



Central European Daily

The daily was written by CSOB in collaboration with KBC and the Central European Partners

Headlines

Currencies: Better performance equities supports CEE currencies, except Czech koruna

Fixed Income: Higher Polish inflation figures favour a July rate-hike

Currencies

Currencies	Close	change
EUR/CZK	28.55	0.1%
EUR/HUF	253.2	-0.1%
EUR/PLN	3.824	-0.3%
USD/PLN	2.880	0.2%
EUR/SKK	34.29	0.1%
EUR/USD	1.331	-0.1%
USD/JPY	122.4	0.6%

After a fairly weak opening above 3.84, the **Polish zloty** recouped part of the recent losses and retreated into the EUR/PLN 3.82 area benefiting from an improvement in regional sentiment later in the session. Along with the subdued reaction from bonds to the CPI numbers (which the zloty basically ignored) this only confirms the wait-and-see mode currently in place for the PLN.

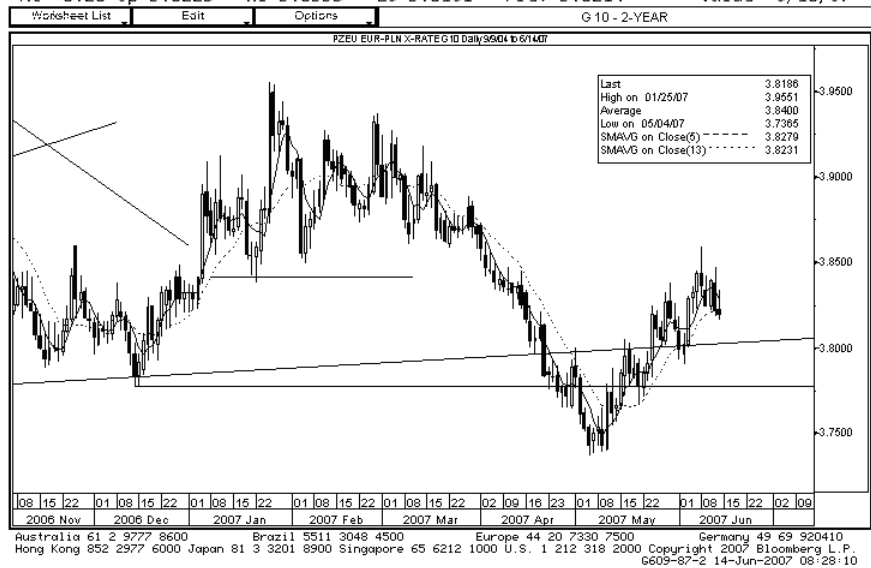
Even though we would be cautious not to overestimate the importance of yesterday's rebound with global yields no longer rising and equities doing stronger, the worst seems to be over for the PLN. This would suggest more consolidation or even an extension of yesterday's gains in the hours to come. The regional sentiment will once again be the driver as the domestic calendar contains only the non-market-moving money supply data.

The **Hungarian forint** witnessed a second wave of selling in the morning and the market tested the 255.00 level again triggered by developments in core bond and equity markets. Similarly to last Friday's move, the market started with a sharp weakening, but then calmed down and stabilized between 253.00-253.50. As we noted earlier, the positive fundamental outlook makes the HUF a good bet around 254.00-255.00, while prevailing volatility makes carry trades less attractive for the short-term hence the lack of risk appetite could be behind the forint vulnerability. Opening new HUF positions may require relatively large appetite for risk, which may be later rewarded with higher return, while more conservative players could decide to wait for some stabilization before positioning back into HUF.

Yesterday the **Czech koruna** surprisingly failed to track the positive reversal in the regional sentiment driven by the better performance of global stock and bonds markets. Hence the Czech currency stayed near nine-month highs at EUR/CZK 28.56. Today, the koruna still has the chance to catch up with the gains of the region as the positive sentiment on the emerging markets could prevail at least in the morning session. Nevertheless we cannot exclude the scenario in which the koruna once again ignores the regional optimism and stays under pressure. This would mean the EUR/CZK could test further resistances of the euro at 28.585/28.615

The **Slovak koruna** slightly corrected its previous losses and finished the session stronger at EUR/SKK 34.28 on the back of falling US yields. Today, the economic calendar is fairly light with only the May harmonized inflation for release. This figure should not play a role in today's trading, but the central bank usually comments on it. The koruna will remain sensitive to global markets development, with global yields in the focus. A modest consolidation of the currency could arrive on the market. However, until tomorrow's release of US inflation data, we do not expect any significant change of market sentiment.

EURPLN ↑ 3.8186 - .0028 WACH 3.8171/3.8201 WACH
 At 8:28 Op 3.8225 Hi 3.8335 Lo 3.8161 Prev 3.8214 Value 6/18/07



EUR/PLN: zloty shows quite good resilience in the face of the upheaval in core markets.

Fixed income

Bonds 2Y	Close	
Czech Rep.	3.50	0.05
Hungary 3Y	7.34	0.07
Poland	4.93	0.01
Slovakia	4.10	-0.40
Eurozone	4.50	0.00
USA	5.09	0.04

Bonds 10Y	Close	
Czech Rep.	4.37	0.00
Hungary	7.03	0.08
Poland	5.53	0.05
Slovakia 7Y	4.88	0.13
Eurozone	4.65	0.03
USA	5.22	-0.01

The higher than expected Polish May CPI was the highlight of the session, but **Polish bond markets** exhausted from continued selling in recent days took the report rather lightheartedly. In yoy terms inflation came in at 2.3% , i.e. 0.2 pp. above the market consensus and our expectations. In a reaction, yields inched up by 2-3 bps for longer maturities before retreating to pre-PCI levels in-line with core markets and held flat at the short end of the curve. Going into the details of the report the higher than expected number was mainly the result of the higher than expected rise in food prices (particularly fruit) and mildly faster fuel price growth. The implied core CPI turned out higher than in April as well. The market expected the net (ex food and fuel) inflation to stabilize at 1.5% y/y, instead the report confirmed our estimate of 1.6% y/y. While the data underpin our baseline scenario that inflation will reach a local peak in June (2.5-2.6% y/y) they will probably have little direct implications for monetary policy. We've tended to treat the expected (temporary) rise in inflation this month as a convenient circumstance (rather than reason) for the MPC to hike rates in July, but we have also stressed repeatedly that in the end the Council would put little weight to current data and focus on the 5-7 quarter perspective instead. This remains our conviction and we have no reason to change our view that rates will go up preventively once again in July to 4.50%, something the market does not yet fully appreciate.

Regarding today's trading, the subdued reaction to the CPI numbers clearly suggests that Polish bonds will continue to look to core markets for inspiration today. In this respect the US PPI numbers will be of utmost importance and if the report comes in benign for the third month running this may mark an end to recent selling wave as treasuries were already reluctant to move lower after the strong retail sales data and higher-than-expected US import prices yesterday.

The **Hungarian bonds** suffered again from currency volatility. The market not just followed core markets, but even underperformed them, as investors are demanding compensation for volatility as well. As a consequence, spreads over eurozone widened and the inversion of the curve continued to decrease. Selling pressure is more concentrated on the 5Y and 10Y segments, while the sub-2Y area seems relatively protected. Sentiment did not improve much after EU Commission reassured that the Hungarian Convergence Program is on track, which should have had a fairly positive impact otherwise.

On Wednesday, **Czech bonds** could not find any incentives on the domestic market and mirrored eurozone bond developments, losing ground. The auction of 4.70%/2022 was not fully successful. The demand for CZK 7 mld. exceeded the offer only 1.1 times with no interest from abroad. At the end, the ministry of finance sold bonds for CZK 4.3 bln., the rest the ministry kept for himself. However, the reason was not in high yields only, but very likely the ministry also does not need so much money at the moment. The trading session closed sooner and could not follow the yield decrease on core markets. Therefore, the Czech yield curve moved higher by 3 to 6 bps and flattened.

Today, the Czech PPI will be released. It should fall, but will hardly influence the market. Therefore, Czech bonds might copy core markets developments, where there is a possibility of some consolidation. However, the mood for bonds may remain still negative.

Tables of rates

IBOR 3M			Close			FRA 3x6			Close			Central Bank Rate		
Czech Rep.	2.92	0.01	Czech Rep.	3.23	-0.01	Czech Rep.	2.75	25						
Hungary	7.81	0.00	Hungary	7.52	0.03	Hungary	8.00	25						
Poland	4.47	0.00	Poland	4.70	0.01	Poland	4.25	25						
Slovakia	4.27	0.00	Slovakia	4.29	0.00	Slovakia	4.25	-25						
Eurozone	4.15	0.00	Eurozone	4.36	0.00	Eurozone	3.75	25						
USA	5.36	0.00	USA	5.39	0.01	USA	5.25	25						

IRS 2Y			Close			IRS 10Y			Close			STOCKS			close		
Czech Rep.	3.74	0.01	Czech Rep.	4.52	0.03	PX	1842.6	-0.1%									
Hungary	7.38	0.04	Hungary	6.98	0.09	BUX	26469.8	0.6%									
Poland	5.27	0.05	Poland	5.62	0.02	WIG	63845.7	0.6%									
Slovakia	4.71	0.05	Slovakia	4.96	0.02	Eurostoxx	4399.11	0.3%									
Eurozone	4.75	0.01	Eurozone	4.93	0.03	DAX	7662.5	0.0%									
USA	5.54	0.04	USA	5.39	-0.01	S&P	1504.3	0.4%									

Closing or snapped values at 16:30 CET, change is over previous day, last change in bps

Calendar

Period	Period	KBC	Consensus	Previous
Thursday June 14				
09:00 CZ PPI m/m y/y	May 07	0.3/3.8	0.4/3.8	0.6/3.7
09:00 SK HICP m/m y/y	May 07	0.2/1.7	0.2/1.7	0.1/1.9
14:00 PL M3 y/y	May 07	18.7		19.0
Friday June 15				
09:00 CZ Current account (CZK bn)	April 07	-5.5	-9.0	8.3
09:00 HU Industrial production y/y, details	April 07			
14:00 PL Budget Deficit PLN bn	May 07	4.43		2.07
14:00 PL Current Account EUR m	April 07	-500	-535	-300
14:00 PL Trade balance EUR m	April 07	-400		-200

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