

Rates and FX Outlook

Polish Financial Market

June 2013

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Summary

- ▶ **It is widely expected that the MPC will cut interest rates again by 25bps in June. This is also our scenario and we see another rate cut of the same scale in July, while the market is pricing-in a more significant monetary easing.** It is worth noting, however, that FRA market adjusted upwards during May, which was in line with broader correction in different asset classes (sell-off in Polish bonds, weakening of the zloty). We maintain our scenario of gradual economic recovery during 2013, though it would be hard to achieve the GDP growth much above 1% in 2013 as a whole given the low reading for 1Q. As CPI inflation is likely to reach the bottom in June (nearing zero) and the second half of the year should bring an increase in both core and headline CPI measures, we do not think the Monetary Policy Council should continue the easing cycle after the holiday period in August.
- ▶ In the short-term we see some market strengthening at the front of the curve (FRA and short-dated bonds), as our forecasts for the upcoming macroeconomic releases are below market consensus in terms of the most closely watched indicators: CPI inflation and industrial production. This would probably give some fuel for the market to expect more monetary easing, especially if the MPC does not shut the door for such a possibility after the June's meeting.
- ▶ **As regards the long-end of the curve**, after recent significant correction, we see some room for Polish bonds to unwind at least a part of sell-off, though it will be dependent mostly on global factors (US data, Fed's approach to QE). Bond market will be still more responsive to macro data (especially from the US) and central banks' action. The debate around when and how the Fed should start to 'taper off' its bond purchases is gaining momentum. We see the recent macro improvement as being rather fragile (for example, latest ISM reading) justifying the Fed's cautious approach. We maintain our view of higher yields of Polish Treasury papers in the second half of the year.
- ▶ **After the EURPLN touched nearly 4.30 in late May a visible correction was initiated at the beginning of June.** We expect average EURPLN at 4.23 this month. The zloty will be supported by a decline of yields of Polish bonds.
- ▶ **Many commentators in Poland see a possibility of budget amendment amid lower-than-planned tax revenues. This would lead to higher supply of bonds on the market. However, in our opinion, the issue is a bit more complicated.** As the Polish debt/GDP ratio (as calculated based on domestic methodology) exceeded 50% level in 2011, the relation of budget deficit to revenues in 2013 cannot exceed the level planned for 2012, so the room for increase of deficit is limited (especially due to lower revenues). So the overall public finance deficit will be probably higher, but not the central budget – details on page 10.

Short- and Medium-term Strategy: Interest rate market

| | Change (bps) | | Level | Expected trend | |
|-------------------|--------------|---------|---------|----------------|----|
| | Last 3M | Last 1M | end-May | 1M | 3M |
| Reference rate | -0.75 | -0.25 | 3.00 | ↘↘ | ↘↘ |
| WIBOR 3M | -99 | -34 | 2.74 | ↘↘ | ↘↘ |
| 2Y bond yield | -75 | 11 | 2.70 | ↘ | ↘ |
| 5Y bond yield | -50 | 34 | 3.11 | ↘ | → |
| 10Y bond yield | -40 | 32 | 3.57 | ↘ | → |
| 2/10Y curve slope | 35 | 21 | 87 | ↗ | ↗ |

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: Another rate cut by the MPC in June should lead to fall in money market rates, though we still perceive current pricing by the FRA market exaggerated (refi rate at 2.25% against our view of one 25bps cut less). Another considerable fall in inflation and no signs of significant recovery would probably keep market in this dovish mood for a few months before the correction.

Short end: Front ends of curves (both bonds and IRS) saw some correction at the end of May, but we still see relatively weak macro data releases for May (our CPI and core inflation as well as production forecasts below market consensus), which may lead to moderate strengthening.

Long end: After recent significant correction, we see some room for Polish bonds to unwind at least a part of sell-off, though it will be dependent mostly on global factors (US data, Fed's approach to QE). We maintain view of higher yields in 6M horizon.

Risk factors to our view: The main risk for short-end of the curve is the scenario of a no rate cut by the MPC in June, which would lead to earlier-than-expected correction on the money market and front-end of bond curve. As regards the long-end, the key is global mood in terms of expectations regarding QE.

Short- and Medium-term Strategy: FX market

| | Change (%) | | Level | Expected trend | |
|--------|------------|---------|---------|----------------|----|
| | Last 3M | Last 1M | end-May | 1M | 3M |
| EURPLN | 3.2 | 3.6 | 4.29 | ↘ | ↘ |
| USDPLN | 4.0 | 3.9 | 3.30 | ↘ | ↘ |
| CHFPLN | 1.1 | 2.2 | 3.46 | ↘ | ↘ |
| GBPPLN | 4.3 | 2.1 | 5.02 | ↘ | ↘ |
| EURUSD | -0.8 | -0.3 | 1.30 | → | ↗ |

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: After a sudden surge recorded in late May the exchange rate approached nearly 4.30. We expect the recovery started at the beginning of June to be continued later in the month. The zloty should benefit from some decline of yields of Polish bonds, driven by, among others, rhetoric of the MPC.

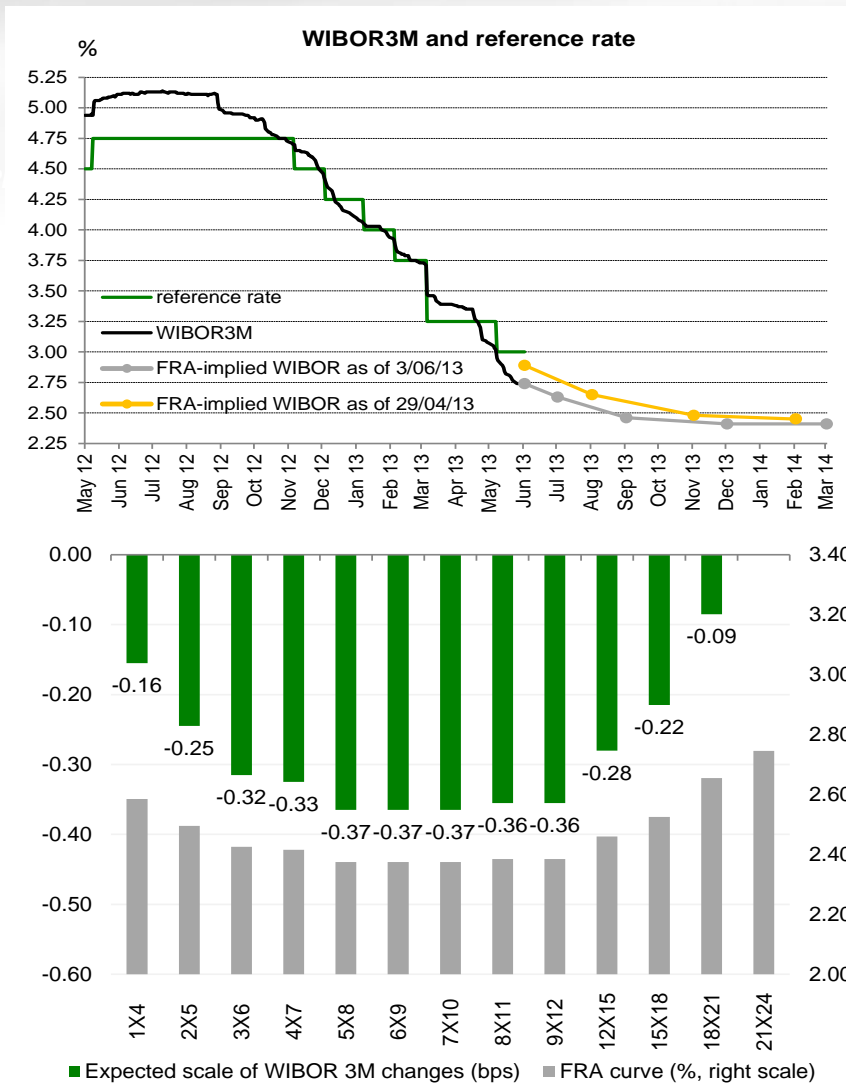
USD: Uncertainty what the Fed will do with the QE3 should limit the upside potential for the EURUSD. Furthermore, market expects more actions from the ECB and this could also weigh on the euro. We expect average EURUSD at 1.30 in June. The decline of the EURUSD from current level will offset possible further decline of the EURPLN and thus the USDPLN should be close to 3.26 on average this month.

CHF: The recovery of the zloty vs. the euro should support the domestic currency vs. the Swiss franc. We expect the exchange rate to retreat further from local peak at nearly 3.47 and reach ca. 3.40 on average in June.

Risk factors to our view: US nonfarm payrolls and decision of the ECB may trigger (even) higher volatility on the market in coming days. Combination of better-than-expected data from the US and any market disappointment regarding the ECB's willingness to take more actions may again hit the zloty.

Domestic Money Market: FRA corrected, but still too aggressive

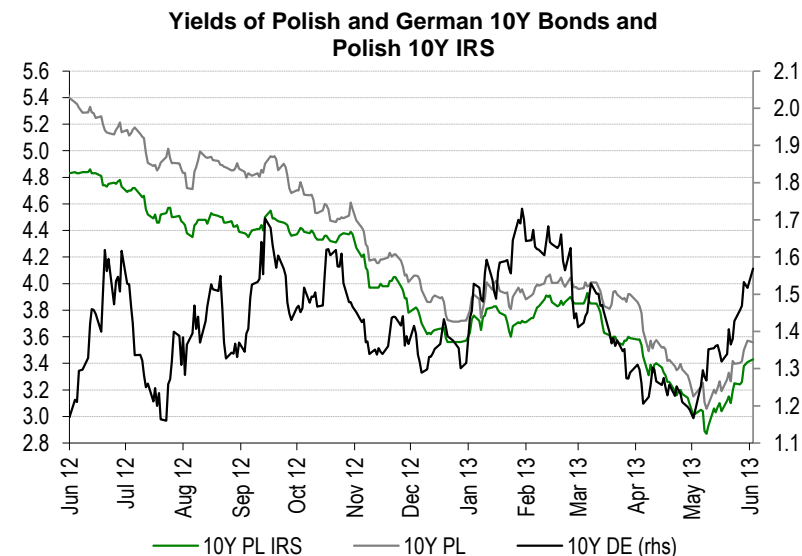
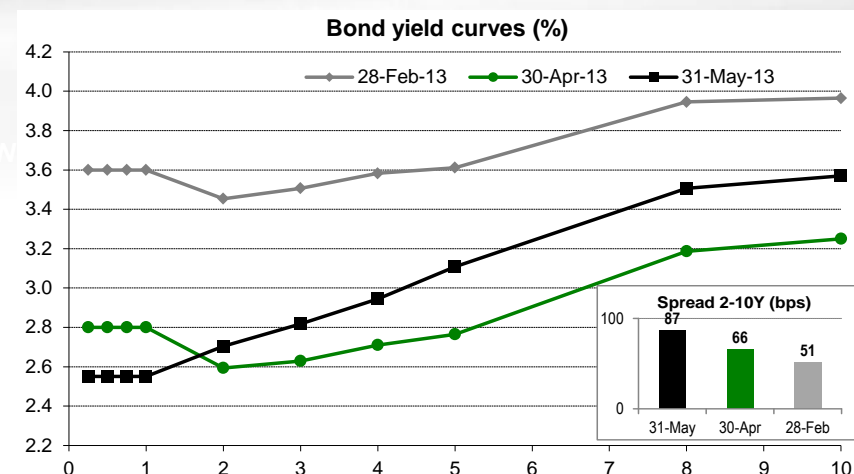
- ▶ The MPC's decision to cut rates by 25bps in May together with relatively weak macro data caused sharp decline in WIBOR across the board. In monthly terms rates fell between 24bps (for 1M) and 37bps (for 6M, 9M and 12M). One should notice that WIBOR between 3M and 12M ended the month well below the reference rate (by 26-35bps).
- ▶ Two days after the Council's decision in May we noted some profit taking on FRA market. The sell-off intensified in the last week of May (FRA 6x9 and 9x12 increased by over 10bps). However, at the end of month rates were still below the level at the end of April.
- ▶ Currently, both OIS and FRA markets are pricing-in rate cuts by ca. 75bps in 9 months horizon with the first cut expected in June.
- ▶ Definitely, 'no rate cut' in June would be a surprise and it might negatively affect the market. But it is not our scenario, we see two reductions by 25bps in both June and July. While we still see FRA rates as too low, rate cut in June together with relatively weak macro data for May might bring some short-term strengthening.



Sources: Thomson Reuters, BZ WBK

Domestic IRS and T-Bond Market: Yields higher, curve steeper

- Strengthening on the T-bonds and IRS markets after the May's MPC decision did not last long. Two days after the decision the correction has started, with significant steepening, especially in 2-10Y sectors. While we did expect the steepening, the increase of yields and IRS rates on mid- and long-end of curves came earlier as compared to our forecasts, triggered by speculation on the Fed's exit from QE3.
- We think that the market will be more and more vulnerable to upcoming data releases. As long as CPI is falling (and moving closer to zero in June – our forecast is 0.3%YoY) and there will be no strong signs of economic recovery, more monetary easing might be priced-in. Therefore the front end of curves should be well supported.
- In case of 10Y it has been the first serious correction after ca. 180 bps rally (in one year period). We agree with steepening trend and we see even higher yields in 2H13. Nevertheless, in the short-term, yields of 10Y bonds look quite attractive, though dependent on global trend – spread 10Y over Bunds around 200bps.

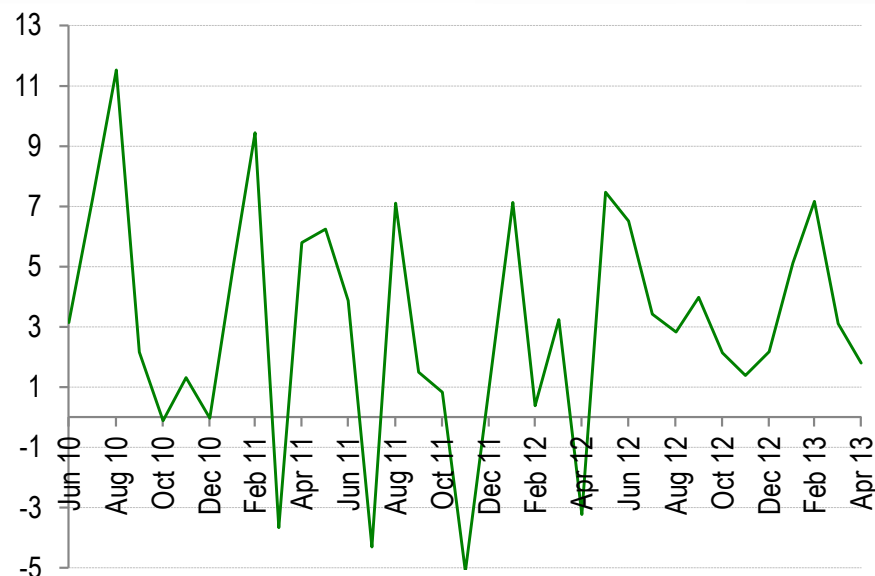


Sources: Reuters, MF, BZ WBK

Demand Corner: Pace of foreigners' buying faded in April

- ▶ Foreign investors increased their holdings of Polish marketable debt for the 12th month in a row to fresh record high at PLN207.1bn in April. Still, it is worth to notice that monthly nominal pace of buying was the lowest since November 2012 (PLN1.79bn vs. +PLN3.46bn on average in the last six months).
- ▶ Foreign investors hold 29% of total issuance of OK0715 (vs. 20% in March) after buying PLN1.6bn of this bond. They doubled their holdings of PS0418 (from 9% to 18% of total issuance), but trimmed engagement in other PS bonds (net sellers in general in the middle of the curve).
- ▶ Polish banks sold bonds worth ca. PLN4.6bn (nearly as much as they purchased in March) and terminated the series of three months buying in a row.
- ▶ On the other hand, Polish pension funds bought debt for the first time since July 2012 and the amount was the highest in the last 12 months (PLN2.1bn).

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

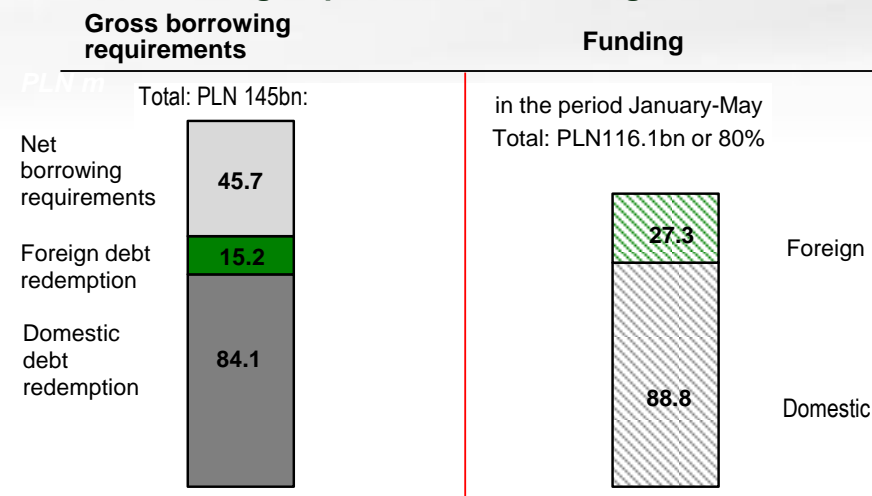


Sources: MF, BZ WBK

Supply Corner: Good funding progress so far

- In May the Ministry of Finance sold T-bonds worth PLN12bn in total vs. PLN16.8bn in April. In April-May period the Ministry has completed 82% of Q2 issuance plan.
- Issuance plan for June assumes one regular auction (June 6th), at which 5Y benchmark PS0718 and floating-rate T-bonds WZ0119 worth PLN2-6bn will be offered. The offer on the switch tender (June 19) will depend on market conditions. The Ministry plans to buy back OK0713 and DS1013.
- Poland has already financed over 80% of its total 2013 gross borrowing needs at the end of May. Consequently, the Ministry of Finance plans to limit its Treasury Securities supply in summer, probably to just one auction per month. According to MinFin, net debt issuance until year-end will be negative (lower new supply than redemptions plus interest payments). In the case of significant deterioration in market conditions, the Ministry might return to offering only T-bills, refraining from offering T-bonds for some time.

Gross borrowing requirements' financing in 2013



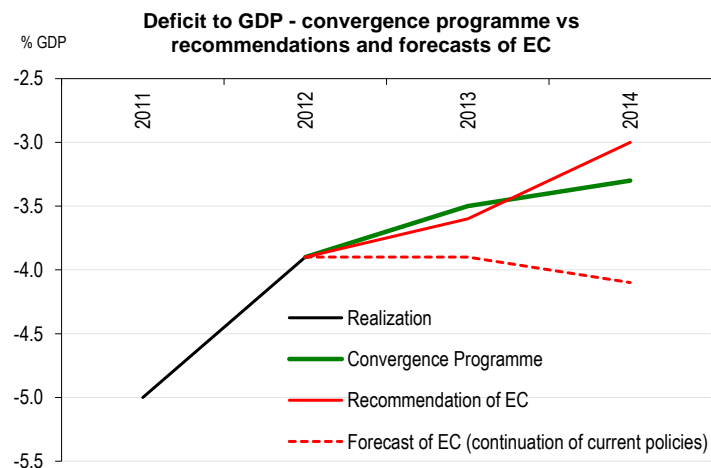
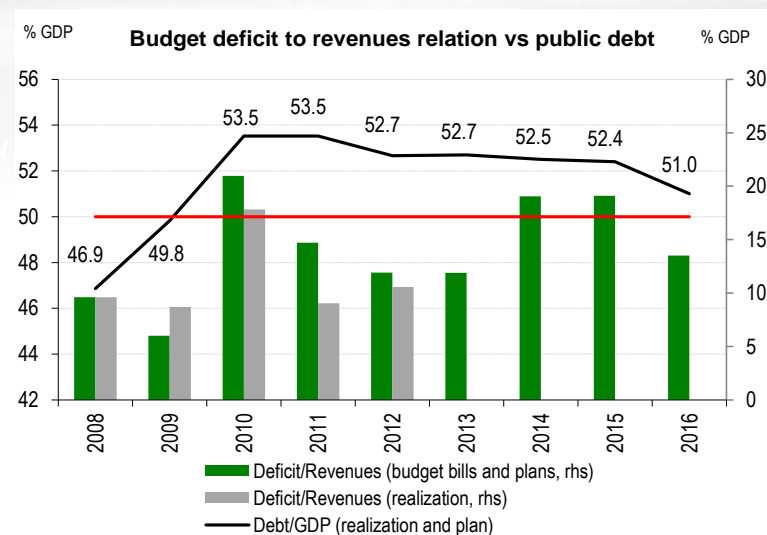
Auction schedule for June

| Auction date | Settlement date | T-bonds to be offered | Planned offer (PLN bn) |
|--------------|-----------------|-----------------------|------------------------|
| 6 Jun 2013 | 13 May 2013 | PS0718 /WZ0119 | 2.0 – 6.0 |

Sources: MF, BZ WBK

Supply Corner: Higher deficit, but not necessarily bond supply

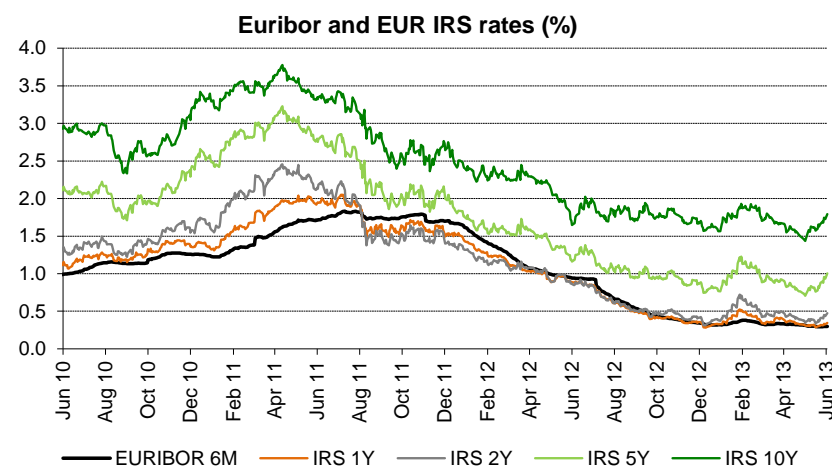
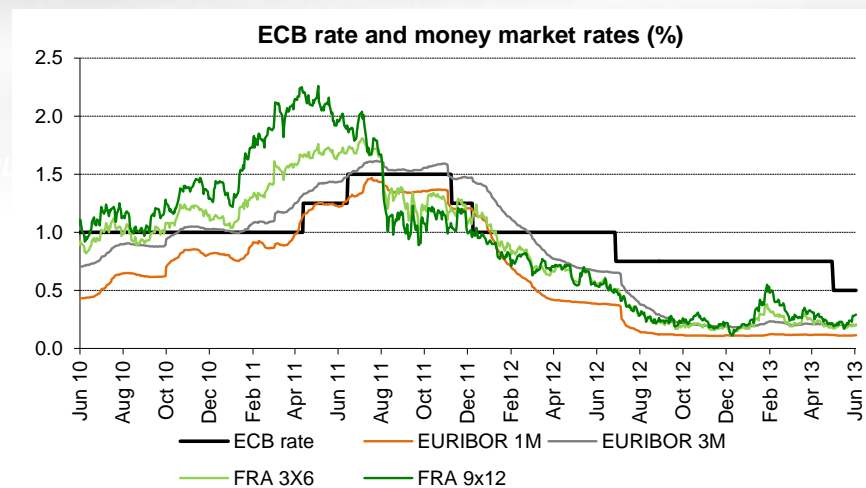
- As the Polish debt/GDP ratio (as calculated based on domestic methodology) exceeded 50% level in 2011, the relation of budget deficit to revenues in 2013 cannot exceed the level planned for 2012. For 2013 the government planned it exactly at this level, so the budget amendment (suggested by many commentators) is not obvious at all
- This means that the government might be forced to cut expenses (being pro-cyclical) or to increase the overall deficit in public finance sector with the central budget unchanged (for example by decreasing subsidy to social Security Fund, which would borrow on the market).
- Overall, the risk of higher public deficit is quite high (and also risk of debt/GDP above 55%), but this would not necessarily mean higher debt supply on the T-bond market).
- Moreover, preliminary plan of deficit-to-revenue ratio for 2014 is significantly higher than for 2013, and it surely will be revised downwards, especially as the European Commission called on the government to implement more austerity.



Sources: Government, European Commission

International Money Market and IRS: Gradual increase in IRS

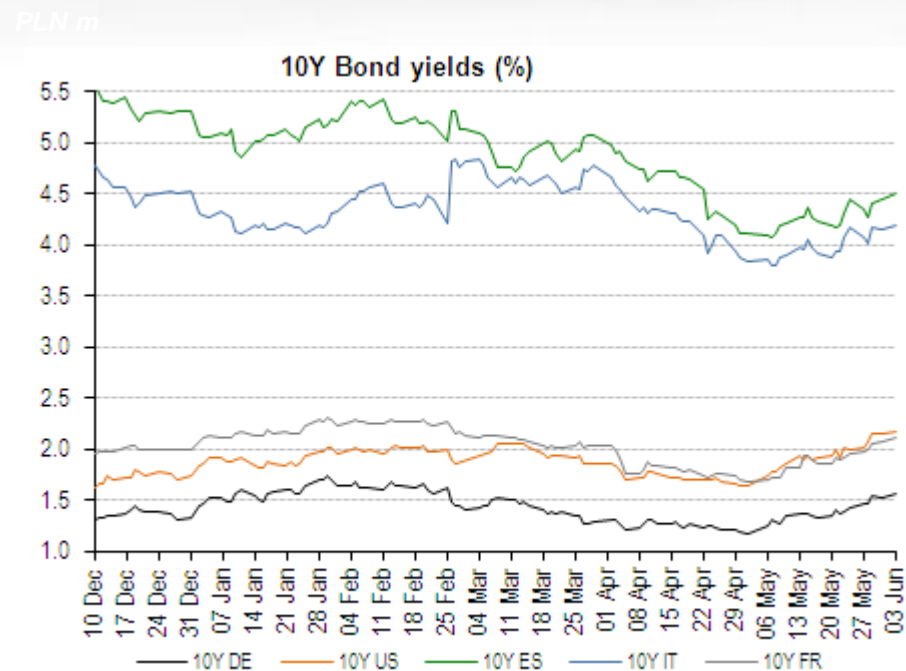
- ▶ EURIBOR rates have remained at low levels due to May's rate reduction and dovish tone of the ECB's Governor. A possibility of negative deposit rate was another factor stabilising money market rates at low levels.
- ▶ In May EUR IRS rates have started increasing after reaching minimum levels at the beginning of that month. The changes in swap rates have been highly correlated to increase in German 10Y benchmark. In monthly terms the IRS curve has shifted up by only 6bps at the short end and nearly 30bps in case of 10Y. What is more, despite upward move EUR IRS rates up to 5Y ended May still below 1%.
- ▶ The June's ECB meeting will be interesting as new GDP and CPI projections will be released. In our opinion, there is risk of a downward revision. Apart from the macro projections investors will focus on any news on non-conventional measures.
- ▶ To sum up, we still foresee EURIBOR rates to oscillate near current level in medium term (even up to 3 months). We uphold our scenario of further gradual EUR swap rates increase.



Sources: Thomson Reuters, ECB, BZ WBK

International Bond Market: Significant bonds sell-off

- The risk of limiting QE3 by Fed or even early exit from asset purchase program remains a key factor influencing financial markets globally. Consequently, due to significant sell-off of 10Y UST and 10Y Bunds, their yields temporarily exceeded 2.23% (the highest level since March 2012) and 1.50% (the highest level since end-February), respectively. Also yields of peripheral bonds (both Spanish and Italian) ended May nearly 30bps higher than at the end of April.
- In coming weeks bond market will be still more responsive to macro data (particularly from the US) and central banks' action. The debate around when and how the Fed should start to 'taper off' its bond purchases is gaining momentum. We see the recent macro improvement as being rather fragile (for example, latest ISM reading) justifying the Fed's cautious approach.
- All in all, our baseline scenario has remained unchanged – we expect a moderate, gradual increase in yields of the US Treasuries and German bonds till year-end.

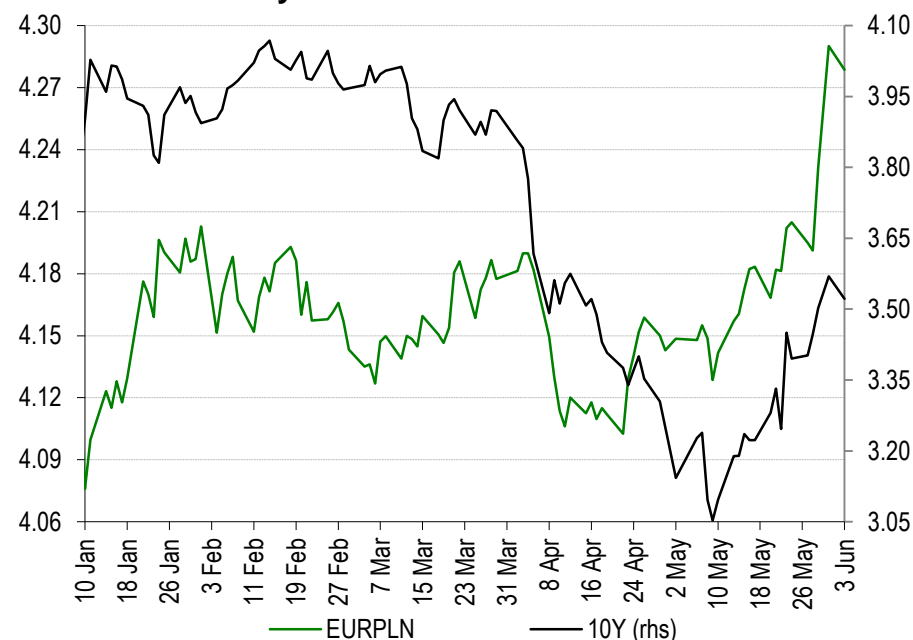


Sources: Thomson Reuters, BZ WBK

Foreign Exchange Market: Sharp (temporary) zloty depreciation

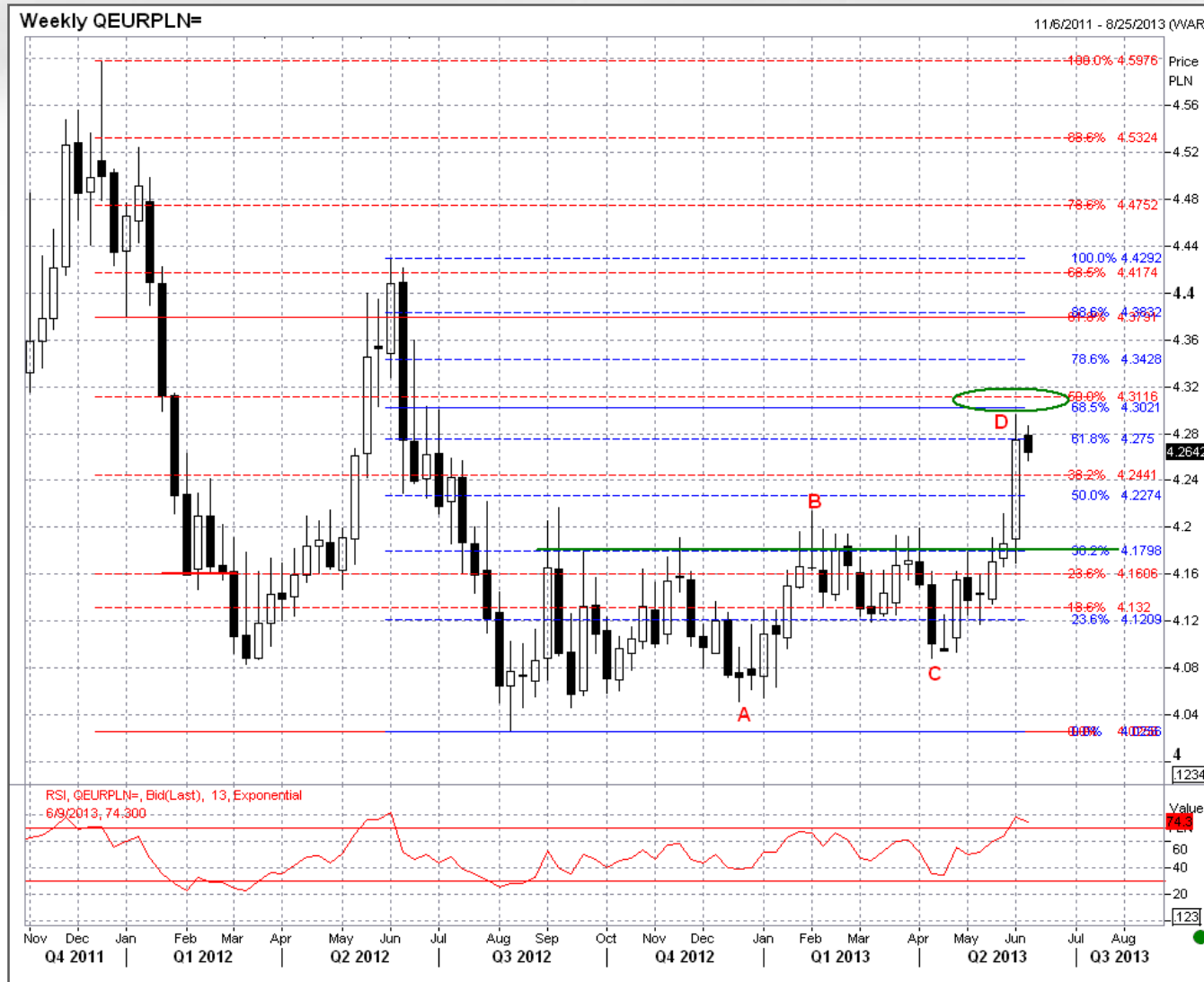
- ▶ During the final days of May the zloty lost quite visibly vs. main currencies. Weekly depreciation versus the euro was the biggest since last week of August 2012. The EURPLN broke the resistance at ca. 4.20 and surged to nearly 4.30.
- ▶ The main driver of sudden zloty depreciation were worries over terminating/limiting the QE3 by the Fed. Additionally, we saw very low liquidity on the FX market in Poland due to market holiday. Rising yields of domestic debt magnified the depreciation of the zloty.
- ▶ We expect the zloty to recover slightly vs. the euro in June (average EURPLN at 4.23). Yields of Polish bonds seem now more attractive and this impression may be further strengthened by next NBP rate cut as soon as in the first week of June.
- ▶ The risk factor to scenario of stronger zloty is connected mainly to US data (NFP), which may influence market perception as regards further Fed action and thus global market sentiment.

EURPLN and yield of 10Y Polish benchmark



Sources: Reuters, BZ WBK

FX Technical Analysis Corner: Room for correction of the EURPLN



- ▶ The EURPLN touched 4.12 in first half of May, level pointed in April.
- ▶ However, in the following weeks the exchange rate broke the resistance at ca. 4.20 and surged to nearly 4.30.
- ▶ EURPLN approached a resistance area consisting of two Fibon retracement levels. Additionally, AB/CD~0.886, one of Fibonacci vital ratios.
- ▶ These circumstances should support a move down of the EURPLN back towards ca. 4.20.

Sources: Reuters, BZ WBK

FX Technical Analysis Corner: Room for lower EURUSD



- ▶ Scenario of lower EURUSD materialized, the exchange rate broke even the support at 200-day MA. The downward momentum was halted at 88.6% of move up recorded from early April to early May.
- ▶ For the current peak at ca. 1.311 AB/CD~0.685 and BC/CD~0.618 which makes a move down quite likely.
- ▶ Additionally, ADX is well below 20, suggesting the strength of recent increase is very low. We see also slight divergence with the RSI (oscillator does not rise further together with the EURUSD).
- ▶ First support is again at 200-day MA.

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 | 1,595.3 | 1,625.9 | 370.1 | 389.1 | 393.8 | 442.2 | 377.8 | 394.2 | 401.4 | 452.5 |
| GDP | %YoY | 3.9 | 4.5 | 1.9 | 1.0 | 3.5 | 2.3 | 1.3 | 0.7 | 0.5 | 0.7 | 1.1 | 1.6 |
| Domestic demand | %YoY | 4.6 | 3.6 | -0.2 | -0.6 | 2.2 | -0.4 | -0.8 | -1.6 | -0.9 | -0.7 | -0.2 | -0.7 |
| Private consumption | %YoY | 3.2 | 2.6 | 0.8 | 0.7 | 1.7 | 1.3 | 0.2 | -0.2 | 0.0 | 0.7 | 0.9 | 1.2 |
| Fixed investments | %YoY | -0.4 | 8.5 | -0.8 | -3.3 | 6.8 | 1.4 | -1.7 | -4.1 | -2.0 | -5.0 | -3.0 | -3.0 |
| Unemployment rate ^a | % | 12.4 | 12.5 | 13.4 | 13.9 | 13.3 | 12.3 | 12.4 | 13.4 | 14.3 | 13.4 | 13.5 | 13.9 |
| Current account balance | EURm | -18,129 | -17,977 | -13,480 | -5,393 | -4,515 | -2,203 | -3,285 | -3,477 | -2,645 | -507 | -1,275 | -965 |
| Current account balance | % GDP | -5.1 | -4.9 | -3.5 | -1.4 | -5.1 | -4.6 | -4.1 | -3.5 | -3.0 | -2.6 | -2.0 | -1.4 |
| General government balance | % GDP | -7.9 | -5.0 | -3.9 | -3.9 | - | - | - | - | - | - | - | - |
| CPI | %YoY | 2.6 | 4.3 | 3.7 | 1.0 | 4.1 | 4.0 | 3.9 | 2.9 | 1.3 | 0.5 | 0.8 | 1.3 |
| CPI ^a | %YoY | 3.1 | 4.6 | 2.4 | 1.4 | 3.9 | 4.3 | 3.8 | 2.4 | 1.0 | 0.3 | 1.0 | 1.4 |
| CPI excluding food and energy prices | %YoY | 1.6 | 2.4 | 2.2 | 1.3 | 2.5 | 2.5 | 2.1 | 1.7 | 1.2 | 1.0 | 1.3 | 1.5 |

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

^a 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 ^a | % | 3.50 | 4.50 | 4.25 | 2.50 | 4.50 | 4.75 | 4.75 | 4.25 | 3.25 | 2.75 | 2.50 | 2.50 |
| WIBOR 3M | % | 3.94 | 4.54 | 4.91 | 2.95 | 4.97 | 5.04 | 5.06 | 4.57 | 3.77 | 2.93 | 2.52 | 2.58 |
| Yield on 2-year T-bonds | % | 4.72 | 4.81 | 4.30 | 2.85 | 4.66 | 4.71 | 4.22 | 3.61 | 3.29 | 2.68 | 2.63 | 2.78 |
| Yield on 5-year T-bonds | % | 5.31 | 5.44 | 4.53 | 3.19 | 5.02 | 4.93 | 4.43 | 3.75 | 3.49 | 2.94 | 3.08 | 3.23 |
| Yield on 10-year T-bonds | % | 5.74 | 5.98 | 5.02 | 3.66 | 5.58 | 5.38 | 4.91 | 4.22 | 3.95 | 3.43 | 3.57 | 3.68 |
| 2-year IRS | % | 4.73 | 4.98 | 4.52 | 2.85 | 4.83 | 4.91 | 4.47 | 3.85 | 3.43 | 2.69 | 2.58 | 2.69 |
| 5-year IRS | % | 5.25 | 5.24 | 4.47 | 3.09 | 4.82 | 4.86 | 4.37 | 3.84 | 3.52 | 2.90 | 2.92 | 3.03 |
| 10-year IRS | % | 5.40 | 5.33 | 4.56 | 3.51 | 4.88 | 4.88 | 4.47 | 4.01 | 3.76 | 3.26 | 3.45 | 3.58 |
| EUR/PLN | PLN | 3.99 | 4.12 | 4.19 | 4.17 | 4.23 | 4.26 | 4.14 | 4.11 | 4.16 | 4.18 | 4.20 | 4.13 |
| USD/PLN | PLN | 3.02 | 2.96 | 3.26 | 3.15 | 3.23 | 3.32 | 3.31 | 3.17 | 3.15 | 3.22 | 3.17 | 3.06 |
| CHF/PLN | PLN | 2.90 | 3.34 | 3.47 | 3.37 | 3.50 | 3.55 | 3.44 | 3.40 | 3.38 | 3.39 | 3.38 | 3.33 |
| GBP/PLN | PLN | 4.66 | 4.75 | 5.16 | 4.90 | 5.07 | 5.26 | 5.22 | 5.09 | 4.88 | 4.91 | 4.91 | 4.89 |

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

^a at the end of period

Economic Calendar and Events

| Date | | Event: | Note: |
|-----------|----|---|--|
| 5-Jun | PL | MPC Meeting – interest rate decision | We expect the MPC to cut rates by 25 bps, in line with expectations |
| | DE | Auction of 5Y bonds | Offer: €4bn |
| 6-Jun | PL | Auction of bonds: PS0718 and/or WZ0119 | Offer: PLN2.0-6.0bn |
| | EZ | ECB Meeting – interest rate decision | - |
| 12-Jun | DE | Auction of 2Y bonds | Offer: €5bn |
| 13-Jun | PL | CPI for May | Our forecast: 0.5%YoY (below consensus at 0.7%YoY) |
| 14-Jun | PL | Core inflation for May | We expect core CPI after excluding food and energy prices at 0.9%YoY |
| 18-Jun | PL | Employment and wages for May | We and market expect employment decline by 1%YoY and moderate growth of wages (by 2.7%YoY vs market expectations at 2.6%) |
| 19-Jun | PL | Industrial output and PPI for May | We foresee a decrease in production (by 2.1%YoY vs consensus at -1.5%). We predict PPI at -2.2%YoY |
| | PL | Switch tender | OK0713 and DS1013 will be repurchased, while offer will depend on the market conditions |
| | DE | Auction of 10Y bonds | Offer: €5bn |
| 20-Jun | EU | Eurogroup meeting | - |
| TBA | PL | Retail sales for April | Our forecast: 0.4%YoY (confirming weakness of consumer demand) |
| 25-Jun | HU | NBH Meeting - interest rate decision | - |
| 27-Jun | IT | Auction of medium-long term bonds | - |
| 28-29-Jun | EU | Meeting of the European Council | |
| 3-Jul | PL | MPC Meeting – interest rate decision | We expect rate cut by 25bps |
| 4-Jul | EU | ECB Meeting – interest rate decision | - |

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

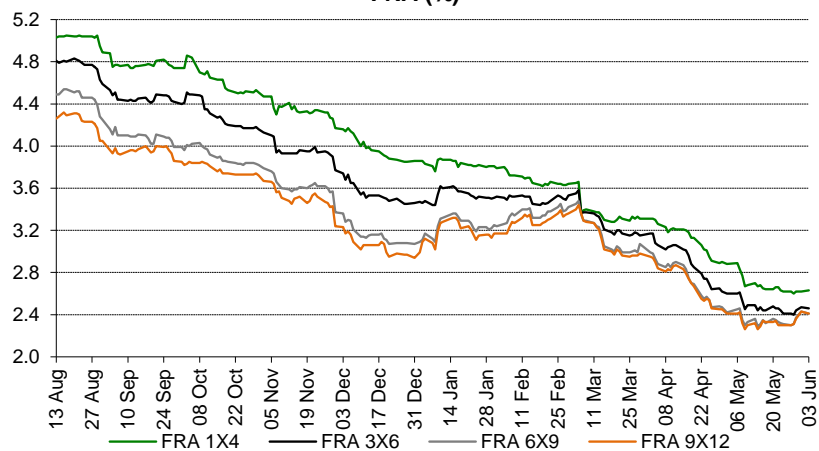
Money market rates (%)

| | Reference | Polonia | WIBOR (%) | | | | OIS (%) | | | | FRA (%) | | | |
|---------------------|-----------|---------|-----------|------|------|------|---------|------|------|------|---------|------|------|------|
| | rate (%) | (%) | 1M | 3M | 6M | 12M | 1M | 3M | 6M | 12M | 1x4 | 3x6 | 6x9 | 9x12 |
| End of May | 3.00 | 2.91 | 3.01 | 2.74 | 2.66 | 2.65 | 3.22 | 3.12 | 3.02 | 2.93 | 2.62 | 2.47 | 2.43 | 2.43 |
| Last 1M change (bp) | -25 | -19 | -24 | -34 | -37 | -37 | 17 | 27 | 32 | 38 | -28 | -15 | -4 | -2 |
| Last 3M change (bp) | -75 | -79 | -79 | -99 | -101 | -95 | -38 | -38 | -36 | -36 | -101 | -102 | -96 | -92 |
| Last 1Y change (bp) | -175 | -200 | -191 | -237 | -247 | -249 | -140 | -152 | -166 | -175 | -250 | -266 | -260 | -248 |

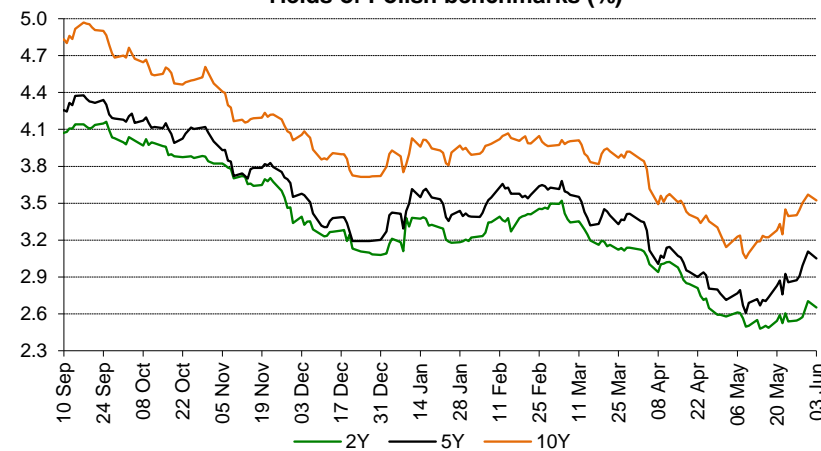
Bond and IRS market (%)

| | T-bills | BONDS | | | | IRS | | | Spread BONDS / IRS (bps) | | |
|----------------------|---------|-------|------|------|------|------|------|----|--------------------------|-----|--|
| | 52-week | 2Y | 5Y | 10Y | 2Y | 5Y | 10Y | 2Y | 5Y | 10Y | |
| End of May | 2.55 | 2.70 | 3.11 | 3.57 | 2.66 | 3.01 | 3.41 | 4 | 10 | 16 | |
| Last 1M change (bps) | -25 | 11 | 31 | 27 | -3 | 18 | 27 | 14 | 13 | -1 | |
| Last 3M change (bps) | -105 | -75 | -50 | -40 | -87 | -61 | -44 | 12 | 11 | 4 | |
| Last 1Y change (bps) | -226 | -208 | -191 | -188 | -223 | -177 | -142 | 15 | -14 | -46 | |

FRA (%)



Yields of Polish benchmarks (%)



Sources: Thomson 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 |
|--|---------------|---------------|---------------|---------------|---------------|--------------|---------------|---------------|--------------|----------------|--------------|---------------|----------------|
| T-bonds auction | 17,358 | 10,391 | 8,081 | 16,817 | 12,003 | 5,000 | 9,000 | 1,000 | 5,500 | 10,000 | 3,100 | | 93,247 |
| T-bills auction | 3,603 | 1,747 | 3,084 | | | | | | | | | | 8,434 |
| Retail bonds | 150 | 154 | 154 | 154 | 154 | 154 | 154 | 113 | 154 | 154 | 114 | 157 | 1,766 |
| Foreign bonds/credits | 4,140 | 1,301 | | | | 1,800 | | | | | 2,000 | | 9,241 |
| Prefinancing and financial resources at the end of 2012 | 24,400 | | | | | | | | | | | | 24,400 |
| Total | 49,651 | 13,593 | 11,319 | 16,971 | 12,157 | 6,954 | 9,154 | 1,113 | 5,654 | 10,154 | 5,214 | 157 | 137,088 |
| Redemption | 11,686 | 13,854 | 2,791 | 16,157 | 2,340 | 1,859 | 13,423 | 3,191 | 1,122 | 25,128 | 2,256 | 2,369 | 96,176 |
| Net inflows | 37,965 | -261 | 8,528 | 814 | 9,817 | 5,095 | -4,269 | -2,078 | 4,532 | -14,974 | 2,958 | -2,212 | 40,912 |
| Rolling over T-bonds | | | 4,827 | | | | | | | | | | 4,827 |
| Buy-back of T-bills/bonds | | | | | | | | | | | | | 0 |
| Total | 37,965 | -261 | 13,355 | 814 | 9,817 | 5,095 | -4,269 | -2,078 | 4,532 | -14,974 | 2,958 | -2,212 | 45,739 |
| <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 | 0 | 11,686 |
| February | 0 | 2,190 | 148 | 2,338 | 11,516 | 13,854 |
| March | 0 | 2,329 | 212 | 2,541 | 250 | 2,791 |
| April | 16,025 | 0 | 132 | 16,157 | 0 | 16,157 |
| May | 0 | 2,223 | 117 | 2,340 | 0 | 2,340 |
| June | 0 | 1,747 | 112 | 1,859 | 0 | 1,859 |
| July | 13,205 | 0 | 218 | 13,423 | 0 | 13,423 |
| August | 0 | 1,997 | 248 | 2,245 | 946 | 3,191 |
| September | 0 | 0 | 176 | 176 | 946 | 1,122 |
| October | 23,913 | 0 | 265 | 24,178 | 950 | 25,128 |
| November | 0 | 1,332 | 208 | 1,540 | 716 | 2,256 |
| December | 0 | 2,223 | 146 | 2,369 | 0 | 2,369 |
| Total 2013 | 63,144 | 15,633 | 2,075 | 80,852 | 15,324 | 96,176 |
| Total 2014 | 61,666 | 6,110 | 1,698 | 69,474 | 14,825 | 84,300 |
| Total 2015 | 78,880 | | 628 | 79,508 | 17,448 | 96,956 |
| Total 2016 | 59,378 | | 485 | 59,863 | 14,329 | 74,192 |
| Total 2017 | 67,278 | | 91 | 67,369 | 16,871 | 84,240 |
| Total 2018+ | 179,992 | | 3,288 | 183,280 | 134,966 | 318,247 |

Sources: MF, BZ WBK

2. Polish bonds: supply recap (cont.)

Schedule wholesale bonds redemption by holders (data at the end of April 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 | 1 | 0 | 0 | 0 | 0 | 22 | 0 | 0 | 24 |
| Q3 2013 | 9,073 | 1,030 | 1,287 | 187 | 235 | 113 | 19 | 1,301 | 13,244 |
| Q4 2013 | 12,105 | 1,244 | 7,071 | 914 | 609 | 116 | 127 | 1,772 | 23,958 |
| Total 2013 | 21,179 | 2,274 | 8,358 | 1,101 | 844 | 251 | 145 | 3,073 | 37,226 |
| | 57% | 6% | 22% | 3% | 2% | 1% | 0% | 8% | 100% |
| Total 2014 | 37,460 | 9,415 | 4,602 | 2,778 | 3,375 | 390 | 253 | 3,684 | 61,956 |
| | 60% | 15% | 7% | 4% | 5% | 1% | 0% | 6% | 100% |
| Total 2015 | 29,664 | 24,216 | 8,641 | 12,292 | 10,285 | 221 | 361 | 4,528 | 90,208 |
| | 33% | 27% | 10% | 14% | 11% | 0% | 0% | 5% | 100% |
| Total 2016 | 19,321 | 9,984 | 3,789 | 21,316 | 5,111 | 54 | 83 | 3,048 | 62,705 |
| | 31% | 16% | 6% | 34% | 8% | 0% | 0% | 5% | 100% |
| Total 2017 | 26,850 | 13,346 | 5,766 | 14,584 | 7,387 | 49 | 176 | 3,286 | 71,444 |
| | 38% | 19% | 8% | 20% | 10% | 0% | 0% | 5% | 100% |
| Total 2018+ | 72,577 | 40,222 | 20,313 | 63,061 | 16,855 | 216 | 340 | 9,481 | 223,064 |
| | 33% | 18% | 9% | 28% | 8% | 0% | 0% | 4% | 100% |

Sources: MF, BZ WBK

3. Polish bonds: demand recap

Holders of marketable PLN bonds

| | Nominal value (PLN, bn) | | | | Nominal value (PLN, bn) | | | % change in April | | | Share in TOTAL (%) in Apr |
|-----------------------------|-------------------------|------------|------------|--------------|-------------------------|-------------|-------------|-------------------|-------|-------|---------------------------|
| | End Apr'13 | End Mar'13 | End Jan'13 | End Dec 2012 | End 3Q 2012 | End 2Q 2012 | End 1Q 2012 | MoM | 3-mth | YoY | |
| Domestic investors | 346.9 | 347.9 | 339.8 | 337.5 | 341.8 | 352.9 | 361.4 | -0.28 | 3.59 | -1.78 | 62.6 (-0.3pp) |
| Commercial banks | 99.5 | 104.1 | 92.9 | 87.8 | 102.0 | 102.1 | 110.9 | -4.42 | 7.07 | -5.47 | 18.0 (-0.9pp) |
| Insurance companies | 51.5 | 51.4 | 51.9 | 52.8 | 54.7 | 57.0 | 54.3 | 0.13 | -0.84 | -7.01 | 9.3 |
| Pension funds | 115.1 | 113.0 | 113.6 | 117.4 | 116.7 | 120.3 | 120.7 | 1.85 | 1.37 | -6.72 | 20.8 (0.3pp) |
| Mutual funds | 43.9 | 42.1 | 41.4 | 41.7 | 32.5 | 33.0 | 31.3 | 4.20 | 6.05 | 32.55 | 7.9 (0.3pp) |
| Others | 37.0 | 37.3 | 40.0 | 37.8 | 35.9 | 40.5 | 44.3 | -0.8 | -7.6 | 2.5 | 6.7 |
| Foreign investors* | 207.1 | 205.3 | 195.0 | 189.9 | 184.2 | 174.0 | 163.2 | 0.87 | 6.18 | 29.43 | 37.4 (0.3pp) |
| Banks | 38.4 | 37.3 | 30.4 | 28.4 | 27.8 | 22.6 | 24.3 | 3.03 | 26.27 | 72.90 | 6.9 (0.2pp) |
| Non-bank fin. sector | 159.9 | 159.0 | 156.2 | 153.1 | 147.5 | 143.1 | 131.7 | 0.55 | 2.35 | 22.49 | 28.9 (0.1pp) |
| Non-financial sector | 5.2 | 5.4 | 4.8 | 5.2 | 5.6 | 5.2 | 4.4 | -4.62 | 6.96 | 18.75 | 0.9 (-0.1pp) |
| TOTAL | 554.0 | 553.1 | 534.8 | 527.4 | 526.0 | 526.9 | 524.7 | 0.15 | 2.10 | 7.95 | 100 |

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

Sources: MF, BZ WBK

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 | 43.0 |
| Belgium | 30.3 | 8.8 | 40.0 | 37.0 | 62.0 |
| Finland | 6.8 | 5.6 | 12.4 | 12.4 | 35.0 |
| France | 105.5 | 61.6 | 171.1 | 170.0 | 58.0 |
| Germany | 157.0 | 17.1 | 174.1 | 174.1 | 46.0 |
| 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 | 61.0 |
| Netherlands | 31.5 | 15.2 | 46.7 | 50.0 | 53.0 |
| Portugal | 5.9 | 7.4 | 13.3 | 3.0 | 84.0 |
| Spain | 61.9 | 48.4 | 133.3 | 113.4 | 55.0 |
| Total | 584.3 | 220.0 | 832.2 | 772.3 | 55.0 |

*/ YtD (year calendar) data for 2013

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) | |
|----------------|---------|-------|---------------------|-------|------------------------|-------|---------------------------|-------|------------------------|-------|
| | 2013F | 2014E | 2013F | 2014E | 2013F | 2014E | 2013F | 2014E | 2013F | 2014E |
| Poland | 1.1 | 2.2 | 1.4 | 2.0 | -2.5 | -2.4 | -3.9 | -4.1 | 57.5 | 58.9 |
| Czech Republic | -0.4 | 1.6 | 1.9 | 1.2 | -2.4 | -2.5 | -2.9 | -3.0 | 48.3 | 50.1 |
| Hungary | 0.2 | 1.4 | 2.6 | 3.1 | 2.5 | 2.6 | -3.0 | -3.3 | 79.7 | 78.9 |
| EU | -0.1 | 1.4 | 1.8 | 1.7 | 1.6 | 1.9 | -3.4 | -3.2 | 89.8 | 90.6 |
| Euro area | -0.6 | -0.3 | 1.6 | 1.5 | 2.5 | 2.7 | -2.9 | -2.8 | 95.5 | 96.0 |
| Germany | 0.4 | 1.8 | 1.8 | 1.6 | 6.3 | 6.1 | -0.2 | 0.0 | 81.1 | 78.6 |

Main market indicators (%)

| | Reference rate (%) | | 3M market rate (%) | | 10Y yields (%) | | 10Y Spread vs Bund (bps) | | CDS 5Y | |
|----------------|--------------------|------|--------------------|------------|----------------|------------|--------------------------|------------|--------|------------|
| | 2012 | 2013 | 2012 | end of May | 2012 | end of May | 2012 | end of May | 2012 | end of May |
| Poland | 4.25 | 2.50 | 4.11 | 2.74 | 3.72 | 3.57 | 241 | 205 | 80 | 76 |
| Czech Republic | 0.05 | 0.05 | 0.18 | 0.14 | 1.86 | 1.76 | 54 | 24 | 63 | 59 |
| Hungary | 5.75 | 4.00 | 5.75 | 4.38 | 6.23 | 5.76 | 492 | 424 | 269 | 286 |
| Euro area | 0.75 | 0.50 | 0.19 | 0.20 | | | | | | |
| Germany | | | | | 1.32 | 1.52 | | | 39 | 28 |

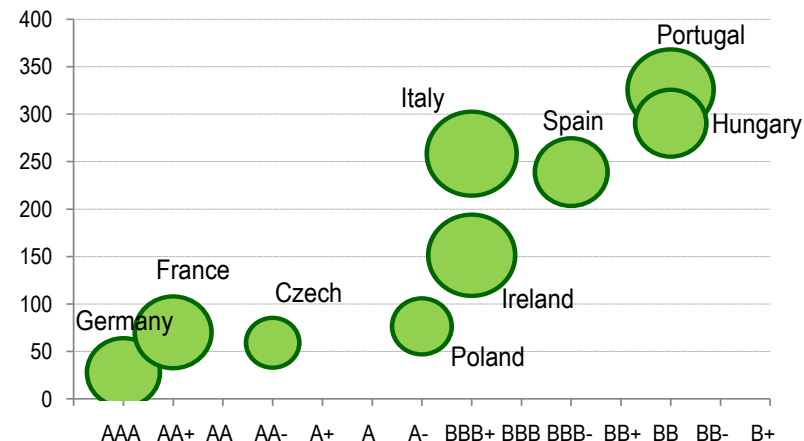
Sources: EC – Spring 2013, stat offices, central banks, Reuters, BZ WBK

5. Poland vs other countries (cont.)

Sovereign ratings

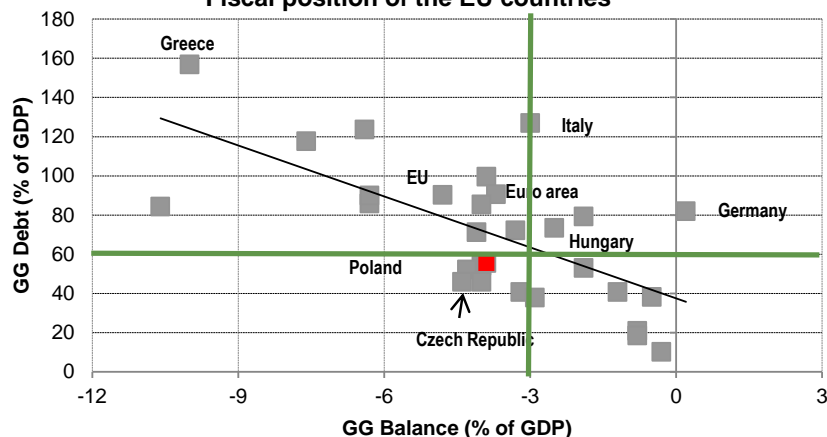
| | S&P | | Moody's | | Fitch | |
|----------|--------|----------|---------|----------|--------|----------|
| | rating | outlook | rating | outlook | rating | outlook |
| Poland | A- | stable | A2 | stable | A- | positive |
| Czech | AA- | stable | A1 | stable | A+ | stable |
| Hungary | BB | stable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

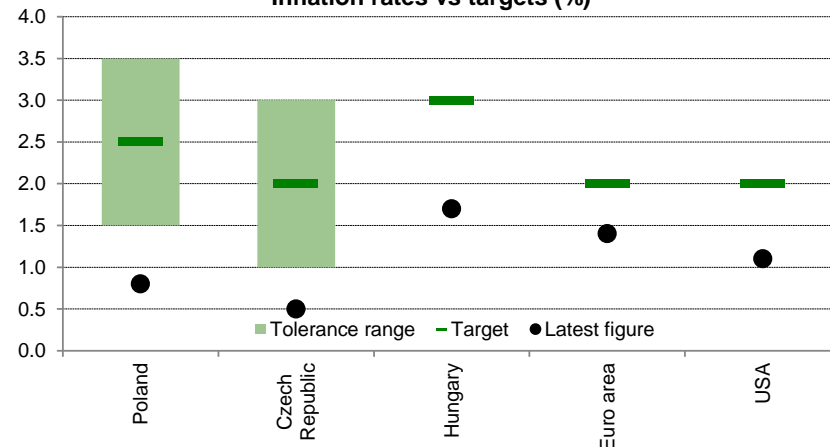


Note: Size of bubbles reflects the debt/GDP ratio

Fiscal position of the EU countries

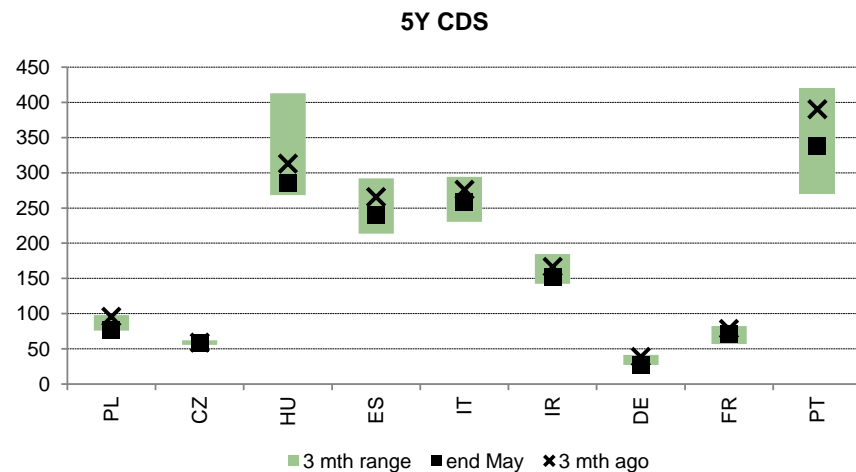
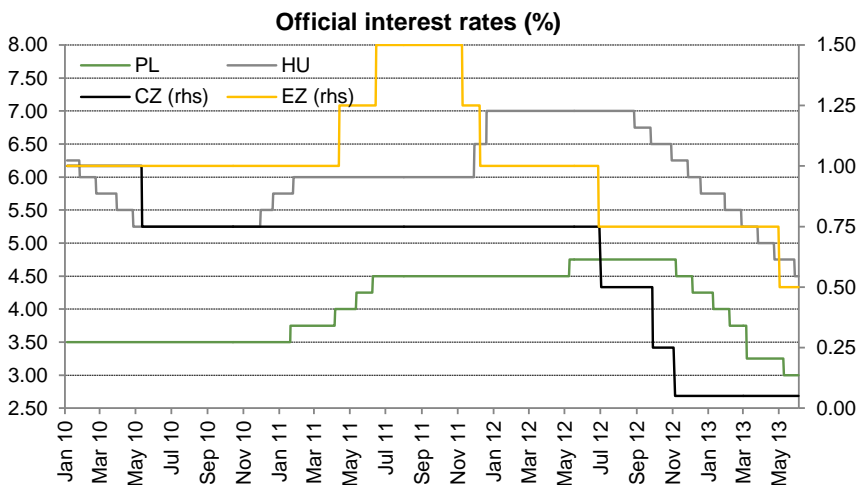
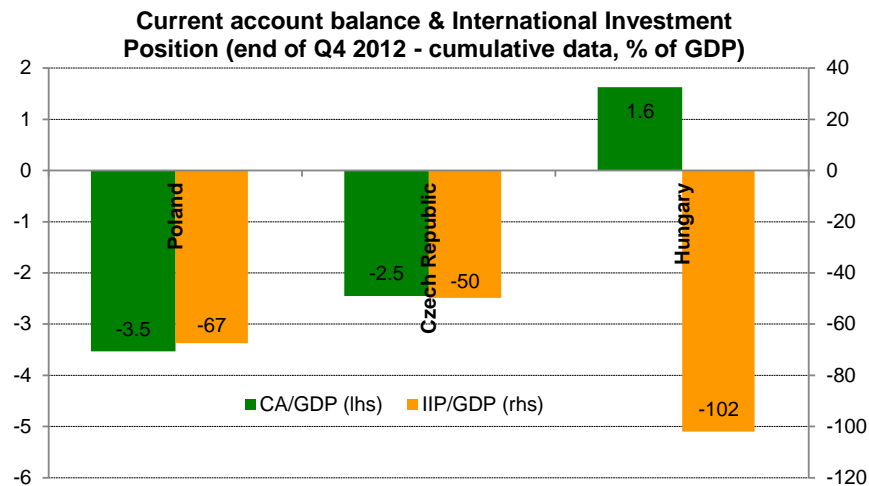
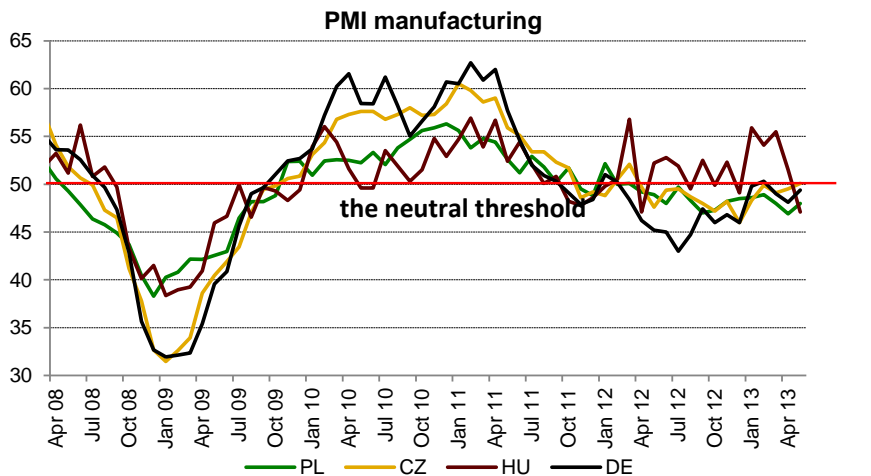


Inflation rates vs targets (%)



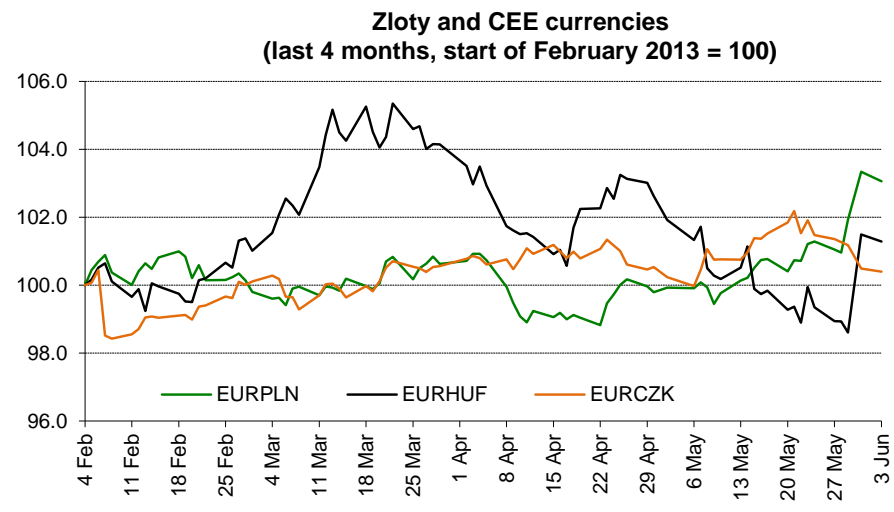
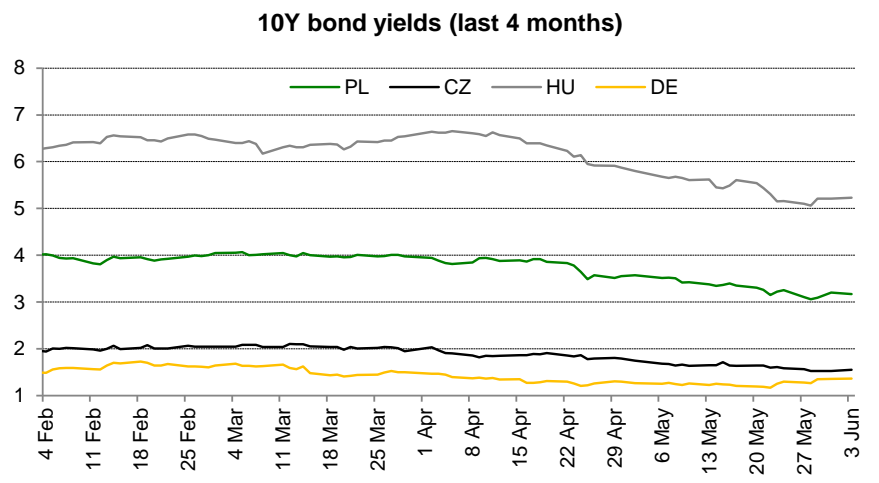
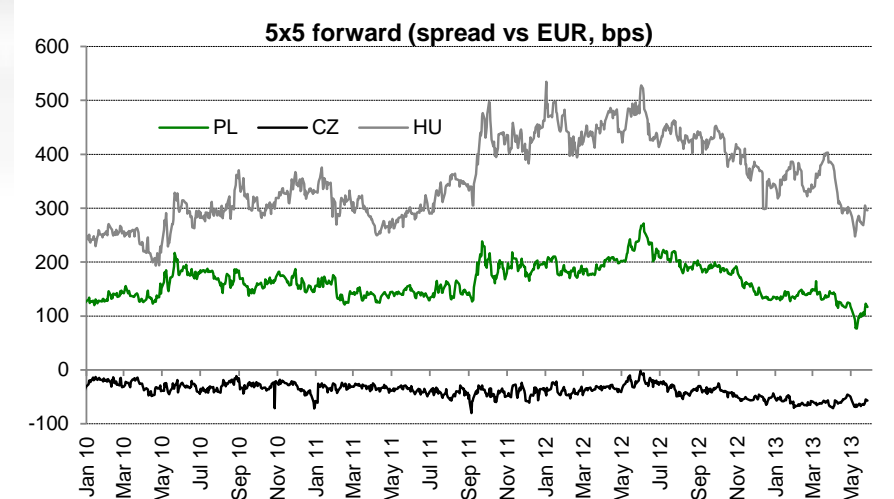
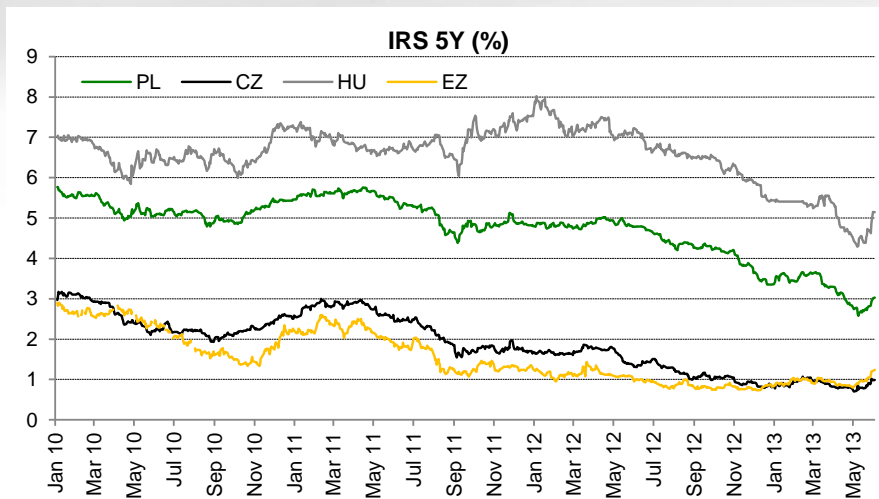
Source: rating agencies, Reuters, BZ WBK, EC

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 | |
| Euro zone | Forecast | 0.50 | 0.75 | 0.50 | | | | Rates on hold this month. In June investors will concentrate on a new macro forecasts and any hint on non-conventional measures. |
| | Market implied » | | | | 0 | -1 | -2 | |
| UK | Forecast | 0.50 | 0.50 | 0.50 | | | | We do not expect any changes in the BoE monetary policy, however this month meeting will grab some attention as it is Governor King's final meeting. |
| | Market implied » | | | | -1 | -2 | -2 | |
| US | Forecast | 0-0.25 | 0-0.25 | 0.25 | | | | Investors concentrate on Fed's tone. Investors will focus on any hints on QE tapering. |
| | Market implied » | | | | 0 | 0 | 1 | |
| Poland | Forecast | 3.00 | 4.25 | 2.50 | | | | We expect the MPC to cut rates by 25bps., in which the reference rate to 2.75%, new historical low. This is in line with market view, but in following months we see lower scale of easing. |
| | Market implied » | | | | -16 | -45 | -60 | |
| Czech Republic | Forecast | 0.05 | 0.05 | 0.05 | | | | The same story as in previous month. The CNB will concentrate on non-standard measures and it might use FX interventions against the koruna. |
| | Market implied » | | | | 30 | 27 | 26 | |
| Hungary | Forecast | 4.50 | 5.75 | 4.00 | | | | The NBH has continued easing cycle. We expect further gradual cuts in rates to 4.00% at the end of 2013. |
| | Market implied » | | | | -28 | -81 | -113 | |

This analysis is based on information available until 3rd June 2013 and has been prepared by:

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