Bank Zachodni WBK

Eyeopener – CPI data key for interest rate market

13 July 2012

- **Weak sentiment after disappointing Fed minutes**
- **Correction of the zloty, Polish debt keeps strengthening**
- **Belka revived expectations for interest rate cuts**
- **Today, data on inflation and balance of payments**

During Thursday's session poor moods dominated the market because investors were still disappointed with lack of suggestions about QE3 in the USA. Moreover, the fears about prospects of economic growth and peripheries of the euro-zone are still present. The risk aversion's increase caused the continuation of selloff on the stock exchanges and increase of prices of assets which are considered as safe. The German 10Y bonds' yields reached the lowest level in last few weeks (1.236%) and Dutch 2Y bond yields fell below zero. On the other hand the Spanish and Italian bond yields increased (by ca. 10bp), but it was to some extent a correction after recent strengthening rather than the escape from euro zone peripheries' assets, what is confirmed by result of Italian treasury bills' auction. Italy sold 12M bills worth EUR 7.5bn by quite good demand (the demand-to-supply ratio amounted to 1.55) and lower yields (2.70% against 3.97% a month before). The macroeconomic data released yesterday surprised positively: the industrial output in the euro zone increased in May by 0.6% in monthly terms (the market expected -0.1%MoM) and the initial jobless claims in the USA amounted to 350k (the four-year low), but it didn't have significant influence on the market.

Today in the morning Moody's cut the rating of Italy by two levels due to fear of strong increase in costs of financing for this country. On the other hand the China's GDP data was released, which confirmed growth slowdown to 7.6%, the slowest pace since 2009. What is interesting, the Chinese data triggered rise on the stock markets in Asia, boosting hopes that Chinese central bank will decide for stronger impulse in order to stimulate the economy.

During Thursday's session the US dollar gained against euro, supported by the hopes for QE3. From the opening level of 1.2235 EURUSD decreased to 1.2165, the lowest level since mid-2010. In the second half of the day euro regained some of the losses and consolidated slightly above 1.2180. In Friday's morning EURUSD amounts to slightly below 1.22. Today the Italian debt's auction takes a central stage. The moods are still not so positive, taking into consideration the remaining fears about economic growth, but also Italian rating's cut.

Zloty underwent correction after recent gains. EURPLN and USDPLN for a whole day moved in upward trend. EURPLN climbed from 4.188 at the opening to ca. 4.210 and USDPLN from 3.423 to 3.455. The zloty's quotations during Asian session remained quite stable and in the morning ERUPLN amounts to ca. 4.20 and USDPLN slightly above 3.443. Today besides foreign factors the attention will be paid to domestic data, mainly June's CPI and balance of payments for May.

Domestic debt market has continued rallying, especially on mid and long-end of the curve (yield of 10Y benchmark fell by 10bps to 5%). FRA and IRS rates also declined, with FRA9x12 decrease to 4.49%, i.e. ca 65bps below WIBOR3M. Interest rate and debt markets were supported by dovish rhetoric of Marek Belka, the NBP's governor. Today, the key event will be CPI data release. We think that the June CPI could surprise the market players on the negative side, giving some impulse for profit taking.

Deputy minister of finance Dominik Radziwiłł said that the MF might conclude financing of 2012 borrowing needs in Q3 and start pre-financing of 2013 borrowing needs in Q4, but its scale will likely be lower than in the previous year. At the same time deputy finance minister Hanna Majszczyk announced that budget deficit reached the level of PLN21.2bn at the end of June (or 60.5% of annual plan). Majszczyk added that budget revenues from VAT in 2012 might be lower than assumed in the full year plan, but reaching 2012 budget revenue plan is unthreatened due to NBP profit.

According to Bloomberg, Marek Belka said that the MPC may cut interest rates to stimulate the economy if needed. Also, he added he does not expect a sudden spike in inflation, while economic growth may slow down to 2%. Such comments seem to suggest that NBP President starts regretting the interest rate hike decision made in May. In turn, Andrzej Bratkowski reinforced his dovish stance, saying that a rate cut would be justified in September and it should be deep (50bp). Interestingly, the NBP President's opinion has softened quite quickly, even though since the last MPC meeting there were no important data releases that could change outlook for inflation or GDP. However, it is worth recalling that one week before MPC meeting in May Bloomberg cited another Belka's comment that was perceived as very dovish, and at the meeting he backed motion to raise interest rates.

According to NBP's report on business climate in Q2 2012, the condition of Polish companies is still good, but expectations for next quarters are deteriorating, which is reflected in falling investment activity and trimming plans of increasing employment and wages.

Institute of Agricultural and Food Economics estimates that prices of food an non-alcoholic beverages increased in June by 0.5%MoM, which is roughly in line with our prediction, assuming a rise in CPI inflation to 4.4%YoY.

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F/X rates (today's opening)

EURUSD	1.2204	CADPLN	3.3798
USDPLN	3.4405	DKKPLN	0.5645
EURPLN	4.1990	NOKPLN	0.5638
CHFPLN	3.4966	SEKPLN	0.4900
JPYPLN*	4.3407	CZKPLN	0.1655
GBPPLN	5.3126	HUFPLN*	1.4510

*for 100JPY/100HUF

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The zloty trading ranges

	min	max	open	close	fixing
EURPLN	4.1791	4.2136	4.1879	4.2145	4.2008
USDPLN	3.4130	3.4600	3.4229	3.4592	3.4383
EURUSD	1.2165	1.2238	1.2235	1.2184	-

T-bonds

Bond (term)	Yield (%)	Change (bp)	Last auction	Average yield
OK0114 (2Y)	4.59	-2	14.03	4.535
PS0417 (5Y)	4.65	-7	20.06	4.784
DS1021(10Y)	5.00	-10	10.05	5.349

IRS rates (Mid)

TERM	PL		US		EA	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1L	4.93	-7	0.44	-3	0.72	-3
2L	4.67	-7	0.47	-3	0.71	-4
3L	4.55	-8	0.57	1	0.79	-3
4L	4.52	-8	0.68	0	0.92	-3
5L	4.51	-9	0.87	1	1.09	-3
8L	4.57	-9	1.35	-2	1.55	-3
10L	4.55	-10	1.60	-2	1.77	-2

WIBOR rates

TERM	%	Daily change (bp)
O/N	4.84	-1
T/N	4.85	-1
SW	4.84	1
2W	4.85	0
1M	4.91	-1
3M	5.13	-1
6M	5.16	-1
9M	5.16	-1
1Y	5.16	-1

FRA rates (Mid)

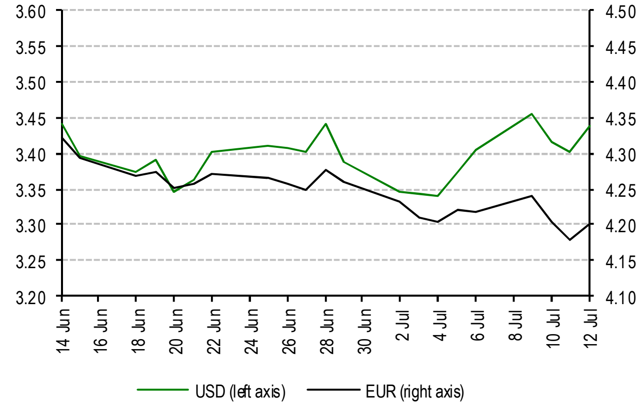
TERM	%	Daily change (bp)
1x2	4.94	1
1x4	5.12	-1
3x6	5.06	-1
6x9	4.77	-5
9x12	4.49	-17
3x9	5.01	-6
6X12	4.75	-9

Measures of fiscal risk

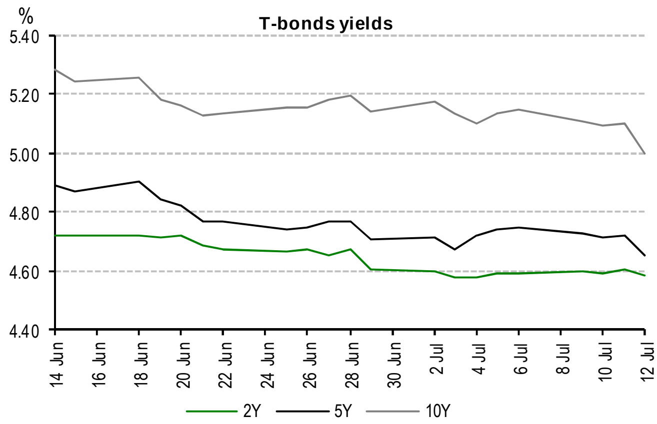
Country	CDS 5Y		Spread 10Y*	
	Value	Change (bp)	Value	Change (bp)
Poland	193.2	-5	3.73	-8
Czech Republic	132.4	2	127	-8
Hungary	501.2	2	6.72	-3
Greece	37030.5	0	23.62	-84
Spain	558.7	1	5.36	6
Italy	493.5	5	4.60	6
Portugal	845.9	0	9.41	1
Ireland	538.8	-4	5.07	3
Germany	88.4	-1	--	--

* 10Y treasury bonds over 10Y Bunds

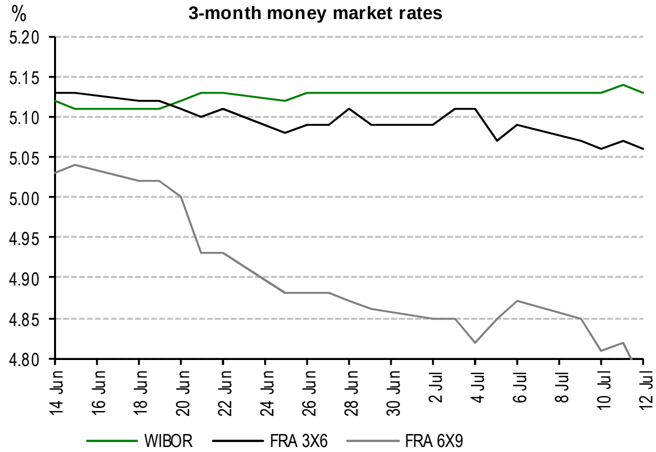
Zloty exchange rate (fixing)



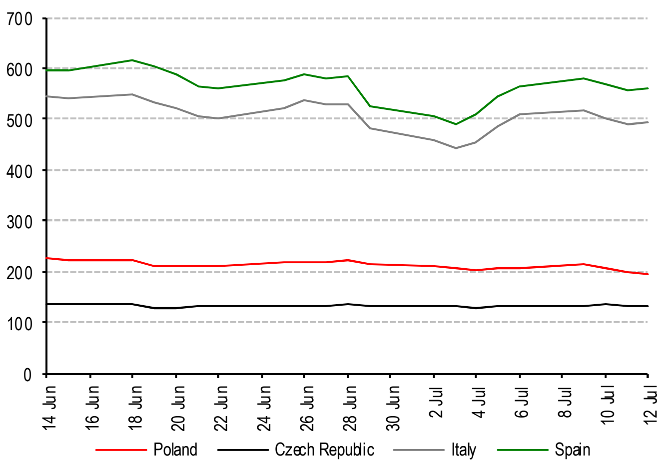
T-bonds yields



3-month money market rates



CDS 5Y



Source: Reuters

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	ACTUAL VALUE	LAST VALUE*
		FRIDAY (6 July)						
12:00	DE	Industrial output	May	%MoM	0.5	-	1.6	-2.2
14:30	US	Non-farm payrolls	Jun	k	89	-	80	77
14:30	US	Unemployment rate	Jun	%	8.2	-	8.2	8.2
		MONDAY (9 July)						
3:30	CN	CPI	Jun	%YoY	2.3	-	2.2	3.0
8:00	DE	Exports	May	%MoM	0.3	-	3.9	-1.7
10:30	EZ	Sentix index	Jul	pts	-26.6	-	-29.6	-28.9
		TUESDAY (10 July)						
		No important data releases						
		WEDNESDAY (11 July)						
14:30	US	Trade balance	May	$bn	-48.7	-	-48.7	-50.1
20:00	US	Fed minutes						
		THURSDAY (12 July)						
11:00	EZ	Industrial output	May	%MoM	-0.1	-	0.6	-0.8
14:30	US	Import prices	Jun	%MoM	-1.5	-	-2.7	-1.0
14:30	US	Initial jobless claims	Week	K	372	-	350	374
		FRIDAY (13 July)						
3:30	CN	GDP	Q2	%YoY	7.6	-	7.6	8.1
14:00	**PL**	**CPI**	**Jun**	**%YoY**	**4.1**	**4.4**		**3.6**
14:00	**PL**	**Money supply**	**Jun**	**%YoY**	**11.5**	**11.6**		**11.4**
14:00	**PL**	**Exports**	**May**	**€m**	**12 076**	**12 196**		**11 582**
14:00	**PL**	**Imports**	**May**	**€m**	**12 605**	**12 811**		**12 001**
14:00	**PL**	**Balance of payments**	**May**	**€m**	**-258**	**-246**		**-573**
15:55	US	Flash Michigan index	Jun	pts	-	-		73.2

Source: BZ WBK, Reuters, Parkiet;

** in case of the revision, the data is updated*

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