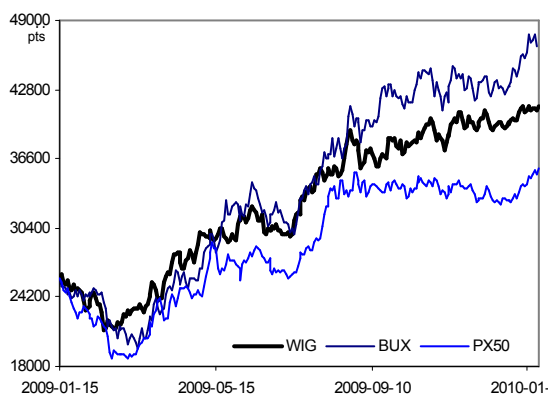




Equity Market

WIG	41 256
Median 2009 P/E	15.2
Median 2010 P/E	14.1
Avg daily trading volume (3M)	PLN 1 345m

WIG vs. indices in CEE region



Top Ratings:

Overweight:

Defensive companies: PGNiG, TPSA, LWB, Bank Handlowy

Underweight:

Large banks (PKO BP, Pekao, BZWBK), KGHM, Lotos

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Equity Market In 2010

Investment Strategy

Despite the improving macroeconomic situation in Poland (positive surprises are still quite possible) and due to the uncertain situation in global markets and the expected supply of stocks in the secondary market from the State Treasury (PLN 35bn), we expect 2010 to be weaker for the stock market than is expected under the market consensus (-5/+5% vs. +10-15%). We have particular concerns for the first half of the year, when we recommend taking advantage of the good opening to the year (WIG20: 2500-2550) and increasing exposure to defensive companies (PGNiG, TPSA, LWB, Bank Handlowy) at the expense of high-beta companies (big banks, KGHM, Lotos).

In 2009, we witnessed high volatility in the prices of shares, commodities and currencies. During the first two months of the year, investors closed positions in practically speaking all assets with any risk component. Since March, we have been observing rapid increases in prices, which discounted the upcoming economic revival, harbingered by the rising leading indicators. This has been accompanied by a weakening USD and interest rates virtually at 0% in the USA and a very low level in Euroland. Low expectations for macroeconomic data and company earnings have left a lot of room for huge surprises on the upside. The result has been a dramatic increase in the appetite for risk over the course of the following months. The strategic consensus for 2010 is very similar: 10-15% increase in stock prices, weak USD, expensive commodities, emerging markets as the investment blockbuster. The equity market does like to take us by surprise, however.

In our strategy for 2009, we accurately predicted that the declines in share prices at the start of the year would provide an excellent opportunity to buy, because the global economy would not go into a free fall, as many analyses published at the time suggested. That said, we believe that the phase of rebound after the sharp drops in industrial production and consumption is already over, or rather that is generously discounted by the markets. According to Commerzbank's forecasts for this year, the US GDP will increase by 2.5% (compared to the 2.5% decline in 2009), with inflation at 1.8% (compared to 0.3% deflation in 2009). For Poland, we expect GDP growth at 3%, with industrial production increasing by 10% and consumption by 3-4%.

In the following months, the macroeconomic data, and in particular industrial production data, will improve considerably in the USA as well as in Poland, showing rapid y/y growth due to, inter alia, restocking and low base of comparison. Still, we believe that investors have already discounted the data that are in line with market consensus. Better-than-expected macroeconomic data, in particular from the labor market and the realm of consumption, will be interpreted as a harbinger of faster interest rate increases (leading to a stronger dollar, the closing of carry trades, and a dynamic 2-4 month correction in upwards trend). In turn, any data below expectations, especially on consumption, will bring about an understandable disappointment and generate concerns about the condition of the economy in 2011-2012. The latter scenario appears more likely to us, given how "sluggish" the revival has been on the demand side (private consumption) in developed countries.



Are the United States, which we believe will determine the global sentiment to equity markets, undergoing a lasting economic revival or a mere rebound? In the past, each period of boom on US stock markets entailed increased consumption driven by increased household indebtedness relative to the GDP. Deleveraging, or more precisely, non-increase in this indicator in the 1970s entailed a horizontal trend for the indexes. The 2003/2007 boom and bull market came at a cost of an increase in US household debt from 80% to 96% of GDP. We find it hard to imagine that the FED should allow the problem to deepen further. The element that kept many investors away from the equity market in early 2009 and made it impossible to take advantage of the strong rebound will cause worries in 2010 as well.

In 2010, the increase in risk aversion in equity markets is likely to be driven directly by such factors as the need to cool down the Chinese economy, which grew at over 10% in late 2009 and early 2010 while borrowing expanded by over 30% (this might be a particularly heavy blow to commodity markets), capital problems faced by European banks, including those caused by the requirements of Basel 2, and the considerable problems with public debt in such countries as Greece, Ireland, Italy or Spain.

Given the structure of assets of the individual groups of investors present on the WSE, 2010 will be another year when the local market will be driven by global capital flows rather than domestic macroeconomic conditions and company earnings. We do not expect retail clients who invest in the stock market directly or through investment funds to increase their activity over the next few months (their funds remain deposited with the banks). Demand for equities from pension funds will remain steady, but if the government's plans to reduce premiums paid to them from 7.3% of salaries to 3% become law in the parliament, the funds' purchasing power will be considerably reduced (stocks currently account for 31% of their assets). This is particularly important in the context of the Treasury's plans to sell state-owned shares (for a total of ca. PLN 30bn in H1'10) – this supply should saturate the demand from domestic capital (individuals and institutions). This means that the broad market is likely to underperform the blue chip index, which is where the global capital flows.

Given global and local conditions, especially the planned IPOs, we expect the stock market to disappoint investors in 2010. We believe indexes will shift by -5%/+5%. The year will start strong, but the ensuing months will bring a correction to the upwards trend that has held sway over the market since March 2009. As a result, our strategic recommendation for H1 2010 is increasing portfolio allocation to defensive companies (PGNiG, TPSA, LWB, Bank Handlowy) at the expense of high-beta companies (big banks, Lotos, KGHM). In the case of small and medium companies, careful selection will be the key and the broad market will underperform WIG20.

Global Economy Rising after the Crisis

- The economic situation in the world will be improving, although given the investors' mounting expectations, disappointments will become increasingly frequent.
- Investors will pay less and less attention to leading indicators, which might start to go down from their current levels (at the moment they remain above 50, harbingering economic growth), and more and more attention to hard macroeconomic data, which must now confirm that economic growth is here to stay (the cycle). In the developed countries, this applies particularly to the labor market and to consumption, as well as the real-estate market.
- As the macroeconomic data improve, the inflationary pressure will be on the rise and central banks will give up on monetary loosening. At present, the market consensus still expects first interest rate increases in late Q3 or early Q4. If the macroeconomic data are close to expectations, we would expect interest rate hikes earlier, towards mid-year, which will push up market interest rates at the short end of the yield curve, cooling down the equity and commodities market for several months.
- The emerging markets, whose growth is forecasted at 5.5-6%, and in particular the Asian countries (7%), will lead the world in growth. The CEE region, which is more dependent on the situation in Europe's biggest economies and more indebted than Asia, will see ca. 3% GDP growth.
- The fastest-growing economies in the region should be Russia and Turkey (5%), while Hungary and Bulgaria will fall behind, hovering on the brink of recession.

Poland: the Battle Has Been Won

Despite the breakdown in external markets and the considerable drop in investment (lack of bank financing, reduction in foreign investment, counterbalanced by increase in state- and EU-funded infrastructural investment), and thanks to the strong internal consumer demand, the Polish economy has emerged from the global crisis in a much better shape than most macroeconomists forecasted as recently as a year ago. 2010 is also looking better than the current consensus assumes.

The leading indicators for industrial production in Poland, as well as for the key buyers of Polish exports in the EU (i.e. primarily Germany), confirm that economic revival is indeed happening. This leads to stabilization in the labor market, which has recorded much more limited reduction in employment than the analysts forecasted as recently as a few months ago. As a result, the negative impact of the crisis on consumer demand is more limited, making it possible to rebuild demand fairly quickly. The economy has achieved equilibrium when the PLN is considerably weaker, to the joy of exporters as they prepare for considerable increases in volumes.

According to the consensus forecast, the Polish GDP grew by 1.2-1.5% in 2009, which is an excellent result in comparison to other European countries (Euroland -3.9%, Czech Republic -4.8%, Hungary -6.5%) and a good score compared to other emerging markets (India, China +7%). Thanks to the depreciation of its currency and the relative strength of its internal demand, Poland felt the collapse in demand less than other countries of the region.

The outlook for 2010 remains optimistic, with GDP set to increase by 2% according to the consensus and 3% according to BRE Bank, but this no longer looks that impressive in comparison with the other emerging markets due to, inter alia, a base effect. Economic growth will be accompanied by declining inflation and increasing employment. As salaries start to go up, consumer demand will recover, although nearly twice as slow as manufacturing (year on year).

Macroeconomic forecasts for Poland in 2010

	GDP		CPI	
	2010	2010	2010	2010
IBnGR	2.2%	2.4%	IMF	2.2% 2.6%
CASE	3.2%	2.1%	NBP	3.5-4% 2.5%
KE	1.8%	1.9%	OECD	2.5% 2.2%
BRE BANK	3.0%	2.8%	Danske Bank	2.0% 3.0%
BPH	2.0%		Ceska Sporitelna	2.6%
Bank of America Merrill Lynch	3.5%	3.0%	Deutsche Bank	1.2% 2.9%
Pekao	1.7%	2.8%	UniCredit MIB/CA-IB	2.3%
Bank Zachodni	1.6%	2.3%	DZ Bank	2.3% 2.3%
Brown Brothers	2.0%		Goldman Sachs	2.8%
Capital Economics	1.0%	2.2%	Invest Bank	3.1% 2.4%
Citigroup	2.6%		Moody's Economy.com	1.8%
Commerzbank	3.0%	3.6%	Morgan Stanley	2.8% 2.6%
Raiffeisen Zentralbank Österreich	1.3%	2.4%	PKO Bank Polski	1.8%
Royal Bank of Canada	2.0%	2.6%	PKPP Lewiatan	2-2.5%

Source: PAP, Bloomberg

Macroeconomic forecasts for Poland by quarter (BRE Bank)

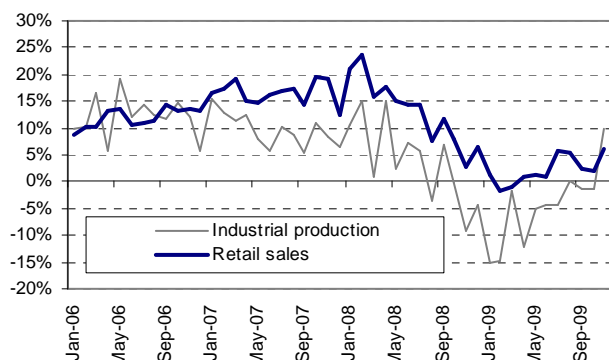
	GDP	CPI	Unemployment	Salaries	Consumption	Industrial production
Q4'09	3.2%	3.3%	12.0%	4.0%	2.2%	7.0%
Q1'10	3.1%	3.2%	12.6%	4.5%	2.6%	8.7%
Q2'10	2.9%	2.2%	12.2%	4.8%	3.0%	10.1%
Q3'10	3.9%	2.1%	12.3%	5.0%	3.3%	8.7%
Q4'10	4.1%	2.7%	12.5%	5.2%	3.6%	9.6%
Q1'11	3.7%	2.7%	12.4%	5.3%	3.7%	10.1%
Q2'11	4.0%	2.8%	10.8%	5.4%	4.3%	9.0%

Source: BRE Bank

The Revival In Industrial Production...

The industrial production data for November, recently released by the Central Statistical Office, indicate y/y growth of 9.8% (vs. -1.3% y/y in October). November is the first month whose y/y base of comparison encompasses a period of breakdown caused by the global crisis. In the next few months, this effect will send the y/y growth rate above 10%, which in turn will boost investor sentiment. Of course, in addition to this statistical artifact, the observed economic revival is hugely impacted by the revival in the German economy as well as the situation in the construction industry, which remains strong (+10% y/y, partially because the weather conditions made work on infrastructural projects possible).

Industrial production and retail sales

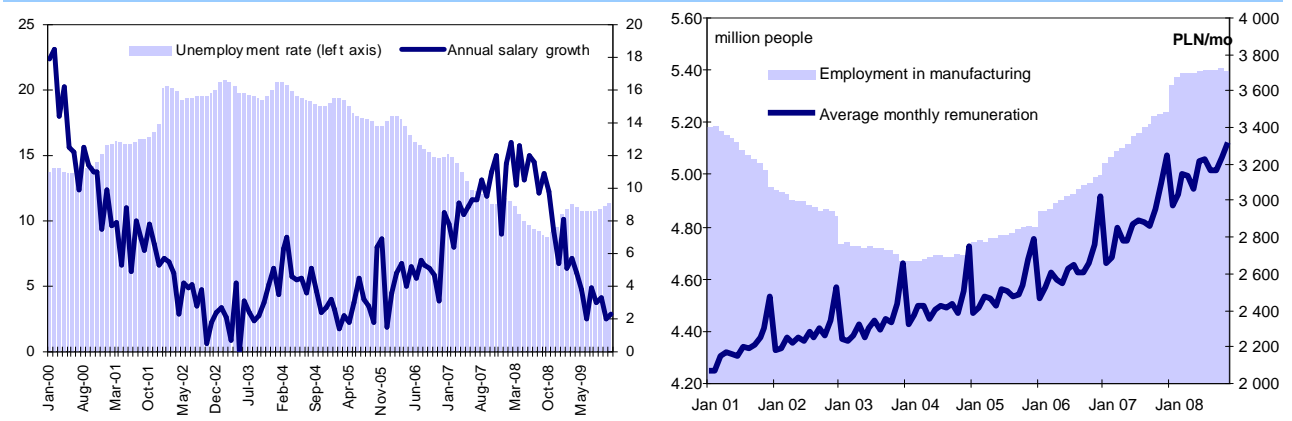


Source: Central Statistical Office

... Supports The Labor Market, Which ...

Contrary to expectations, the labor market proved extremely resilient to the impact of the crisis, which might be a consequence of the recruiting problems the employers had faced prior to the crisis. While company sales broke down quite dramatically in early 2009, production started to recover just a few months afterwards. Companies reacted very fast to the decline in demand, cutting their costs, for example by laying staff off in the early stages of the crisis or even before it hit Poland (but was visible in other countries), allowing them to stay in the black. In the meantime, the government's relief programs made it possible to make working time more flexible (shorter hours in lieu of layoffs), which further moderated the impact of the crisis. The labor market has now stabilized. In November, employment fell by a mere 2,000 m/m, which might be due to seasonal factors. As the economic situation improves, internal demand remains strong and international trade recovers, there should be a lasting reversal in employment trends in the ensuing months, accompanied by further increase in salaries (this time in real terms).

Unemployment, salary growth, employment in manufacturing, average remuneration

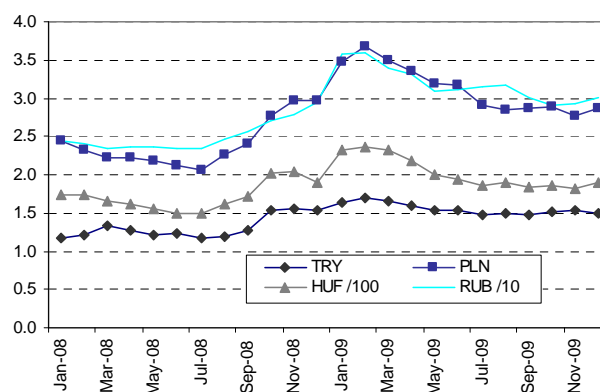


Source: Central Statistical Office

... Supports Private Consumption

Despite the considerable decline in industrial production and the increasing unemployment, domestic consumption fell y/y for only two months. In 2010, we expect consumption to increase further at 3-4% y/y, which will impact employment and the companies' expenditure on salaries. Stronger consumption growth will reduce the delayed impact of the deterioration in the labor market in H1'10. As employment grows, consumption growth should become faster in H2'10.

Zloty compared to other currencies in the region



Source: NBP, Bloomberg

Still No Breakthrough in Investment

2010 should bring further increases in expenditure on infrastructure construction. We should not expect a breakthrough, however, as far as private investment is concerned, as capacity utilization remains low and bank financing is restricted (as international groups continue to deleverage).



Public Finances under Control

As far as public finances are concerned, the situation of the national budget improved at the end of 2009, as expected. The deficit will be lower than the previous estimate of PLN 27.2bn, thanks to higher revenues (+PLN 11bn vs. plans, including PLN 9bn in additional tax revenue, of which PLN 5bn came from the VAT). Revenue from abroad (from the EU) will, in turn, be PLN 8-9bn below the planned amounts. All told, the public sector deficit should be lower than the 6.3% estimate, and with the estimated 1.7% growth in 2009, the debt to GDP ratio should be ca. 49.7%. Until now, the government has been planning a deficit of PLN 52bn in 2010, which appears very conservative given that consumption is growing much faster than the budget foresees and that inflation and proceeds from privatization are both likely to be higher. In addition, 2010 revenue will be boosted by NBP's profits for 2009, estimated at PLN 4-10bn (depending on exchange rate assumptions). All in all, the state's borrowing needs, estimated at PLN 203bn, should in fact be PLN 23-33bn lower.

**Key macroeconomic data for Poland**

GDP and industrial production	Jun 09	Jul 09	Aug 09	Sep 09	Oct 09	Nov 09	Dec 09
GDP	1.1%			1.7%			3.2%
Domestic demand	-2.1%			-1.2%			0.8%
Retail consumption	1.7%			2.2%			2.2%
Gross fixed capital formation	-3.0%			-1.5%			-4.0%
Value added	0.8%			1.8%			
Manufacturing	-5.0%			-0.2%			
Construction	4.6%			7.2%			
Market services	2.9%			2.0%			
Industrial production y/y	-4.5%	-4.4%	0.1%	-1.3%	-1.3%	9.8%	15.3%
Industrial production m/m	6.0%	-2.6%	-4.4%	15.0%	1.9%	-3.3%	1.7%
Retail sales y/y	0.4%	3.6%	3.1%	0.7%	0.7%	3.9%	6.3%
Retail sales m/m	1.6%	5.6%	-3.5%	-0.7%	3.7%	-6.5%	22.6%
Labor market	Jun 09	Jul 09	Aug 09	Sep 09	Oct 09	Nov 09	Dec 09
Avg. salary in the enterprise sector (PLN)	3287.88	3361.90	3268.69	3283.18	3312.32	3403.92	3595.98
Salaries in the enterprise sector y/y	2.0%	3.9%	3.0%	3.3%	2.0%	2.3%	4.9%
Salaries in the enterprise sector m/m	2.9%	2.3%	-2.8%	0.4%	0.9%	2.8%	5.6%
Employment in the enterprise sector y/y	-1.9%	-2.2%	-2.2%	-2.4%	-2.4%	-2.2%	-1.8%
Employment in the enterprise sector m/m	-0.2%	-0.1%	-0.1%	-0.1%	0.0%	0.0%	-0.1%
Unemployment rate	10.6%	10.7%	10.8%	10.9%	11.1%	11.4%	11.9%
Foreign trade	Jun 09	Jul 09	Aug 09	Sep 09	Oct 09	Nov 09	Dec 09
Current-account balance (EUR m)	-11	-570	124	-57	-991	-2510	
Balance of trade in goods, transactions (EUR m)	-109	-488	-348	-4	-819	-590	
Exports by transactions y/y (EUR)	-21.4%	-23.5%	-20.8%	-17.1%	-17.6%	-1.3%	
Imports by transactions y/y (EUR)	-32.0%	-29.5%	-27.8%	-26.4%	-21.7%	-10.5%	
Current-account balance (% of GDP)	-2.7%	-2.7%	-2.4%	-1.8%	-1.7%	-2.4%	
Price	Jun 09	Jul 09	Aug 09	Sep 09	Oct 09	Nov 09	Dec 09
Consumer price index m/m	0.2%	0.1%	-0.4%	0.0%	0.1%	0.3%	0.2%
Consumer price index y/y	3.5%	3.6%	3.7%	3.4%	3.1%	3.3%	3.7%
Core inflation (excl. food, energy) y/y	2.7%	2.9%	2.9%	2.9%	2.9%	2.8%	2.9%
Producer price index m/m	0.8%	-1.5%	-0.4%	-0.2%	0.4%	-0.3%	-0.1%
Producer price index y/y	4.1%	2.8%	2.2%	1.6%	2.0%	2.0%	2.2%
Monetary aggregates	Jun 09	Jul 09	Aug 09	Sep 09	Oct 09	Nov 09	Dec 09
M3 money supply (PLN bn)	693.7	689.4	685.4	691.3	711.2	699.7	701.5
Money supply y/y	14.4%	11.9%	9.0%	9.6%	11.9%	7.9%	5.3%
Loans for households y/y	35.7%	32.1%	27.9%	26.3%	20.4%	18.3%	
Loans for businesses y/y	14.7%	11.4%	7.3%	6.5%	2.8%	-0.2%	
Household deposits y/y	24.7%	22.5%	20.6%	19.9%	19.3%	17.4%	1.2%
Corporate deposits y/y	7.2%	3.0%	2.7%	3.3%	3.5%	7.1%	-2.7%
Interest rates	Jun 09	Jul 09	Aug 09	Sep 09	Oct 09	Nov 09	Dec 09
NBP intervention rate	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%
Lombard rate	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Deposit rate	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
3M WIBOR	4.34%	4.07%	4.08%	4.08%	4.08%	4.09%	4.17%
Yield on 2Y bonds	5.29%	5.00%	5.11%	5.13%	5.01%	5.14%	5.22%
Yield on 5Y bonds	5.83%	5.47%	5.66%	5.72%	5.71%	5.69%	5.96%
Yield on 10Y bonds	6.27%	6.11%	6.12%	6.18%	6.15%	6.19%	6.26%

Source: BRE Bank SA; numbers in italics are forecasts

The World: USA Shapes Global Sentiment to Equities, China to Commodities

Analysts agree that in 2010 the emerging markets will continue to be the driving force of the global economy. Although the developed countries will see economic growth, they will continue to face structural problems, such as high debt, which will limit the rebound in consumption. The second half of the year will show whether what we are observing right now is merely a rebound following the 2007/2008 breakdown in the economy, which will be followed by a period of stagnation (0-1% growth in 2011-12) or whether the economy is starting another growth cycle at a pace close to its potential growth rate. The key questions are: what will be the behavior of the American consumer and might the Chinese economy need cooling down due to stimulus packages.

We believe the sentiment towards the equity market will continue to be shaped by the economic situation in the USA, which has a strong impact on the EU, even if the each year the relative importance of the US vs. BRIC is decreasing. The consensus forecast for the USA, Japan and Germany shows that growth of at least 2% y/y is expected, with further improvements coming the following year. In the case of China, nearly 9.5% growth in the GDP is expected.

Forecasted rate of economic growth in selected developed and developing countries

	Real GDP growth (%)			Inflation rate (%)		
	2009	2010	2011	2009	2010	2011
Developed markets						
USA	-2.50	2.50	3.00	-0.30	1.80	1.50
Japan	-5.20	2.00	2.00	-1.40	-0.80	0.60
Euroland	-3.90	1.50	1.70	0.30	1.10	1.70
Germany	-4.80	2.30	1.50	0.30	0.90	1.40
France	-2.10	1.70	1.50	0.10	1.30	1.50
Italy	-4.70	1.30	1.50	0.70	1.00	1.50
Spain	-3.60	0.00	0.80	-0.30	1.40	1.80
United Kingdom	-4.70	1.00	1.80	2.10	2.30	1.50
Emerging markets						
Brazil	0.15	4.75	4.20	4.30	4.40	4.40
Russia	-7.70	3.00	4.50	11.00	9.00	8.85
India	7.10	8.00	7.70	9.80	8.60	5.70
China	8.50	9.40	8.80	-0.65	2.75	3.00
South Korea	-0.50	3.95	4.50	2.90	2.90	2.80
Turkey	-5.60	3.75	4.00	6.10	6.60	6.20
Hungary	-6.30	0.00	2.50	4.40	4.00	3.00
Poland	1.20	2.00	3.20	3.70	2.60	2.50

Source: Commerzbank, Bloomberg

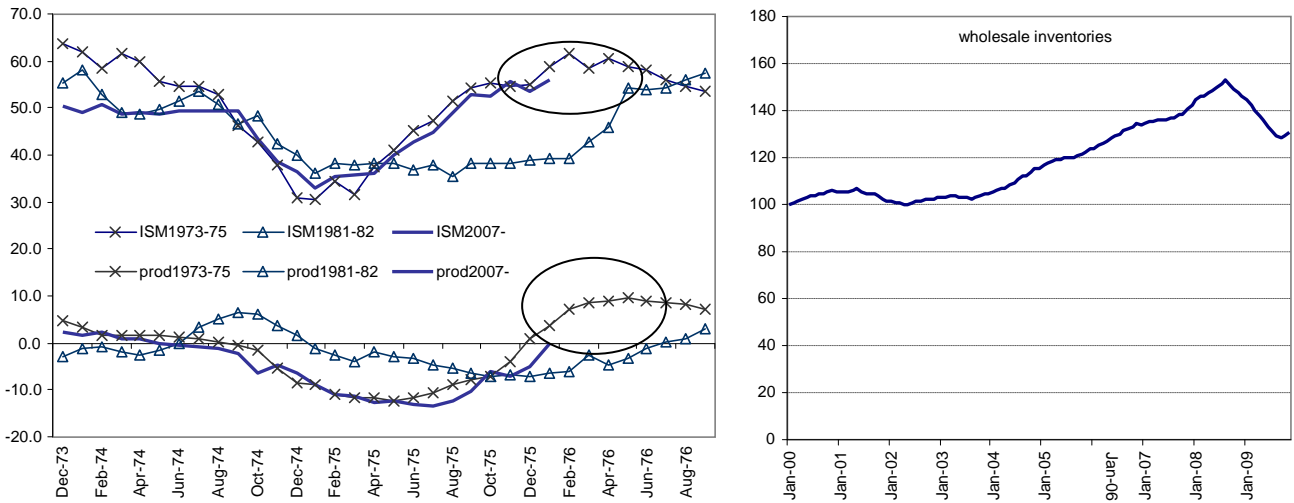
Among Central and Eastern European countries, Turkey and Russia can boast the highest forecasted growth figures. Still, in 2010 these countries will not return to their GDP level from before crisis. In this context, Poland's situation looks truly excellent. Hungary and Bulgaria face much bigger problems.

USA: World's Biggest Economy Navigates Past an Iceberg

This appears to be a fitting summary of the year 2009 in the American economy. Thanks to aggressive policies on the part of the FED and the government, it was possible to bring stability to the financial system and stimulate the economy, which is now set to grow for at least several months. We need to wait before we can say whether this is a lasting revival and how smoothly the withdrawal from the stimulus-based policies will be. There is no doubt that multiple structural problems of the American economy remain unsolved; that said, stabilization is clearly apparent in the key sectors (labor market, real-estate market) and some other sectors are entering a growth phase (manufacturing). There appears to be no threat to a positive momentum in the horizon of several months.

In this report, we return to the revised data concerning the relationship between industrial output and the ISM index, which allows us to say where we are compared to the previous recessions of 1973-75, 1981-82, and the 1930s.

ISM and industrial production in economic cycles in the USA, wholesale inventories (2000=100)

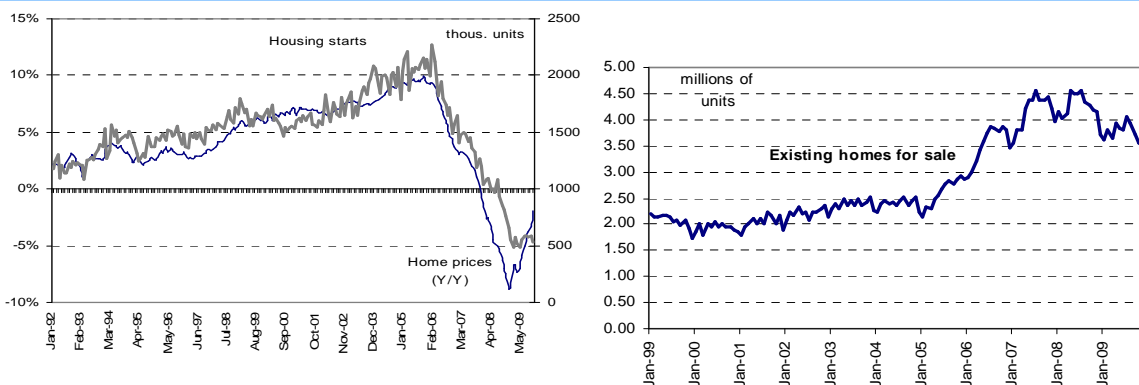


Source: Bloomberg

If we look at the ISM and production data, the current recession is very much alike to that from the 1970s. So far, the rate at which the ISM index recovers from recession levels is almost identical, and it influences the industrial production growth index, which has a 4-5 delay. The recession of the 1980s played out very differently. The ISM index remained at recession levels for 10 months longer, meaning that it took as much longer for industrial production to regain momentum. The current ISM levels are already high, and will be hard to beat, but this does not have much relevance except for sentiment. What is important is that the index stays over 50 points. Note that, back in 1976, ISM moved persistently downwards but production still increased at a rate of 10%. At present, the ISM data suggest that we are in for at least several months of growth in industrial production, if only due to restocking (inventories are at historically low levels compared to consumption).

The real estate market, whose breakdown was one of the direct causes of the recession, is reaching stability. New housing starts are somewhere in the 530-590,000 bracket, which is accompanied by the deceleration of the rate at which property prices are falling y/y (-1.9% in October). There is still a surplus of unsold homes, however, which will delay any major revival in the sector. We should also remember that in 2009 stimulus packages directed towards housing demand were available.

Housing starts and real-estate prices in the USA (left) and existing homes for sale



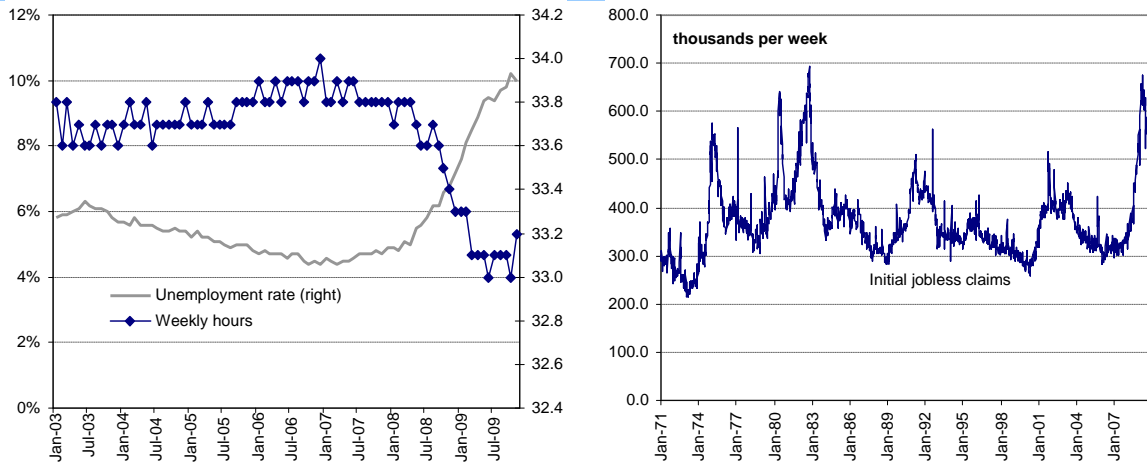
Source: Bloomberg

As expected, the labor market is reaching stability. Although employment is not rising yet, this can be seen clearly in the declining number of initial jobless claims (at the height of the crisis, the number of new unemployed increased to nearly 700,000, which is a level similar to that observed during the crisis from the early 1980s, the current figure is 430,000 per week), as



well as the gradual increase in weekly working hours. This means that the cycle of layoffs is over and companies are now increasing their output by prolonging the working hours of their employees. In the next stage, we can expect employment to increase.

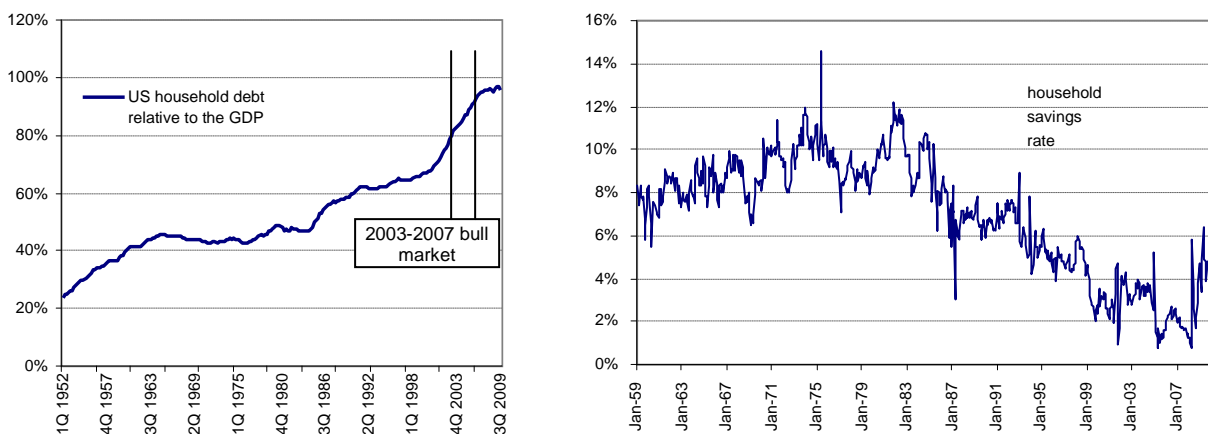
Data from US labor market



Source: Bloomberg

In the short term, the improvement in the labor market will make at least a partial revival in demand, which is of crucial importance if the current revival is to be a lasting one. The problem that remains is the financial condition of households, whose long-term debt approaches 100% of the GDP. It is hard to expect the FED to keep the cost of money low, allowing this debt to grow further, which happened after the recession in the early years of this decade and which gave a considerable growth impulse to stock markets. The 2003-2007 bull market came at a cost of an increase in US household debt from 80%% to 96% of GDP. In the ensuing years, we are more likely to see gradual deleveraging, as was the case in 1960s/1970s (savings rate of 8-10% vs. 4.7% currently). As far as 2010 is concerned, it is risky to speculate on consumer demand in the context of debt, given that consumption should increase as employment and income go up (not merely salaries, but equity income as well), with the savings rate unchanged. Debt constitutes a long-term problem, all the more so that improvements in the economic situation will entail higher interest rates and therefore higher debt servicing costs.

US household debt relative to GDP, savings rate

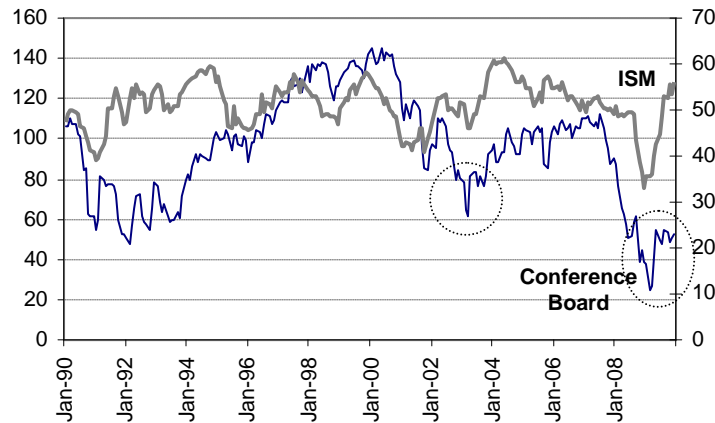


Source: Bloomberg

For now, Consumer Board confidence indicators do not confirm the American's increased proclivity to savings. Following a rebound after the very sharp drops in 2007-2008, the indicator has been stable for six months now. This is the same situation as during the previous economic cycle, when the CB indicator did not budge until the situation in the labor market started to improve, which led to further increase in the Americans' debt. We believe this is one of the key indicators to watch in the upcoming months. If it fails to go up, the revival in

manufacturing may turn out to be a mere rebound rather than the start of the new economic cycle, as the ISM seemed to suggest.

Consumer sentiment in the USA vs. ISM Manufacturing

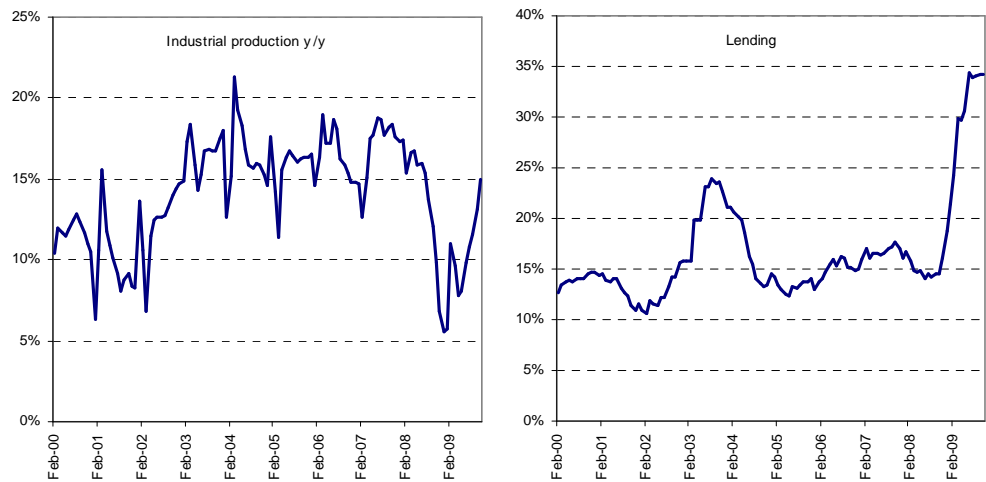


Source: Bloomberg

China As The Driving Force

Stimulus packages applied by the Chinese government allowed the biggest emerging economy to record over 8% GDP growth in 2009. The Q4'09 forecast indicates 10.5% y/y growth. Industrial production is once again growing at nearly 20% y/y. Increasingly frequently, however, the question appears whether the very fast increase in lending might not cause the Chinese economy to “overheat” – and indeed whether the Chinese government is not going to launch a cooling-down process in the upcoming weeks. The first symptoms are already here (increase in the reserve requirement for the banks). For now, inflation remains under control, not exceeding 1% y/y.

Industrial production and lending growth in China (y/y)



Source: Bloomberg

Macroeconomic Data and the Equity Market

Given the structure of assets held by the various groups of investors present on the WSE, 2010 will be another year when the local market will be driven by global capital flows rather than domestic macroeconomic conditions and company earnings. It seems that the market should remain highly volatile, because the investors have already "made their bets" and the upcoming months will show who was right and who was wrong. The most important "bets" are the following:

- Will the USD be weak or strong?
- Will interest rate hikes come in late Q3'09 or earlier?
- Is the situation in commodities, and in particular metals, a speculative bubble or are investors discounting the future combination of reviving demand and insufficient supply?
- Will the emerging markets outperform the mature markets by a large margin? Will China continue to drive the global economy?

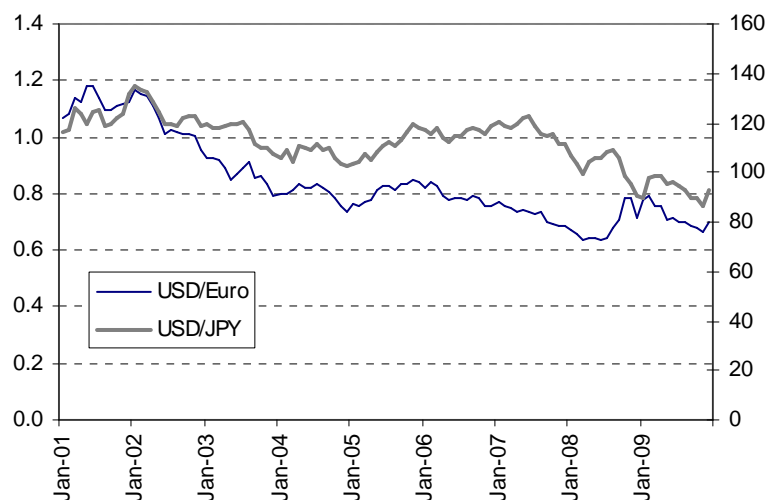
Analyses prepared by the global investment banks suggest that the consensus is quite clear: the dollar will remain weak, interest rate hikes will not come early, commodities will remain expensive and the emerging markets (Asia, South America and CEE, in that order) are a better investment alternative than equities in the developed markets. When the consensus is that strong, it is usually worthwhile to consider the alternative. Polish equities are tightly correlated with the German DAX, and therefore the WSE should more closely follow the developments in stock exchanges of the developed countries rather than Asia or South America.

Will the USD be Weak or Strong?

Getting the answer to this question right is most likely the key to successful investment strategy in 2010. The vast majority of strategic analyses for 2010, prepared by the global investment banks, assume that the USD will be weak and considers its potential appreciation the main risk factor.

We believe one of the factors that increase the likelihood of the appreciation of the dollar vs. EUR may be the fact that the pace at which the individual members of the EU are emerging from the crisis varies considerably, which may turn out to be a considerable difficulty for Euroland as a whole, given especially that interest rate hikes are approaching. While such countries as Germany or France are coping with the crisis quite well (the reforms carried out in Germany proved particularly effective), and should record GDP growth of ca. 2% in 2010, Portugal, Greece, Spain, Italy and Ireland are still struggling with the recession and their mounting debt. As a reminder, the budget deficit is 8.5% in Portugal, 10% in Spain and 13% in Greece. Public debt exceeds 80% of the GDP in Portugal, and 110% in Italy and Greece. These countries will continue to need low interest rates to support their economies; in turn, mounting inflationary expectations in Germany, the Benelux countries and France will pressure the ECB towards hikes. With these variations between the individual economies, the ECB is likely to react later than the FED, which will reduce the current interest rate disparity (1.00% in Euroland, 0.25% in the USA) and could lead to USD appreciation against the prevalent expectations.

USD vs. EUR, JPY



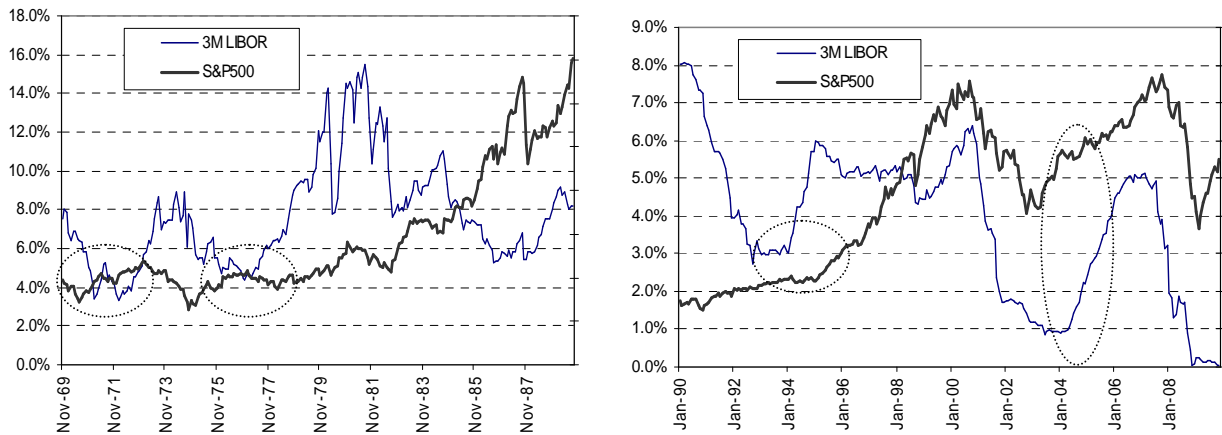
Source: Bloomberg

This is a possible strategy for 2010. In the long term, the economic position of the heavily indebted USA will deteriorate, and that should be a lasting trend.

Interest Rate Hikes in the USA and the Stock Market

Commerzbank's forecasts for the USA point to 2.5% GDP growth in 2010 and increase in inflation from -0.3% in 2009 to 1.8%. A forecast like this is close to the market consensus, which foresees the first interest rate hikes in late Q3 or early Q4 2010. In the previous cycles, interest rate increases tended to have a negative, though short-lasting, impact on the equity market. The hikes constituted a part of the upwards part of the economic cycle, which means that the ensuing economic growth and improving company earnings made shares attractive again soon afterwards. Let us point out that at present the American economy is struggling with problems resembling those from '76-'78 (deleveraging of households, high commodity prices, risk of inflation), when the correction was deeper and spread out over a longer period. Interest rate hikes in 1990s and 2000s were a part of the credit boom that energized the economy via domestic consumption, which is unlikely to be repeated in the current situation.

S&P500 and interest rate increases

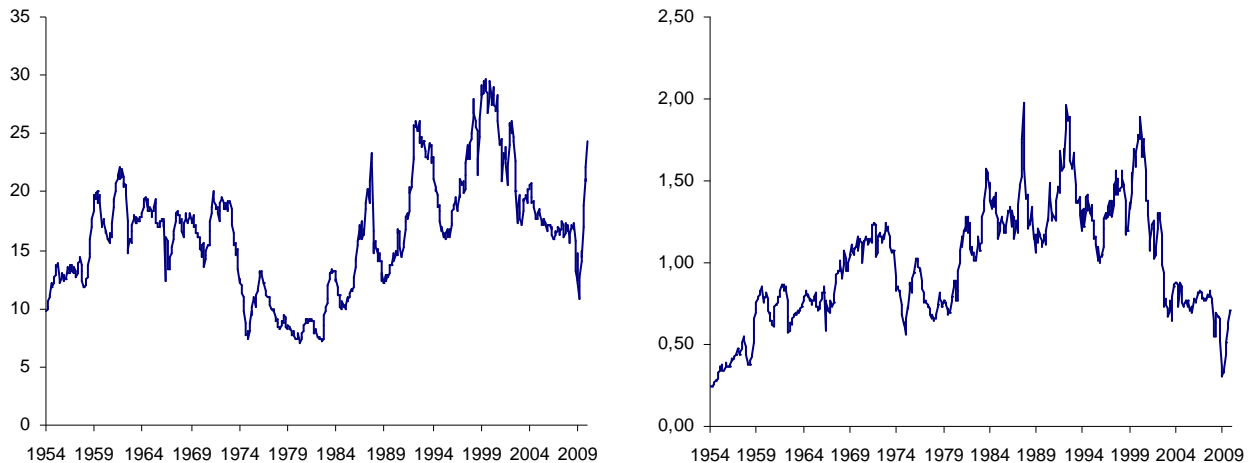


Source: Bloomberg

S&P500 Valuations Discount 29% Increase in EPS in 2010

The current (last four quarters) P/E for S&P500 companies is 24, illustrating on the one hand the decline in company earnings due to the crisis, and the sharp increase in the indexes on the other, which already discount economic revival and EPS growth. How strong will this growth be? Assuming that a justified level of the 10Y Bonds/(E/P) ratio at the end of 2010 is 0.72 (average for the past 8 years, illustrating a full cycle), and that the yield on 10Y bonds will increase to 4.2% by the end of the year, investors are expecting a 29% increase in EPS. This implies a P/E of 17.2. The expectation of such an increase in the EPS appears rational, given that using P/E for S&P500 we can estimate EPS decline over the past 12 months at 25%.

P/E (left) and 10YBonds/(E/P) for S&P500

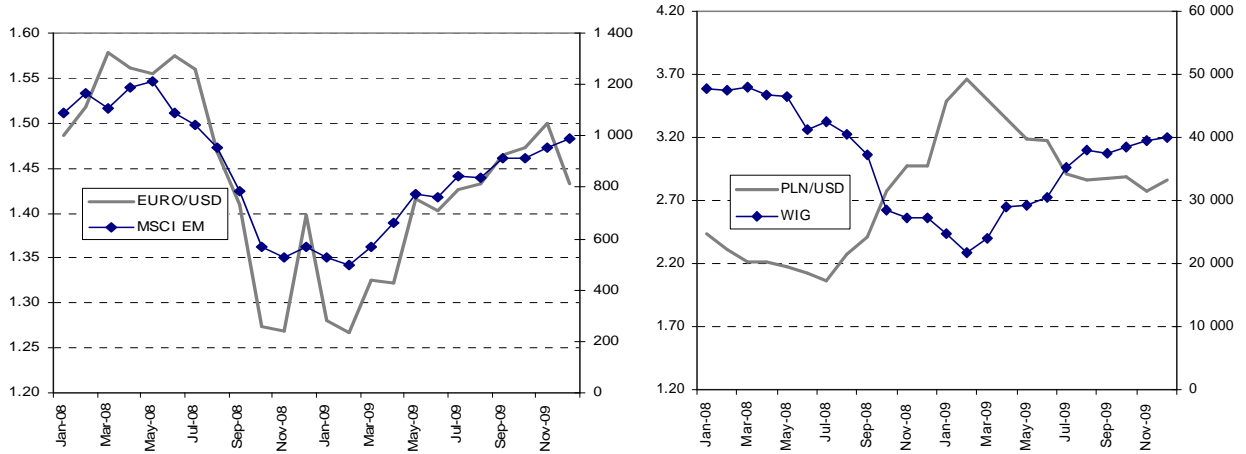


Source: Bloomberg

Forex Market and the WSE

The relationship between equity markets in the emerging markets and the USD remains strong, as confirmed by the correlation between the WIG and PLN/USD. For the first time in history, the combination of a weak dollar and extremely low interest rates in the USA has given an impulse for carry trades, which used to be reserved for the JPY.

WIG vs. USD/PLN, correlation of emerging markets and EUR/USD



Source: NBP, Bloomberg

Where Will the Money for the Boom Come From? Where Will the Money for IPOs and SPOs Come From?

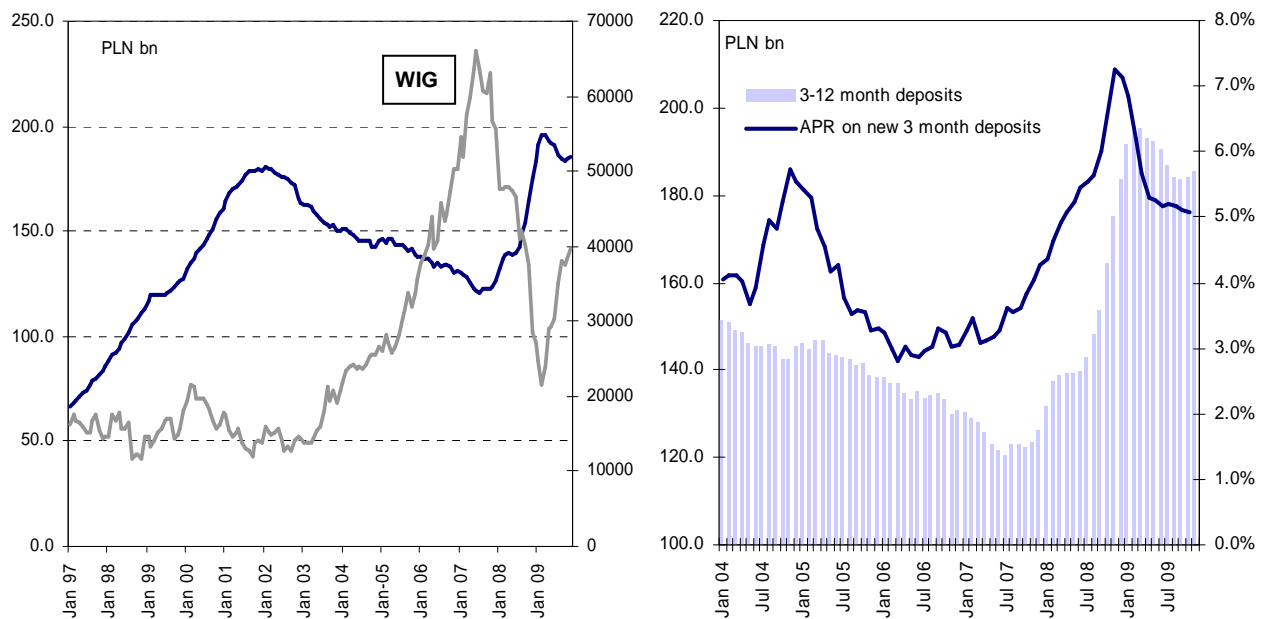
In accordance with the recently published data, in H1 2009 (the data for FY2009 will not be available until February), the breakdown of WSE trading volumes among the individual categories of investors was as follows: individuals investing directly 28%, domestic financial institutions 37%, foreign investors 35%. We have attempted to analyze the potential demand by each of these groups, taking into consideration the planned share offerings in the primary and secondary market. Our conclusions:

- Retail investors are still placing their savings at banks. Despite the stock market boom, three-months deposits are being converted into 3-6 month deposits, which does not harbingers increased interest in the equity market in the near future (this also applies to equity-focused investment funds). This is in line with the current policies of the banks.
- Funds keep flowing into pension funds.
- Foreign investors.
- The value of IPOs may exceed PLN 35bn.

Individual Investors Still Choose Deposits

The correlation between the WIG and retail deposits is very high, as shown by the chart below. Individual clients invest in the WSE directly or through investment funds (TFI). In 2009, despite the rapid growth in stock market indexes and the decline in APRs on new bank deposits from 7% to 5.2%, there was no considerable outflow of funds to the equity market. As their three-month deposits expired, clients opened new, 3-6 month deposits. Given the slump in the equity market we are expecting, we can hardly expect individual investors to return to the WSE in the upcoming months, regardless of whether they invest directly or through investment funds.

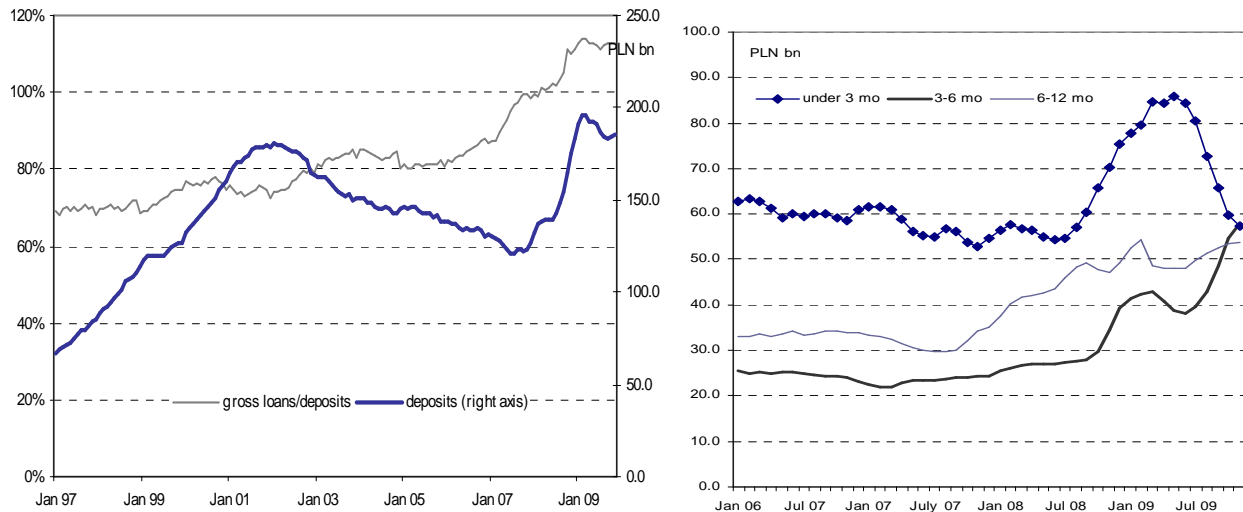
Household term deposits vs. WIG (left), deposits vs. APRs on new 3M deposits



Source: NBP, WSE

In the latter case, another factor that limits the demand for investment fund units is the policy of the banks, which, compared to the previous upswing cycle in the WSE (2002/2003) are no longer over-liquid. The ratio of gross loans to deposits is now above 110%. In the previous cycle, when the banks launched TFI-oriented sales strategies (as this was a high-margin product), the ratio amounted to 75%. To sum up, new funds from individual clients will continue to flow into the stock market, but not in such amounts as during the previous boom. This should entail decreased interest in SME stocks.

Deposits vs. the ratio of loans to deposits (left), deposits by maturity



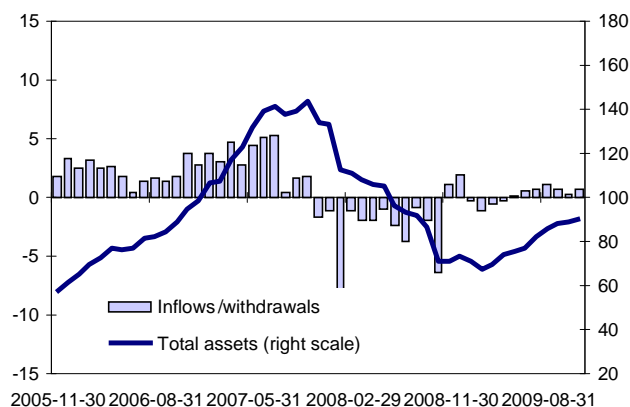
Source: NBP, WSE

Assets of Investment and Pension Funds

Assets of domestic financial institutions still constitute an important component of demand on the WSE. Given the scale of funds that flow into pension funds (PLN 1.7-1.8bn per month on average), as well as their earlier underweighting of equities, relative purchasing power is shifting towards them. Approximately 1/3 of the funds is allocated to shares. In the case of investment funds, we are still not seeing considerable capital inflows, for reasons described above.

Investment funds have not rebuilt their position following the crisis. As of the end of December, their assets totaled PLN 93bn, including PLN 27bn in equity-focused funds. We estimate the total value of shares held by investment funds at PLN 33bn, i.e. nearly PLN 20bn less than pension fund holdings. At the height of the previous boom, investment funds managed PLN 144bn, including PLN 63bn allocated to equities. We do not expect the situation to change considerably over the next six months. Investment funds will record total monthly inflows of PLN 0.7-1bn, of which ca. PLN 35-40% will go towards the purchase of equities.

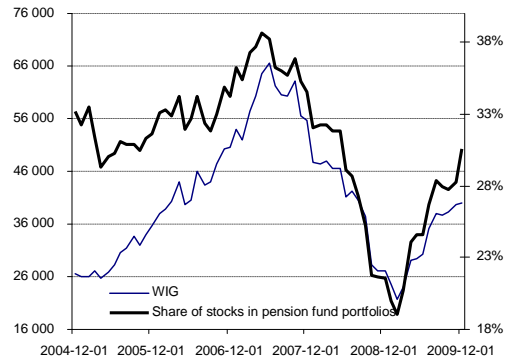
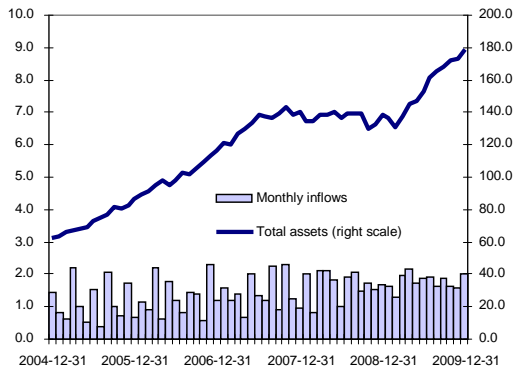
Total assets of investment funds



Source: NBP, WSE

At the end of December, pension fund assets totaled PLN 179bn, including 30.6% in equities. The share of equities in the funds' portfolios, even though it has increased over the recent months, remains below the long-term average, which can be estimated at ca. 32% (during a bull market), with a maximum of 39% in 2007. Monthly capital inflows into pension funds hover around a PLN 1.8bn average.

Assets of investment and pension funds



Source: Anality Online

Assuming that pension funds will get PLN 22bn in new funds in 2010 and that they will invest 31% of this sum in equities, we can estimate the potential demand from them at PLN 6.8bn. On the optimistic assumption that the value of the funds' equity portfolios expands by 10% this year (WIG), at the end of the year equities will account for 31.7% of their overall portfolios, which is slightly below the long-term average. The decision to boost allocation to equities by this amount entails additional demand of PLN 0.5bn. In the scenario of a stable macroeconomic environment and acceptably priced IPOs, the aggregate demand from pension funds (primary and secondary market) can be estimated at a minimum of PLN 7.5bn. This is 21% of the value of upcoming IPOs (plus the Treasury's minority packages). A question arises: where is the money for the secondary market going to come from?

When estimating inflows into pension funds, a risk factor are the government's plans to considerably reduce the proportion of social security premiums directed towards them (and divert them to the Social Insurance Institution, ZUS) with the view towards improving the situation of the national budget. Such ideas are being generated both in the Ministry of Labor and in the Ministry of the Economy. The planned changes are of three types:

- People who turn 55 (women) or 60 (men) will be allowed to move funds amassed by pension funds to ZUS, which will be in charge of disbursing their pensions. It is estimated that over 250,000 men and 100,000 women could have this option in 2010.
- People who turn 65 and whose pension from ZUS is not lower than two minimum pensions (PLN 2700, 2x PLN 1350 at the moment) will have the opportunity to withdraw all their money from pension funds and use them as they wish.
- Mandatory premium paid to pension funds will be reduced from 7.3% to 3% of salaries.

Should the parliament pass these proposals into law, without a simultaneous reduction in the cap on the funds' allocation to equities, the impact on the WSE would be negative. In the case of the two former proposals, they might be forced to sell assets. On the assumption that all pensioners transfer their pensions to ZUS in 2010, the decrease in the funds' assets can be estimated at PLN 4.5-5bn, i.e. 2.7% of their total assets. While the cap on equity allocation does not influence the market per se in any significant way, combined with the planned reduction in premiums paid to pension funds (reduction in annual inflows from PLN 22bn to PLN 9bn) and with the increased supply of shares from IPOs, the funds' demand for stocks in the secondary market will be considerably reduced.

Supply of New Shares: the Treasury Will Dominate the Market

In accordance with the government's budget proposal and promises, in 2010 we should see more big privatizations carried out through the WSE, which will significantly boost the supply of equities. The total value of shares to be issued or sold by the Treasury, Treasury-controlled companies and private issuers amounts to PLN 35bn, most of which will be concentrated in H1'10.

**Share offerings coming in 2010 (PLN billion)**

Company	Sector	Value of the offer	Expected timing
PZU	Finance	10.0	May
Tauron	Energy	6.0	After the summer or in June
PGE	Energy	6.0	Not before May
Enea	Energy	1.3	1Q
Polkomtel	Telecommunications.	6.0	2Q
LW Bogdanka	Coal mining	1.3	After the summer
KGHM	Metals	2.2	January
TPSA	Telecommunications.	1.0	1H
Millennium*	Finance	0.4	1Q
Other private issuers		1.2	
TOTAL		35.4	

Source: BRE Bank Securities

In accordance with what the State Treasury is saying, the biggest offering of 2010, coming in May, and one of the biggest in the history of the WSE will be the sale of shares in PZU. The total value of this stake is estimated at PLN 10bn. Another huge privatization to be carried out through the WSE will be the IPO of the energy producer and distributor Tauron (the value of shares to be issued/sold is ca. PLN 6-8bn). In late Q1 or early Q2, Polkomtel may appear on the stock market, although now that PKN Orlen has met its loan covenants it cannot be precluded that Polkomtel's Polish shareholders will decide not to divest it. This transaction could amount to ca. PLN 5-6.5bn. The treasury is also considering selling its remaining shares in LW Bogdanka (PLN 1.3bn, second half of the year), 10-20% stake in PGE (PLN 6bn for 15% at the current market price, most likely in the second half of the year), a 15% stake in Enea (PLN 1.3bn) and a 4.7% stake in TPSA (PLN 1bn). In the early days of January, the Treasury sold a 10% stake in KGHM (PLN 2.06bn), 56% of which was bought by domestic institutions. In addition, there will be private IPOs for a total of at least PLN 1.0-1.5bn.

Sector Allocation

Our suggestions for portfolio allocations in 2010 are based on the assumption that the Polish equity market will have either gained or lost up to 5 percent of its value by the end of the year, with weaker performance seen during the first six months. Accordingly, we provide separate suggestions for sector allocations for the first half-year and the full year 2010.

In the next six months, we would remain underweight on large banks (not because of fundamentals, but because of factors like a large supply of competitive equity from national insurer PZU, and considerable exposure to international fund flows), companies with exposure to commodity price fluctuations (KGHM, Lotos), which we expect to experience a deeper downward correction, and chemical producers (Ciech is the only chemical company not affected by dwindling demand for fertilizers). Further, we expect better performance from the media sector (a late-cycle industry), IT companies (government orders), telecoms (which are a defensive sector, and which include the dividend-paying TPSA), and manufacturers (industrial production is expected to increase significantly this year).

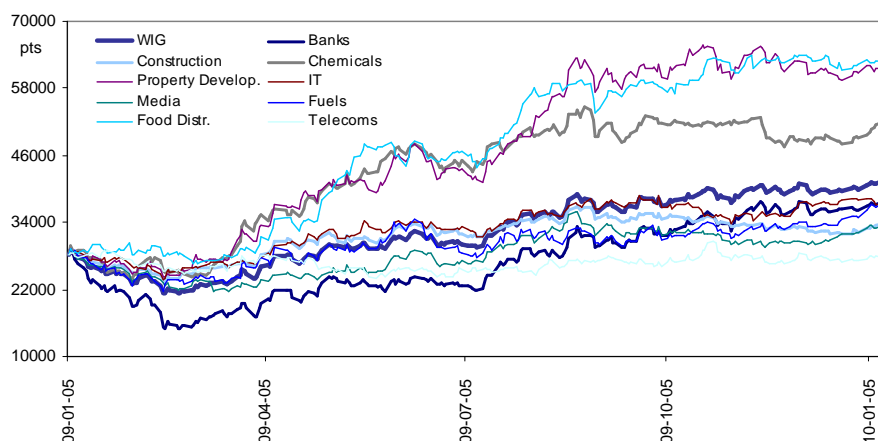
Recommended Sector Allocations

Sector	Recommended Allocation	
	2010 First-Half	2010
METALS	Underweight	Underweight
BANKS	Underweight	Neutral
MEDIA	Overweight	Overweight
IT	Overweight	Overweight
FUELS	Neutral	Neutral
POWER UTILITIES	Underweight	Neutral
CHEMICALS	Underweight	Underweight
TELECOMS	Overweight	Neutral
CONSTRUCTION	Neutral	Overweight
PROPERTY DEVELOPERS	Neutral	Neutral
RETAILERS	Neutral	Neutral
MANUFACTURERS	Overweight	Neutral

Source: BRE Bank Securities

Summing up, we would advise investors to stay underweight in commodity- and chemical stocks, and to overweight media and IT. As the year progresses, sentiment to the construction sector (which is attractively priced at the moment) is going to improve on the back of increasing demand which will reduce the downward pressure on margins.

Sector performance in 2009



Source: BRE Bank Securities based on Bloomberg data

Changes in sector indexes in 2009

WIG	Banks	Construction	Chemicals	Property Developers
45%	33%	19%	86%	112%
Media	Fuels	Food Producers	Telecoms	IT
17%	31%	129%	-3%	30%

Source: WSE

Current ratings by BRE Bank Securities

Company	Rating	Expected 2010/09 Growth			FY2010E Multiples	
		Sales	EBIT	EPS	P/E	EV/EBITDA
AB	Buy	2.79%	32.73%	18.67%	10.73	8.05
ACTION	Buy	-31.69%	-18.58%	-13.61%	10.54	7.62
AGORA	Buy	0.83%	64.15%	67.63%	19.44	6.37
ASBIS	Accumulate	13.62%	336.08%	-	12.94	15.33
ASSECO POLAND	Buy	5.63%	4.59%	-1.77%	12.57	6.26
BUDIMEX	Accumulate	23.82%	18.34%	9.51%	10.69	8.07
BZWBK	Hold	5.87%	15.59%	13.57%	15.01	
CENTRUM KLIMA	Buy	4.44%	4.87%	15.86%	12.93	8.49
CEZ	Hold	-1.20%	-6.74%	-6.48%	10.59	2.46
CIECH	Hold	4.70%	33.18%	-	14.67	5.97
CYFROWY POLSAT	Accumulate	5.06%	33.04%	30.07%	14.4	9.81
DOM DEVELOPMENT	Accumulate	-21.61%	-62.15%	-63.59%	38.21	30.72
ELEKTROBUDOWA	Hold	0.15%	-9.71%	1.62%	16.23	10.78
EMPERIA HOLDING	Hold	6.66%	10.38%	11.23%	12.4	6.96
ERBUD	Accumulate	29.65%	-4.59%	7.56%	13.88	9.54
EUROCASH	Hold	6.46%	11.63%	11.48%	19.36	9.9
GETIN	Accumulate	6.17%	81.37%	99.93%	13.88	
HANDLOWY	Hold	-4.30%	8.32%	9.61%	15.87	
ING BSK	Hold	5.24%	12.69%	12.69%	14.32	
J.W. C.	Buy	21.66%	58.60%	61.54%	2.78	1.9
KĘTY	Hold	9.00%	-0.78%	23.71%	13.84	7.48
KGHM	Reduce	2.08%	-9.04%	-0.84%	9.4	6.58
KOMPUTRONIK	Hold	-10.58%	362.27%	247.90%	11.79	7.42
KREDYT BANK	Hold	2.20%	294.61%	294.61%	32.66	
LOTOS	Reduce	22.40%	-6.20%	-46.16%	10.55	14.44
LW BOGDANKA	Buy	0.89%	-6.55%	-9.94%	15.44	7.38
MILLENNIUM	Accumulate	19.17%	-	-	24.42	
MONDI	Hold	40.07%	178.66%	208.27%	17.7	9.21
MOSTOSTAL WARSZAWA	Buy	4.52%	-21.33%	0.92%	12.19	6.33
NETIA	Hold	2.59%	-	-	47.63	4.64
PBG	Hold	25.83%	2.55%	12.12%	13.32	8.54
PEKAO	Reduce	10.66%	24.36%	24.49%	15.64	
PGE	Buy	-1.54%	-5.63%	-1.81%	12.3	5.31
PGNiG	Accumulate	2.04%	138.15%	118.43%	11.66	5.56
PKN ORLEN	Buy	17.33%	25.13%	3.76%	10.91	6.95
PKO BP	Reduce	6.21%	32.23%	33.99%	15.62	
POLICE	Hold	9.12%	98.13%	93.48%		10.36
POLIMEX MOSTOSTAL	Accumulate	1.56%	-20.07%	-3.46%	13.29	7.43
POLNORD	Buy	36.06%	-47.85%	-88.85%	195.8	31.74
RAFAKO	Buy	24.84%	25.43%	63.21%	14.65	6.55
SYGNITY	Buy	11.48%	97.81%	90.58%		7.46
TPSA	Accumulate	-2.98%	7.60%	15.18%	13.02	4.05
TRAKCJA POLSKA	Hold	2.72%	-45.87%	-40.57%	16.73	8.9
TVN	Buy	15.26%	-9.21%	-45.58%	34.72	11.35
ULMA	Hold	27.42%	611.71%	-	18.45	5.44
UNIBEP	Buy	36.01%	-8.87%	-12.43%	12.64	8.45
WSiP	Hold	1.00%	3.77%	5.16%	12.7	8.67
ZA PUŁAWY	Hold	17.89%	49.13%	21.75%	20.59	8.53

Source: BRE Bank Securities



Banks

- In contrast to the aggressive growth strategies announced by Bank Millennium (FY12E ROE at 15%), Bank Handlowy (FY12 ROE at 20%), and Getin Noble Bank (FY10 ROE at 20%), we predict a deterioration in the long-term returns on equity of Polish banks (a decline to 16%-17% from 20% in 2007), in line with a global trend toward maintenance of higher Tier 1 capitals.
- At the same time, banks cannot count on fast volume growth because they lack the structural surplus liquidity observed at the beginning of the previous cycle, and due to a lack of cash supply from foreign institutions (as international banks are in the process of restructuring their balance sheets). We predict that the overall loan and deposit portfolios of the Polish financial sector will expand by 7% and 8% respectively in 2010. In subsequent years, the growth rates will increase to low double digits.
- In spite of stifled volume growth, Polish banks stand to benefit from improving macro conditions and returns on assets (the FY09 ROA of the banks in our coverage universe contracted to 1.3% from 2.0% in 2008 and 2.5% in 2007; in the next two years, we expect the indicator to return to 2.0–2.1%).
- According to our estimates, the sector's FY2010 net income will increase 23% vis-à-vis 2009 (FY10E ROA at 1.5%, FY12 ROE at 12%-13%), driven by stronger revenues (+7%), slower cost growth (+3.6%), and slightly lower costs of risk (1.3% of net loans vs. 1.6% in 2009).
- Prices of bank stocks already reflect the hopes that the stabilization of the financial system is permanent, and that it can support earnings growth. But earnings growth over 20% is not discounted yet.
- We see more upside potential in smaller banks that grow more rapidly amid economic recovery.
- Our recommendation for the first half of 2010 is to take positions in banks paying high dividends (Bank Handlowy), so as to avoid the negative effects of exchange rate fluctuations, large equity supply from privatized companies, high comparable base for volume growth, rising retail loan provisions, and expected interest-rate hikes. In the second half of the year, volumes are expected accelerate, forex movements will play a decreasing role (long-term strengthening of the zloty, smaller share of foreign-currency loans), and investors will start to discount the reduction in loan-loss provisions predicted for 2011, which should lead to a robust rise in profits (Getin Holding).

Key Ratings: Bank Handlowy (Buy), Getin Holding (Buy), ING BSK (Accumulate), Kredyt Bank (Accumulate)

In the last few months, three Polish banks: Millennium, Bank Handlowy, and Getin Noble Bank, announced very ambitious growth plans through 2012, with far-reaching ROA targets. In the unlikely event that these targets are achieved, the market valuations of these three players, as well as most other banks, would rise considerably. Another conclusion that can be drawn from the three growth strategies is that their authors anticipate continued economic growth in the next three years. We share this view, as reflected in our GDP growth forecasts of 3% in 2010 and 4.4% in 2011.

Our predictions might not hold if it turns out that we overestimated the Polish economy's growth potential (Polish banks have very limited exposure to foreign assets). The key consideration is the unemployment rate, which has a direct effect on loan-loss provisions. Balance-sheet pressures will play a decreasing role in our opinion, thanks to prudent approaches to future volume growth.

The financial crisis is changing the face of the global financial sector. In December 2009, the Basel Committee on Banking Supervision announced a set of proposals aimed at improving the quality and safety of bank operations. Among the main consequences of the resulting regulations will be: (i) slower long-term growth rates, in particular in developed markets, and (ii) lower ROEs. Polish banks will be among those least affected by the Basel guidelines, thanks to the quality composition of their Tier 1 capitals (of the banks in our coverage universe, only Kredyt Bank, Millennium, and PKO BP use Tier 2 capital), and strong lending capacity (the average ratio of loans to deposits for listed banks is 90%). However, the capital requirements will prevent returns on equity from climbing back to their historical 20% highs.

The outlook for the first half of 2010 is tough. High provisions for retail loan losses, sluggish growth in new business, decreasing trading income (which is expected to remain under pressure throughout the year), and potential equity offerings (in addition to the SPOs of PKO



BP and Millennium), will keep investors away from the bank sector. In the second half of the year, investors are expected to focus on FY2011 growth prospects, which are much better than this year, with net sector earnings surging by an expected 45% (the Bloomberg consensus estimates for year-on-year bank earnings growth as of 8 January were 36% for 2011 and 20% for 2009).

In our opinion, small banks offer the most upside potential. Our top pick for the coming months is Bank Handlowy, which combines handsome dividends (DY=4.7%) with ambitious earnings targets (Handlowy wants to increase ROE over 20%, and achieve a target ROA of more than 2.5%). Further, Getin Holding is a good investment choice for the year (the bank has set its FY10 ROE target at a lofty 20%). Investors might be concerned about the bank's high retail-loan provisions and the potential impact of a weaker zloty on the balance sheet, but these threats will disappear in the latter part of the year. Our next best bet is ING BSK, which managed to maximize its advantages (liquid balance sheet and increasing retail lending leading to stronger margins) in the generally tough 2009, increasing operating income before provisions by a very impressive 25%. ING BSK is still trading at a considerable discount to peer multiples (FY09 P/E' at 15.6 vs. an 18.2 median), which it seems to hold in spite of predictions of continued 2010 growth (FY10E P/E = 13.7 vs. 16.3). Finally, Kredyt Bank is valued at 13x FY10E P/BV, reflecting the low expectations that investors have for the bank sector. As macroeconomic conditions improve, and once the bank completes its provision-raising cycle, it will offer considerable upside potential.

Fuels

- **Oil refiners: overweight PKN Orlen versus Lotos. Oil fundamentals are still weak, but crack spreads may improve if crude prices stabilize (due to a strong dollar). The Urals/Brent differential continues to expand toward an expected \$2/Bbl.**
- **PKN Orlen is expected to divest Polkomtel and Anwil, improve profits generated by the petrochemical business, and continue to generate solid profits from the retail business. Cash flows will increase once CAPEX decreases. Buy on weakness.**
- **Lotos is trading at a considerable premium to PKN Orlen on EV/EBITDA, and has more expensive capacity. Lotos's refinery business is expected to show quarter-on-quarter deterioration in earnings quality, and a higher net debt, in Q409. The company's capacity will increase in H2 2010 after the launch of a new hydrocracking unit. Sell now, buy in six months.**
- **PGNiG: The stock offers upside potential ahead of strong earnings from the Trade&Storage business expected in Q409 and Q1 2010. We predict a tightening in margins earned on sales of imported gas, an increase in CAPEX, and an increase in net debt, in H2 2010. Accumulate now, sell after Q1 2010 earnings announcement.**

Key Ratings: LOTOS (Reduce), PGNiG (Accumulate), PKN Orlen (Buy)

As sentiment to financial markets started to recover in 2009, so did prices of oil, and hence also the values of oil refiners, in particular those with strong upstream businesses (OMV +64%, MOL +72%). In keeping with the general upturn, Lotos shares surged 166% last year, though the rally was probably owed to the laying to rest of the rumors about the company's bankruptcy, which caused it to depreciate a staggering 73% in 2008. At the current price level, it is a good time to cash out of Lotos, which is expected to increase its debt and generate weaker profits from the refining business in coming quarters. What is more, tangible effects of the '10+' upgrade program will not materialize before the second half of the year (when the company plans to launch a new HC unit). The publication of Q1 2010 earnings around mid-year should create an opportunity to buy Lotos shares again, at a cheaper price.

PKN Orlen is expected to outperform the WIG20 index this year, in an improvement from 2009, when shares were under pressure due to concerns that the company would not be able to fulfill loan covenants, and due to weak earnings generated by the petrochemical business, and a large debt. These factors will play a diminishing role going forward, thanks in no small part to planned major divestments, but also owing to the improved performance of the retail and petrochemical businesses. 2010 earnings growth should also be supported by crack spreads, which are expected to expand in the absence of speculative run-ups in oil prices caused by a weak dollar. Note also that PKN shares have been rallying recently, in line with the global upswing in sentiment toward oil companies, and they will probably take a downward turn in the near future in keeping with the expected sentiment downturn. We advise investors to take advantage of any such weakness to buy PKN.

PGNiG was one of the WIG20's biggest losers in 2009 (rising just 5% during the year compared to the index's 33% gain), which was probably partly an indirect effect of its better-than-average performance in the crisis year 2008, but first and foremost a consequence of the weak earnings performance of the Trade&Storage business, caused by an unfavorable wholesale tariff regime. The regime changed to PGNiG's advantage in Q309, suggesting tremendous potential for earnings growth in the peak-demand seasons of Q4 2009 and Q1 2010, when households as well as business customers have increased natural-gas usage. Assuming no interruptions in gas supply by Gazprom (so far, the Russians have been showing good will and selling Poland more gas even though their contract has not been renewed yet), we expect PGNiG to turn a record profit in Q1 2010, and to report a full-year bottom-line figure over PLN 2 billion in 2010. If these expectations prove accurate, the company offers strong rates of return in a market which is expected to be weak in the initial months of the year. We maintain an accumulate rating on PGNiG, and we recommend cashing out after the Q1 2010 earnings announcement in anticipation of a reversal in the favorable relationships between imported gas prices and local tariff prices.

Chemicals

- **Ciech is positioned for the strongest earnings recovery in 2010, fueled by stabilized prices of petroleum products, and expanding margins on organic chemicals. Ciech is due for an ownership change, and should be able to secure long-term financing for itself. Buy after Q409 earnings.**
- **Market conditions remain challenging for fertilizer producers, but 2010 earnings should improve vis-à-vis dismal 2009 results. Sell after Q409 earnings. ZAP and ZCH Police are due to undergo privatization later in the year.**
- **Synthos should regain positive momentum in quarterly earnings in H2 2010 after a shrinkage in margins in Q409 and Q1 2010 caused by high prices of butadiene. Buy after Q1 2010 earnings.**

Key Ratings: Fertilizer producers (Negative)

All Polish chemical stocks except ZCH Police rallied in 2009, fueled by a pickup in the global chemical market, and inventory rebuilding. The top performer was Synthos (+164%), whose Q109 earnings results exceeded analyst expectations thanks to cheap petrochemical materials, government aid for the auto industry, and competitive EUR/PLN exchange rates. As the year progressed, prices of raw materials and the value of the zloty increased, dampening the momentum. These factors will affect Synthos's Q409 and Q1 2010 earnings (rapid hikes in butadiene prices, seasonally weak demand for EPS), and we would not consider the stock until after first-quarter earnings, once the market realizes that 2010 profits have no chance of matching the strong 2009 results. We see more near-term upside potential in Ciech, whose upcoming quarterly earnings should reflect the positive trends observed in the market of organic chemicals (stronger margins on TDI and epoxy resins, combined with expanding sales volumes). The ongoing privatization processes could also add value to Ciech shares, though this will be owed to the promise of stronger support from a private investor and achievement of refinancing arrangements with lenders, rather than a very unlikely tender-offer premium. We have very low expectations with respect to earnings upside offered by fertilizer producers like ZAP, ZAT, and ZCH Police, as the purchasing power of farmers (measured as the ratio of fertilizer prices to grain prices) remains low. Any improvement that might be owed to the closing gap between Polish and European natural-gas prices (an effect of a flat wholesale tariff of PGNiG and higher prices resulting from the formulas used in oil-linked contracts) and stronger sales of chemicals (especially at ZAP) is already priced in. Moreover, international fertilizer producers have been gaining in value lately on high expectations of investors who are eager to see the recovering global economy restore prosperity to the farming industry, but who, we believe, are in for a big disappointment. In light of these facts, we would consider selling fertilizer stocks after Q409 earnings, and buying them back toward the end of the year. Shareholders of ZA Puławy and ZCH Police should look out for privatization news in the second half of 2010. Any speculation about the possible merger of the two companies is bound to hurt the value of the former.

Power Utilities

- **Major developments coming up in the first half of 2010 include the IPO of Tauron, the divestment by the State Treasury of a large portion of its holdings in Enea, and a possible supply of PGE shares (after a lockup is lifted in May), all of which will keep investors bearish on power stocks.**
- **Our advice for the next six months is to overweight Polish power companies versus CEZ, whose earnings are expected to be weighed down by cheap**

contractual electricity sales and low spot prices. The Czech utility should see an improvement in the second half of the year, once EEX prices rebound, and after the company launches its first wind farm in Romania.

- **Our top pick for 2010 is PGE, which is due to move into the WIG20 index, and whose earnings are expected to accelerate in 2011. Buy CEZ after Q1 2010 earnings. Look into Enea as an interesting bet for the first half of the year.**

Key Ratings: PGE (Buy)

As a typically defensive sector, power utilities could not offer superior returns in the rallying market of 2009. Moreover, investor sentiment last year was additionally affected by a downturn in electricity prices on European exchanges, affecting producer earnings due to low spot prices and the implications for forward contract prices. All this had a negative effect on the performance of CEZ (which gained just 8% in 2009), which received a hard blow in late 2009 when investors had to make room in their portfolios for the debuting PGE. CEZ's earnings performance last year was also far from stellar. After a record first quarter, the company was faced with weaker demand from industrial electricity buyers, and a series of contract cancellations by customers. We do not expect CEZ's situation to change much in the next two quarters, and the Q1 2010 report will be the first to show the full impact of EUR 5-7/MWh price reductions on electricity sales and profit margins. In the second half of 2010, however, we expect a major shift in sentiment after CEZ opens its first wind farm in Romania (and starts to generate income from "green certificates"), which will coincide with a recovery in spot prices fueled by rising demand, and with an increase in the value of CO₂ emission certificates. Summing up, we advise underweighting CEZ in the first half of the year, and buying its stock after the summer vacation season.

The Polish power industry is immune to external price fluctuations, and enjoyed earnings growth in 2009. The values of listed power utilities were additionally supported by good prospects for fiscal 2010 (steady profits, relatively strong sales and distribution volumes). Players like PEP, ENEA, and Kogeneracja gained between 50% and 70% during 2009, though, given their sizes and free floats, the scale of this appreciation seems modest compared to their large international peers. Moreover, in case of ENEA, price rallies were additionally triggered by speculation about an acquisition by an industry investor and a possible tender-offer premium. This year, the Polish sector of power utilities has a bigger representation, and is about to gain a new member in Tauron, set for a market debut early this summer. Tauron's IPO (estimated at PLN 6bn minimum), combined with a free-float increase by ENEA and the May expiration of the lockup on the State Treasury's PGE shares, could have negative implications for energy shares. But it seems to us that the large equity supply is already priced in, and that a shift in sentiment could come after PGE is added to the WIG20 index in March. PGE is our top sector pick for 2010, because of its attractive price, a possible divestment of Polkomtel (resulting in additional dividends), strong earnings prospects after the launch of a new generator in 2011, and vertical integration, positioning the company to maximize the benefits of future hikes in electricity prices. For the first half of the year, we also give a positive rating to ENEA, whose earnings are expected to grow on higher distribution prices and steady wholesale prices. Note also that the State Treasury intends to resume efforts to privatize ENEA, which may again give rise to speculation about a tender offer premium.

Mines, Metals

- **Rallying copper prices cannot be explained with either demand / supply trends, or with disappointing 2010 demand forecasts for developed markets. Today's apparent balance of supply and demand has been achieved largely through purchases by China, or more specifically by the State Reserve Bureau (whose stockpiling is not tracked by metal exchanges). Once the Chinese economy starts to cool down, copper prices are bound to take a nosedive, with negative implications for KGHM's value.**
- **Polish coal is trading at levels that guarantee big profits for LW Bogdanka. The company is forging ahead with its capacity expansion program, expected to boost sales volumes by nearly 2 million tons in 2011 (+40% vs. 2010).**

Key Ratings: KGHM (Reduce), LW Bogdanka (Buy)

According to ICSG statistics, global demand for copper shrunk 0.8% during the first nine months of 2009, including a 45% surge in China and an 18.5% drop in other countries. Primarily responsible for the shrinkage were highly industrialized countries which account for 29% of global demand: Japan (-34%), USA (-22%) and EU (-22%). During the same period,

mine output increased 2.9%, and refined copper output declined 0.5%. The huge Chinese imports were largely owed to continued inventory building by the SRB. Global demand is clearly still weak, and the high prices quoted on the LME are a consequence of investors' betting on a weak dollar, and the SRB's reserve buildup. The SRB's completely unpredictable decisions make pointless any attempts at a fundamental analysis of the copper market. In our opinion, the risks entailed in an investment in KGHM (stemming from an expected downward correction in copper prices) outweigh the rewards, and we recommend reducing the stock.

In spite of downward pressure on prices created by cheaper Russian coal, LW Bogdanka has managed to maintain strong sales volumes and good selling prices. The rate of the price decline has been slower than expected, probably thanks to expensive rates charged by Upper Silesian mines which sell their coal for PLN 270 per ton, but remain barely above break even. In our opinion, a forecasted 23% drop in LW Bogdanka's 2010 earnings is not going to materialize. Assuming that coal prices decrease a little over 6%, the company should deliver a profit exceeding PLN 180m (a revision from an original forecast of PLN 142m; the consensus estimate is PLN 128m) this year. Further, LW Bogdanka is going to see a sharp increase in 2011 profits following completion of the first stage of its expansion plan (2011 sales volumes are expected to surge 35%, with coal prices remaining flat vs. 2010). The Polish coal market is currently shaped by recovering demand on the one hand, and high imports of cheaper coal from Russia on the other hand. Most severely hurt by the Russian imports are the Silesian mines which, even though they charge 6% more for one gigajoule of coal energy than LW Bogdanka, seem to be unable to turn a profit and generate cash for future capacity-enhancing projects. As their sales fall, and expenses remain untackled, their unit costs increase. These favorable market conditions are expected to work to LW Bogdanka's advantage throughout 2010.

Telecoms

- **Throughout 2009, TPSA was involved in negotiations to stop telecom regulator the UKE from splitting its business into retail and network operations. Luckily for the incumbent, the negotiations were a success. 2010 will be a year of restructuring for TPSA, which needs to adjust its expenses to market reality.**
- **We remain convinced that TPSA can offer its shareholders dividends of PLN 1.5 per share (plus buyback), suggesting a gross yield of 9.2% at the current price level. In spite of increased expenses on broadband infrastructure development, the company's ratio of FCF to EV remains at 10-12%.**
- **Netia took full advantage of TPSA's UKE-induced distraction to reinforce its presence in the market of broadband services, thus proving itself to be the leading alternative provider of Internet services in Poland. Now that TPSA is back in the game, the altnet is going to have a more challenging 2010.**

Key Ratings: TPSA (Accumulate)

The medium-term outlook for TPSA is brighter than in 2009. The company remains a high-dividend-yielding stock in spite of a higher CAPEX. When analyzing the telecom's deal with the regulator (which agreed to shelve the functional-division plan in exchange for investment commitments on TPSA's part), investors tend to focus on resulting future CAPEX, and fail to notice the benefits. One of the positive outcomes of the agreement is establishment of the terms of wholesale access to TPSA's network infrastructure (cost plus method instead of retail minus), which will enable the operator to compete more effectively for broadband internet users. This year, we expect a continuing reduction of the asymmetry in mobile termination rates (the difference in MTRs between the incumbent and new entrants is higher in Poland than anywhere else in Europe), which is essential for TPSA to be able to compete with P4 in the pre-paid market. We believe that the company achieved its PLN 3bn FCF target in 2009. TPSA still needs to adjust its costs to the current market situation, which we should see happening in each coming quarter. Investors should welcome the company's downsizing announcement expected after Q4 2009 earnings.

Netia fully capitalized on TPSA's weakness in 2009 by strengthening its presence in broadband access services. The company's current share price accurately reflects its value and future prospects in our opinion. We want to point out the levels of free cash flows generated by Netia and TPSA. Netia's revised budget assumes that the ratio of CAPEX to revenue will reach 15% in 2010, and we predict that it will decrease by a further 2 ppts in subsequent years. Based on our estimates, this suggests that Netia should reinvest about 60% of future EBITDA in order to remain competitive. In case of TPSA, these ratios are much lower (thanks to scale and mobile telephony) even during periods of heightened capital expenditure necessitated by regulatory requirements. In effect, TPSA's ratios of FCF to EV are more



attractive (at 11%) than Netia's, even given the latter's forecasted strong annual earnings growth in coming years (the altnet is expected to achieve an FCF/EV ratio of 11 in 2012).

Media

- **The main beneficiaries of the 3% increase in advertising expenses predicted in 2010 will be television networks (+4%) and Websites (+16%). Outdoor expenses are expected to rise 3%. Radio and newspaper advertising will remain flat at 2009 levels.**
- **Media companies like Agora, Cyfrowy Polsat, and TVN, will be strongly influenced by the expected strengthening of the zloty.**
- **We recommend overweighting companies that generate revenues from advertisement sales: TVN (with a forecasted FCF/EV of 4.3% in FY10 and 6.0% in FY11), and Agora (FY10E FCF/EV = 9.3%, FY11E FCF/EV = 8.4%).**
- **We would overweight WSiP and Cyfrowy Polsat vs. the broad market in the first half of 2010, and underweight them in the second half.**

Key Ratings: TVN (Buy), Agora (Buy)

It seems that the advertising market is poised for a rebound after a tough 2009. We expect a 3% increase in 2010 based on 3.0% GDP growth projections for Poland, and an appreciating zloty, even if the actual inflation rate is lower than analysts predict. Advertising expenses will still show year-on-year contraction against a high base in Q1 2010, to embark on a sustained upward trend in subsequent quarters.

The main beneficiaries of ad-spend growth will be television broadcasters, who are expected to record a 4% increase in 2010 revenues after a period of unprecedented double-digit losses. Online advertising will remain the growth leader, gaining as much as 16%, with increasing contributions from display ads. Contrary to prevailing opinions, we expect newspaper and radio revenues to remain steady at last year's levels. Expenses on outdoor advertisements are expected to rise 3%.

Based on the assumptions laid out above, our top picks in the media sector are Agora and TVN, whose current market values do not fully reflect the upcoming increase in advertising expenses. In case of Agora, 2010 earnings results will be additionally supported by savings achieved in 2009. In turn, TVN will benefit from the troubles of rival public broadcaster TVP (expected to post a pre-tax loss of over PLN 100m) which will allow commercial broadcasters to gradually eliminate discounts offered to advertisers. Further, TVN's future earnings prospects could be boosted by the passing of new multimedia laws, legalizing product placement, and lifting commercial-airtime restrictions currently imposed on private TV broadcasters (on the downside, access to more TV ad-time will drive advertisers away from other media, most notably print).

Since Agora's current share price reflects the company's growth prospects to a larger extent than TVN, we recommend overweighting the latter in 2010. A good time to increase positions in Agora will come after investors have adjusted their portfolios to account for the planned changes in the composition of the WIG20 index in early Q2 2010.

For Cyfrowy Polsat, the main earnings driver in 2010 will be its broadband Internet offer launched jointly with Sferia. Other supporting factors include an expected appreciation of the zloty against the euro, and a decrease in the costs of set-top box subsidies resulting from a slower expansion of the subscriber base and a large share of rental STBs. CPL is a defensive stock, and we recommend overweighting it in the first half of the year and underweighting in the second half.

The implementation of a new national curriculum in 2009 forced WSiP to increase advertising expenses on the one hand, but allowed the company to capture a bigger piece of the textbook market on the other hand. There is a tender offer in progress on 100% of WSiP shares, but we doubt that current shareholders will be tempted to sell at the cheap price of PLN 16 offered by the buyer. We recommend overweighting WSiP in the first half of 2010, and underweighting the stock in the second half.

IT

- **An increase in corporate and institutional demand for IT services and computer hardware is not likely to occur earlier than in late 2010.**
- **On the upside, there is an upcoming influx of large e-government orders.**
- **We would overweight companies focused on catering to the public sector.**
- **In the second half of 2010, we also recommend overweighting hardware distributors.**

Key Ratings: Asseco Poland (Buy), Sygnity (Buy)

We do not expect a shift in demand from banks, corporations, or the energy industry, earlier than in 2011. On a positive note, IT companies can expect increased demand from the government sector this year. The Polish Ministry of the Interior and Administration plans to spend a total of PLN 408m this year following PLN 3.5bn of expected contract awards aimed at accelerating e-government progress. We think that these plans are overly optimistic, and that most of the e-government projects will be postponed until 2011. The first tenders should be announced in late Q1 / early Q2 2010.

Our top IT picks for 2010 are companies with established track records in serving the government sector. The growth potential offered by the e-government initiatives seems not yet priced in the shares of Asseco Poland (11.4x FY10E P/E after adjustment for treasury stock), Sygnity, or Qumak Sekom. But companies like ATM and Comarch can also look forward to increasing their business thanks to government orders.

Hardware distributors will remain under the influence of the trends observed in 2009 well into 2010, when their sales are expected to pick up. Throughout this period, large players will be widening their advantage over small companies. In spite of recent rallies, we still see upside potential in AB (12.4x FY09/10 P/E), Action (10.9x FY10E P/E), and Asbis (11.5x FY10E P/E). Komputronik's earnings in the first half of 2010 will remain under pressure due to a continuing restructuring of Karen, and to uncertainty about whether outstanding payments can be recovered from the bankrupt Techmex. Since profit-taking may temporarily affect the performance of these distributors in the next six months, we recommend underweighting them in H2 2010.

Construction

- **Concerns over tight profits on future contracts, fueled by increasing competition, will continue to keep sentiment to the construction sector bearish until the end of the first quarter, even in spite of good Q409 earnings, prompting a neutral three-month rating.**
- **The competitive pressures are expected to ease in the spring, with the influx of new orders for road construction and housing (and power plant orders, expected to come on line in late 2010). Certain builders are expected to disappoint with the profits generated on contracts captured in 2009. We recommend overweighting construction stocks starting in Q2 2010.**
- **Our top picks are cheap companies with well-developed infrastructure- and power-engineering businesses, and with large cash resources, like Polimex Mostostal, Mostostal Warszawa, and Rafako. We would also recommend watching smaller industrial and power-plant builders like Instal Kraków, Projprzem, Prochem, Bipromet, Remak, and Energomontaż Południe, as well as Ulma, Unibep, and Hydrobudowa Polska.**

Key Ratings: Mostostal Warszawa (Buy), Unibep (Buy), Rafako (Buy), Polimex Mostostal (Accumulate), Erbud (Accumulate)

The construction sector's median FY10 P/E ratio stands at a historically low level of 13.2.

Sentiment to the construction sector should turn to positive in the spring, after good earnings reports and thanks to reduced competition. In case of some companies, e.g. Unibep, temporary problems with order portfolios might coincide with low margins on new contracts, affecting earnings results. But this is already priced in.

Our expectations of a decrease in competition are based on the fact that most builders have almost filled up their 2010 order books, on the upcoming outpour of power-engineering and road-building orders (estimated at PLN 16bn), and on increasing demand for construction services (in particular housing construction).



We estimate that road-contract awards will amount to PLN 10bn in H1 and PLN 6bn in H2 2010, and we reckon that the value of power-plant orders will increase from PLN 3bn in the first half to PLN 13bn in the second half of 2010. Moreover, residential developers are expected to start construction on about 20,000 new units for an estimated PLN 3.5bn in the next six months, in an effort to meet increasing demand for small flats and replenish their housing stocks. The pickup in demand for commercial properties will be much less pronounced, and industrial construction will remain stagnant until 2011.

A PLN 3.6bn CAPEX budget of the national railroad system operator PKP PLK is not going to be a source of lucrative contract opportunities for track developers this year.

Construction companies can expect an increase in costs, including costs of labor, starting in H2 2010, though certainly not at the breakneck speed observed in 2006 through 2008.

Low investor confidence in construction stocks has brought the prices of small and medium-sized companies down to very attractive levels offering much more upside potential than the prices of their larger peers. In addition to Unibep, we would encourage investors to look at power-engineering firms like Energomontaż Południe and Remak, and industrial builders like Instal Kraków, Projprzem, Prochem, or Bipromet (even though a major upturn in demand for their services is not expected until 2011, these companies own valuable property assets and have sizable cash resources). Further, ABM Solid is a bargain, and Hydrobudowa Polska is also low-priced in addition to facing the prospect of being sold by its owner PBG. Our least favorite construction pick is Mostostal Zabrze, whose earnings are expected to deteriorate this year.

Property Developers

- **Housing developers are trading at attractive price levels. Going forward, we expect an increased supply of homes to be met by strong demand. We are overweight on residential developers in the first half of 2010, and neutral in the second half (after real-estate stocks realize their upside potential) as we wonder about the shape of future trends in the mortgage- and property-finance policies of Polish banks.**
- **In commercial real-estate, we expect a continuing downward trend in effective rental rates (due to increasing vacancy rates in expanding office space, and due to cost-cutting by tenants) as well as yields. As rental rates approach their local lows, the number of property deals will rise (though not much given the expected interest-rate hikes in developed countries).**
- **We recommend overweighting housing developers and underweighting commercial developers. We have a buy rating on J.W. Construction and Polnord, and an accumulate rating on Dom Development. We also have a positive outlook on Gant and Triton Development.**

Key Ratings: J.W. Construction (Buy), Polnord (Buy), Dom Development (Accumulate)

Most residential developers are trading at discounts to their NAV and BV. Demand for first homes is expected to remain high in Poland, and developers who can offer the most popular small flats to prospective buyers should see their sales grow in 2010. In turn, sales of big upmarket apartments will be slow unless sellers are willing to reduce prices. We expect the volume of mortgage loans to increase from PLN 40bn in 2009 to PLN 45bn in 2010. Selling prices will remain steady in the first six months of the year, while average listing prices could decline slightly. The government's subsidized-mortgage program *Rodzina na Swoim* is going to become much less popular in 2011 after home prices go up, boosting revenues for developers in 2010.

We expect firms with strong liquidity like Dom Development and J.W. Construction to launch a number of new projects in 2010. By mid-year, Polish banks should relax their lending criteria, and reduce required downpayments toward real-estate financing from 40%, to 20-30%. We estimate the number of housing starts in H1 2010 at 20,000 (in 2009, they approximated 70,000). All in all, the nearest future of the Polish housing industry depends on the lending policies of banks.

In commercial real-estate, we expect a decrease in effective rental rates due to an increasing supply of new space. At the same time, we predict a downward trend in yields, though the declines will not be big due to forecasted interest-rate hikes. All in all, we do not expect a major upward shift in the value of commercial developments in 2010.



International investors are showing an increasing interest in Polish commercial spaces. Sales at high yields can be expected chiefly of companies that have inflated LTV ratios, and that need to restructure their property portfolios (such as Orco or Atlas Estates). Less restrictive bank policies will improve developer capacity to finance new commercial projects.

International real-estate markets, in particular in developed countries, are under pressure from expected interest-rate cuts and declining demand, which could lead to a downturn in the prices of residential as well as commercial spaces. But these trends will not have much influence on Polish property developers, except maybe for multinationals like GTC.



Current ratings by BRE Bank Securities

Company	Rating	Target Price	Current Price	Rating Date	Price on Rating Day	FY2009 P/E
AB	Buy	15.13	16.08	2009-08-06	11.55	12.8
ACTION	Buy	18.49	16.14	2009-12-22	15.98	8.9
AGORA	Buy	23.70	22.38	2009-11-13	19.75	32.7
ASBIS	Accumulate	4.23	4.50	2009-12-02	3.68	
ASSECO POLAND	Buy	71.90	60.65	2009-11-19	57.30	12.6
BUDIMEX	Accumulate	82.50	81.20	2010-01-06	75.75	12.0
BZWBK	Hold	195.40	190.00	2010-01-19	190.00	17.2
CENTRUM KLIMA	Buy	15.10	12.19	2009-11-06	11.50	15.0
CEZ	Hold	140.60	144.10	2009-11-04	143.80	1.5
CIECH	Hold	39.90	36.75	2009-12-03	37.49	
CYFROWY POLSAT	Accumulate	14.90	15.36	2009-12-02	13.88	18.6
DOM DEVELOPMENT	Accumulate	50.10	44.44	2009-11-05	44.00	14.5
ELEKTROBUDOWA	Hold	169.30	177.00	2009-12-04	170.00	16.7
EMPERIA HOLDING	Hold	70.30	85.85	2009-09-04	72.30	14.1
ERBUD	Accumulate	53.50	54.50	2010-01-06	47.15	16.3
EUROCASH	Hold	9.90	17.89	2009-05-06	9.81	22.2
GETIN	Buy	10.20	8.80	2010-01-19	8.80	27.9
HANDLOWY	Buy	90.30	73.55	2010-01-19	73.55	17.4
ING BSK	Accumulate	811.60	739.00	2010-01-19	739.00	16.0
J.W. CONSTRUCTION	Buy	14.00	13.07	2009-12-02	11.26	4.6
KĘTY	Hold	115.40	123.00	2009-11-05	106.80	16.9
KGHM	Reduce	90.40	109.00	2009-12-01	107.80	9.5
KOMPUTRONIK	Hold	11.56	10.70	2009-12-08	11.39	40.7
KREDYT BANK	Accumulate	15.30	14.10	2010-01-19	14.10	130.3
LOTOS	Reduce	26.60	32.02	2009-12-01	31.94	5.7
LW BOGDANKA	Buy	80.10	81.80	2009-12-15	70.00	13.6
MILLENNIUM	Hold	4.33	4.49	2010-01-19	4.49	
MONDI	Hold	56.00	77.90	2009-09-03	51.00	54.5
MOSTOSTAL WARSZAWA	Buy	79.60	62.00	2009-12-02	68.00	12.2
NETIA	Hold	4.30	4.58	2009-11-06	4.36	
PBG	Hold	212.00	216.00	2009-11-12	218.50	15.2
PEKAO	Hold	181.50	176.00	2010-01-19	176.00	19.6
PGE	Buy	27.49	24.60	2009-11-04	23.00	12.8
PGNiG	Accumulate	4.11	3.82	2009-11-13	3.73	25.4
PKN ORLEN	Buy	38.20	35.75	2009-11-18	31.97	11.5
PKO BP	Hold	39.60	38.90	2010-01-19	38.90	21.1
POLICE	Hold	5.50	6.05	2009-12-14	5.02	
POLIMEX MOSTOSTAL	Accumulate	4.50	4.24	2010-01-06	4.00	13.1
POLNORD	Buy	46.80	34.00	2009-12-15	31.77	21.7
RAFAKO	Buy	11.60	11.56	2009-09-25	9.74	23.5
SYGNITY	Buy	18.10	13.60	2009-12-15	14.15	
TELEKOMUNIKACJA POLSKA	Accumulate	19.20	16.13	2009-10-30	17.58	14.9
TRAKCJA POLSKA	Hold	4.20	4.17	2010-01-06	4.10	9.9
TVN	Buy	14.60	14.40	2009-12-02	12.55	19.1
ULMA CONSTRUCCION POLSKA	Hold	82.20	87.90	2010-01-06	84.50	
UNIBEP	Buy	6.60	5.93	2010-01-06	5.58	11.5
WSiP	Hold	17.20	16.44	2009-09-03	16.61	13.4
ZA PUŁAWY	Hold	80.20	89.50	2010-01-06	80.90	25.2



Ratings issued in the past month

Company	Rating	Old Rating	Target Price	Rating Date
ACTION	Buy	Buy	18	2009-12-22
BUDIMEX	Accumulate	Hold	83	2010-01-06
ERBUD POLIMEX	Accumulate	Hold	54	2010-01-06
MOSTOSTAL	Accumulate	Buy	4.5	2010-01-06
TRAKCJA POLSKA ULMA	Hold	Accumulate	4.2	2010-01-06
CONSTRUCCION PL	Hold	Accumulate	82	2010-01-06
UNIBEP	Buy	Hold	6.6	2010-01-06
ZA PUŁAWY	Hold	Accumulate	80	2010-01-06

Ratings Statistics

	All					For Issuers Who Are Clients of BRE bank Securities					
	Sell	Reduce	Hold	Accumulate	Buy	Sell	Reduce	Hold	Accumulate	Buy	
count	0	4	19	10	15	count	0	1	5	3	7
% of total	0.0%	8.3%	39.6%	20.8%	31.3%	% of total	0.0%	6.3%	31.3%	18.8%	43.8%



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**List of abbreviations and ratios contained in the report.**

EV – net debt + market value (EV – economic value)

EBIT – Earnings Before Interest and Taxes

EBITDA – EBIT + Depreciation and Amortisation

PBA – Profit on Banking Activity

P/CE – price to earnings with amortisation

MC/S – market capitalisation to sales

EBIT/EV – operating profit to economic value

P/E – (Price/Earnings) – price divided by annual net profit per share

ROE – (Return on Equity) – annual net profit divided by average equity

P/BV – (Price/Book Value) – price divided by book value per share

Net debt – credits + debt papers + interest bearing loans – cash and cash equivalents

EBITDA margin – EBITDA/Sales

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A recommendation is valid for a period of 6-9 months, unless a subsequent recommendation is issued within this period. Expected returns from individual recommendations are as follows:

BUY – we expect that the rate of return from an investment will be at least 15%

ACCUMULATE – we expect that the rate of return from an investment will range from 5% to 15%

HOLD – we expect that the rate of return from an investment will range from -5% to +5%

REDUCE – we expect that the rate of return from an investment will range from -5% to -15%

SELL – we expect that an investment will bear a loss greater than 15%

Recommendations are updated at least once every nine months.

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Comparative – based on a comparison of valuation multipliers of companies from a given sector; simple in construction, reflects the current state of the market better than DCF; weak points include substantial variability (fluctuations together with market indices) as well as difficulty in the selection of the group of comparable companies.