Bank Zachodni WBK

Eyeopener – Local bonds hurt by CPI forecast

6 November 2007

- **The zloty traded in narrow range yesterday, slightly stronger today**
- **Significant in FRA rates and bond yields after release of the pessimistic CPI forecast by FinMin**
- **Today we will get the euro zone's data on PMI services and retail sales**

The start of the week in the domestic FX market was quite calm. The zloty fluctuated in narrow ranges against the major currencies. At the end of the domestic session the EURPLN rate was close to the opening levels and reached 3.65, while the USDPLN rate was at 2.521. After the session's close the domestic currency appreciated due to some improvement in moods in the global markets, stronger to the dollar as it weakened against the euro. Today at the opening the EURPLN rate was slightly above 3.64, while the USDPLN rate slightly below 2.51.

There were significant moves in the fixed income market. In the morning the Ministry of Finance released its inflation forecast. According to the spokesman of the ministry, consumer prices rose 0.7%MoM in October, which may mean that CPI inflation will accelerate to as much as 3.0%YoY. Although the Ministry of Finance did not give details of its forecast, such strong acceleration of inflation is most likely related to estimates of strong increase in food prices. After the release of the forecast we decided to upwardly revise our forecast of inflation in October to 2.8%YoY from 2.6% predicted earlier. Overall, there was a slight steepening of the yield curve during the yesterday's session. The 2-10 spread rose from 5bp to 9bp. What is interesting, after the release of the MinFin's forecast the 5Y bonds were hurt the most and their yields rose by 12 bp. This resulted in a decline of 5-10 spread to -18 bp.

What is important MPC member Halina Wasilewska-Trenkner said (in an interview with Reuters) after release of the finance ministry's forecast that the MPC knew the number during the meeting, so they are no surprise to the Council. The MPC member stated that this will require further actions of the MPC. Marian Noga said (Thomson Financial) that after one more hike this year he does not rule out raising rates three more times the next year. If the Council actually had known the inflation forecast it is surprising why it did not decide for a rate hike already in October.

At the yesterday's tender the Ministry of Finance sold PLN1bn worth of 52-week T-bills. Investors' demand reached PLN1.6bn while average yield was at 5.312%. Additionally the Ministry of Finance announced that at Wednesday's auction it will offer PLN1.7bn worth of 2Y bonds. Moreover, the estimated results of budget performance in October were released – the budget deficit after ten months reached PLN5-5.5bn, i.e. ca. 17.5-18.5% of the full-year plan, against earlier forecasts 14-15%. This was another good news about the budget, however according to deputy finance minister Elżbieta Suchocka-Roguska in October the revenues were slightly lower than predicted, while realisation of spending accelerated. Nevertheless, the deputy minister stressed that tentative calculations may be subject to change.

On Monday in the morning the National Bank of Poland held press conference on the results of the latest inflation projection. Details of the new *Inflation Report* were presented in our yesterday's *Instant comment*.

Yesterday the official start of the Sejm's first meeting after the election took place, while PM Jarosław Kaczyński and his government resigned. According to President's chancellery official Michał Kamiński, the President Lech Kaczyński will designate PO leader Donald Tusk for the new Prime Minister already this week.

During the local session, the dollar slightly gained against single currency to ca. 1.447 from 1.449 at the opening. On international markets high risk aversion persisted, among others due to information about much higher than predicted Citigroup's losses and its president's dismissal. It contributed to investors' flee into save heavens and brought yields of 10Y Treasuries to 4.30%, while yields of 10Y Bunds remained close to opening level of 4.17%. The ISM services index released in the United States in the afternoon was better than expected and reached 55.8 against forecasted 54. This negatively affected the core debt markets and lowered risk aversion in the global markets. As a result, today in the morning yields of 10-year Treasuries and Bunds were even higher than yesterday and reached 4.36% and 4.20%, respectively. The dollar reached new low as the EURUSD clearly exceeded 1.45.

Today, the euro zone's data on retail sales and PMI index for services sector will be published. The market consensus indicates a rise of the PMI to 55.6 pct in October from 54.2 and an increase of retail sales by 1.9%YoY in September after 1.0%YoY rise in the previous month.

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F/X rates (today's opening)

EURUSD	1.4510	CADPLN	2.6943
USDPLN	2.5090	DKKPLN	0.4883
EURPLN	3.6414	NOKPLN	0.4680
CHFPLN	2.1829	SEKPLN	0.3927
JPYPLN*	2.1882	CZKPLN	0.1350
GBPPLN	5.2290	HUFPLN	1.4401

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The zloty trading ranges

	min	max	open	close	fixing
EURPLN	3.6417	3.6553	3.6456	3.6484	3.6446
USDPLN	2.5148	2.5229	2.5163	2.5219	2.5181
EURUSD	1.4451	1.4493	1.4488	1.4470	-

T-bonds

TERM	BOND	Yield (%)	Change (bp)	Last auction	Average yield
2Y	OK0709	**5.50**	**5**	3.10	5.284
5Y	PS0412	**5.78**	**12**	17.10	5.718
10Y	DS1017	**5.59**	**9**	10.10	5.699

IRS rates (Mid)

TERM	PL		US		EA	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1Y	5.65	11	4.56	3	4.61	-1
2Y	**5.78**	**14**	4.43	6	4.50	1
3Y	5.80	15	4.50	6	4.46	0
4Y	5.78	13	4.61	6	4.44	0
5Y	**5.76**	**13**	4.71	6	4.45	0
8Y	5.64	8	4.94	7	4.52	0
10Y	**5.58**	**7**	5.05	5	4.58	1

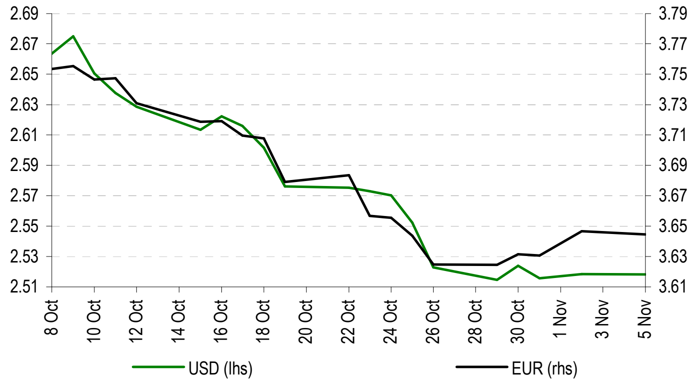
WIBOR rates

TERM	%	Daily change (bp)
O/N	4.88	-3
T/N	4.88	-4
SW	4.94	-2
2W	4.95	-1
1M	5.00	0
3M	5.22	1
6M	5.41	3
9M	5.49	3
1Y	5.59	2

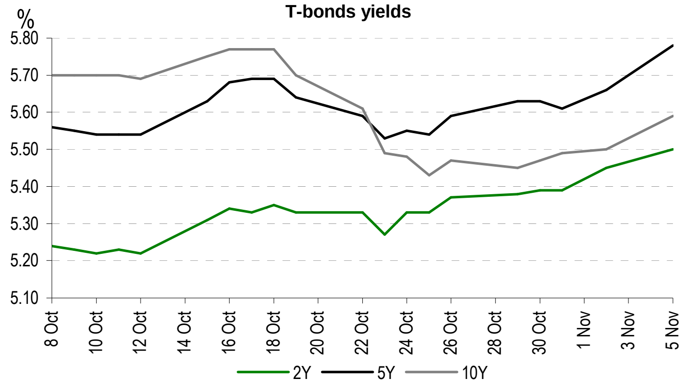
FRA rates (Mid)

TERM	%	Daily change (bp)
1X2	5.18	3
3X6	5.49	9
6X9	5.64	13
9X12	5.70	14
3X9	5.61	12
6X12	5.72	15

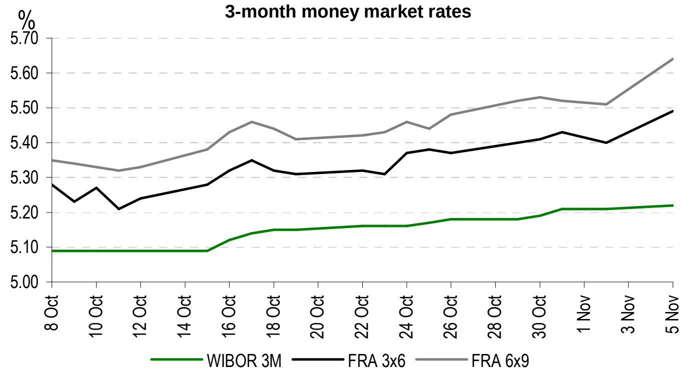
Zloty exchange rate (fixing)



T-bonds yields



3-month money market rates



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