

Eyeopener – Markets in panic again

17 March 2008

- Risk aversion grows again on international markets
- Next emergency Fed's actions not very effective
- Today, local market awaiting labour market data; new important publications abroad

On Friday, after the session with quite high volatility, at the end of the day the zloty was slightly stronger as compared to morning levels both against the euro and the dollar. During the day there was a turmoil connected with events in the United States. After quite positive data on the US core inflation the zloty appreciated, though the information on diminished liquidity of Bear Stearns bank resulted in strengthening of the euro against the zloty. Lowering of the Hungary's rating from stable to negative by the S&P agency also contributed to a temporary, slight zloty depreciation. Overall, the Friday session showed that the Polish financial market remains quite resistant to moods fluctuation in the foreign markets. Today in the morning the influence of the situation abroad to Polish currency was stronger due to further increase of fears over financial markets stability in the US, despite further emergency actions taken by Fed. On Sunday night the Fed lowered the discount rate by 25 bp to 3.25% and announced a new credit programme allowing borrowing money by the primary market dealers directly from the Fed. Despite this, the equity markets in Asia plummeted, the EURPLN rate rose at the opening above 3.55, and the USDPLN rate increased to 2.253, with the EURUSD rate at 1.58.

The euphoria in the Polish debt market after lower than expected inflation subsided on Friday and investors' activity was limited. At the longer end of the curve the yields increased on higher risk aversion. The fall of bond prices took place in a moment, when at the opening of the US market there was a fall of Bear Stearns stock prices decline by 50%. Today the domestic debt market will await the wages data, though until their release the market will be affected by the moods abroad.

In the first part of the Friday session the dollar slightly appreciated against the single currency to 1.553 from 1.562 at the opening. The lower than expected US inflation was factor supporting the dollar, while the higher the forecasted inflation in the euro zone did not weaken it. The US inflation decelerated in February to 2.3% from the 2.5% in January. The euro zone inflation amounted in February to 3.3%YoY, which is the highest level in almost 14 years against expectations of stabilization at January levels of 3.2%. In the second part of the session the dollar started to clearly weaken and the EURUSD rate set a new record high level reaching 1.568. Moreover the dollar reached the weakest level in 12 years against

the yen and new all time record against the Swiss franc breaking psychological barrier of 100 against the yen and of 1 versus the Swiss franc. This was caused mainly by information about situation of the Bear Stearns, which had to get additional financing from the Fed and JPMorgan Chase. The market sentiment was also negatively influenced by report of the Fitch Ratings agency about a possibility of larger losses in mortgage portfolios of the US banks. In reaction to events in the market the Fed said in a special statement that it "is monitoring market developments closely and will continue to provide liquidity as necessary to promote the orderly functioning of the financial system". The reaction took place already last night. However, despite the Fed's actions and information about acquisition of Bear Stearns by JPMorgan, sentiment in the global markets remained poor. As a result of increase in risk aversion, EURUSD rose to 1.59 last night which was followed by a correction to around 1.58. Yields of 10Y Treasuries and Bunds dropped to 3.36% and 3.69%, respectively.

This week we will get a bulk of important data both locally and internationally. Today's data from the labour market (at 13:00 GMT) as well as output and PPI figures (due on Wednesday) should be rather strong, confirming continuation of relatively fast economic expansion in the first quarter of this year. Our forecast for wage growth is below market consensus (we predict 10.9%YoY rise versus market consensus of 11.1%YoY; while our forecast of employment growth is consistent with market consensus of 5.8%YoY), however not to the extent that would persuade the MPC to delay the next rate hike. Minutes of the MPC meeting in February may show reasons that convinced the Council to act quickly. The most important event abroad will be the meeting of American central bank. Amid increasingly pessimistic news from the US economy, another Fed's rate cut is a deal done, and the question concerns a scale of easing. Currently the market is pricing in a 75 bp rate reduction. Before the decision, there will be several important data from the US, so the first part of the week may be again a test period for the dollar. The end of the week may be more peaceful, due to market holiday in many countries abroad.

Perhaps in the nearest days we will see the decision of energy market regulator about a hike in gas prices, which will be important for inflation path in the near future. However, according to today's press, the decision that was expected today, will be delayed, so the new tariffs will not become effective since 1 April, and moreover the regulator will approve price hikes lower than 20%, against ca. 30% proposed by the gas company.

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F/X rates (today's opening)

EURUSD	1.5770	CADPLN	2.2666
USDPLN	2.2532	DKKPLN	0.4764
EURPLN	3.5530	NOKPLN	0.4411
CHFPLN	2.2870	SEKPLN	0.3753
JPYPLN*	2.3145	CZKPLN	0.1417
GBPPLN	4.5443	HUFPLN	1.3628

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The zloty trading ranges

	min	max	open	close	fixing
EURPLN	3.5270	3.5450	3.5393	3.5365	3.5307
USDPLN	2.2580	2.2780	2.2656	2.2640	2.2664
EURUSD	1.5533	1.5680	1.5619	1.5618	-

T-bonds

TERM	BOND	Yield (%)	Change (bp)	Last auction	Average yield
2Y	OK0709	6.20	-1	2.01	6.189
5Y	PS0412	6.19	0	5.03	6.167
10Y	DS1017	5.98	3	13.02	5.785

IRS rates (Mid)

TERM	PL		US		EA	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1Y	6.37	1	2.39	-4	4.38	2
2Y	6.25	0	2.51	-2	4.04	1
3Y	6.14	1	2.82	1	3.97	3
4Y	6.05	1	3.13	-1	3.96	2
5Y	5.99	1	3.40	1	4.01	2
8Y	5.85	4	3.97	3	4.21	3
10Y	5.79	4	4.22	3	4.33	3

WIBOR rates

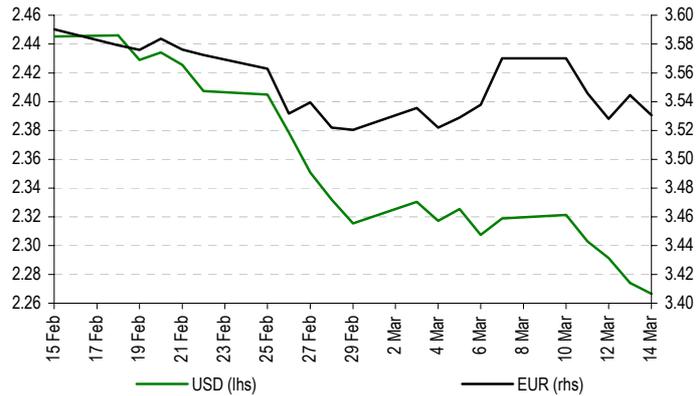
TERM	%	Daily change (bp)
O/N	5.70	-1
T/N	5.70	-1
SW	5.71	0
2W	5.72	0
1M	5.77	-1
3M	6.01	-2
6M	6.30	-2
9M	6.36	-2
1Y	6.44	-2

FRA rates (Mid)

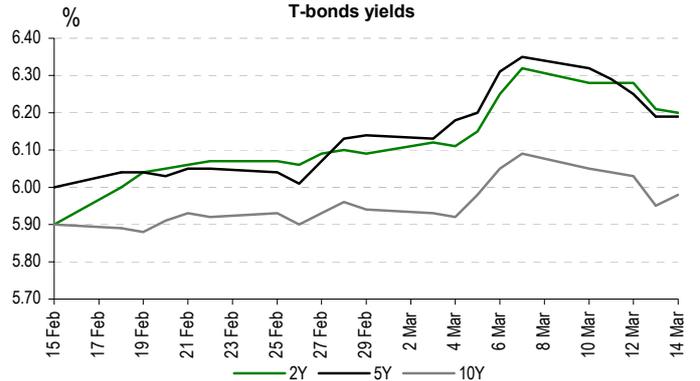
TERM	%	Daily change (bp)
1X2	5.86	2
3X6	6.28	-1
6X9	6.33	1
9X12	6.29	-1
3X9	6.36	2
6X12	6.35	3

* for 100 JPY

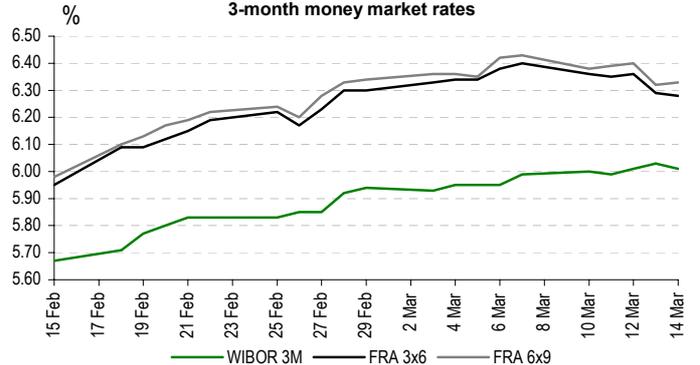
Zloty exchange rate (fixing)



T-bonds yields



3-month money market rates



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