Bank Zachodni WBK

Eyeopener – Fed concerned about inflation

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- **Further zloty strengthening, record high stock prices in Warsaw Stock Exchange**
- **Stabilisation in bond market, next MPC member suggesting possible rate hikes**
- **Market likely to focus today on the ECB meeting, the statement may be hawkish, heralding more rate hikes in the pipeline**

Yesterday once again the Polish currency appreciated against the euro as well as the dollar. The ERUPLN rate fell again breaking 3,83 level and at the end of the session amounted to 3,826. USDPLN rate fell from 2.856 top 2.848. This strengthening was in line with new records at Warsaw Stock Exchange and weakening of low-yielding currencies (yen and Swiss franc).

What is interesting the Czech government decided that no date of euro zone entry is going to be set at present. Till now the single currency adoption was scheduled for 2010, however the widening of budget deficit above 3% of GDP was the factor that contributed to abandoning this date.

In the fixed income market after Tuesday weakening this time bond prices did not change significantly. A slight rise of yield at the longer end of the yield curve was connected with further weakening of long term German Bunds and to some extent also comments of Stanisław Nieckarz. The MPC member considered as a one of the doves in the Council said that the GDP growth may reach 7.5%YoY in Q1 and from Q2 the growth is going to slow down to ca. 6%YoY in Q4 and average of ca. 5% in 2008. In his opinion despite an expected lower GDP growth rate, the situation in the labour market, where the possible wages growth connected with job migration may not be compensated by the rise of labour productivity, may change the risks balance to higher inflation pressure. Stanisław Nieckarz noticed that the expectations of interest rate hikes had been stimulated, thus he did not exclude a preventive move in the nearest months. He added that he did not think inflation would break the target this year. It was another MPC member that used to vote against interest rate hikes and now did not exclude such possibility. In our view such comments even more strengthen expectations of interest rate hikes in the nearest two months (possibly already in April).

The Ministry of Finance sold PLN1.8bn of 10Y DS1017 bonds at average yield of 5.244% with investors' demand of PLN3.47bn.

The EURUSD rate was traded in a narrow range yesterday and eventually it showed a moderate rise if opening and close levels are compared (1.3445 vs. 1.344). Stabilisation on international FX market was connected with the fact that investors awaited the publication of Fed March minutes. However, it did not affect the dollar market, though a substantial weakening in the stock exchange and fixed markets took place. Today in the morning the dollar depreciated against the euro to 1.346 as market players expect a hawkish statement of the European Central Bank. Also, worries about perspectives of the US economy as well weakening in carry trade currencies (Japanese yen and Swiss frank) could have played a role.

Yields of 10-year Treasuries were quite stable yesterday at the level of 4.72% when the market awaited the publication of FOMC minutes, in which the key factor was the assessment of risk factors for inflation. German Bunds weakened again with 10-year yield rising to 4.14%. On the other hand, investors were buying equities and US bonds.

Fed minutes surprised the market with the extent the US central bank was worried over possible inflation pressure. The statement included in the report, which said "further policy firming might prove necessary to foster lower inflation" caused the market to lower expectations for rate cuts in the US. Concerns over inflation prospects were confirmed later by comments of Fed representatives Jeffrey Lacker oraz Michael Moskow.

Today at 9:00 GMT we will see final Q4 GDP data in the euro zone. Analysts expect 3.3%YoY rise against previous 2.7%. At 11:45 GMT the European Central Bank will announce decision on interest rates. After series of good data from the euro zone, investors will be waiting for the ECB statement that may retain hawkish tone. We believe there will be some hints regarding timing of the next rate hike (in our view it will take place in June). At 12:30 GMT there will be publication of import prices in the US. Market consensus shows a rise by 0.9% in March against 0.2% last month.

At the opening, zloty was at 3.83 against euro and 2.85 against dollar. Sentiment in the morning may be spoiled by drops of stock prices in US and Asia. During the session, investors will be positioning ahead of tomorrow's inflation data from the US (PPI) and Poland (CPI).

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F/X rates (today's opening)

EURUSD	1.3467	CADPLN	2.4820
USDPLN	2.8459	DKKPLN	0.5130
EURPLN	3.8324	NOKPLN	0.4723
CHFPLN	2.3415	SEKPLN	0.4121
JPYPLN*	2.3904	CZKPLN	0.1369
GBPPLN	5.6162	HUFPLN	1.5585

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The zloty trading ranges

	min	max	open	close	fixing
EURPLN	3.8236	3.8366	3.8358	3.8263	3.8279
USDPLN	2.8467	2.8582	2.8558	2.8481	2.8509
EURUSD	1.3415	1.3439	1.3425	1.3439	-

T-bonds

TERM	BOND	Yield (%)	Change (bp)	Last auction	Average yield
2Y	OK0709	**4.71**	**-1**	4.04	4.694
5Y	PS0412	**5.04**	**1**	22.03	4.967
10Y	DS1017	**5.24**	**1**	10.01	5.234

IRS rates (Mid)

TERM	PL		US		EU	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1Y	4.71	1	5.32	1	4.31	1
2Y	**4.89**	**-1**	5.12	2	4.33	3
3Y	4.99	0	5.07	2	4.33	3
4Y	5.05	2	5.08	2	4.33	3
5Y	**5.08**	**-1**	5.11	2	4.33	4
8Y	5.15	1	5.20	1	4.37	3
10Y	**5.17**	**0**	5.27	1	4.42	3

WIBOR rates

TERM	%	Daily change (bp)
O/N	4.11	0
T/N	4.11	0
SW	4.12	0
2W	4.13	0
1M	4.18	-1
3M	4.29	0
6M	4.46	-1
9M	4.58	1
1Y	4.68	0

FRA rates (Mid)

TERM	%	Daily change (bp)
1X2	4.31	0
3X6	4.58	-3
6X9	4.77	-2
9X12	4.86	2
3X9	4.70	0
6X12	4.86	2

Zloty exchange rate (fixing)

T-bonds yields

3-month money market rates

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