

Weekly economic update

8 – 14 April 2013

Central banks' decisions were the main drivers of the global and domestic markets last week. First, the Bank of Japan, headed by the new governor Haruhiko Kuroda, decided to double the value of purchased assets in two years' time. Monthly purchases of debt securities are to amount ca. USD74bn (1.4% of Japan's GDP). Such an aggressive monetary easing triggered a massive sell-off of the yen, but stock and bond markets climbed on this news. According to Polish deputy finance minister, Wojciech Kowalczyk, move of the Bank of Japan was the main culprit behind strengthening of Polish bonds, which gained from 8bps in 2Y sector (reaching new all-time low at 3.06%) to almost 20bps in 5- and 10Y sector. Moves of the bond curve caused that IRS between 1 and 5Y dropped to the lowest levels in history. Declaration of the ECB governor, who said that the bank is considering standard and non-standard measures in order to support situation in the euro zone and that it is important for him to maintain the unity of the zone, pushed the EURUSD exchange rate strongly up, and helped the zloty to gain against the dollar. Plans of Hungarian central bank to stimulate the economy caused a temporary weakening of the forint, but in the end its proposals proved not as controversial, as investors feared (we elaborate more on this issue in FX market section), so the forint pared its losses, which also positively affected the zloty against the dollar.

Central banks will remain on stage this week, but in our view their impact will not be as significant as in the previous days. We are expecting – like the market – that the MPC will leave interest rates unchanged. In our view possible changes in the statement (like stressing that the Council is in the wait-and-see mode and importance of upcoming data) will not significantly alter market expectations about future decisions. Comments of the MPC members may prove more important. Still, the zloty and domestic interest rate market will rather remain stable until the results of MPC meeting are published. Higher volatility is however possible in the following days, under influence of global events. Technical analysis is suggesting that in April the EURPLN may recede from local peaks. Uncertainty about further decisions of the MPC and about economic outlook in Poland and abroad cause that potential for strengthening of the zloty is limited.

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (8 April)							
9:00	CZ	Industrial output	Feb	%YoY	-5.0	-	-4.1
10:30	EZ	Sentix index	Apr	pts	-14.1	-	-10.6
12:00	DE	Industrial output	Feb	%MoM	0.1	-	0.0
TUESDAY (9 April)							
8:00	DE	Exports	Feb	%MoM	-0.3	-	1.4
WEDNESDAY (10 April)							
	PL	MPC decision		%	3.25	3.25	3.25
20:00	US	Minutes Fed					
THURSDAY (11 April)							
11:00	PL	Bond auction					
14:30	US	Initial jobless claims	week	k	360	-	385
FRIDAY (12 April)							
	EZ	Meeting of euro zone ministers of finance					
11:00	EZ	Industrial output	Feb	%MoM	0.1	-	-0.4
14:00	PL	Money supply	Mar	%YoY	5.8	5.7	5.6
14:30	US	Retail sales ex autos	Mar	%MoM	0.1	-	1.0
15:55	US	Flash Michigan	Apr	pts	78.3	-	78.6

Source: BZ WBK, Bloomberg, Reuters, Parkiet

Maciej Reluga Chief economist +48 22 586 8363

Piotr Bielski +48 22 586 8333

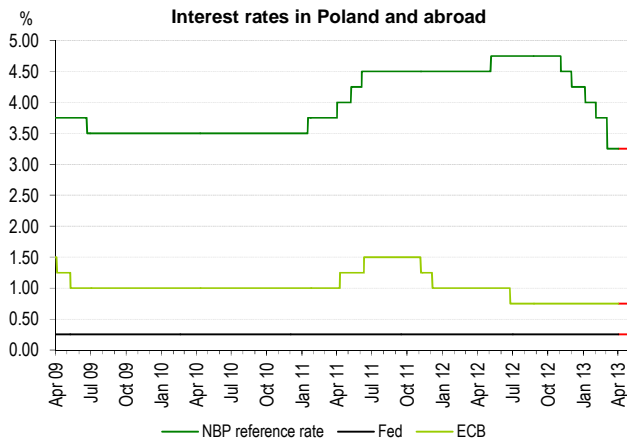
Agnieszka Decewicz +48 22 586 8341

e-mail: ekonomia@bzwbk.pl

Marcin Sulewski +48 22 586 8342

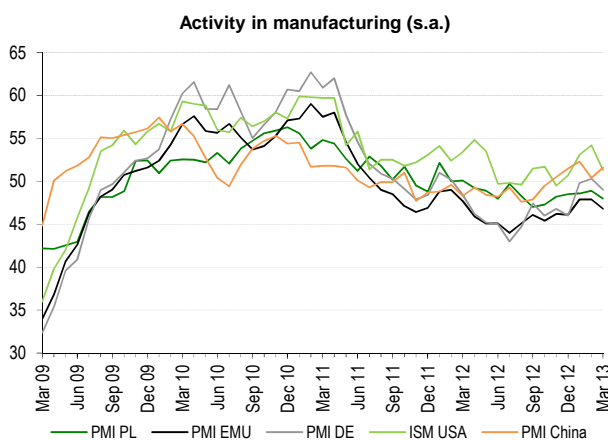
Marcin Luziński +48 22 586 8362

What's hot this week – ECB eases its tone, what about the MPC?

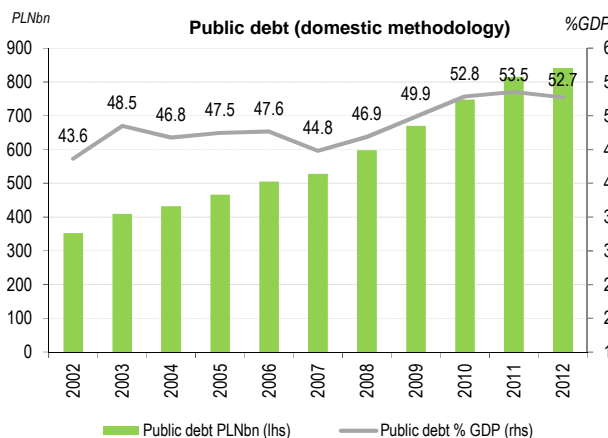


- Under impact of pessimistic information from the economy, the ECB decided to ease its tone, suggesting a possibility of interest rate cut or other unconventional actions.
- The MPC after recent, deeper than expected, cut in March, left door open for further rate cuts, but – as statement and comments suggested – this can occur only if macroeconomic scenario proves significantly weaker than this outlined in the NBP projection.
- This month rates will remain on hold (the MPC needs at least 2-3 months to assess the situation). Statement can include some slight changes, like reintroduction of sentence (removed last time), that further decisions will depend on upcoming data. However, in our view the Council will not suggest clearly that recent data raised probability of occurrence of scenario supporting further rate cuts.

Last week in the economy – PMI indexes show no recovery



- The PMI index for Polish manufacturing slid markedly to 48.0 in March from 48.9 in February and proved weaker than expected. Deterioration of employment, output and new export orders was recorded. This gauge clearly shows that industrial activity was shrinking in Q1. Moreover, a plunge of output prices subindex reflected the lack of cost pressure.
- Final estimates of PMI indexes for manufacturing in the euro zone and in Germany proved slightly better than flash, but services indexes clearly disappointed. In due course, composite PMI indexes for the euro zone are suggesting that pace of decline of economic activity strengthened for the second month in a row. Even though they suggest that GDP contracted in 1Q less considerably than in 4Q2012, there are worries that the widely expected recovery of European economy may be delayed.



- Public debt at the end of 2012 amounted to PLN840.5bn, i.e. by ca. 3% more than one year earlier. At the same time, debt-to-GDP ratio (according to domestic methodology) fell from 53.5% at the end of 2011 to 52.7%. General government debt (according to ESA95 methodology) amounted to PLN886.8bn at the year-end, which makes 55.6% of GDP versus 56.4% at the end of 2011.
- This was the first decline of debt-to-GDP ratio since 2007. We do not expect this tendency to continue this year, mainly due to slower nominal GDP growth accompanied by higher than last year nominal deficit of public finances.

Quote of the week – March's budget revenues better than in February

Hanna Majszczyk, deputy finance minister, Reuters, April 4

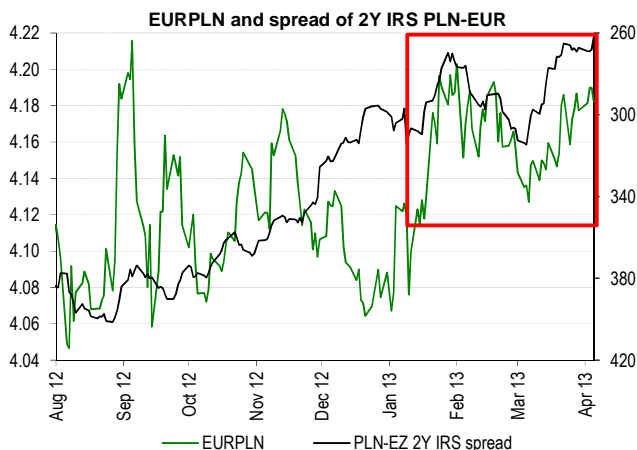
Our tentative estimates show that budget deficit amounted to PLN25bn after March, but it may prove lower in the end. Revenues were better than in February, VAT tax receipts were also satisfactory.

Ludwik Kotecki, MF chief economist, Gazeta Wyborcza, April 2

First signals on March's tax receipts are calming. But I do not want to say that we are happy and look at the situation through pink-tinted glasses, but to explain that when economy is slowing down, this does not automatically mean a need to amend budget bill.

Even though results of budget in the two first months of the year were very weak (mainly as a result of low tax revenues), flash FinMin's estimates for March suggest an improvement – the deficit after three months of the year was record-high, but in March alone it was almost a half of the one recorded one year ago. We do not know any details yet, but the Ministry said it was due to some improvement in tax revenues (including VAT). Still, we estimate this year's shortfall in tax receipts at ca. PLN18bn. Despite higher-than-assumed inflow of NBP profit (possibly ca. PLN5bn), amendment of budget bill in H2 cannot be ruled out.

Foreign exchange market – MPC will probably not affect the zloty



EURPLN may stay below recent peaks

- During the past week the EURPLN stayed in the upward trend initiated at the beginning of March. After the release of rather weak data in the euro zone, Poland and CEE region, the exchange rate tested the resistance area at 4.19-4.20.
- Due to strong surge of the EURUSD the zloty gained versus the dollar. The USDPLN plunged from 3.27 to 3.21. Earlier in the week it reached nearly 3.285 – highest level since mid-November 2012.

- The market is unanimous in the opinion the MPC will leave interest rates unchanged this month. We expect the volatility of the EURPLN to be subdued as investors will wait for the decision and the statement of the Council. Only in the following days some more visible and long-lasting moves are possible.

- Since the last week of July 2012 the EURPLN broke 4.20 only four times and only for a few hours. Technical analysis suggests that in April the EURPLN may retreat from recent peaks. Still, the uncertainty related to next decisions of the MPC and the pace at which the situation in the domestic and global economy will improve shall constrain the room the zloty's appreciation.

Euro under the impact of the ECB and US data

- The ECB meeting and US data had biggest impact on the EURUSD during the past week. Slightly less optimistic outlook for euro zone's economy presented by the central bank dragged the exchange rate down to ca. 1.275. However, in the following days the euro was recovering fast due to declaration on readiness to take further actions to support the Euroland's economy. Monthly US nonfarm payrolls number was weakest since June 2012 and this also hit the dollar. Consequently, at the end of the week the EURUSD was close to 1.30.

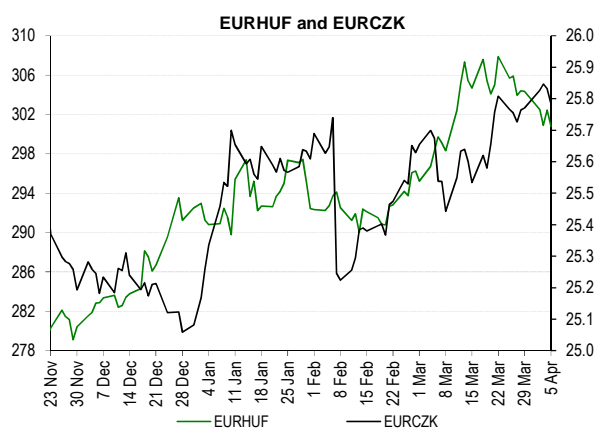
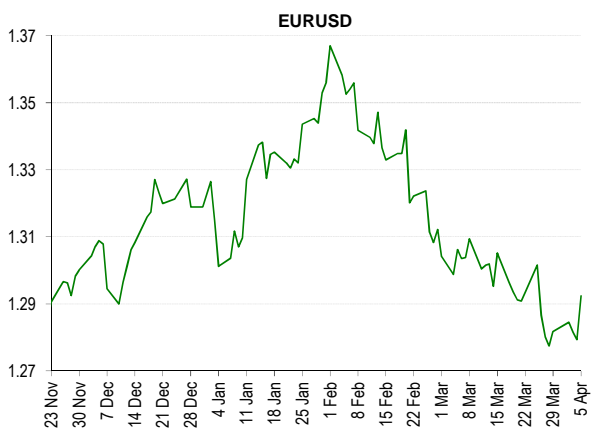
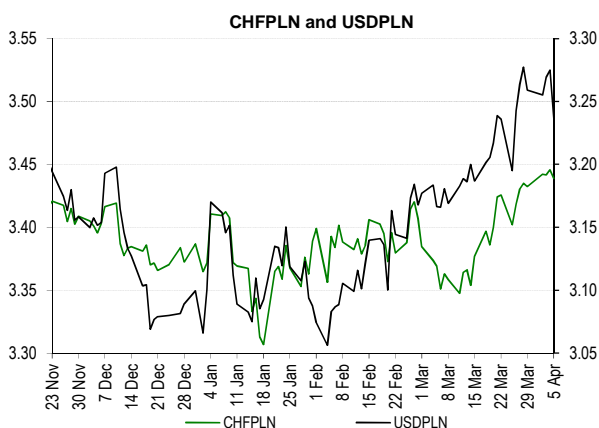
- The EURUSD 4th time since end March tested the support at 1.278 and this week's attempt was again unsuccessful. Since the beginning of February the EURUSD stays in the downward trend but recent surge questions the continuation of this tendency.

- The end of the coming week may be particularly vital for the EURUSD as more US data will be released. Last labour market data disappointed and fuelled hopes the Fed will keep QE3 alive in coming months. More weak data may put further pressure on the greenback.

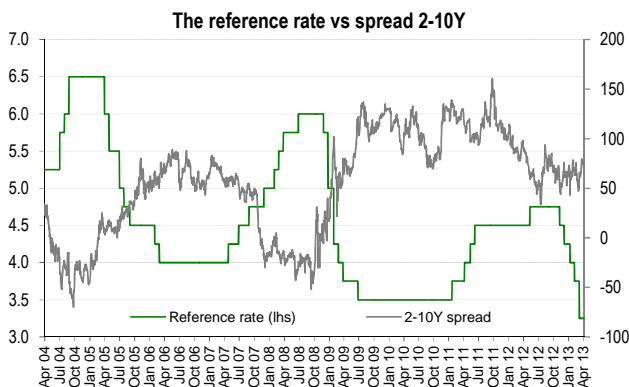
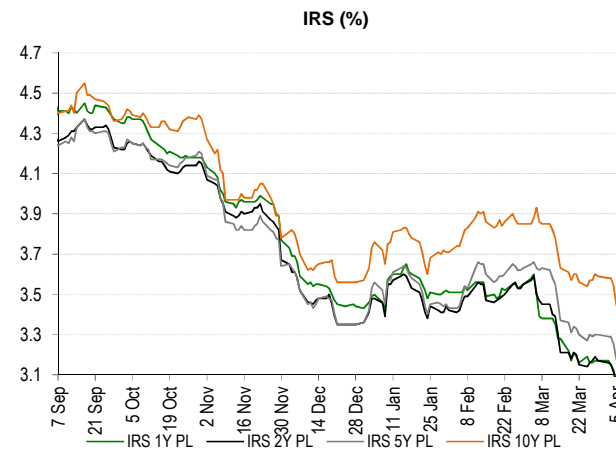
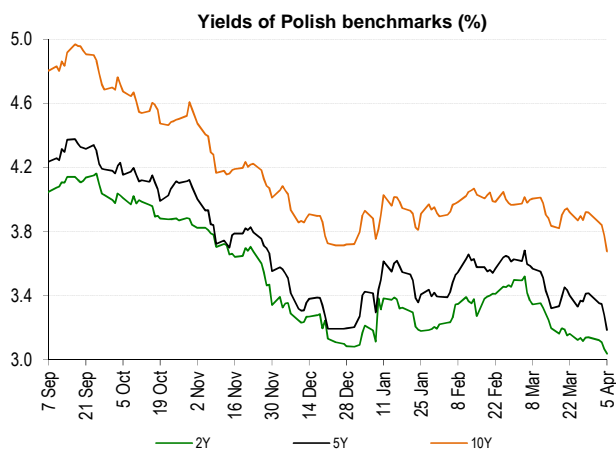
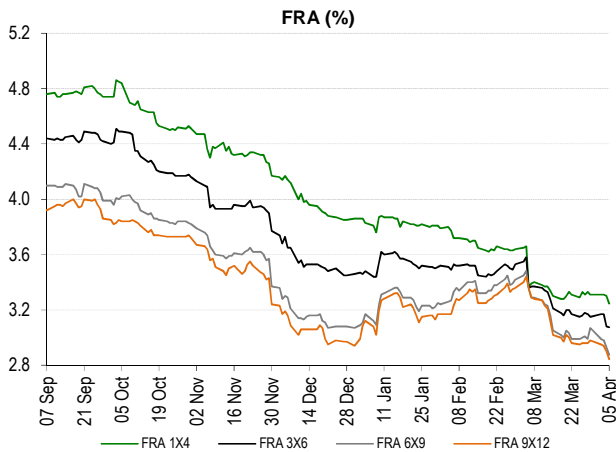
Forint gains versus the euro

- The forint continued to recover vs. the euro during the past week, though at some point investors started to worry again that MNB may conduct too expansive monetary policy. In the second part of the week the MNB accepted a Funding for Growth Scheme aiming at stimulating the domestic economy. The plan includes, among others, allotment of HUF250bn to commercial banks that will be able to borrow at 0% and lend further to small and medium companies at maximum 2% cost. As the plan occurred to be less controversial than the market had feared, the forint gained versus the euro.

- The EURCZK increased from 25.7 to 25.9 in response to weaker than expected Czech PMI for manufacturing data. This fuelled expectations for intervention of CNB on the FX market. Still, in the following days the Czech koruna managed to pare losses.



Interest rate market – The MPC's meeting and auction results crucial for market



FRA contracts lower and lower...

▪ Last week WIBOR rates have continued gradual downward trend. In weekly terms the scope of decline amounted to only 2bps and at the end of week rates for all tenors were at 3.37% (flat WIBOR curve from 1M to 12M). FRA market has remained more vulnerable. Significant decrease in bond yields and IRS rates pushed FRA rates down, in particular for longer terms (to the lowest level in history).

▪ Currently, FRA market is pricing-in rates cut by almost 50bps in 9 months horizon. We think this situation will not change after the MPC meeting. Less optimistic assessment of economic outlook in the euro zone, presented by the ECB at its April's meeting will probably not weigh on MPC's views on domestic growth path to the extent to send a clear signal about possible next interest rate cuts.

... just like bond yields and IRS rates

▪ End of the week brought a marked strengthening of bonds, so domestic benchmarks are closing the week at all-time lows. Bonds were gaining thanks to strengthening German debt (10Y Bund is oscillating slightly above support at 1.20%), thanks to expectations for MPC interest rate cuts and announced actions of the Bank of Japan. Deputy finance minister Wojciech Kowalczyk said that last decision of the Japanese central bank caused "an intensified inflow of Asian capital" on the Polish market, strengthening mostly the longer end of the curve. In weekly terms, yields of 10Y dropped by 25bps and yields of 2Y by 10bps.

▪ IRS rates were also declining due to strengthening debt. They reached new all-time lows, at 3.05% for 2Y, 3.18% for 5Y and 3.45% for 10Y. IRS curve remains relatively steep, with 2-10 spread at ca. 40bps. What is more, IRS-WIBOR6M spread approached minimums from the end of 2012.

MPC meeting and bond auction in spotlight

▪ Wednesday's MPC decision and Thursday's bond auction are the most important events of the interest rate market this week. We are expecting, like the market, that the MPC will keep interest rates unchanged. Thus, investors will focus on statement and on the post-meeting press conference. The tone of the official communique will be probably changed somehow as compared to last month, however we think it is quite unlikely that the Council will clearly signal that the probability of scenario supporting further rate cuts has increased.

▪ On the first auction in April, the Finance Ministry will offer long papers with fixed (DS1021) and floating rate (WZ0124), worth PLN2-5bn in total. Final value of the offer will be published on Tuesday. Current market situation is favourable for the auction, so we are expecting that the Ministry will have no major problems with tapping the market. It is probable 10Y paper will be placed with the lowest yields ever.

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