

# **Rates and FX Outlook**

Polish Financial Market

April 2013

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# Summary

- ▶ **In March the MPC surprised by cutting official rates by 50bps, in which the reference rate to 3.25% - the lowest level in history.** The Council said that this decision „complements the monetary policy easing cycle commenced in November 2012”. The MPC adopted wait and see mode, which, in practice, means that the Council will monitor macro data and judge how recent monetary easing influenced inflation path and pace of recovery of the Polish economy. **Our baseline scenario assumes flat rates not only in April, but also till year-end, though there is a risk that very low inflation rate and slow recovery process will put pressure on the MPC to deliver more easing. Most probably, some members will wait as long as until July’s projection.**
- ▶ **Weak macro data from real economy and fast disinflation have renewed market expectations that the MPC will continue monetary easing in coming months. FRA contracts are pricing-in rate cuts by 50bps in 6 months horizon.** While we think these are too aggressive expectations, the upcoming macro data will be supportive for WIBOR, FRA and front ends of IRS and bond curves, keeping rates near the all-time lows. The long ends of the curves will remain under influence of situation on Bunds. Additionally, in the short run the release of the general government deficit figure for 2012 might be important for the market, as this will determine whether the European Commission will lift the excessive deficit procedure. At the same time, further fiscal consolidation is questionable and there is a substantial risk of budget revision this year. We estimate a shortfall in this year’s tax revenues at ca. PLN18bn, which will be partly covered by the central bank profit and possibly higher income from dividends. Some spending cuts, probably including lower subsidy to ZUS, will be needed to keep the deficit as planned. Still, financing this year’s borrowing requirements is going smoothly (80% likely in June), so there should not be a considerable problem with placement of additional supply in the second half of the year (though most likely with slightly higher yields). In the worst case, the Ministry of Finance will pre-finance less borrowing needs for the next year.
- ▶ **The domestic currency was under negative pressure coming not only from monetary easing by the MPC, but also due to concerns about the euro zone (Italy and Cyprus). Consequently, the EURPLN increased towards 4.20, and this level has effectively stopped further increase.** Given the current situation (European uncertainty) and the prospects of slow rebound in economic activity in Poland (which will keep interest rate cuts expectations alive), we expect the EURPLN to stabilise in the range of 4.12-4.20.

## Short- and Medium-term Strategy: Interest rate market

|                   | Change (bps) |         | Level     | Expected trend |    |
|-------------------|--------------|---------|-----------|----------------|----|
|                   | Last 3M      | Last 1M | end-March | 1M             | 3M |
| Reference rate    | -100         | -50     | 3.25      | →              | →  |
| WIBOR 3M          | -72          | -34     | 3.39      | →              | →  |
| 2Y bond yield     | 6            | -31     | 3.14      | ↘              | →  |
| 5Y bond yield     | 21           | -20     | 3.41      | ↘↘             | ↘  |
| 10Y bond yield    | 20           | -5      | 3.92      | ↘↘             | ↘  |
| 2/10Y curve slope | 14           | 26      | 78        | ↘              | ↘  |

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

### PLN Rates Market: our view and risk factors

**Money market:** Unexpected rate cut by 50bps in March caused significant decline in money market rates. We foresee WIBOR rates to stabilise in coming months assuming that the MPC will keep interest rates unchanged. However, FRA contracts have declined further at the beginning of April and fully discount rate reduction by 50bps due to weak macro data and sharp CPI fall. We think that market might overshoot interest rate cuts expectations.

**Short end:** Front end of curves (both bonds and IRS) strengthened significantly after the MPC's decision to trim rates by 50bps. Persisting expectations that the Council will continue monetary easing and strong foreign capital inflows caused significant strengthening at the beginning of April. We think that that front ends of curves should remain strong due to still weak macro data from real economy (industrial output, retail sales) and disinflation trend should stabilise yields and IRS rates near current level in 1M horizon. We still expect upward move in 2H 2013.

**Long end:** Long-term instruments are more vulnerable to situation on core markets (in particular Bunds) rather than to domestic macro data. At the beginning of April strong inflow into bond markets caused significant decline in both yields and IRS rates. We foresee normalisation of situation on the euro zone peripheries, which will result in increasing yields of 10Y Bund, which will consequently put negative pressure on domestic 10Y sector in the second half of 2013.

**Risk factors to our view:** Further monetary easing by the MPC due to no recovery, which would cause significant decline in market rates and bond yields, pushing rates to fresh all-time lows. However, ending the easing cycle might push bond yields higher again. Another risk factors include: GG deficit for 2012 above 3.5% and a budget amendment with additional supply of Treasury papers.

## Short- and Medium-term Strategy: FX market

|        | Change (%) |         | Level     | Expected trend |    |
|--------|------------|---------|-----------|----------------|----|
|        | Last 3M    | Last 1M | end-March | 1M             | 3M |
| EURPLN | 2.2        | 0.5     | 4.18      | →              | →  |
| USDPLN | 5.1        | 2.9     | 3.26      | →              | ↘  |
| CHFPLN | 1.3        | 0.4     | 3.43      | →              | ↘  |
| GBPPLN | -1.2       | 2.9     | 4.95      | →              | ↘  |
| EURUSD | -2.8       | -2.3    | 1.28      | →              | ↗  |

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

### PLN FX Market: our view and risk factors

**EUR:** The zloty weakened due to unexpected rate cut (by 50bps) in March and uncertain situation in the euro zone (lack of new government in Italy, Cyprus' bailout). In 1M horizon situation on the EURPLN will not change significantly - we foresee horizontal trend due to still alive rate cuts expectations and prolonged problems in Italy. In medium term the zloty should gradually strengthen due to signals of rebound in economy.

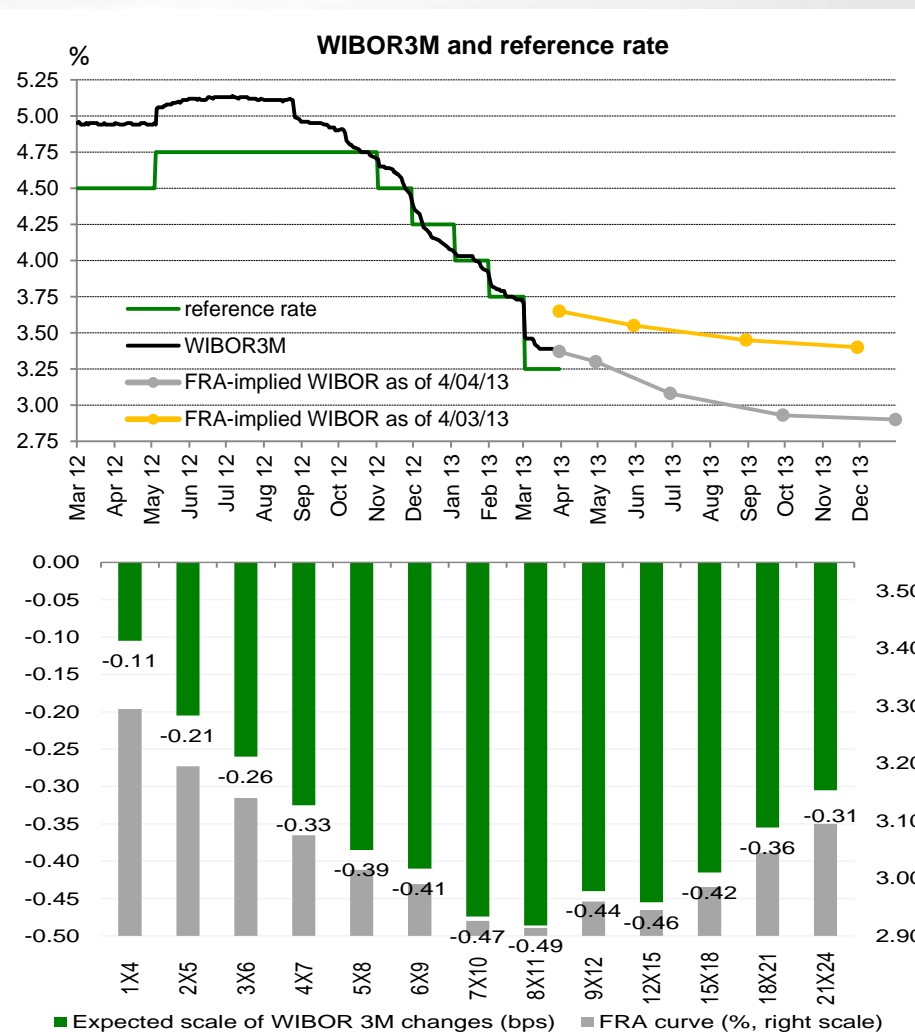
**USD:** We foresee some rebound, assuming the EURUSD rate returns to ca. 1.30 or even higher in 3M horizon due to stabilisation of situation on peripheries. Consequently, the USDPLN should remain more volatile during the month, but stay more or less flat at the end of April as compared with March-end.

**CHF:** Situation does not change significantly in comparison with the previous month. While we predict the CHFPLN to remain relatively steady in April, in longer horizon we foresee the zloty to strengthen gradually against the CHF.

**Risk factors to our view:** We acknowledge two main risk factors for the PLN: (1) the MPC will decide to cut rates after weak Q1 GDP data (due for release at the end of May) and (2) the 2012 general government deficit, which will be released on 22 April. If the GG deficit proves higher than we expect (above 3.5% of GDP), this will put downward pressure on the zloty, with possibility of testing 4.20 by the EURPLN.

# Domestic Money Market: Too aggressive expectations for easing

- WIBOR rates declined significantly during the past month due to surprising decision of the MPC. Most visible move was recorded in case of 1M and 3M rates (42bps and 35bps). Long end declined by slightly over 20bps. WIBOR rates ended the Q1 at the lowest level in history.
- The Council's decision also pushed FRA contracts down (mainly 1x4 and 3x6). Despite suggestion of the end of easing cycle, FRA rates have remained sensitive to macro data (CPI, retail sales), which renewed expectations for further monetary easing and caused FRA 6x9 and 9x12 drop below 3%.
- FRA market has started again to price-in rate cuts by nearly 50bps in next 6 months. Though we see a risk of further easing, the market is likely to overshoot expectations. Still, upcoming macro data will confirm downward trend of inflation and no significant improvement in real economy, therefore the room for upward correction seems to be currently limited.

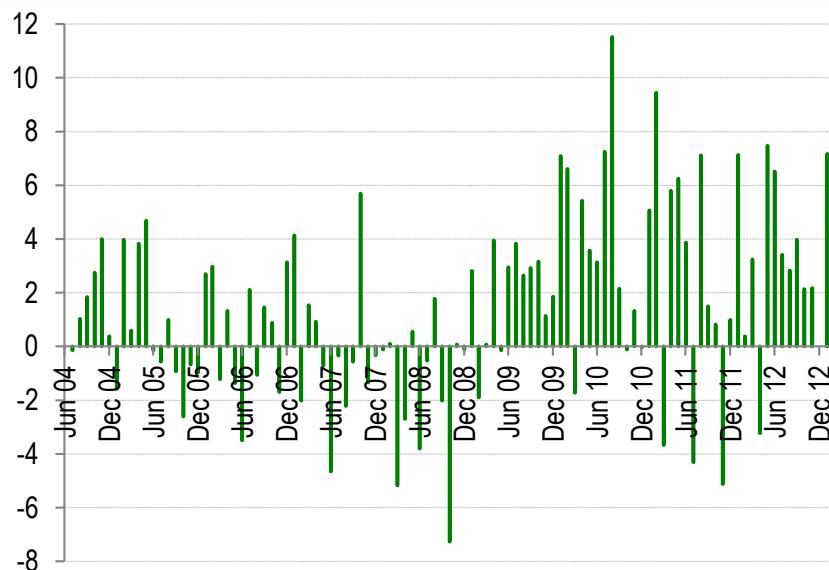


Sources: Reuters, BZ WBK

## Demand Corner: Foreigners continue to accumulate Polish debt

- At the end of February foreign investors held Polish marketable zloty-denominated bonds worth PLN202.2bn. This means that after the biggest nominal monthly increase since May 2012 (PLN7.2bn), the 10th consecutive record was established.
- Foreign investors continued to hold rather limited amount of new 2Y and 5Y benchmarks offered recently by the Ministry of Finance (OK0715 and PS0418). At the end of February they held only 9% and 6% of the total issue, respectively.
- Domestic banks increased holdings of bonds and their total portfolio reached the highest value since September'12. During the two first months of the year Polish banks bought debt worth PLN11.6bn.

Monthly change of bond holdings of foreign investors (in PLNbn)

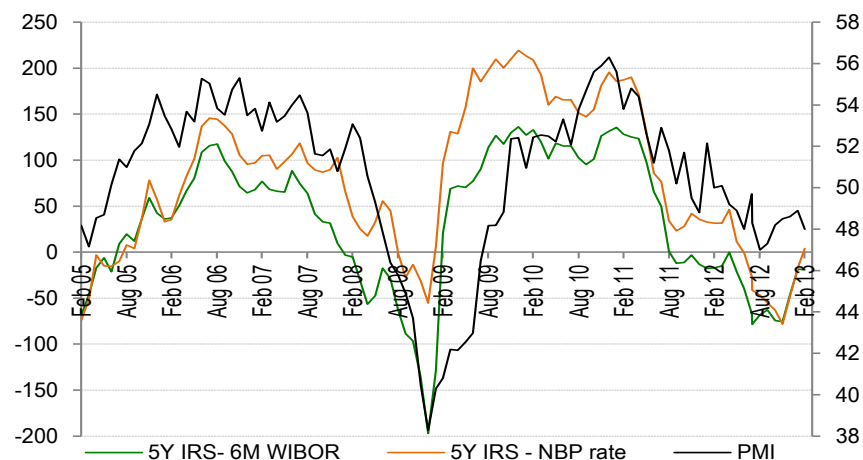


Sources: MF, BZ WBK

## Domestic IRS and T-Bond Market: New record-lows

- The March's MPC decision and macro data (CPI and retail sales) caused decline in bond yields and IRS (the latter reached fresh record lows). Further decline in CPI and quite weak data from real economy shall support the front end of bond and IRS curves, long end will rely on the situation on core markets.
- As the chart shows, historically the spread between IRS and WIBOR6M/NBP reference rate was following the business cycle. We still expect that the annual GDP growth will reach a bottom in 1Q. Therefore, the following quarters may bring further narrowing of spreads between IRS and WIBOR/NBP reference.
- Investors will also focus on release of the 2012 general government deficit (April 22). We and market foresee the deficit at 3.5% of GDP. However there is an asymmetric risk of higher reading and materialisation of such scenario might result in profit taking along the curve, especially at the long-end, as it puts into question lifting the excessive deficit procedure.

PMI for Polish manufacturing and spread of 5Y IRS vs. 6M WIBOR and NBP reference rate



Sources: Reuters, Markit, CB, BZ WBK

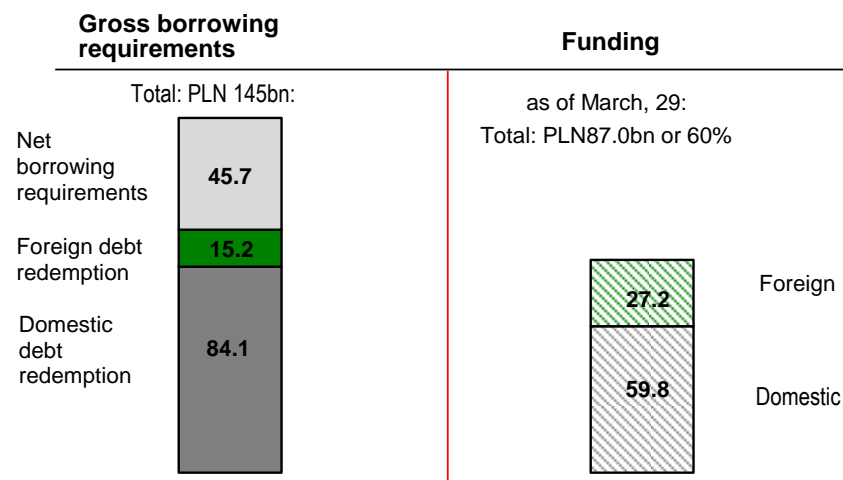


## Supply Corner (1): 80% of borrowing needs in mid-year realistic

- ▶ The first quarter of 2013 was favourable for the Poland's MF as regards issuance on the domestic debt market. The Ministry successfully launched T-bonds worth nearly PLN41bn during standard and switch tenders (up by 4%YoY).
- ▶ The Ministry of Finance will offer T-bonds worth PLN25-35bn in Q2 2013 on 5-6 regular auctions, in which PLN7-15bn will be offered in April. The Ministry might conduct only one switch tender, probably in June. Foreign financing will be determined by the situation not only on the international market, but also on the domestic one. The Ministry does not rule out its activity on the core markets or private placement.
- ▶ Still solid demand from non-residents and liquidity situation (flows from maturing PS0413 and coupon payments amount to PLN24bn in April) should support auction results in Q2.
- ▶ All in all, we think that there is quite realistic that ca. 80% of borrowing requirements will be fulfilled till the end of June (the MF's target).

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### Gross borrowing requirements in 2013



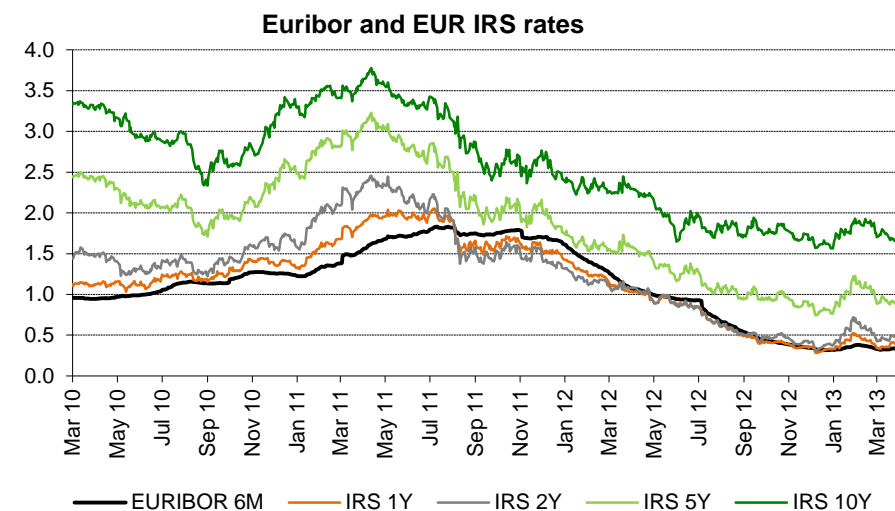
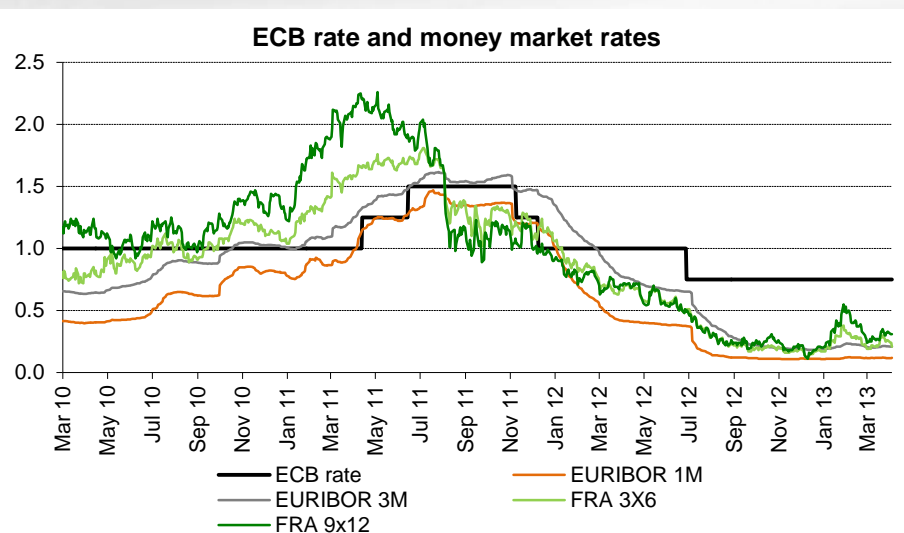
Sources: MF, BZ WBK

## Supply Corner (2): Risk of higher debt supply

- ▶ Faced with lower GDP growth, the Ministry might be forced to recalculate the 2013 budget deficit target at PLN35.6bn. Despite a large gap in VAT receipts in February we maintain our estimate that shortfall of tax receipts might reach ca. PLN18bn. PLN m
- ▶ We predict that the gap could be partly offset by revenues from NBP's profit (ca. PLN5bn, the final figure might be announced in the second half of April), possible (a bit) higher income from dividends (the Ministry wants the state-own companies to pay higher dividends than previously assumed) and discipline in spending. All in all, the budget deficit could be higher by some PLN10bn. Therefore, the risk of the 2013 budget amendment later this year still persists, which, in practice, has already been pre-announced by the MF's officials.
- ▶ Higher deficit would translate into higher borrowing needs and the additional offer represents more or less T-bonds offer at one or two standard auction. However, even in a scenario of significant tax revenue gap, the 2013 gross borrowing needs will be still slightly lower as compared to 2012.
- ▶ We would like to highlight that Poland's public finance liquidity management amounted to PLN30.5bn at the end of March. It is a positive surprise, especially that the Ministry did not assume it in calculation of net borrowing requirements. The value of public finance liquidity management is changing from month to month, however, any sum at the end of the year means lower net borrowing requirements.
- ▶ We can see no major threats for the gross borrowing requirements financing, in particular if the Ministry achieves its target at the end of June (80% of completion). Therefore, a negative reaction to budget amendment should be rather short-lived, giving investors some opportunity to purchase T-bonds with more attractive yields.

## International Money Market and IRS: Near record lows again

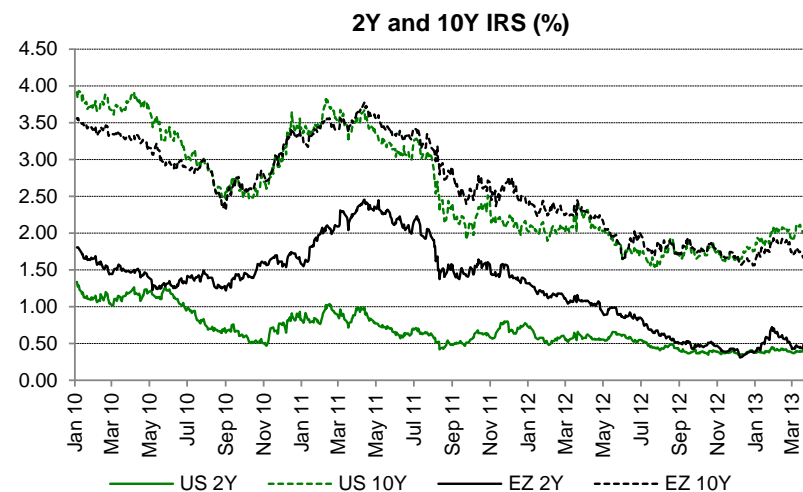
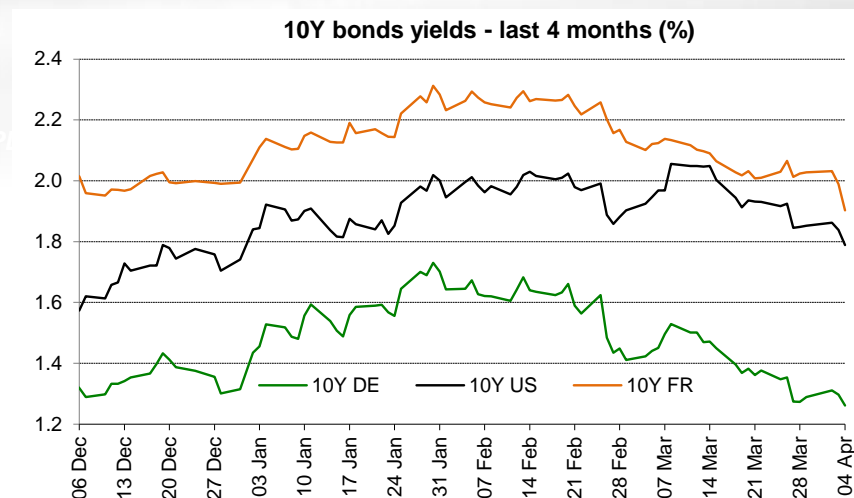
- ▶ Prolonged political instability in Italy (after February's elections) and situation in Cyprus have favoured lower money market and IRS rates, which in the mid of March were close to their record lows. While EURIBOR rates were almost flat at the end of March, FRA contracts and IRS (up to 5Y) slightly increased.
- ▶ Due to some changes in investors' mood IRS curve slightly flattened in March, with 2-10Y IRS spread narrowing to 119bps (down from March's high at 133bps). EURIBOR-ECB's refi rate spreads were almost at the same level during the month (but showing some light narrowing in comparison with the end of 2012).
- ▶ Liquidity situation in the European banking system will support money market rates in coming week. What is more, the uncertain situation in the euro zone (political deadlock in Italy and situation in Cyprus) should also keep IRS rates near current levels.
- ▶ We uphold our medium term view, assuming a gradual rise in market rates in mid-2013.



Sources: Reuters, ECB, BZ WBK

## International Bond Market: Higher appetite for safe-haven assets

- The increased uncertainty surrounding not only Italian political situation, but also previously unseen depositor haircuts in Cyprus triggered risk-off sentiment. Investors shifted their capital onto safe haven assets, which boosted both Bunds and the US Treasuries. Bunds proved to be one of the month's strongest performers (10Y yield fell by 30 bps from month highs).
- In the periphery, both Spanish and Italian bonds sold off through the second half of March after some strengthening in the first part of the month. All in all at the end of March yields were almost flat. Notwithstanding, auctions of peripheral debt on primary markets have attracted much lower demand than in previous month despite yields increase.
- Situation on the euro zone peripheries is still uncertain. Therefore, despite some increase in yields of Bunds and US Treasuries after announcement of the bailout agreement between Cyprus and the Troika, we foresee horizontal trend in yields of safe haven assets this month. But in medium term we maintain our forecasts of yields increase.

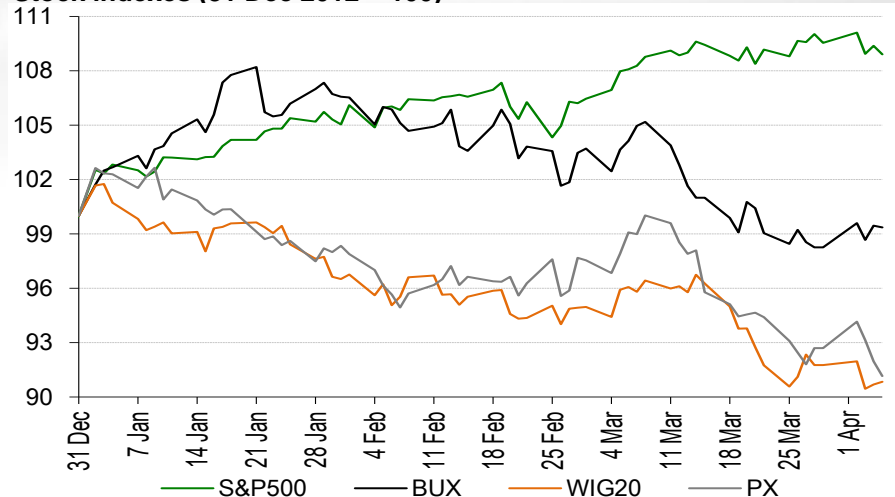


Sources: Reuters, BZ WBK

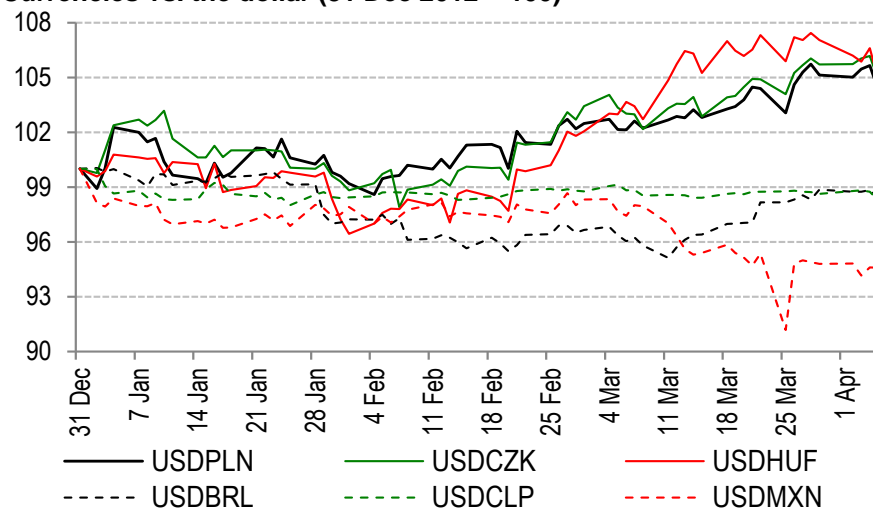
## Foreign Exchange Market: Zloty to remain roughly stable

- ▶ The zloty remained under negative pressure in March, this time not only due to domestic factors, but also due to global events.
- ▶ Polish data (particularly CPI and retail sales for February) fuelled market expectations for more NBP rate cuts. Furthermore, investors became more concerned over the future of the euro zone due to the case of Cyprus and data on economic activity.
- ▶ Though the correction of recent surge of PMI for euro zone's and German manufacturing was not something unusual, the market seems to worry about economic outlook in Europe. Uncertainty over further developments weighs on both CEE currencies and stock prices. On the other hand, US indexes reached record high amid signals of acceleration of pace of economic growth. This backs currencies of countries close to the US.
- ▶ We expect more dovish data from Poland that together with European uncertainty will limit the room for zloty's appreciation. On the other hand, any moves of EURPLN towards 4.20 would be temporary again.

Stock indexes (31 Dec 2012 = 100)



Currencies vs. the dollar (31 Dec 2012 = 100)



Sources: Reuters, BZ WBK

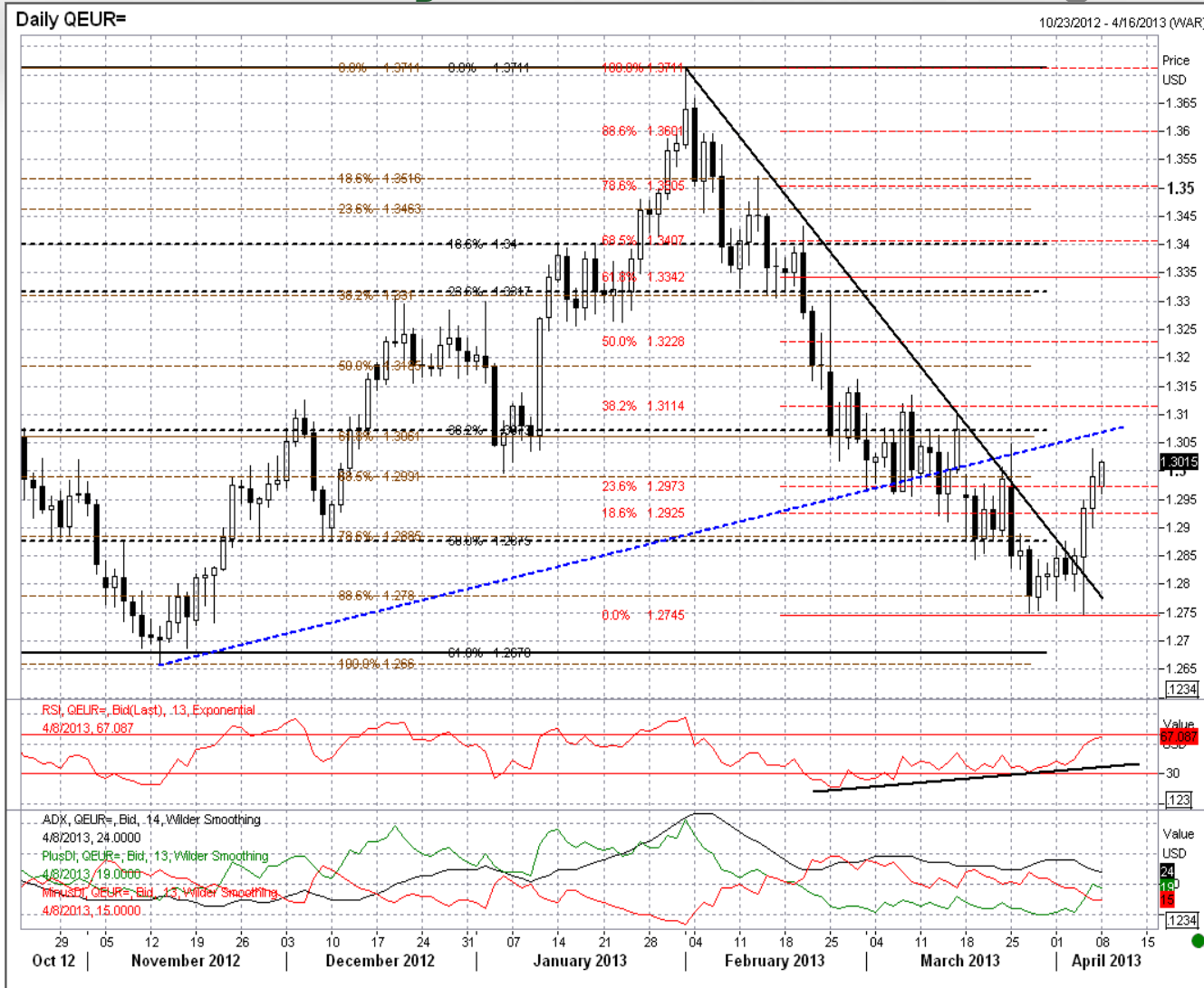
# FX Technical Analysis Corner: EURPLN still in wide range



- ▶ EURPLN declined just below 4.12 and just as we suggested last time, it rebounded from local low in March.
- ▶ In the last couple of months if EURPLN broke 4.20, it was only temporary and we saw this pattern also in early April. Additionally, ratios of length of last waves (marked red) are close to Fibonacci ratios ( $AB/CD \sim 1.618$ ).
- ▶ ADX shows the upward trend is not too strong (oscillator is well below 20-25) and thus we do not expect any breaking changes in April. The EURPLN is likely to stay in the range of 4.12-4.20.

Sources: Reuters, BZ WBK

# FX Technical Analysis Corner: EURUSD heading towards 1.31



- ▶ EURUSD rebounded from the trend line only temporarily and in the following weeks headed south.
- ▶ EURUSD tested the support at 1.278 (88.6% retracement of upward move observed from mid-November) three times.
- ▶ The divergence with the RSI persists and ADX indicates the trend has changed (though the strength of upward momentum is rather moderate).
- ▶ Additionally, EURUSD broke the upper line of the downward channel and two first resistance levels (1.292 and 1.297). Next target for EURUSD is at just above 1.31.

Sources: Reuters, BZ WBK

# Macroeconomic Forecasts

| Poland                               |       | 2010    | 2011    | 2012    | 2013    | 1Q12   | 2Q12   | 3Q12   | 4Q12   | 1Q13   | 2Q13   | 3Q13   | 4Q13   |
|--------------------------------------|-------|---------|---------|---------|---------|--------|--------|--------|--------|--------|--------|--------|--------|
| GDP                                  | PLNbn | 1,416.6 | 1,523.2 | 1,595.9 | 1,629.6 | 370.7  | 388.3  | 392.1  | 444.8  | 380.0  | 394.1  | 398.6  | 456.9  |
| GDP                                  | %YoY  | 3.9     | 4.3     | 2.0     | 1.2     | 3.6    | 2.3    | 1.4    | 1.1    | 0.8    | 0.9    | 1.2    | 1.9    |
| Domestic demand                      | %YoY  | 4.6     | 3.4     | 0.1     | -0.3    | 2.5    | -0.4   | -0.7   | -0.7   | -1.0   | -0.4   | 0.0    | 0.3    |
| Private consumption                  | %YoY  | 3.2     | 2.5     | 0.5     | 1.0     | 1.7    | 1.2    | 0.1    | -1.0   | 1.0    | 0.8    | 1.0    | 1.4    |
| Fixed investments                    | %YoY  | -0.4    | 9.0     | 0.6     | -2.3    | 6.0    | 1.3    | -1.5   | -0.3   | -4.0   | -4.0   | -2.0   | -1.0   |
| Unemployment rate <sup>a</sup>       | %     | 12.4    | 12.5    | 13.4    | 14.0    | 13.3   | 12.3   | 12.4   | 13.4   | 14.4   | 13.4   | 13.4   | 14.0   |
| Current account balance              | EURm  | -18,129 | -17,977 | -13,480 | -8,623  | -4,515 | -2,203 | -3,285 | -3,477 | -3,585 | -1,127 | -1,879 | -2,032 |
| Current account balance              | % GDP | -5.1    | -4.9    | -3.5    | -2.2    | -5.1   | -4.6   | -4.1   | -3.5   | -3.3   | -2.9   | -2.6   | -2.2   |
| General government balance           | % GDP | -7.9    | -5.0    | -3.5    | -3.5    | -      | -      | -      | -      | -      | -      | -      | -      |
| CPI                                  | %YoY  | 2.6     | 4.3     | 3.7     | 1.2     | 4.1    | 4.0    | 3.9    | 2.9    | 1.3    | 0.7    | 1.2    | 1.6    |
| CPI <sup>a</sup>                     | %YoY  | 3.1     | 4.6     | 2.4     | 1.7     | 3.9    | 4.3    | 3.8    | 2.4    | 1.0    | 0.6    | 1.4    | 1.7    |
| CPI excluding food and energy prices | %YoY  | 1.6     | 2.4     | 2.2     | 1.2     | 2.5    | 2.5    | 2.1    | 1.7    | 1.1    | 0.9    | 1.3    | 1.6    |

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

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



# Interest Rate and FX Forecasts

| Poland                      |     | 2010 | 2011 | 2012 | 2013 | 1Q12 | 2Q12 | 3Q12 | 4Q12 | 1Q13 | 2Q13 | 3Q13 | 4Q13 |
|-----------------------------|-----|------|------|------|------|------|------|------|------|------|------|------|------|
| Reference rate <sup>a</sup> | %   | 3.50 | 4.50 | 4.25 | 3.25 | 4.50 | 4.75 | 4.75 | 4.25 | 3.25 | 3.25 | 3.25 | 3.25 |
| WIBOR 3M                    | %   | 3.94 | 4.54 | 4.91 | 3.48 | 4.97 | 5.04 | 5.06 | 4.57 | 3.77 | 3.37 | 3.37 | 3.42 |
| Yield on 2-year T-bonds     | %   | 4.72 | 4.81 | 4.30 | 3.26 | 4.66 | 4.71 | 4.22 | 3.61 | 3.29 | 3.11 | 3.25 | 3.40 |
| Yield on 5-year T-bonds     | %   | 5.31 | 5.44 | 4.53 | 3.50 | 5.02 | 4.93 | 4.43 | 3.75 | 3.49 | 3.30 | 3.51 | 3.68 |
| Yield on 10-year T-bonds    | %   | 5.74 | 5.98 | 5.02 | 3.97 | 5.58 | 5.38 | 4.91 | 4.22 | 3.95 | 3.77 | 3.97 | 4.18 |
| 2-year IRS                  | %   | 4.73 | 4.98 | 4.52 | 3.27 | 4.83 | 4.91 | 4.47 | 3.85 | 3.43 | 3.14 | 3.20 | 3.30 |
| 5-year IRS                  | %   | 5.25 | 5.24 | 4.47 | 3.39 | 4.82 | 4.86 | 4.37 | 3.84 | 3.52 | 3.25 | 3.34 | 3.47 |
| 10-year IRS                 | %   | 5.40 | 5.33 | 4.56 | 3.83 | 4.88 | 4.88 | 4.47 | 4.01 | 3.76 | 3.62 | 3.85 | 4.08 |
| EUR/PLN                     | PLN | 3.99 | 4.12 | 4.19 | 4.14 | 4.23 | 4.26 | 4.14 | 4.11 | 4.16 | 4.16 | 4.15 | 4.10 |
| USD/PLN                     | PLN | 3.02 | 2.96 | 3.26 | 3.10 | 3.23 | 3.32 | 3.31 | 3.17 | 3.14 | 3.13 | 3.10 | 3.03 |
| CHF/PLN                     | PLN | 2.90 | 3.34 | 3.47 | 3.35 | 3.50 | 3.55 | 3.44 | 3.40 | 3.39 | 3.37 | 3.35 | 3.31 |
| GBP/PLN                     | PLN | 4.66 | 4.75 | 5.16 | 4.86 | 5.07 | 5.26 | 5.22 | 5.09 | 4.88 | 4.83 | 4.87 | 4.85 |

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

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

# Economic Calendar and Events

| Date   |    | Event:   | Note:   |
|--------|----|--|---|
| 10-Apr | PL | <b>MPC Meeting – interest rate decision</b>        | <b>We expect the MPC to keep rates unchanged</b>  |
|        | DE | Auction of 2Y bonds                                | Offer: €5bn   |
| 11-Apr | PL | <b>Auction of bonds: DS1023, WZ0124</b>            | <b>Offer: PLN2.0-5.0bn</b>  |
|        | IT | Auction of medium-long term bonds                  | -   |
| 12-Apr | EU | Eurogroup meeting                                  |   |
| 15-Apr | PL | <b>CPI for March</b>                               | <b>Our forecast: 1.0%YoY (slightly below consensus at 1.1%YoY)</b>  |
| 16-Apr | PL | <b>Core inflation for March</b>                    | <b>We expect core CPI after excluding food and energy prices at 1.0%YoY</b>   |
| 17-Apr | PL | <b>Employment and wages for March</b>              | <b>We expect employment decline by 0.9%YoY and subdued growth of wages (by 2.1%YoY)</b>                                 |
|        | DE | Auction of 10Y bonds                               | Offer: €4bn   |
| 18-Apr | PL | <b>Industrial output and PPI for March</b>         | <b>Our forecast of industrial output: -1.4%YoY (slower decline than consensus at -2.4%). We predict PPI at -0.7%YoY</b> |
|        | SP | Auction of bonds                                   | -   |
| 22-Apr | PL | <b>General government deficit and debt in 2012</b> | <b>We predict the general government deficit at 3.5% of GDP</b>   |
| 23-Apr | PL | <b>Retail sales for March</b>                      | <b>Our forecast: +0.1%YoY (confirming weakness of consumer demand)</b>  |
|        | PL | <b>Auction of bonds: OK0715, WZ0117, PS0418</b>    | <b>Offer: PLN5.0-10.0bn</b>   |
|        | HU | NBH Meeting - interest rate decision               | -   |
| 24-Apr | DE | Auction of 30Y bonds                               | Offer: €2bn   |
| Apr-   | IT | Presidential election in Italy                     |   |
| 2-May  | EU | ECB Meeting – interest rate decision               | -   |
|        | CZ | CNB Meeting – interest rate decision               | -   |
| 8-May  | PL | <b>MPC Meeting – interest rate decision</b>        | -   |

# Annex

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

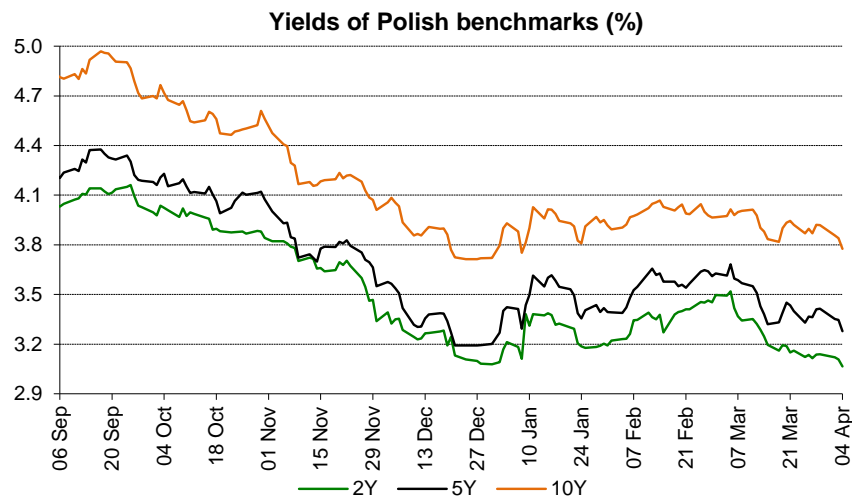
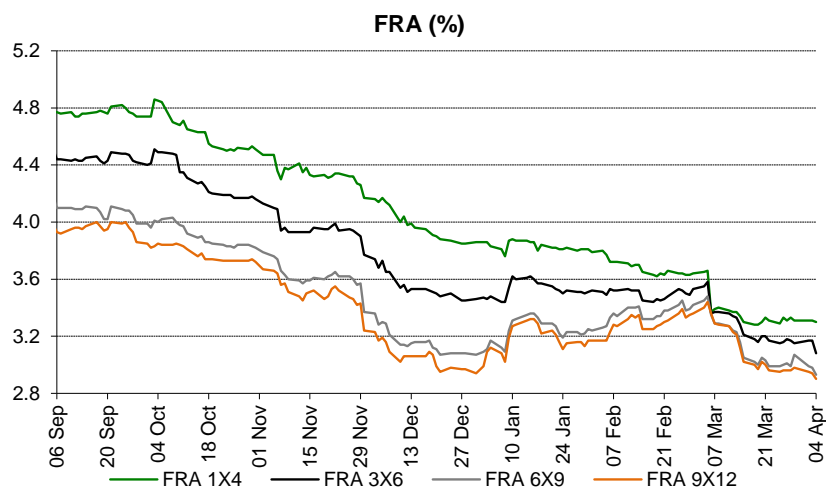
# 1. Domestic markets performance

## Money market rates (%)

|                     | Reference | Polonia | WIBOR (%) |      |      |      | OIS (%) |      |      |      | FRA (%) |      |      |      |
|---------------------|-----------|---------|-----------|------|------|------|---------|------|------|------|---------|------|------|------|
|                     | rate (%)  | (%)     | 1M        | 3M   | 6M   | 12M  | 1M      | 3M   | 6M   | 12M  | 1x4     | 3x6  | 6x9  | 9x12 |
| End of March        | 3.25      | 3.3     | 3.39      | 3.39 | 3.39 | 3.39 | 3.22    | 3.12 | 3.02 | 2.93 | 3.31    | 3.15 | 3.07 | 2.98 |
| Last 1M change (bp) | -50       | -40     | -41       | -34  | -28  | -21  | -38     | -38  | -36  | -36  | -32     | -34  | -32  | -37  |
| Last 3M change (bp) | -100      | -44     | -82       | -72  | -69  | -59  | -81     | -71  | -36  | -25  | -55     | -31  | 0    | 4    |
| Last 1Y change (bp) | -125      | -122    | -133      | -155 | -157 | -158 | -102    | -111 | -121 | -131 | -164    | -178 | -180 | -180 |

## Bond and IRS market (%)

|                      | T-bills | BONDS |      |      |      | IRS  |      |    | Spread BONDS / IRS (bps) |     |  |
|----------------------|---------|-------|------|------|------|------|------|----|--------------------------|-----|--|
|                      | 52-week | 2Y    | 5Y   | 10Y  | 2Y   | 5Y   | 10Y  | 2Y | 5Y                       | 10Y |  |
| End of March         | 3.25    | 3.14  | 3.41 | 3.92 | 3.17 | 3.30 | 3.59 | -3 | 11                       | 33  |  |
| Last 1M change (bps) | -35     | -32   | -20  | -5   | -36  | -32  | -26  | 4  | 12                       | 21  |  |
| Last 3M change (bps) | -55     | 6     | 21   | 20   | -19  | -6   | 2    | 25 | 27                       | 18  |  |
| Last 1Y change (bps) | -125    | -145  | -154 | -162 | -167 | -158 | -138 | 22 | 4                        | -24 |  |



Sources: Reuters, NBP, BZ WBK

## 2. Polish bonds: supply recap

### Total issuance in 2013 by instruments (in PLNm, nominal terms)

|  | Jan           | Feb           | Mar           | Apr           | May          | Jun          | Jul           | Aug           | Sep          | Oct            | Nov          | Dec        | Total          |
|--|---------------|---------------|---------------|---------------|--------------|--------------|---------------|---------------|--------------|----------------|--------------|------------|----------------|
| <b>T-bonds auction</b>   | 17,358        | 10,391        | 8,081         | 15,000        | 6,150        | 5,000        | 10,500        | 1,000         | 5,500        | 11,000         | 3,100        |            | 93,080         |
| <b>T-bills auction</b>   | 3,603         | 1,747         | 3,084         |               |              |              |               |               |              |                |              |            | 8,433          |
| <b>Retail bonds</b>  | 150           | 154           | 154           | 154           | 154          | 154          | 154           | 113           | 154          | 154            | 114          | 157        | 1,766          |
| <b>Foreign bonds/credits</b>                                   | 4,140         | 1,301         |               |               | 2,000        | 1,800        |               |               |              |                | 2,000        |            | 11,241         |
| <b>Prefinancing and financial resources at the end of 2012</b> | 24,400        |               |               |               |              |              |               |               |              |                |              |            | 24,400         |
| <b>Total</b>   | <b>49,651</b> | <b>13,593</b> | <b>11,318</b> | <b>15,154</b> | <b>8,304</b> | <b>6,954</b> | <b>10,654</b> | <b>1,113</b>  | <b>5,654</b> | <b>11,154</b>  | <b>5,214</b> | <b>157</b> | <b>138,920</b> |
| <b>Redemption</b>  | 11,686        | 13,854        | 2,791         | 22,261        | 4,024        | 1,894        | 13,497        | 3217.5        | 561          | 24,213         | 408          | 183        | 98,589         |
| <b>Net inflows</b>   | <b>37,965</b> | <b>-261</b>   | <b>8,527</b>  | <b>-7,107</b> | <b>4,280</b> | <b>5,060</b> | <b>-2,843</b> | <b>-2,105</b> | <b>5,093</b> | <b>-13,059</b> | <b>4,806</b> | <b>-26</b> | <b>40,331</b>  |
| <b>Rolling over T-bonds</b>                                    |               |               | 4,827         |               |              |              |               |               |              |                |              |            | 4,827          |
| <b>Buy-back of T-bills/bonds</b>                               |               |               |               |               |              |              |               |               |              |                |              |            | 0              |
| <b>Total</b>   | <b>37,965</b> | <b>-261</b>   | <b>13,354</b> | <b>-7,107</b> | <b>4,280</b> | <b>5,060</b> | <b>-2,843</b> | <b>-2,105</b> | <b>5,093</b> | <b>-13,059</b> | <b>4,806</b> | <b>-26</b> | <b>45,158</b>  |
| <i>Coupon payments</i>   | 2,492         |               |               | 7,322         |              |              | 1,955         |               | 1,497        | 9,685          |              |            | 22,951         |

Note: Our forecasts – shaded area

## 2. Polish bonds: supply recap (cont.)

Schedule Treasury Securities redemption by instruments (in PLNm)

|                    | Bonds          | Bills         | Retail bonds | Total domestic redemption | Foreign Bonds/Credits | Total redemptions |
|--------------------|----------------|---------------|--------------|---------------------------|-----------------------|-------------------|
| January            | 10,001         | 1,592         | 93           | 11,686                    |                       | 11,686            |
| February           |                | 2,190         | 148          | 2,338                     | 11,516                | 13,854            |
| March              |                | 2,329         | 212          | 2,541                     | 250                   | 2,791             |
| April              | 16,025         | 0             | 132          | <b>16,157</b>             | 0                     | <b>16,157</b>     |
| May                | 0              | 2,223         | 117          | <b>2,339</b>              | 2,567                 | <b>4,906</b>      |
| June               | 0              | 1,747         | 112          | <b>1,859</b>              | 2,666                 | <b>4,525</b>      |
| July               | 13,205         | 0             | 218          | <b>13,423</b>             | 4,900                 | <b>18,323</b>     |
| August             | 0              | 1,997         | 248          | <b>2,245</b>              | 946                   | <b>3,191</b>      |
| September          | 0              | 0             | 176          | <b>176</b>                | 946                   | <b>1,122</b>      |
| October            | 23,913         | 0             | 265          | <b>24,178</b>             | 950                   | <b>25,129</b>     |
| November           | 0              | 1,332         | 208          | <b>1,540</b>              | 716                   | <b>2,256</b>      |
| December           | 0              | 2,223         | 146          | <b>2,368</b>              | 0                     | <b>2,368</b>      |
| <b>Total 2013</b>  | <b>64,090</b>  | <b>15,317</b> | <b>2,283</b> | <b>81,690</b>             | <b>15,891</b>         | <b>97,581</b>     |
| <b>Total 2014</b>  | <b>61,666</b>  | <b>6,110</b>  | <b>1,698</b> | <b>90,276</b>             | <b>14,825</b>         | <b>105,102</b>    |
| <b>Total 2015</b>  | <b>87,202</b>  |               | <b>628</b>   | <b>59,586</b>             | <b>17,448</b>         | <b>77,034</b>     |
| <b>Total 2016</b>  | <b>59,378</b>  |               | <b>485</b>   | <b>79,365</b>             | <b>14,329</b>         | <b>93,694</b>     |
| <b>Total 2017</b>  | <b>70,694</b>  |               | <b>91</b>    | <b>59,469</b>             | <b>16,871</b>         | <b>76,340</b>     |
| <b>Total 2018+</b> | <b>208,911</b> |               | <b>3,288</b> | <b>213,794</b>            | <b>134,966</b>        | <b>348,760</b>    |

Sources: MF, BZ WBK

## 2. Polish bonds: supply recap (cont.)

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

|                    | Foreign investors | Domestic banks | Insurance Funds | Pension Funds | Mutual Funds  | Individuals | Non-financial sector | Other        | Total          |
|--------------------|-------------------|----------------|-----------------|---------------|---------------|-------------|----------------------|--------------|----------------|
| Q1 2013            | 0                 | 0              | 0               | 0             | 0             | 0           | 0                    | 0            | 0              |
| Q2 2013            | 7,788             | 4,274          | 2,167           | 2,202         | 829           | 59          | 299                  | 2,926        | 20,545         |
| Q3 2013            | 9,125             | 766            | 1,145           | 687           | 197           | 143         | 16                   | 1,353        | 13,431         |
| Q4 2013            | 8,785             | 1,409          | 7,177           | 4,005         | 835           | 117         | 64                   | 1,772        | 24,165         |
| <b>Total 2013</b>  | <b>25,698</b>     | <b>6,449</b>   | <b>10,489</b>   | <b>6,894</b>  | <b>1,862</b>  | <b>344</b>  | <b>379</b>           | <b>6,052</b> | <b>58,167</b>  |
|                    | <b>44%</b>        | <b>11%</b>     | <b>18%</b>      | <b>12%</b>    | <b>3%</b>     | <b>1%</b>   | <b>1%</b>            | <b>10%</b>   | <b>100%</b>    |
| <b>Total 2014</b>  | <b>36,947</b>     | <b>8,619</b>   | <b>4,957</b>    | <b>4,233</b>  | <b>2,898</b>  | <b>412</b>  | <b>120</b>           | <b>3,770</b> | <b>61,956</b>  |
|                    | <b>60%</b>        | <b>14%</b>     | <b>8%</b>       | <b>7%</b>     | <b>5%</b>     | <b>1%</b>   | <b>0%</b>            | <b>6%</b>    | <b>100%</b>    |
| <b>Total 2015</b>  | <b>26,139</b>     | <b>22,008</b>  | <b>7,760</b>    | <b>11,919</b> | <b>6,590</b>  | <b>224</b>  | <b>583</b>           | <b>5,024</b> | <b>80,247</b>  |
|                    | <b>33%</b>        | <b>27%</b>     | <b>10%</b>      | <b>15%</b>    | <b>8%</b>     | <b>0%</b>   | <b>1%</b>            | <b>6%</b>    | <b>100%</b>    |
| <b>Total 2016</b>  | <b>19,149</b>     | <b>9,361</b>   | <b>3,620</b>    | <b>19,771</b> | <b>6,907</b>  | <b>55</b>   | <b>74</b>            | <b>3,735</b> | <b>62,673</b>  |
|                    | <b>31%</b>        | <b>15%</b>     | <b>6%</b>       | <b>32%</b>    | <b>11%</b>    | <b>0%</b>   | <b>0%</b>            | <b>6%</b>    | <b>100%</b>    |
| <b>Total 2017</b>  | <b>25,888</b>     | <b>11,365</b>  | <b>5,684</b>    | <b>14,159</b> | <b>6,750</b>  | <b>57</b>   | <b>83</b>            | <b>3,292</b> | <b>67,278</b>  |
|                    | <b>38%</b>        | <b>17%</b>     | <b>8%</b>       | <b>21%</b>    | <b>10%</b>    | <b>0%</b>   | <b>0%</b>            | <b>5%</b>    | <b>100%</b>    |
| <b>Total 2018+</b> | <b>61,172</b>     | <b>35,084</b>  | <b>19,391</b>   | <b>56,595</b> | <b>16,347</b> | <b>198</b>  | <b>385</b>           | <b>7,886</b> | <b>197,059</b> |
|                    | <b>31%</b>        | <b>18%</b>     | <b>10%</b>      | <b>29%</b>    | <b>8%</b>     | <b>0%</b>   | <b>0%</b>            | <b>4%</b>    | <b>100%</b>    |

Sources: MF, BZ WBK

## 3. Polish bonds: demand recap

### Holders of marketable PLN bonds

|                             | Nominal value (PLN, bn) |         | Nominal value (PLN, bn) |          |          | % change in February |       |       | Share in TOTAL (%) in Feb |
|-----------------------------|-------------------------|---------|-------------------------|----------|----------|----------------------|-------|-------|---------------------------|
|                             | End Feb                 | End Jan | End 2012                | End 2011 | End 2010 | MoM                  | 3-mth | YoY   |                           |
| <b>Domestic investors</b>   | 343.0                   | 339.8   | 337.5                   | 349.8    | 354.2    | 0.94                 | 3.33  | -3.13 | 62.9 (-0.6pp)             |
| <b>Commercial banks</b>     | 99.4                    | 92.9    | 87.8                    | 103.3    | 110.4    | 7.01                 | 8.72  | -6.92 | 18.2 (0.9pp)              |
| <b>Insurance companies</b>  | 51.0                    | 51.9    | 52.8                    | 55.5     | 59.5     | -1.77                | -5.82 | -6.53 | 9.4 (-0.4pp)              |
| <b>Pension funds</b>        | 113.3                   | 113.6   | 117.4                   | 122.2    | 117.0    | -0.26                | -5.06 | -5.95 | 20.8 (-0.5pp)             |
| <b>Mutual funds</b>         | 42.1                    | 41.4    | 41.7                    | 31.7     | 30.2     | 1.90                 | 8.66  | 36.54 | 7.7                       |
| <b>Others</b>               | 37.2                    | 40.0    | 37.8                    | 37.1     | 37.0     | -7.2                 | 2.6   | -10.3 | 6.8 (-0.7pp)              |
| <b>Foreign investors*</b>   | 202.2                   | 195.0   | 189.9                   | 152.5    | 124.8    | 3.67                 | 7.70  | 26.37 | 37.1 (+0.6pp)             |
| <b>Banks</b>                | 33.8                    | 30.4    | 28.4                    | 16.2     | 21.9     | 11.02                | 21.35 | 53.81 | 6.2 (0.5pp)               |
| <b>Non-bank fin. sector</b> | 159.9                   | 156.2   | 153.1                   | 129.3    | 96.8     | 2.39                 | 5.63  | 21.95 | 29.3 (1.6)                |
| <b>Non-financial sector</b> | 4.9                     | 4.8     | 5.2                     | 4.5      | 4.2      | 1.44                 | -5.57 | 14.46 | 0.9                       |
| <b>TOTAL</b>                | 545.1                   | 534.8   | 502.3                   | 478.9    | 414.7    | 1.94                 | 0.91  | 6.05  | 100                       |

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



## 4. Euro zone bonds: supply recap

### Euro zone's issuance plans and completion in 2013 (€ bn)

|              | Total redemptions | Deficit      | Borrowing needs | Expected bond supply | % of completion (YtD) |
|--------------|-------------------|--------------|-----------------|----------------------|-----------------------|
| Austria      | 15.9              | 6.3          | 22.2            | 22.2                 | 17.0                  |
| Belgium      | 30.3              | 8.8          | 40.0            | 37.0                 | 34.0                  |
| Finland      | 6.8               | 5.6          | 12.4            | 12.4                 | 7.0                   |
| France       | 105.5             | 61.6         | 171.1           | 170.0                | 40.0                  |
| Germany      | 157.0             | 17.1         | 174.1           | 174.1                | 29.0                  |
| Greece       | 9.7               | 11.6         | 21.3            | 0.0                  | -                     |
| Ireland      | 5.1               | 12.5         | 17.6            | 10.0                 | 75.0                  |
| Italy        | 154.7             | 25.5         | 180.2           | 180.2                | 36.0                  |
| Netherlands  | 31.5              | 15.2         | 46.7            | 50.0                 | 41.0                  |
| Portugal     | 5.9               | 7.4          | 13.3            | 3.0                  | 84.0                  |
| Spain        | 61.9              | 48.4         | 133.3           | 113.4                | 39.0                  |
| <b>Total</b> | <b>584.3</b>      | <b>220.0</b> | <b>832.2</b>    | <b>772.3</b>         | <b>36.0</b>           |

Sources: Eurostat, BZ WBK

## 5. Poland vs other countries

### Main macroeconomic indicators (European Commission's forecasts)

|                | GDP (%) |       | Inflation (HICP, %) |       | C/A balance (% of GDP) |       | Fiscal Balance (% of GDP) |       | Public Debt (% of GDP) |       |
|----------------|---------|-------|---------------------|-------|------------------------|-------|---------------------------|-------|------------------------|-------|
|                | 2012F   | 2013E | 2012F               | 2013E | 2012F                  | 2013E | 2012F                     | 2013E | 2012F                  | 2013E |
| Poland         | 2.0     | 1.2   | 3.7                 | 1.8   | -3.6                   | -2.7  | -3.5                      | -3.4  | 55.8                   | 57.0  |
| Czech Republic | -1.1    | 0.0   | 3.5                 | 2.1   | -2.9                   | -2.7  | -5.2                      | -3.1  | 45.5                   | 48.0  |
| Hungary        | -1.7    | -0.1  | 5.7                 | 3.6   | 2.3                    | 3.3   | -2.4                      | -3.4  | 78.6                   | 78.7  |
| EU             | -0.3    | 0.1   | 2.6                 | 2.0   | 0.7                    | 1.4   | -3.5                      | -2.8  | 87.2                   | 89.9  |
| Euro area      | -0.6    | -0.3  | 2.5                 | 1.8   | 1.5                    | 2.2   | -3.8                      | -3.4  | 93.1                   | 95.1  |
| Germany        | 0.7     | 0.5   | 2.1                 | 1.8   | 6.3                    | 6.0   | 0.1                       | -0.2  | 81.6                   | 80.7  |

### Main market indicators (%)

|                | Reference rate (%) |      | 3M market rate (%) |              | 10Y yields (%) |              | 10Y Spread vs Bund (bps) |              | CDS 5Y |              |
|----------------|--------------------|------|--------------------|--------------|----------------|--------------|--------------------------|--------------|--------|--------------|
|                | 2012               | 2013 | 2012               | end of March | 2012           | end of March | 2012                     | end of March | 2012   | end of March |
| Poland         | 4.25               | 3.25 | 4.11               | 3.39         | 3.72           | 3.92         | 241                      | 263          | 80     | 97           |
| Czech Republic | 0.05               | 0.05 | 0.18               | 0.14         | 1.86           | 1.89         | 54                       | 60           | 63     | 62           |
| Hungary        | 5.75               | 5.00 | 5.75               | 4.90         | 6.23           | 6.39         | 492                      | 510          | 269    | 413          |
| Euro area      | 0.75               | 0.75 | 0.19               | 0.21         |                |              |                          |              |        |              |
| Germany        |                    |      |                    |              | 1.32           | 1.29         |                          |              | 39     | 37           |

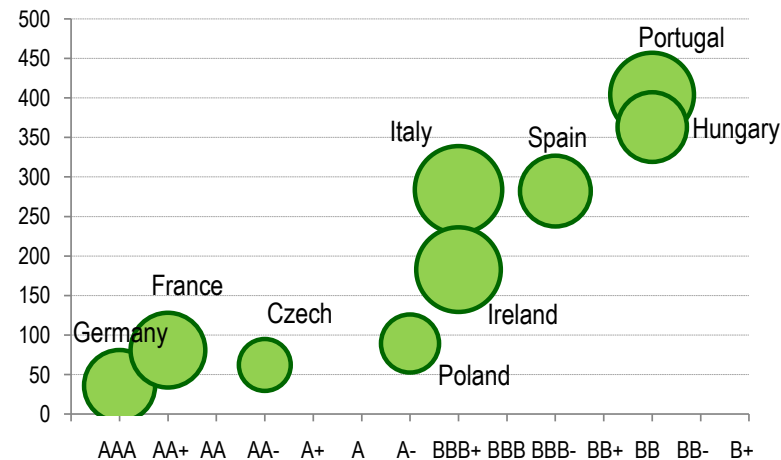
Sources: EC – Winter 2013, stat offices, central banks, Reuters, BZ WBK

# 5. Poland vs other countries (cont.)

Sovereign ratings

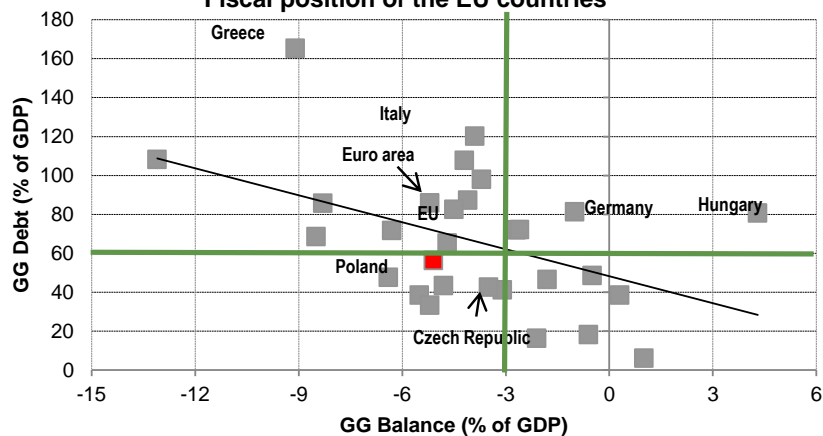
|          | S&P    |          | Moody's |          | Fitch  |          |
|----------|--------|----------|---------|----------|--------|----------|
|          | rating | outlook  | rating  | outlook  | rating | outlook  |
| Poland   | A-     | stable   | A2      | stable   | A-     | positive |
| Czech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

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

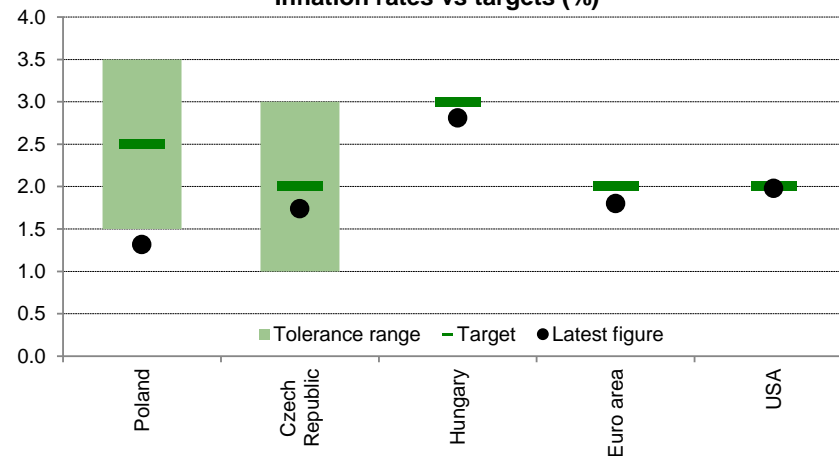


Note: Size of bubbles reflects the debt/GDP ratio

Fiscal position of the EU countries

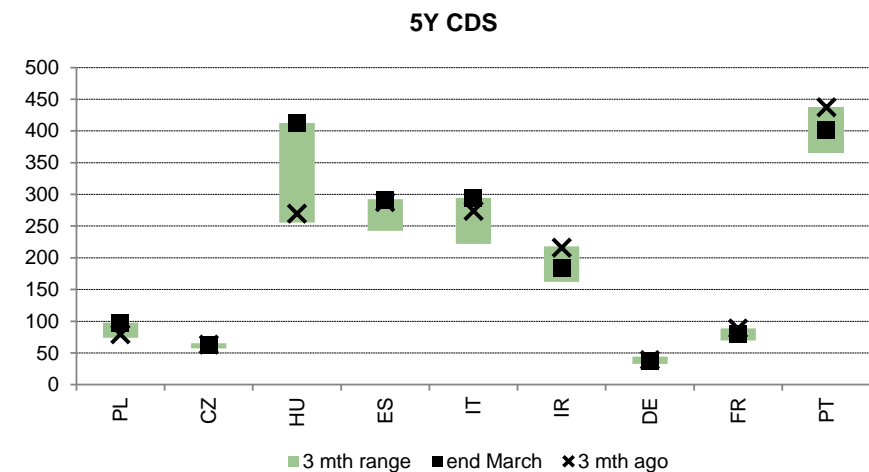
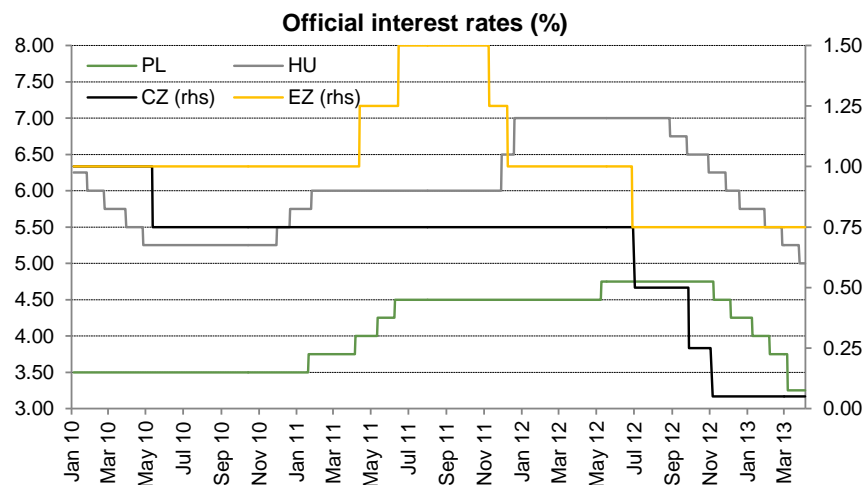
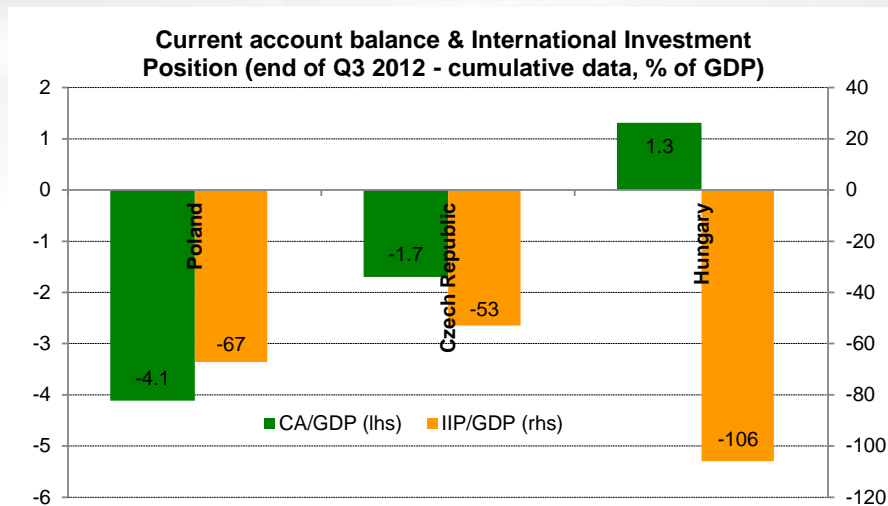
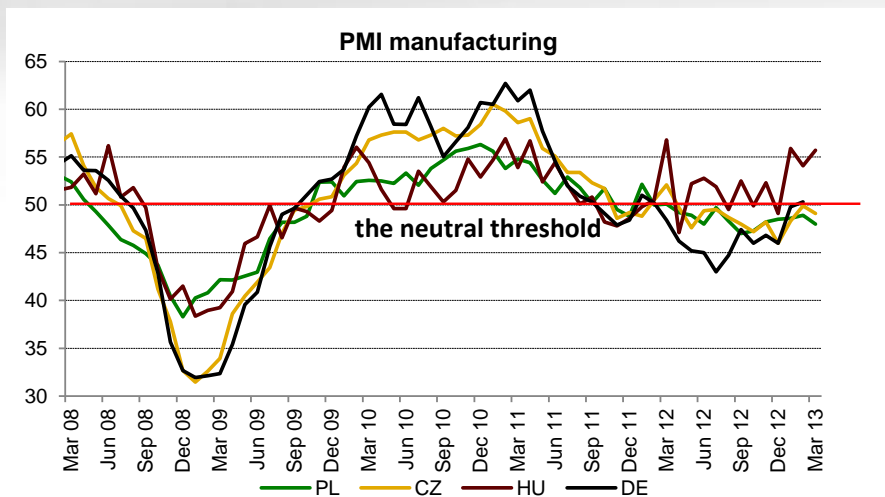


Inflation rates vs targets (%)



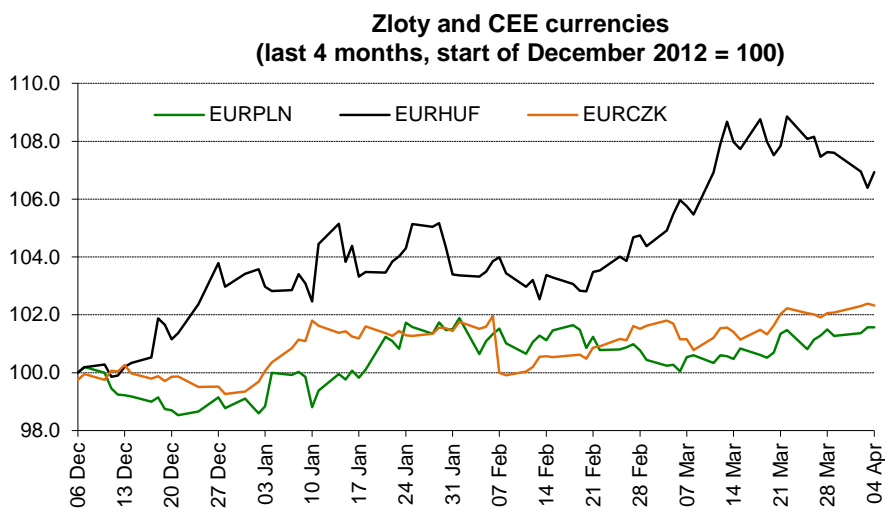
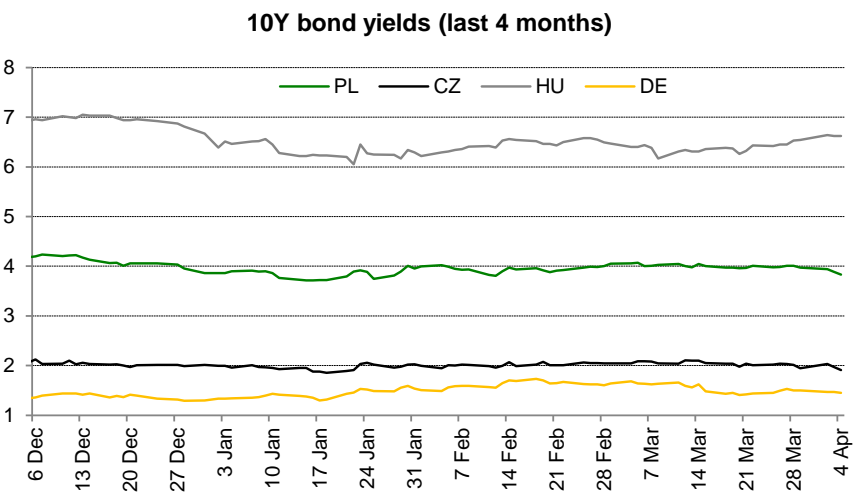
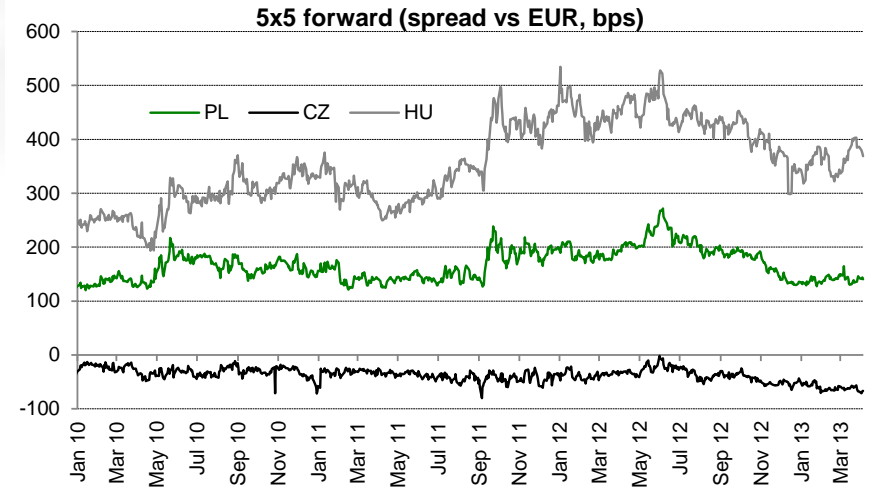
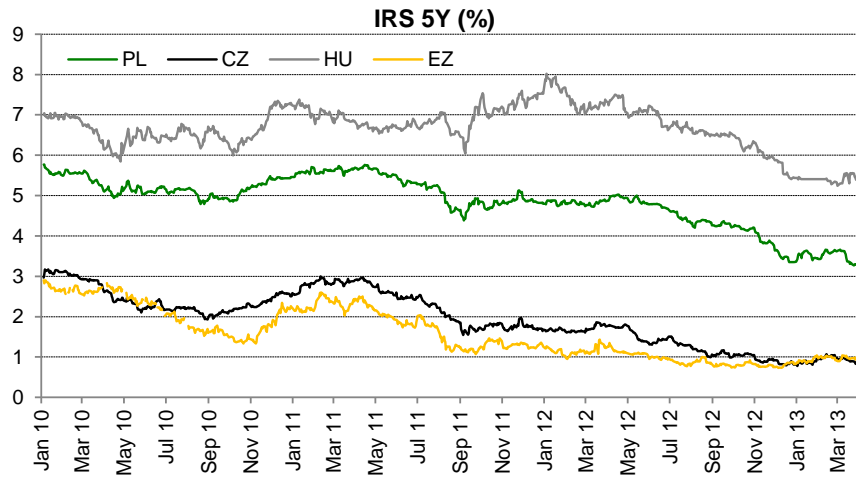
Source: rating agencies, Reuters, BZ WBK, EC

# 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   | 2012   | 2013F | Expected changes (bps) |     |     | Risks/Events   |
|-----------------------|------------------|--------|--------|-------|------------------------|-----|-----|--|
|                       |                  |        |        |       | 1M                     | 3M  | 6M  |  |
| <b>Euro zone</b>      | Forecast         | 0.75   | 0.75   | 0.75  |                        |     |     | The ECB softened its tone on April's meeting. Mr Draghi acknowledged that monetary policy will remain accommodative "as long as needed" and that ECB "stands ready to act"   |
|                       | Market implied » |        |        |       | 0                      | 1   | 0   |  |
| <b>UK</b>             | Forecast         | 0.50   | 0.50   | 0.50  |                        |     |     | As expected, the BoE kept interest rates unchanged in April. The BoE's focus remains overseas.   |
|                       | Market implied » |        |        |       | 0                      | -1  | -2  |  |
| <b>US</b>             | Forecast         | 0-0.25 | 0-0.25 | 0.25  |                        |     |     | Nothing change in the monetary policy outlook. Still any news about possible Fed's exit will strongly affect the UST market.   |
|                       | Market implied » |        |        |       | 0                      | 1   | 4   |  |
| <b>Poland</b>         | Forecast         | 3.25   | 4.25   | 3.25  |                        |     |     | We think that the MPC will keep interest rates unchanged this month, after unexpected cut by 50bps in March. there is a risk that very low inflation rate and slow recovery process will put pressure on the MPC to deliver more easing. Most probably, some members will wait as long as until July's projection. |
|                       | Market implied » |        |        |       | -7                     | -29 | -44 |  |
| <b>Czech Republic</b> | Forecast         | 0.05   | 0.05   | 0.05  |                        |     |     | Rates on hold. There is still a risk that the CNB will intervene directly against the CZK to support GDP growth  |
|                       | Market implied » |        |        |       | 29                     | 30  | 29  |  |
| <b>Hungary</b>        | Forecast         | 5.00   | 5.75   | 5.00  |                        |     |     | The NBH has continued easing cycle. What is more central bank launched the Funding for Growth Scheme (FGS) to boost economy.   |
|                       | Market implied » |        |        |       | -22                    | -66 | -86 |  |

This analysis is based on information available until 4<sup>th</sup> April 2013 and has been prepared by:

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