Bank Zachodni WBK

Eyeopener – Focus on the euro zone summit

21 July 2011

- **Further improvement in market sentiment amid moderate optimism regarding the euro zone summit and negotiations on debt limit in the US**
- **EURPLN below 4.0, slight gains of local bonds**
- **Core inflation stabilised in June**
- **Today focus on the euro zone summit while other events include auction of 10Y bonds locally, auction of 10Y and 15Y bonds in Spain, flash PMIs in the euro zone, many macro indicators in the US and next earnings reports.**

The improvement of sentiment on the global markets, which initiated on Tuesday, continued during yesterday's session. Ahead of today's summit of the euro zone leaders some careful optimism emerged and although the market realises that all the problems cannot be solved by one move, the investors still hope for some progress is stabilising the situation on Greece and other countries burdened with debt problems. This was supported by comments of the German and French politicians, who said that the differences between leaders of particular countries are not as large as the media suggests and they can be ironed out during the euro group meeting so a consensus is probable. The sentiment's improvement was also supported by information about some progress in talks about raising the debt ceiling in the USA. Really good financial results of Apple were offset by weak results of healthcare sector, so the gains of main stock indices in the USA were moderate. Also the data on home sales in the USA disappointed, but it was not crucial for the market. In spite of rising risk appetite recently, the markets are still in vigilant mode and fear that the improved mood be only temporary, especially if the political decision to be made in upcoming days do not live up to expectations. The impact of uncertainty was visible after close of domestic session, when the stock indices in the USA began to lose and eventually ended the day in negative territory. The today's session in Asia was not successful as well, which was due to a drop of flash Chinese PMI in manufacturing for July to 48.9 (for the first time in a year below the neutral mark of 50.0). After yesterday's meeting of the German chancellor and the French president (in which also the ECB Governor took part, though via phone) no important communiqué was issued, but it was stated that the details of agreed solutions will be revealed after today's summit of euro zone leaders.

The euro continued yesterday its upward tendency against the dollar, breaking the level of 1.42 this morning and heading towards resistance at 1.425, which was not broken. Today we expect a stabilisation while awaiting news from the euro zone summit. The further direction of the trading will depend upon the market's interpretation of taken decisions.

The zloty and other CEE currencies also behaved similarly as it happened in Tuesday, gradually trimming the previous losses. The EURPLN rate slid systematically, breaking the psychological level of 4.0 and dropping below 3.99. The CHFPLN declined to 3.421. This morning EURPLN tested the important support at 3.98. If the investors assess the outcome of the euro zone summit positively, a further zloty strengthening towards 3.95 is probable. Otherwise, the resistance may be again at 4.06.

Yields of domestic bonds once again fell slightly (by 2-4 bp), although activity in the market remained small. Investors were waiting for today's events: the meeting of the eurogroup and auction of 10-year bonds, which will measure attitudes towards the Polish securities. Results of today's bond auction in Spain will be also important.

In the core debt markets yields increased amid higher risk appetite. At the end of the day yields on 10-year Bunds and Treasuries were at 2.77% and 2.93%, correspondingly. This morning, they were 2.82% and 2.95%.

Core inflation excluding food and energy prices stabilized in June at 2.4%YoY, despite the drop in the headline CPI growth to 4.2% from 5.0% in May. The data was consistent with our estimates and did not have a significant impact on the market. Two other measures of core inflation also remained unchanged, and one (CPI excluding administered prices) decreased. In the coming months, we expect core inflation to rise, reflecting the fact that the inflationary impulse coming initially from food and fuel markets is gradually spreading to other price categories.

The NBP report on economic climate, published yesterday, showed that situation in the corporate sector has improved slightly in the second quarter, but expectations for the third quarter have deteriorated. In the second quarter firms recorded higher profit margins and improved demand, but they feared the economic downturn and lower demand in the future. The study points to weakening of inflationary expectations, although they remained at elevated levels. The pressure on wages has been growing, although it is still described as moderate (a scale of wage hikes below the long-term average). Firms increased capacity utilization, but investment activity remained low and was expected its decline even more. According to the NBP report, a factor that may influence investment decisions and changes in employment in firms is a sense of uncertainty regarding the outlook for the company and its environment.

ECONOMIC ANALYSIS

ul. Marszałkowska 142. 00-061
email: ekonomia@bzwbk.pl
fax +48 022 586 83 40
Web site: http://www.bzwbk.pl

Maciej Reluga (Chief Economist)	+48 (0) 22 586 83 63
Piotr Bielski	+48 (0) 22 586 83 33
Piotr Bujak	+48 (0) 22 586 83 41
Marcin Sulewski	+48 (0) 22 586 83 42
Marcin Luziński	+48 (0) 22 586 83 62

TREASURY SERVICES

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

F/X rates (today's opening)

EURUSD	1.4287	CADPLN	2.9538
USDPLN	2.7923	DKKPLN	0.5352
EURPLN	3.9835	NOKPLN	0.5124
CHFPLN	3.4004	SEKPLN	0.4373
JPYPLN*	3.5423	CZKPLN	0.1628
GBPPLN	4.5216	HUFPLN*	1.4864

*for 100JPY/100HUF

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The zloty trading ranges

	min	max	open	close	fixing
EURPLN	3.9850	4.0150	4.0065	3.9902	4.0014
USDPLN	2.8002	2.8335	2.8274	2.8107	2.8218
EURUSD	1.4157	1.4240	1.4170	1.4197	-

T-bonds

Bond (term)	Yield (%)	Change (bp)	Last auction	Average yield
OK0713 (2Y)	4.69	-3	9.06	4.848
PS0416 (5Y)	5.27	-3	18.05	5.614
DS1020 (10Y)	5.82	-3	12.01	6.215

IRS rates (Mid)

TERM	PL		US		EA	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1L	4.93	-1	0.47	0	1.90	-1
2L	4.98	-2	0.64	1	1.93	-2
3L	5.07	-2	0.97	2	2.18	0
4L	5.14	-2	1.36	2	2.36	0
5L	5.19	-2	1.76	1	2.56	-1
8L	5.29	-1	2.65	0	2.97	-1
10L	5.31	-1	3.02	1	3.16	-1

WIBOR rates

TERM	%	Daily change (bp)
O/N	4.56	4
T/N	4.56	1
SW	4.55	-1
2W	4.57	0
1M	4.61	-1
3M	4.71	1
6M	4.78	1
9M	4.81	0
1Y	4.86	0

FRA rates (Mid)

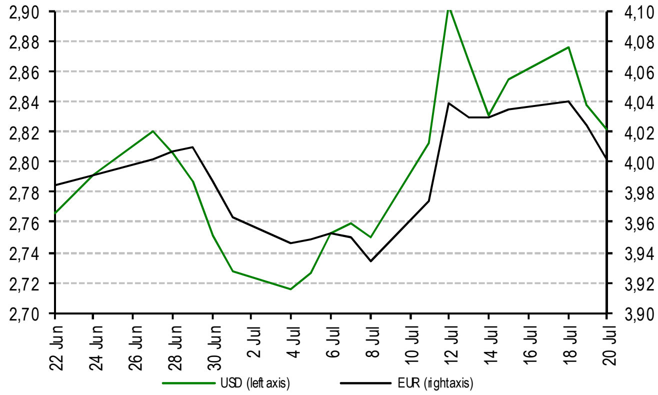
TERM	%	Daily change (bp)
1x2	4.64	-1
1x4	4.74	-1
3x6	4.83	1
6x9	4.91	0
9x12	4.95	0
3x9	4.88	-2
6X12	4.96	-2

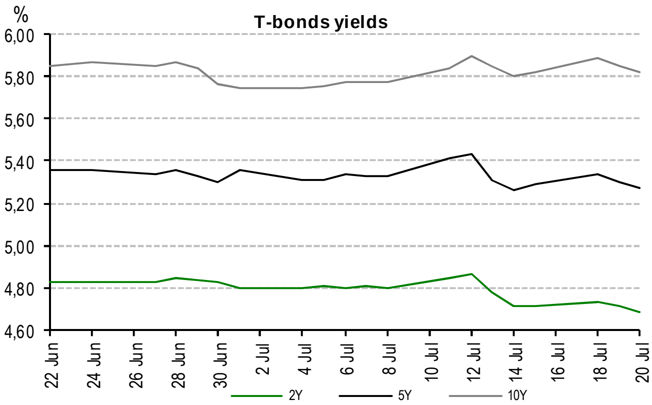
Measures of fiscal risk

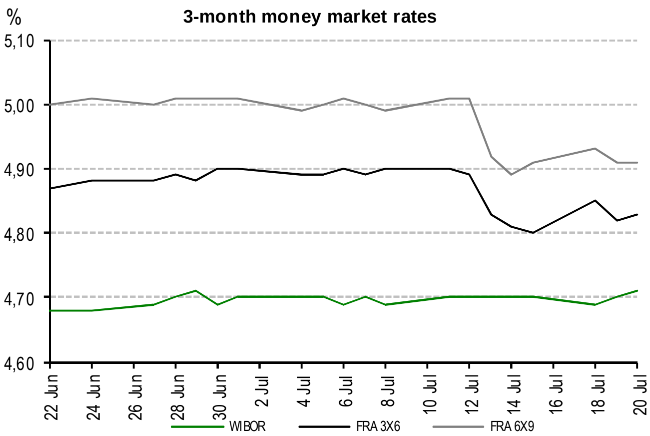
Country	CDS 5Y		Spread 10Y*	
	Value	Change (bp)	Value	Change (bp)
Poland	174.9	0	3.09	-6
Czech Republic	94.6	-3	1.06	-4
Hungary	317.9	-7	4.77	-5
Greece	2826.0	-1	14.79	-72
Spain	354.4	-28	3.27	-15
Italy	303.2	-23	2.89	-13
Portugal	1281.6	0	9.56	-70
Ireland	1249.1	0	10.55	-59
Germany	60.6	-2	--	--

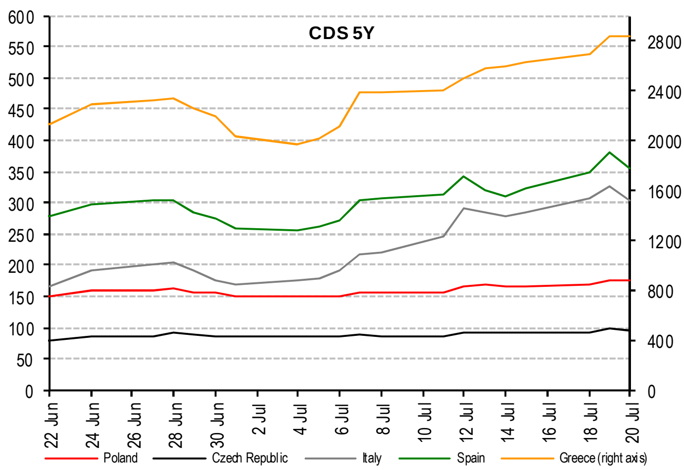
* 10Y treasury bonds over 10Y Bunds

Zloty exchange rate (fixing)









Source: Reuters

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST			LAST VALUE
					MARKET	BZWBK		
		MONDAY (18 July)						
	JP	Market holiday						
14:00	**PL**	**Wages in corporate sector**	**Jun**	**%YoY**	**4.8**	**6.5**	**5.8**	**4.1**
14:00	**PL**	**Employment in corporate sector**	**Jun**	**%YoY**	**3.5**	**3.5**	**3.6**	**3.6**
		TUESDAY (19 July)						
11:00	DE	ZEW index	Jul	pts	-12.4	-	-15.1	-9.0
14:00	**PL**	**Industrial output**	**Jun**	**%YoY**	**5.8**	**4.9**	**2.0**	**7.7**
14:00	**PL**	**Construction and assembly output**	**Jun**	**%YoY**	**18.4**	**18.4**	**17.0**	**23.9**
14:00	**PL**	**PPI**	**Jun**	**%YoY**	**5.6**	**6.0**	**5.6**	**6.3**
14:30	US	House starts	Jun	k	573	-	629	549
14:30	US	Building permits	Jun	k	590	-	624	609
		WEDNESDAY (20 July)						
14:00	**PL**	**Core inflation**	**Jun**	**%YoY**	**2.5**	**2.4**	**2.4**	**2.4**
16:00	US	Home sales	Jun	m	4.90	-	4.77	4.81
		THURSDAY (21 July)						
4:30	CN	Flash PMI – manufacturing	Jul		-	-		50.1
	PL	**Auction of DS1021 bonds worth PLN1.0-3.0bn**						
9:28	DE	Flash PMI – manufacturing	Jul	pts	54.0	-		54.6
9:58	EZ	Flash PMI – manufacturing	Jul	pts	51.5	-		52.0
14:30	US	Initial jobless claims	week	k	415	-		
16:00	US	Leading indicators	Jun	%	0.2	-		0.8
16:00	US	Philly Fed index	Jul	pts	5.0	-		-7.7
		FRIDAY (22 July)						
10:00	DE	Ifo index	Jul	pts	113.8	-		114.5
11:00	EZ	New industrial orders	May	%MoM	0.6	-		0.7

Source: BZ WBK, Parkiet, Reuters

* in case of the revision, the data is updated

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