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CONFIDENTIAL

Warsaw, 2008-10-30

Mr Francesco Papadia
Director General Market Operations
Chairman of the
Market Operations Committee

European Central Bank
Kaiserstrasse 29
D-60311 Frankfurt am Main
Germany

Dear Mr Papadia,

Referring to your yesterday's telephone conversation with Mr. Piotr Wiesiołek - the First Deputy President of the NBP, we would like to present the following reasons explaining why the NBP is applying for the ECB assistance in providing euro liquidity to the Polish banking sector.

In recent years, banks operating in Poland have accumulated considerable exposure to loans denominated in foreign currencies. These are mainly mortgage loans denominated in Swiss francs. The popularity of loans denominated in Swiss francs was a consequence of two major factors: a high positive interest rate differential and the continued nominal appreciation of the Polish currency. Measures undertaken by supervisory authorities (the so-called S Recommendation issued in July 2006) reduced the scale of loans granted in foreign currencies, but did not eliminate the trend completely.

Banks operating in Poland financed these loans in foreign currencies only partially, thus opening on-balance sheet open FX positions. The difference between the banks' foreign currency assets and liabilities as of 31 August 2008 amounted to ██████████ zlotys (██████████ ██████████ EUR, according to exchange rate on that day). Banks secured some of these positions using off-balance sheet transactions, mainly CIRS and FX swaps. Due to the lack of a developed CHF/PLN market, in order to do so, banks used USD/PLN and CHF/USD, as well as EUR/PLN and CHF/EUR swaps. Because FX swaps are short-term operations, banks have

to roll them over. Most banks in Poland have open FX positions in one direction, therefore foreign banks were the main counterparties. The decreased liquidity on international interbank markets, as a result of the reduction of banks' credit limits, led to the situation, which started in the second half of September, where Polish banks have difficulties renewing transactions which hedged them against FX risk. In order to enable banks closing their FX positions the NBP launched FX swaps.

FX swaps are not the only instrument offered to banks recently. It is a part of a package of measures announced by the National Bank of Poland, which also includes:

- open market repo operations with a maturity up to 3 months
- extending the list of assets that may be used as collateral for lombard loans
- reducing the haircut level for lombard loan collateral.

In the letter of October 28, 2008 Mr. Sławomir Stanisław Skrzypek - the President of the NBP, confirmed that we accept the line of action (i.e. the idea of repurchase transactions agreement) suggested in the letter of Mr. Jean-Claude Trichet – the President of the ECB. The amount we kindly propose to be included in such agreement is 10 billion EUR.

We are looking forward to hearing from you.

Yours sincerely,

Krzysztof Senderowicz
Director
Domestic Operations Department
National Bank of Poland