

Eyeopener – Successful auction of Polish bonds

5 August 2010

- Zloty gained thanks to successful auction of local bonds and higher risk appetite
- Sentiment in global markets improved due to better than expected macro figures from the US and earnings reports
- Multiyear Financial Plan discussed in the parliament, but still not published
- Today markets will focus on the ECB meeting, the US jobless claims data and next earnings reports

During the first part of Wednesday's session the sentiment in the market was not very optimistic. Concerns about the condition of the global economy were present in the context of weak US macro data released on Tuesday and the appreciation of the yen (in response to the increase in risk aversion), which may harm the export-oriented economy of Japan. This initially led to a weakening of risky assets and emerging market currencies. At some point, market sentiment towards the currencies of our region has improved a bit due to the fact that the IMF and the EU welcomed Romania's fiscal measures, and recognized that the country meets the conditions necessary to continue using the aid program worth €20bn. Key factors for the markets behaviour in the rest of the day were, however, the macro data from the euro area and the US. PMI index for the service sector in the euro zone rose in July to 55.8, against the expected 56.0 and June's 55.5. Retail sales in June in the euro area was also better than expected, showing an increase of 0.4%YoY against 0.1% expected and 0.6% in May after revision. Better than forecast data were released in the US. The ADP report in July showed an increase in employment of 42k, against the expected 40k and 19k after revision in June. The July ISM index for the service sector was also above forecast, showing an increase to 53.4 against 53.0 expected. There were fairly positive information coming yesterday from international credit markets. Portugal without any problems sold two-year bonds worth €1.165bn (more than planned). After a good macro data from the US and optimistic financial reports of companies published overnight (including a rise in profit forecast by Toyota), stock markets yesterday in the US and today in Asia have strengthened. The exception was China, where investors were alarmed by the tightening of stress-tests conditions by the regulator (doubling of the scale of possible decline in property prices up to 60%).

At the beginning of the yesterday's session the zloty depreciated as there was negative market sentiment globally. The upward trend of the EURPLN was constrained by the level of resistance at 4.02 (indicated in our previous daily reports). Later in the day the zloty was gaining and EURPLN was testing the support at 3.98. The expected trading range for today's session for EURPLN is 3.98-4.00.

The EURUSD remained stable during the first part of the yesterday's session and only after the US data the dollar started to appreciate. The EURPLN declined below the level of support at 1.32 and then headed towards 1.31, indicated in yesterday's Eyeopener. The downward trend was halted at around 1.315. Today we expect EURUSD to rise.

At the beginning of the session the core debt markets reflected concerns about the condition of the global economy, which resulted in declines in yields of Bunds and Treasuries. However, gains in yields were seen later, as a consequence of a rise in risk appetite. At the end of the day, yields of 10Y Bunds and Treasuries were 2.6% and 2.93%.

The domestic debt market rebounded yesterday after earlier weakening was dominated by market correction, preceded by high gains. Even before the auction slight declines in yields were observed, since investors, expecting good sales results, wanted to buy bonds a bit cheaper. The MinFin sold bonds worth PLN6bn (the top limit of planned offer and the record high value of sales at one auction) with demand of PLN12.5bn. The average yield was 4.76% (4.74% at previous auction), while in case of 5Y bonds it was 5.43% (5.37%). In relation to the high demand a top-up tender was held, at which 2Y bond worth PLN750m and 5Y bonds worth PLN450m were sold.

Yesterday in the parliament, Prime Minister Donald Tusk and Finance Minister Jacek Rostowski presented information about the state of public finances. They presented new details of the Multi-Year Financial Plan (contrary to earlier information released by the media, the document has not been officially published yesterday and according to *Rzeczpospolita* daily it will be released within 2-3 days). Changes in the VAT rate will take a slightly different shape than previously reported. The rate of 3% on unprocessed food will rise from 3% to 5% (i.e. the minimum required by the EU, while 6% was previously suggested), and the rate of the processed food will fall from 7% to 5% (rather than 6%). Rates for other goods and services will increase as announced by 1pp (preference to 8% and the standard to 23%). In addition, the VAT rate may conditionally (amid risk of breaching the 55% for the ratio of public debt to GDP) increase by a further 1pp in the middle of 2011 and the next 1pp in the middle of 2012. According to our estimates, changes to the VAT may give a direct effect of about 0.6pp increase in inflation in 2011, though this may be limited by smaller margins for retailers operating on competitive markets. On the other hand, there may be indirect effects and strengthened inflationary expectations (especially that further increases in VAT are possible).

Today, markets will focus on the ECB meeting. The decision on interest rates will be announced at 13:45 CET. It is widely expected that the interest rates will remain unchanged. Amid the inflow of good macro data from the euro area, it is possible that the tone of comments from ECB President will be tightened somewhat, although expectations for interest rate hikes in the euro zone should not strengthen significantly in our view. At 14:30 CET the weekly data from the US labour market will appear (expected decline in new jobless claims to 454k from 457k in previous week). Earnings reports for Q2 will be released, among others, by Barclays, Fannie Mae, Freddie Mac, Rio Tinto and Walt Disney. For international debt markets an important test today will be auction of bonds in Spain, at which papers worth €2.5-3.5bn will be offered.

ECONOMIC ANALYSIS

ul. Marszałkowska 142, 00-061
email: ekonomia@bzwbk.pl

Maciej Reluga (Chief Economist)
Piotr Bielski
Piotr Bujak

fax +48 022 586 83 40
Web site: <http://www.bzwbk.pl>
+48 (0) 22 586 83 63
+48 (0) 22 586 83 33
+48 (0) 22 586 83 41
+48 (0) 22 586 83 42

TREASURY SERVICES

Poznań
Warszawa
Wrocław

+48 (0) 61 856 5814/25
+48 (0) 22 586 8320
+48 (0) 71 370 2587

F/X rates (today's opening)

EURUSD	1.3159	CADPLN	2.9814
USDPLN	3.0310	DKKPLN	0.5353
EURPLN	3.9870	NOKPLN	0.5056
CHFPLN	2.8767	SEKPLN	0.4241
JPYPLN*	3.5173	CZKPLN	0.1619
GBPPLN	4.8170	HUFPLN	1.4186

Financial market review - 4 Aug 10
The zloty trading ranges

	min	max	open	close	fixing
EURPLN	3.9830	4.0258	4.0110	3.9940	4.0200
USDPLN	2.9935	3.0505	3.0350	3.0393	3.0448
EURUSD	1.3130	1.3232	1.3219	1.3143	-

T-bonds

TERM	Yield (%)	Change (bp)	Last auction	Average yield
2Y	4.75	-2	7.07	4.74
5Y	5.42	-3	12.05	5.144
10Y	5.73	-5	16.06	5.791

IRS rates (Mid)

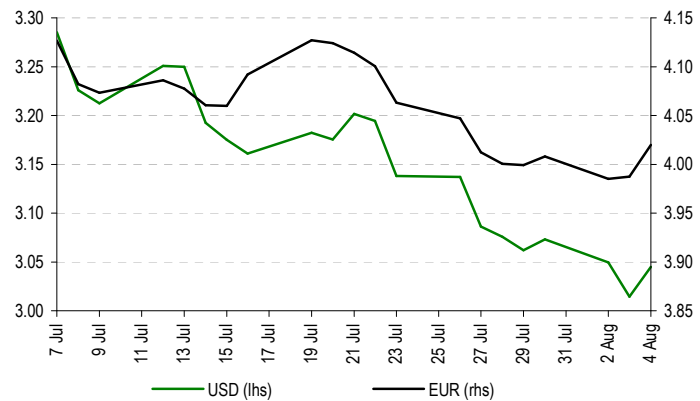
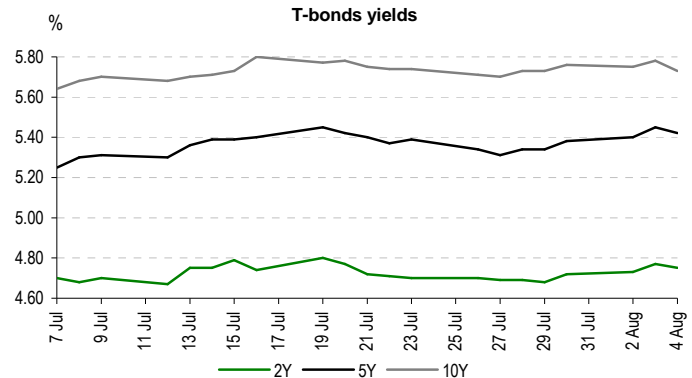
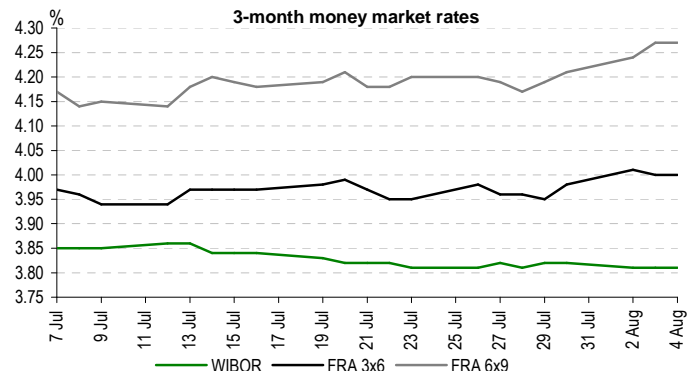
TERM	PL		US		EA	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1Y	4.19	-1	0.46	0	1.22	-3
2Y	4.71	0	0.69	-3	1.39	-4
3Y	4.95	0	1.00	-5	1.62	-11
4Y	5.10	0	1.35	-7	1.86	-6
5Y	5.19	0	1.70	-7	2.10	-7
8Y	5.31	0	2.52	-7	2.65	-8
10Y	5.30	0	2.85	-5	2.89	-8

WIBOR rates

TERM	%	Daily change (bp)
O/N	3.27	1
T/N	3.28	-1
SW	3.34	0
2W	3.44	0
1M	3.60	0
3M	3.81	0
6M	3.99	0
9M	4.19	1
1Y	4.23	0

FRA rates (Mid)

TERM	%	Daily change (bp)
1X2	3.63	0
3X6	4.00	0
6X9	4.27	0
9X12	4.51	0
3X9	4.18	0
6X12	4.46	0

Zloty exchange rate (fixing)

T-bonds yields

3-month money market rates


* for 100 JPY
Source: Reuters

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Additional information is available on request. Please contact Bank Zachodni WBK S.A. Treasury Division. Economic Analysis Unit. ul. Marszałkowska 142. 00-061 Warsaw, Poland. phone (+48 22) 586 83 63. email ekonomia@bzwbk.pl. <http://www.bzwbk.pl>



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