

EYEOPENER

6 November 2014

Rates on hold, although inflation below the target for long

- **Good market mood thanks to US data**
- **Unexpected MPC decision to keep rates on hold triggered temporary zloty strengthening and sharp weakening of bonds**
- **EURUSD slightly lower**
- **Today, ECB and CNB decisions, auction of Polish bonds**

Global market moods were very positive since the start of Wednesday's session. Stock indices were supported by results of election in the US, as investors welcomed the fact that GOP took control over the Senate and increased its majority in the House of Representatives. Additionally, new optimistic data from the US were released in the afternoon. The ADP report, which is seen by investors as a hint before Friday's official data, showed a stronger-than-expected rise in non-farm payrolls in October. Data on German industrial orders, released in the morning, were weaker than expected, signalling that economic growth in the biggest European economy remains weak.

Poland's Monetary Policy Council decided to keep the level of interest rates unchanged. This decision came as a big surprise. We expected a 25-bp cut, which also represented the consensus among market economists. It has to be stressed that the bias was towards an even more significant monetary easing and financial market was pricing-in more than a 25-bp reduction. Therefore, in immediate market reaction to the announcement, we saw bonds sell off. Unfortunately, during the press conference there was no clear indication on future moves or even clear justification of the yesterday's decision. We still see room for one more cut by 25bp (perhaps in December), which is supported by the NBP's new projections (*Inflation Report* will be released on 12 November) and will be confirmed by the next data releases. In any event, the market will probably price in additional monetary easing in the coming months (if not December, then in 1Q15). Therefore, the correction observed after the decision (and possibly in the next few days) may prove temporary, especially if our forecast for a low CPI reading materializes (we expect -0.5%YoY in October). Still, it should be recalled that the day after the CPI publication there will be a flash GDP for Q3, which may be just as important (the MPC suggested that GDP is even more important). Nevertheless, if the market starts to price in very aggressive easing – exceeding additional 50bp – as has been the case in the last few weeks, we would still find this excessive.

EURUSD stayed in the downward trend since the beginning of the day as the dollar was supported by hopes for solid growth of the US economy (additionally fuelled by the result of the US elections).

As 1.246 was reached, the downward impulse halted and some rebound occurred. Today in the morning the exchange rate is close to 1.25 and the outcome of the ECB meeting is likely to be the main event of the day. Investors hope the central bank will sound even more dovish than last month given the recent poor euro zone macro data (including today's morning German release). However, we see the risk that investors will be disappointed and this could support the euro.

Both EUR/PLN and USD/PLN were quite volatile yesterday and the main driver of these moves was the unexpected MPC decision. The zloty gained noticeably as it was announced that rates are left unchanged – EUR/PLN plunged to 4.22 and USD/PLN to 3.375. However, yet before the press conference some rebound was recorded and leaving the door open to more cuts by the MPC prevented the zloty from further appreciation. All in all, EUR/PLN and USD/PLN ended the day close to the opening levels. No big changes occurred over the night and today in the morning EUR/PLN is close to 4.23. Despite the yesterday's more noticeable fluctuations, the situation in has not changed much as the exchange rate is still at an elevated level reached after the sudden increase started in mid-October. The outcome of the today's ECB meeting may decide whether the exchange rate breaks 4.24 or starts to ascend towards 4.18.

The surprising decision of the Polish Monetary Policy Council to leave the NBP interest rates unchanged initiated a sharp weakening of the Polish debt on Wednesday. Yields of the 2Y and 5Y benchmarks surged by c10bps and the yield of the 10Y benchmark rose by over c5bps. The IRS curve moved up at a similar scale. Monthly WIBOR dropped yesterday by 2bp while the 3M and 9M rates by 1bp. The market is clearly disappointed after the MPC decision, as bonds rallied quite significantly before the Central Bank meeting on the back of expectations for monetary policy easing. This factor, and the risk that the ECB may miss investors' expectations for a more dovish tone of the statement than a month ago, could result in further weakening of the Polish bonds today. Moreover, auction of the long term debt may weigh on the 10Y sector. However, it is worth noting that the MPC left the door open for rate cuts and next week's inflation data may revive investors' hopes for more easing to come in the near future. Our CPI forecast (at -0.5% YoY) is below market consensus.

The bond auction results will be closely followed today. The Ministry of Finance intends to issue WZ0124, DS0725 and WS0428 of total value PLN2-4bnn. This will be the last regular auction this year and low supply should support the demand. The yesterday's weakening makes the long term bond more attractive. The auctions results may influence investors' moods before the ECB decision and tomorrow's US nonfarm payrolls data.

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FX market

Today's opening

| | | | |
|---------|--------|---------|--------|
| EURUSD | 1.2514 | CADPLN | 2.9678 |
| USDPLN | 3.3798 | DKKPLN | 0.5684 |
| EURPLN | 4.2295 | NOKPLN | 0.4956 |
| CHFPLN | 3.5133 | SEKPLN | 0.4589 |
| JPYPLN* | 2.9524 | CZKPLN | 0.1522 |
| GBPPLN | 5.4054 | HUFPLN* | 13618 |

*for 100JPY/100HUF

Last session

05.11.2014

| | min | max | open | close | fixing |
|--------|--------|--------|--------|--------|--------|
| EURPLN | 4.2185 | 4.2379 | 4.2271 | 4.2270 | 4.2310 |
| USDPLN | 3.3656 | 3.3998 | 3.3735 | 3.3856 | 3.3887 |
| EURUSD | 1.2456 | 1.2543 | 1.2534 | 1.2489 | - |

Interest rate market 05.11.2014

T-bonds (on the interbank market)**

| Bond (term) | Yield (%) | Change (bp) | Last auction | Average yield |
|--------------|-----------|-------------|--------------|---------------|
| PS1016 (2Y) | 1.76 | 9 | 23.10.2014 | 1.653 |
| DS1019 (5Y) | 2.06 | 8 | 23.10.2014 | 2.007 |
| DS1023 (10Y) | 2.60 | 7 | 03.04.2014 | 4.261 |

IRS rates (on the interbank market)**

| TERM | PL | | US | | EA | |
|------|------|-------------|------|-------------|------|-------------|
| | % | Change (bp) | % | Change (bp) | % | Change (bp) |
| 1L | 1.75 | 10 | 0.34 | 1 | 0.19 | 0 |
| 2L | 1.78 | 10 | 0.73 | 2 | 0.22 | 0 |
| 3L | 1.82 | 9 | 1.14 | 1 | 0.27 | 0 |
| 4L | 1.89 | 8 | 1.49 | 0 | 0.33 | 0 |
| 5L | 1.97 | 8 | 1.76 | 0 | 0.42 | 0 |
| 8L | 2.24 | 8 | 2.25 | 0 | 0.79 | 0 |
| 10L | 2.39 | 6 | 2.46 | 0 | 1.04 | 0 |

WIBOR rates

| TERM | % | Daily change (bp) |
|------|-----|-------------------|
| O/N | 194 | -7 |
| T/N | 194 | -8 |
| SW | 195 | -3 |
| 2W | 195 | -3 |
| 1M | 195 | -2 |
| 3M | 194 | -1 |
| 6M | 194 | 0 |
| 9M | 193 | -1 |
| 1Y | 193 | 0 |

FRA rates (on the interbank market)**

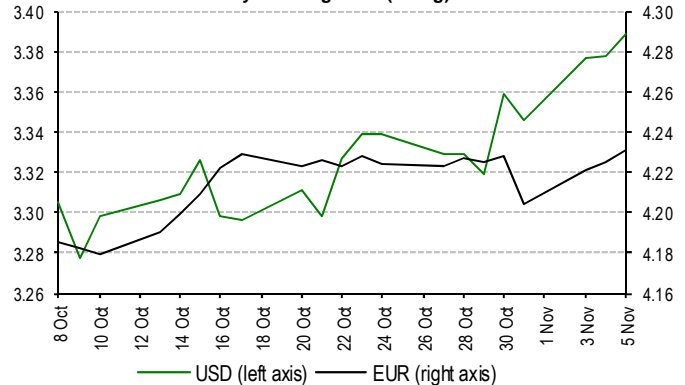
| TERM | % | Daily change (bp) |
|------|-----|-------------------|
| 1x2 | 182 | 19 |
| 1x4 | 179 | 16 |
| 3x6 | 168 | 14 |
| 6x9 | 164 | 14 |
| 9x12 | 166 | 15 |
| 3x9 | 173 | 20 |
| 6x12 | 167 | 17 |

Measures of fiscal risk

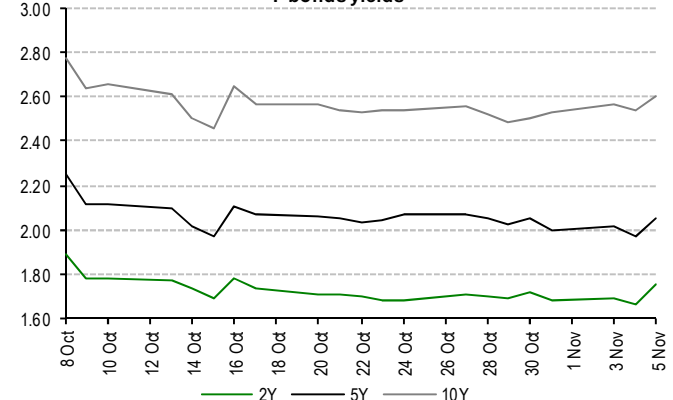
| Country | CDS 5Y | | Spread 10Y* | |
|----------------|---------|-------------|-------------|-------------|
| | Value | Change (bp) | Value | Change (bp) |
| Poland | 66.7 | 0 | 179 | 8 |
| Czech Republic | 46.9 | 0 | 0.08 | 3 |
| Hungary | 179.2 | 0 | 3.12 | -3 |
| Greece | 37030.5 | 0 | 7.19 | 7 |
| Spain | 93.1 | 0 | 137 | 4 |
| Italy | 117.7 | 0 | 161 | 5 |
| Portugal | 192.4 | 0 | 2.49 | 2 |
| Ireland | 56.9 | -1 | 0.95 | 2 |
| Germany | 18.1 | 0 | -- | -- |

* 10Y treasury bonds over 10Y Bunds

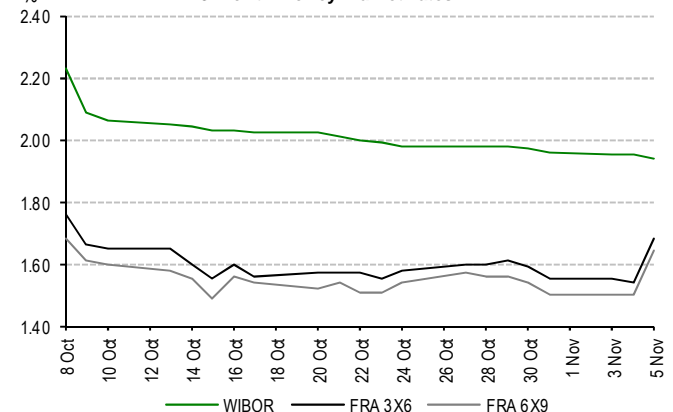
Zloty exchange rate (fixing)



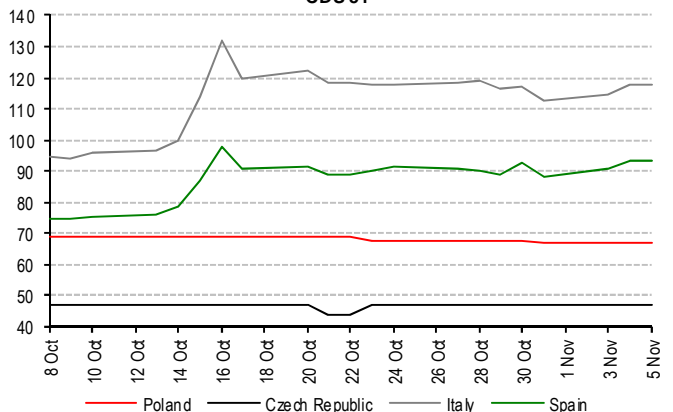
T-bonds yields



3-month money market rates



CDS 5Y



**Information shows mid levels on the interbank market at the end of the trading day

Source: Reuters

Economic calendar

| CET TIME | COUNTRY | INDICATOR | PERIOD | | FORECAST | | ACTUAL VALUE | LAST VALUE* |
|------------------------|---------|------------------------|--------|------|----------|-------|-----------------|----------------|
| | | | | | MARKET | BZWBK | | |
| FRIDAY (31 October) | | | | | | | | |
| 11:00 | EZ | Flash HICP | Oct | %YoY | 0.4 | - | 0.4 | 0.3 |
| 13:30 | US | Personal income | Sep | %MoM | 0.3 | - | 0.2 | 0.3 |
| 13:30 | US | Consumer spending | Sep | %MoM | 0.1 | - | -0.2 | 0.5 |
| 14:00 | PL | Inflation expectations | Oct | %YoY | - | - | 0.2 | 0.2 |
| 14:55 | US | Michigan index | Oct | pts | 86.4 | - | 86.9 | 84.6 |
| MONDAY (3 November) | | | | | | | | |
| 2:45 | CN | PMI – manufacturing | Oct | pts | 50.4 | - | 50.4 | 50.2 |
| 9:00 | PL | PMI – manufacturing | Oct | pts | 50.0 | 49.7 | 51.2 | 49.5 |
| 9:55 | DE | PMI – manufacturing | Oct | pts | 51.8 | - | 51.4 | 49.9 |
| 10:00 | EZ | PMI – manufacturing | Oct | pts | 50.7 | - | 50.6 | 50.3 |
| 16:00 | US | ISM – manufacturing | Oct | pts | 56.5 | - | 59.0 | 56.6 |
| TUESDAY (4 November) | | | | | | | | |
| 16:00 | US | Industrial orders | Sep | %MoM | -0.6 | - | -0.6 | -10.0 |
| WEDNESDAY (5 November) | | | | | | | | |
| | PL | MPC decision | | % | 1.75 | 1.75 | 2.0 | 2.0 |
| 9:55 | DE | PMI – services | Oct | pts | 54.8 | - | 54.4 | 55.7 |
| 10:00 | EZ | PMI – services | Oct | pts | 52.4 | - | 52.3 | 52.4 |
| 14:15 | US | ADP report | Oct | k | 220 | - | 230 | 225 |
| 16:00 | US | ISM – services | Oct | pts | 58.0 | - | 57.1 | 58.6 |
| THURSDAY (6 November) | | | | | | | | |
| 8:00 | DE | Industrial orders | Sep | %MoM | 2.2 | - | 0.8 | -4.2 |
| 9:00 | CZ | Industrial output | Sep | %YoY | 4.4 | - | 8.3 | -5.2 |
| 11:00 | PL | Bond auction | | | | | | |
| 13:00 | CZ | Central bank decision | | % | 0.05 | - | | 0.05 |
| 13:45 | EZ | ECB decision | | % | 0.05 | - | | 0.05 |
| 14:30 | US | Initial jobless claims | week | k | 285 | - | | 287 |
| FRIDAY (7 November) | | | | | | | | |
| 8:00 | DE | Exports | Sep | %MoM | 2.3 | - | | -5.8 |
| 8:00 | DE | Industrial output | Sep | %MoM | 1.8 | - | | -4.0 |
| 14:30 | US | Non-farm payrolls | Oct | k | 230 | - | | 248 |
| 14:30 | US | Unemployment rate | Oct | % | 5.9 | - | | 5.9 |

Source: BZ WBK, Reuters, Bloomberg

* in case of the revision, the data is updated

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