.a.	0.48	n.a.	n.a.	0.0
Non-financial sector	14.2	12.6	12.1	n.a.	n.a.	n.a.	13.13	n.a.	n.a.	3.0 (0.3pp)
Others	16.5	15.9	18.0	4.5	4.7	5.2	3.88	n.a.	n.a.	3.5 (0.1pp)
TOTAL	477.0	472.0	466.3	464.8	574.3	577.9	1.05	-0.24	-16.49	100

*Total for foreign investors does not match sum of values presented for sub-categories due to omission of irrelevantly small group of investors.
Detailed data on foreign investors is available only since April 2014

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	53
Belgium	21.8	9.8	31.6	30.0	80
Finland	6.9	4.8	11.7	11.7	55
France	105.0	70.2	175.2	174.0	81
Germany	144.0	-	144	144.0	60
Greece	16.8	5.6	-	-	-
Ireland	6.9	7.7	14.6	14.6	70
Italy	187.8	27.6	235.4	235.4	75
Netherlands	32.0	15.9	47.9	45.9	76
Portugal	11.4	7.4	18.8	7.2	94
Spain	68.2	36.7	141.3	141.3	75
Total	624.2	189.9	848.2	828.8	73

*/ 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
Poland	1.6	3.2	0.8	1.1	-1.6	-1.7	-4.3	5.7	57.0	49.2
Czech Republic	-0.9	2.0	1.4	0.8	-1.2	-0.4	-1.5	-1.9	46.0	44.4
Hungary	1.1	2.3	1.7	1.0	3.1	3.0	-2.2	-2.9	79.2	80.3
EU	0.1	1.6	1.5	1.0	1.6	1.8	-3.0	-2.5	88.9	89.5
Euro area	-0.4	1.2	1.3	0.8	2.6	2.9	-3.3	-2.6	95.0	96.0
Germany	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 July	2013	end of July	2013	end of July	2013	end of July	2013	end of July
Poland	2.50	2.50	2.71	2.67	4.32	3.39	238	220	79	56
Czech Republic	0.05	0.05	0.05	0.04	2.53	1.47	58	28	60	46
Hungary	3.00	2.10	2.99	2.14	5.71	4.83	377	364	256	172
Euro area	0.25	0.15	0.29	0.21						
Germany					1.94	1.19			26	22

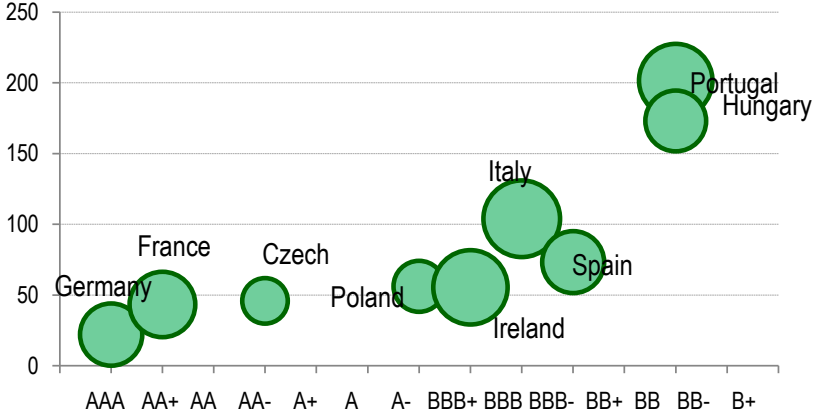
Source: EC – Spring 2014, stat offices, central banks, Reuters, BZ WBK.

5. Poland vs Other Countries (cont.)

Sovereign ratings

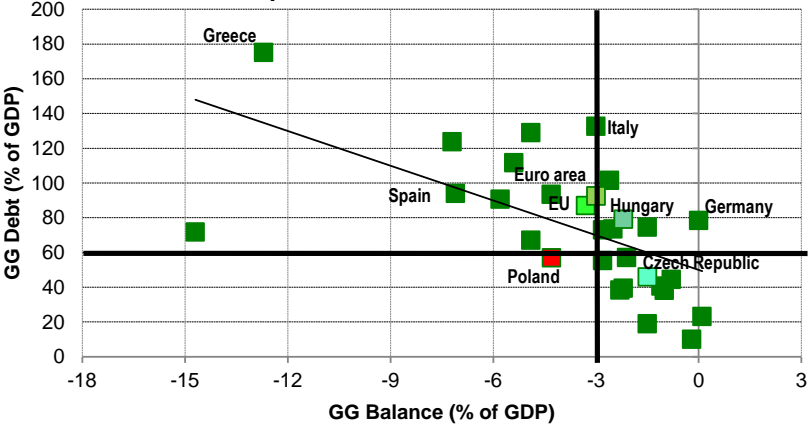
	S&P		Moody's		Fitch	
	rating	outlook	rating	outlook	rating	outlook
Poland	A-	stable	A2	stable	A-	stable
Czech	AA-	stable	A1	stable	A+	stable
Hungary	BB	stable	Ba1	negative	BB+	stable
Germany	AAA	stable	Aaa	negative	AAA	stable
France	AA	stable	Aa1	negative	AA+	negative
UK	AAA	negative	Aa1	negative	AA+	stable
Greece	B-	stable	Caa1	stable	B	stable
Ireland	BBB+	positive	Baa3	positive	BBB+	stable
Italy	BBB	negative	Baa2	stable	BBB+	negative
Portugal	BB	stable	Ba1	stable	BB+	negative
Spain	BBB	stable	Baa3	stable	BBB	stable

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



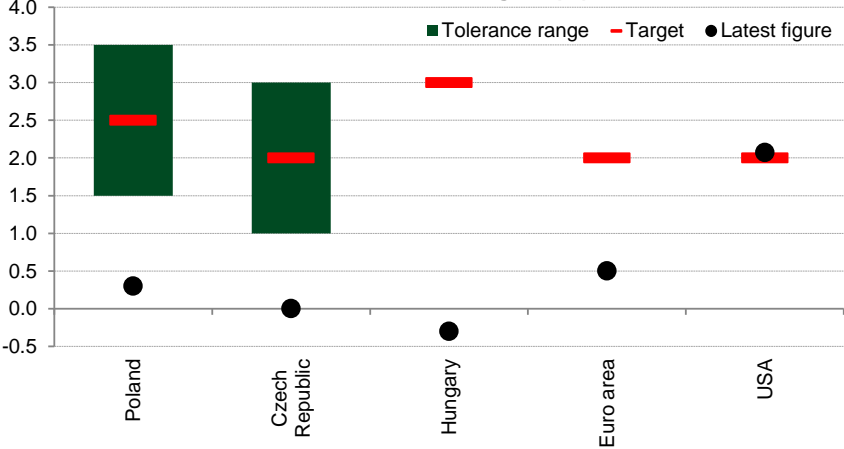
Note: Size of bubbles reflects the debt/GDP ratio

Fiscal position of the EU countries

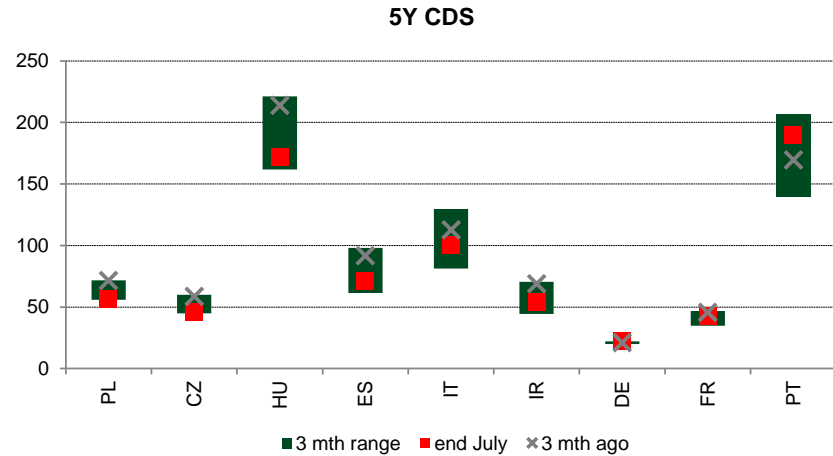
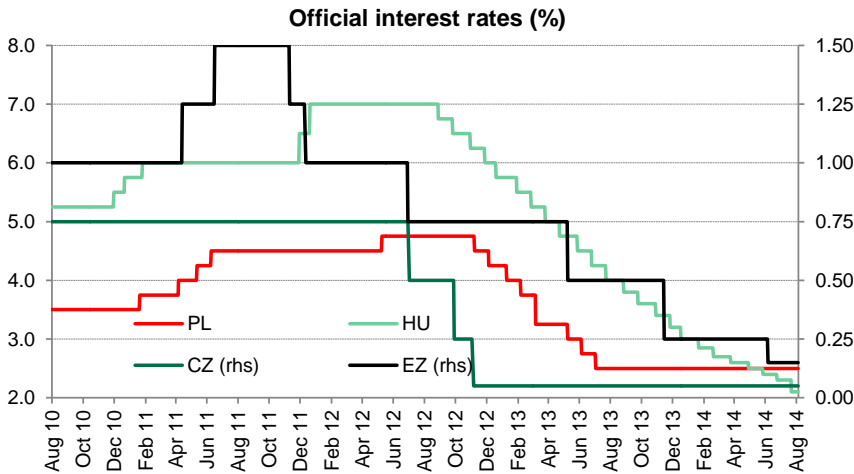
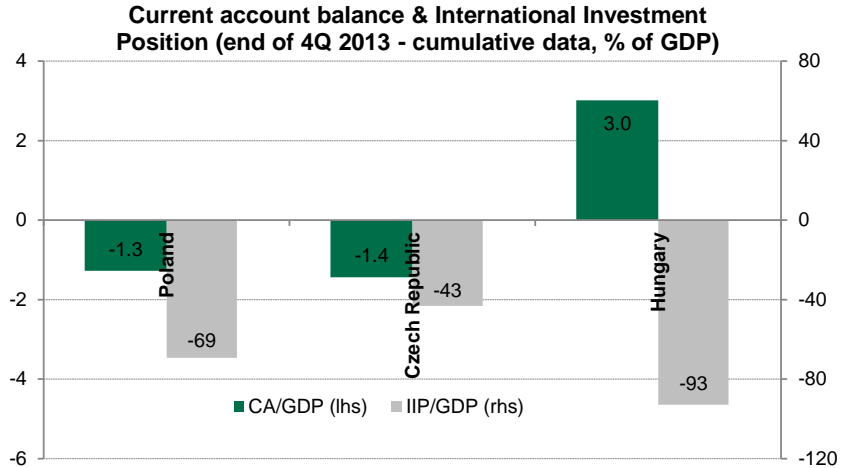
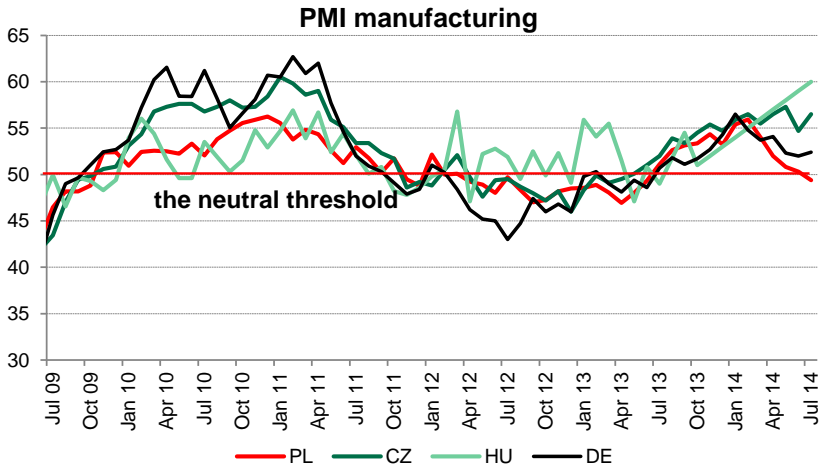


Source: rating agencies, Reuters, EC, BZ WBK

Inflation rates vs targets (%)

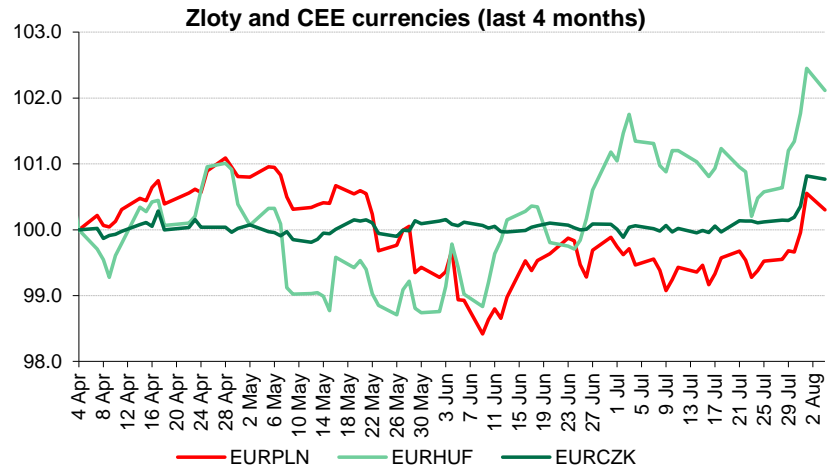
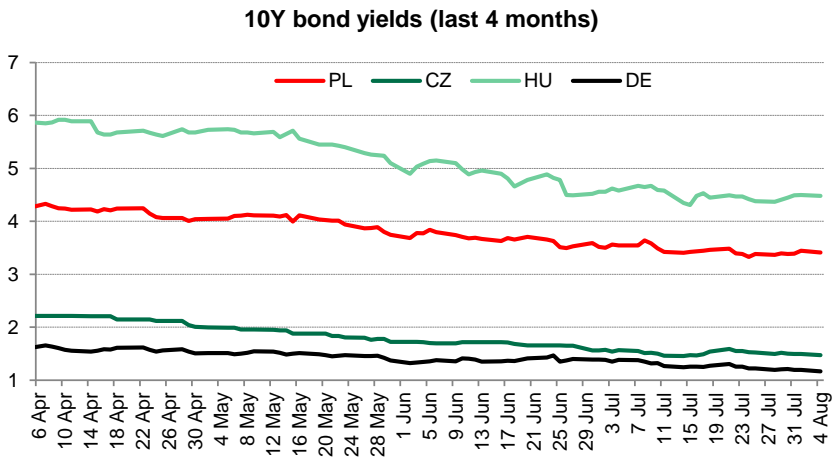
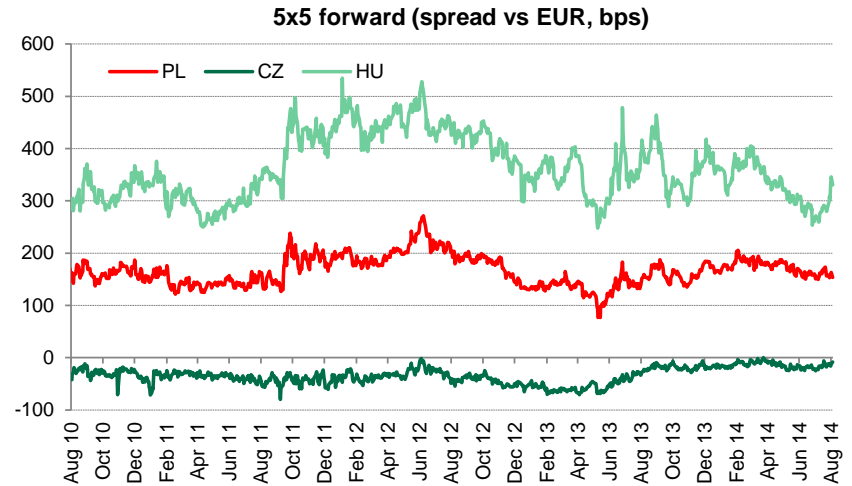
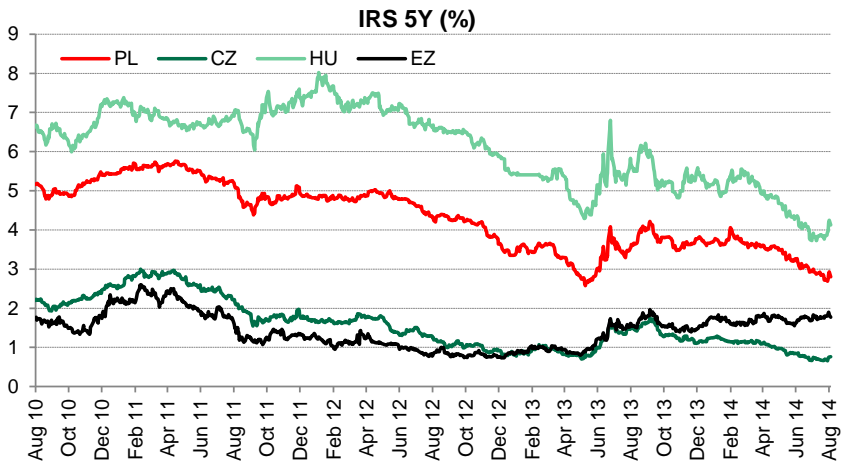


5. Poland vs Other Countries (cont.)



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	
Euro zone	Forecast	0.15	0.25	0.15				We do not expect the ECB to deliver new measures despite further decline in CPI. We think that the ECB will want to assess the effects of the June easing package and that can be done at the earliest at the end of the year.
	Market implied »				21	21	19	
UK	Forecast	0.50	0.50	0.75				In line with expectations BoE kept official interest rate unchanged. However, BoE minutes show differing views about policy tightening, but members had no preset timing for the first increase in official rates. Looking ahead, August will be interesting as the new inflation report will be released.
	Market implied »				4	14	34	
US	Forecast	0-.25	0-.25	0.25				In July the Fed pressed ahead with its plan to wind down its bond purchases, while reaffirming it is in no rush to raise interest rates. However, the rhetoric was less dovish than expected, which increased fear on earlier rate hikes.
	Market implied »				16	24	33	
Poland	Forecast	2.50	2.50	2.50				The MPC has dropped the forward guidance in July but maintained the view that interest rate cuts are not likely. The next decision-making meeting of the MPC is scheduled at the start of September, when the Council will know not only the GDP data for 2Q14 but also the first monthly figures from the third quarter. We expect rates to remain unchanged.
	Market implied »				-14	-27	-38	
Czech Republic	Forecast	0.05	0.05	0.05				In line with expectations, the CNB decided to leave both the key interest rate and FX intervention target unchanged (EURCZK above, but close to 27). However, the central bank also announced that the FX intervention regime will not be terminated before 2016.
	Market implied »				30	29	29	
Hungary	Forecast	2.10	3.00	2.10				Unexpectedly, NBH cut rates by 20bp (more than expected) and announced the end of easing cycle. The bank would like to keep rates low for as long as possible, but does not exclude the possibility of starting another rate reduction.
	Market implied »				4	9	22	

Source: Reuters, BZ WBK

This analysis is based on information available through August 4, 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
Long / Buy	Buy the bond for an expected average return of at least 10bp in 3 months (decline in the yield rate), assuming a directional risk.	Long / Receive fixed rate	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.
Short / Sell	Sell the bond for an expected average return of at least 10bp in 3 months (increase in the yield rate), assuming a directional risk.	Short / Pay fixed rate	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		
Long a spread / Play steepeners	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).		
Short a spread / Play flatteners	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		
Long / Buy	Appreciation of a given currency with an expected return of at least 5% in 3 months.		
Short / Sell	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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