

Eyeopener – FinMin’s inflation forecast today

3 November 2008

- Zloty rebounded, bonds slightly weaker
- Today, T-bill auction, FinMin’s inflation forecast, and activity indicators in the euro zone and US
- This week, central banks’ decisions (next rate cuts expected), US elections, NBP’s 3M repo operations

On Friday after weaker opening connected with strengthening of Japanese yen and US dollar the zloty started to recover against the major currencies amid relatively stable EURUSD rate. The EURPLN rate fell in the course of the day from 3.62 to 3.517 at the end of the session and USDPLN rate declined from 2.852 to 2.775. The currencies in the region also recovered, which was accompanied by stock prices rise in the European markets. After a slight strengthening of the euro vs. the dollar to above 1.27 the EURUSD rate stabilised near this level. At the end of the day the dollar recovered again to 1.268.

In the bond market there was a slight increase of yields, though the liquidity in the markets is still limited. On the other hand FRA and IRS rates recorded a slight fall against the Thursday close.

In the foreign money markets interest rates fell further. In the core debt markets on Friday after a recovery in the first part of the day the prices declined again in the afternoon. Yields of 10Y Treasuries and Bunds were above levels from the opening at 3.93% and 3.87% respectively against 3.92% and 3.78% on Friday morning.

Inflation data in the euro zone for October were in line with expectations and showed a fall of HICP growth rate to 3.2%YoY from 3.6% in September. Inflation data for the US showed a rise of core PCE by 0.2%MoM against expected 0.1% rise. Economic activity data in the US disappointed again. The Chicago PMI index fell again to 37.8 pts from 56.7 pts, while the market consensus pointed to much smaller decline to 48 pts. The US consumer sentiment Michigan index fell in October nearly as expected to 57.6 pts from 70.3 pts.

Amid difficult market conditions, the Ministry of Finance announced that debt issuance policy will be flexible in November. This week’s auction of 5Y bonds was cancelled, while auction of T-bills will take place. The finance ministry is going to offer PLN200-500m and PLN500-1500m of 52-week Treasury Bills.

As usually at the start of the month, today the Ministry of Finance will release inflation forecast for October. We expect a drop in CPI growth to 3.9-4.0%YoY amid monthly increase of 0.1%. Market consensus predicts 4.2%YoY rise. Today in the euro zone and the US the activity indices for the manufacturing indices are going to be released. At 9:00 we will know the PMI index for the euro zone, where the market expects a drop to 41.3 pts from 45 pts in

September. At 15:00 GMT the ISM index will be released, which is forecast to decline to 41.8 pts from 43.5 pts.

Situation in international markets and still high volatility will remain main factors for domestic local markets in near time. This week, there are no domestic macroeconomic data releases in the agenda. However, the NBP is expected to start 3-month liquidity providing operations in the money market, which should help in improving market situation.

An important event, also from the point of view of domestic monetary policy, will be ECB decision on Thursday. Market consensus suggests a rate cut by 50 bp. Also, the Bank of England will announce the decision and is expected to cut rates by 50 bp. Monetary easing cycle is a global phenomenon right now and it affects not only the main central banks. Today during the session in Asia, the central bank in India cut interest rates, and further during the week the Bank of Australia may follow with another 50 bp cut. Some impact on the region may have decision of the Czech central bank, amid a speculation about monetary easing also in this country. In today’s *Rzeczpospolita*, MPC member Jan Czekaj said he does not rule out rate cuts, possibly even this year. For him, the most important data that may increase likelihood of cuts, will be data about industrial production growth.

Opinion that major economies has already fallen into recession will probably be confirmed by data due for release this week. The key focus of attention will be the US non-farm payrolls report due on Friday. Besides, we will get economic activity indicators for services from the euro zone and the US (expectations for further drop). The markets may be also influenced by outcome of the presidential election in the US (election day on Tuesday), as it could remove uncertainty and markets will be looking to see what impact this has on stock prices and risk sentiment in general.

Moreover, this week the European Commission will publish its semi-annual forecasts, which are likely to show significant fall of the forecasted pace of economic growth.

Rebound of the zloty in the past few days does exclude its further weakness in the near term, although the coordinated rescue actions from international institutions for the emerging markets as well as rate cuts by many central banks should support the zloty and limit its volatility. The debt market is unlikely to regain a standard liquidity in the near term, unless situation in the global markets stabilises. Relatively strong fundamentals of the macroeconomic parameters and prospect for the euro zone entry should support the domestic assets and lead to reduction in required risk premium.

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F/X rates (today's opening)

EURUSD	1.2873	CADPLN	2.2854
USDPLN	2.7302	DKKPLN	0.4720
EURPLN	3.5238	NOKPLN	0.4145
CHFPLN	2.3699	SEKPLN	0.3571
JPYPLN*	2.7454	CZKPLN	0.1462
GBPPLN	4.4712	HUFPLN	1.3685

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The zloty trading ranges

	min	max	open	close	fixing
EURPLN	3.5170	3.6556	3.6185	3.5170	3.6330
USDPLN	2.7750	2.8774	2.8522	2.7750	2.8472
EURUSD	1.2670	1.2783	1.2690	1.2682	-

T-bonds

TERM	BOND	Yield (%)	Change (bp)	Last auction	Average yield
2Y	OK0710	6.85	5	6.08	6.471
5Y	PS0413	6.80	2	1.10	5.926
10Y	DS1017	6.60	5	8.10	5.859

IRS rates (Mid)

TERM	PL		US		EA	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1Y	6.53	-1	2.54	3	4.03	2
2Y	6.32	-5	2.75	3	3.69	6
3Y	6.27	-4	3.18	-1	3.91	8
4Y	6.22	-4	3.55	2	3.92	7
5Y	6.17	-3	3.82	-1	4.02	8
8Y	5.99	-3	4.31	-1	4.32	13
10Y	5.82	-5	4.44	6	4.48	14

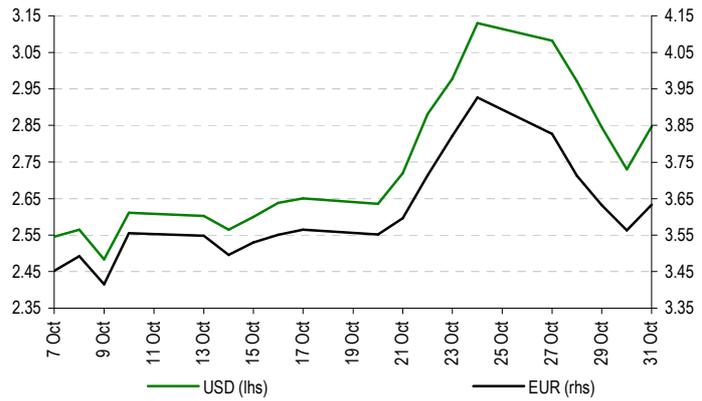
WIBOR rates

TERM	%	Daily change (bp)
O/N	6.28	156
T/N	6.28	2
SW	6.29	0
2W	6.40	1
1M	6.55	-1
3M	6.85	-1
6M	6.88	0
9M	6.90	-1
1Y	6.91	0

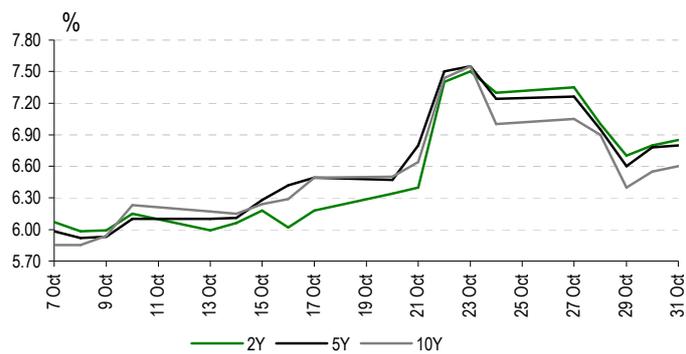
FRA rates (Mid)

TERM	%	Daily change (bp)
1X2	6.55	6
3X6	6.35	-4
6X9	6.15	-3
9X12	5.95	-9
3X9	6.34	-2
6X12	6.14	-3

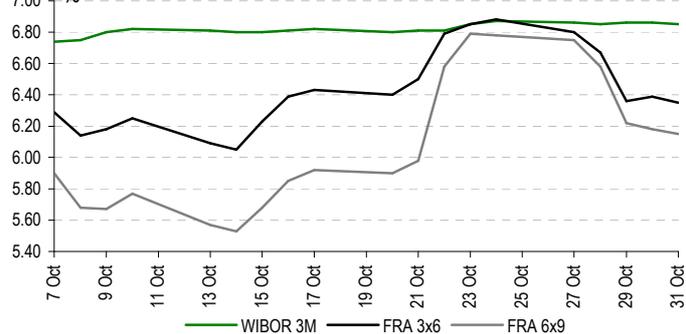
Zloty exchange rate (fixing)



T-bonds yields



3-month money market rates



* for 100 JPY

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