

Eyeopener – Pause in zloty weakening?

6 February 2009

- **Zloty rebounded together with other currencies in the region, further rise in market interest rates**
- **EBC kept rates on hold, BoE cut main rate to 1.0%**
- **Today, US non-farm payrolls data for January**

Yesterday currencies in the region recovered. In the first part of the day the Polish zloty was relatively stable. In the afternoon a significant strengthening of the Czech crown was visible, after the Czech central bank announced the decision to cut interest rates and published (for the first time in history) foreign exchange forecast. The forecast showed EURCZK rate at 25.8 on average in 2009, which is much below current level (27.9 today in the morning). Official rate was down 50 bp to 1.75%. Also, at the end of the session the Hungarian forint appreciated after the news release that the Hungarian central bank will improve liquidity in the foreign currency in the banking sector through FX swap instruments in EURHUF. This would limit demand for euro on the market from commercial banks. The EURPLN rate was down to 4.614 and USDPLN to 3.592 against 4.667 and 3.633 at the opening. Today in the morning the zloty appreciated further to ca. 4.60 against the euro and 3.60 against the dollar. During the day changes in EURUSD were quite limited. In the afternoon the US currency strengthened, but at the end of the day it went back to the opening level finishing the day at 1.284. Today in the morning it was lower at 1.275.

The interest rate market showed further rise in interest rates. IRS curve moved up by 6-10 bp and change in FRA rates was similar. Bond yields were also on the rise. In our opinion, the yields increase is rather a technical correction and we should see another drop in FRA and short-dated IRS after a series of weak upcoming economic data and next rate cuts by the MPC.

MPC member Andrzej Sławiński said yesterday in the interview with TVN CNBC that zloty weakening does not have to lead to higher inflation amid much lower demand in the economy and given quite high margins of importers. On the other hand, MPC's Jan Czekaj said the foreign exchange changes may have an impact on the decision during the next meeting. However, he did not rule out a cut in February and added that rates level is still relatively high as compared to other countries. And thus next moves in rates should take place quite fast. What is more, Czekaj said that official rate reduction to 3.0-3.5% is well justified and he did not exclude a possibility of the MPC cutting rates to below 3% level. Also, dovish member of the Council, Stanisław Nieckarz, was convinced that zloty weakening is of short-term nature and should not be an obstacle to continue with rate cuts, as further monetary easing will improve fundamentals of the Polish economy and thus will help the currency. Dariusz Filar reiterated in an interview with

Rzeczpospolita daily that the zloty weakening advises caution with interest rate reductions. He also added that at the nearest meeting the MPC will discuss a possibility of FX intervention if it appeared that it could threaten the inflation target. On the other hand, Filar also admitted that there should be a recovery in some time and investors "will start to notice that the Polish economy is going to develop better than the region". In our view the recorded scale of zloty depreciation should not be an obstacle in interest rates reduction, as the scale of the economic slowdown (which will be indicated by the January figures) is so significant that the influence of the exchange rate on inflation should not threaten the inflation decline. Nevertheless, due to situation in the FX market the scale of interest rate cut in February will be rather 50 bp than 75 bp.

According to yesterday's report, Fitch Ratings cut 2009 GDP forecast for Poland to 1.2%.

The number of new jobless claims in the US increased last week to the highest level for 26 years, i.e. 626,000. In turn, a rise in labour productivity in Q4 reached 3.2% and was higher than predicted. Factory orders fell by 3.9%MoM versus expected -3%. These data contributed to strengthening in the US debt market in the first part of the day. Later on, there was a correction. German bunds were supported by hints from EBC president that the bank may continue monetary easing to prevent European economy from global recession. Also, good results of bond auctions in France and Spain were positive for the debt market, while in Germany there were next weak data released, showing another decline (-6.9%MoM, -25.1%MoM) in factory orders. Yields of 10Y Treasuries and Bunds fell in the first part of the day from 2.91% and 3.37% to 2.87% and 3.33%, and later on they rebounded to 2.90% and 3.34%.

The ECB left the parameters of monetary policy unchanged and the main refi rate remained at 2%. The president of the ECB suggested that the interest rate reduction at the March meeting would be close to 50 bp rather than 25 bp. In our view there is a possibility that interest rate will be cut even to 1% this year due to very poor prospects of the euro zone economy amid GDP growth contracting in our view by 2% and slight recovery by 0.5% in 2010.

The Bank of England reduced interest rates by 50 bp to 1%, the lowest level in history.

Today at 14:30 CET we will know the US data from the labour market – the crucial figure scheduled for this week. According to market forecasts the non-farm payrolls fell in January by 520k after drop by 524k in December. The unemployment rate is expected to 7.5% from 7.2%.

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F/X rates (today's opening)

EURUSD	1.2757	CADPLN	2.9119
USDPLN	3.6094	DKKPLN	0.6179
EURPLN	4.6045	NOKPLN	0.5266
CHFPLN	3.0774	SEKPLN	0.4361
JPYPLN*	3.9709	CZKPLN	0.1649
GBPPLN	5.2944	HUFPLN	1.5759

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The zloty trading ranges

	min	max	open	close	fixing
EURPLN	4.6140	4.6726	4.6681	4.6140	4.6455
USDPLN	3.5900	3.6492	3.6446	3.5920	3.6112
EURUSD	1.2765	1.2898	1.2838	1.2840	-

T-bonds

TERM	BOND	Yield (%)	Change (bp)	Last auction	Average yield
2Y	OK1110	5.10	6	35.01	5.022
5Y	PS0413	5.41	14	35.02	5.307
10Y	DS1017	5.80	5	17.12	5.724

IRS rates (Mid)

TERM	PL		US		EA	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1Y	4.22	6	1.29	-4	2.01	-3
2Y	4.60	14	1.61	-4	2.17	-2
3Y	4.71	14	2.00	-3	2.49	-1
4Y	4.80	12	2.31	-2	2.76	-1
5Y	4.88	10	2.53	-1	2.99	11
8Y	5.04	6	2.95	0	3.49	0
10Y	5.19	9	3.12	0	3.73	0

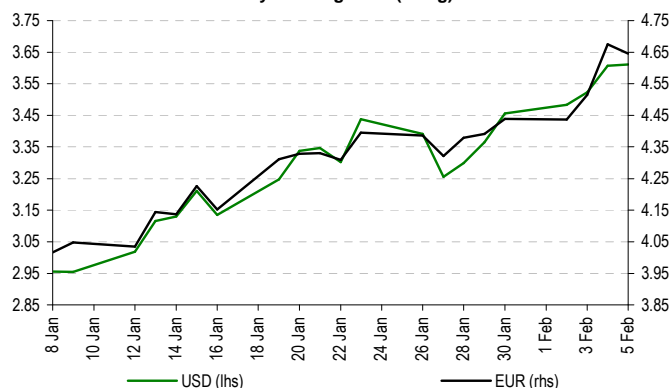
WIBOR rates

TERM	%	Daily change (bp)
O/N	4.24	2
T/N	4.30	2
SW	4.34	0
2W	4.38	-1
1M	4.46	-1
3M	4.74	-2
6M	4.82	-2
9M	4.85	-1
1Y	4.84	-2

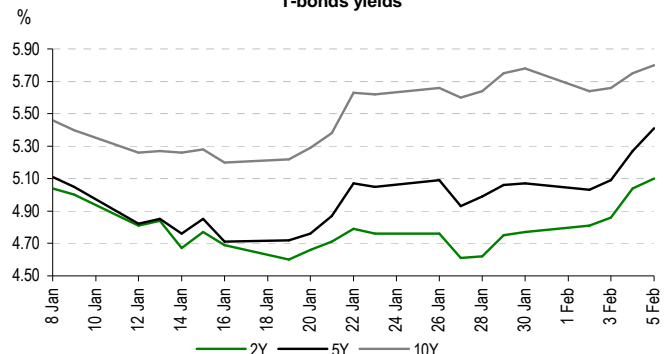
FRA rates (Mid)

TERM	%	Daily change (bp)
1X2	4.13	-16
3X6	3.89	8
6X9	3.90	6
9X12	4.02	10
3X9	4.02	10
6X12	4.05	10

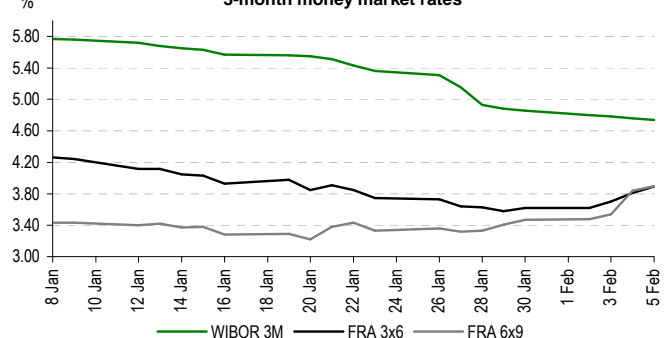
Zloty exchange rate (fixing)



T-bonds yields



3-month money market rates



* for 100 JPY

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