Bank Zachodni WBK

Weekly economic update

21 November – 27 November 2005

Economic data published last week were quite surprising. Although CPI inflation fell weaker than predicted and reached 1.6% instead of widely expected 1.5%, this has not affected conclusions from the data. Except from high fuel prices (in October their growth rate lowered due to effects of reduction in excise tax), there are no signs of strong inflationary pressure currently. What is important, even high oil prices do not lead to intensification of inflationary processes, which was shown well by much lower than expected PPI. From the point of view of monetary policy, which should react rather to imbalance between demand and supply and not to exogenous shocks on oil market, an important fact is that inflation prospects are still favourable despite the economy grows faster and faster. Further strengthening of economic activity was confirmed by better than expected data on industrial output. The most surprising figures last week were data on average wages that showed a jump of 6.4%YoY, twofold higher than the most upbeat forecast. However, it may turn out during the nearest week, when the CSO will reveal detailed data on a structure of wage growth in October that a trend in wages growth rate is less favourable for consumption demand prospects and at the same time less dangerous for inflation prospects.

All in all, the data published last week, although surprising, did not change much the picture of economic situation. The data due for publication in the nearest week (the key numbers will be core inflation measures on Tuesday and retail sales on Friday) probably will also not add much new. They should confirm that the economy gradually gains momentum, but indicate at the same time that the expansion takes place in a way that is not pose serious threat to the medium-term inflation outlook. Taking into account recent comments from a few MPC members, one cannot exclude a rate cut at the next week's meeting of the Council, but only under a condition that GDP data for 3Q05 bitterly disappoints. Besides, central bankers will pay much attention to government's ideas regarding fiscal policy, including the shape of amendment to the 2006 budget.

Economic calendar

Time GMT	COUNTRY	INDICATOR (importance level*)	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
		MONDAY (21 November)					
10:00	**POL**	**Auction of 52-week T-bills PLN500m (M)**					
10:00	EMU	Trade balance (M)	Sep	€bn	-0.3	-	-2.6
		TUESDAY (22 November)					
15:00	**POL**	**Core inflation (H)**	**Oct**	**%YoY**	**1.3**	**1.3**	**1.3**
15:00	**POL**	**Business climate (M)**	**Nov**	**pts**	**-**	**-**	**-**
		WEDNESDAY (23 November)					
10:00	**POL**	**Switch bond auction (M)**					
14:45	EMU	Michigan index (H)	Nov	pts	80.5	-	74.2
		THURSDAY (24 November)					
9:00	EMU	Current account (H)	Sep	€bn	-	-	-2.9
9:00	GER	IFO index (H)	Nov	pts	98.6	-	98.7
	US	Holiday					
		FRIDAY (25 November)					
9:00	**POL**	**Retail sales (H)**	**Oct**	**%YoY**	**6.2**	**5.7**	**5.4**
9:00	**POL**	**Unemployment rate (H)**	**Oct**	**%**	**17.3**	**17.4**	**17.6**

* Importance level: (H)igh, (M)oderate; Source: Parkiet Reuters, BZ WBK

Maciej Reluga Chief economist (+48 22) 586 8363

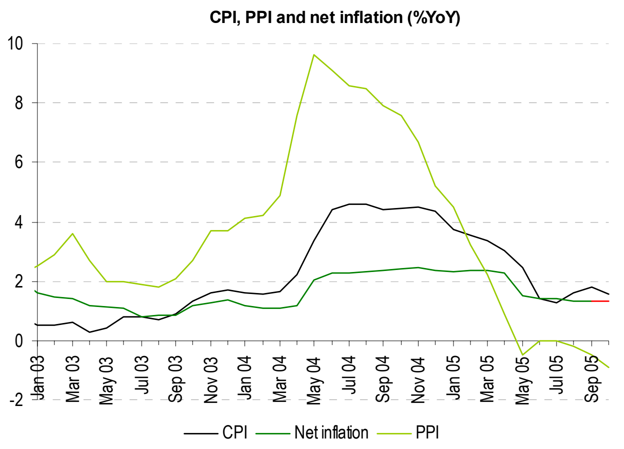
Piotr Bielski (+48 22) 586 8333

Piotr Bujak (+48 22) 586 8341

Cezary Chrapek (+48 22) 586 8342

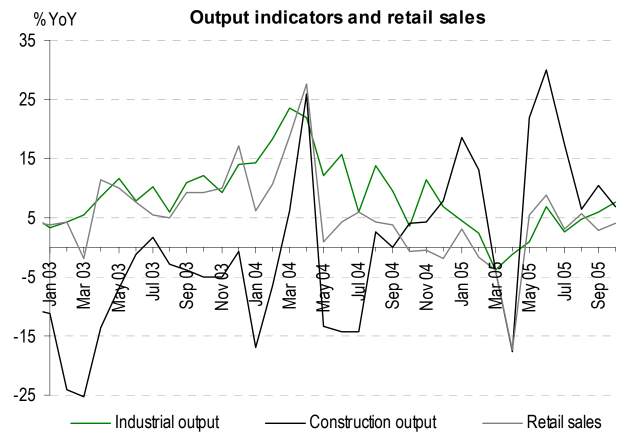
e-mail: ekonomia@bzwbk.pl

What's hot this week – Last data before GDP figures and MPC decision

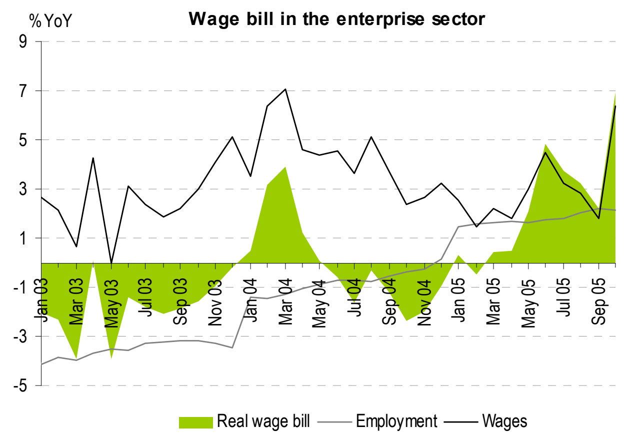


- We estimate that net inflation reached 1.3%YoY, unchanged as compared to September. This would confirm that excepting exogenous factors (fuel and food prices) inflationary pressure remains subdued.
- We do not expect the fresh business climate indicators to change much an assessment of the economic situation.
- We think retail sales growth rate will be much more important hint on economic activity and it should point to gradual revival in consumption demand, but not in a scale that could endanger inflation prospects seriously.
- Prospects for gradual revival in consumption will be confirmed by another fall in the unemployment rate.
- An important information will be data on a structure of wage growth from the CSO bulletin (on Friday), which may help to assess to what extent wage growth in October was a one-off and to what extent represented permanent trend.

Economy last week – Surprising wages and output



- October's inflation fell to 1.6%YoY (instead of expected 1.5%YoY) from 1.8%YoY in September. Positive evaluation of medium-term inflation outlook has not changed – there is still lack of signs of significant inflationary pressure.
- Producer prices fell by 0.9%YoY in October, which shows that it is difficult about pressure on prices even at the level of producers, even despite high oil prices.
- Growth rate of monetary aggregates clearly slowed down in October due to high base effect. The data have no major impact on monetary policy, but one should notice some signs of revival on loan market.
- Industrial output grew 7.6%YoY (seasonally adjusted growth reached 6.8%YoY). Construction output rose 6.8%YoY. Output figures were better than expected and confirmed that one can count on further acceleration of economic growth in the final quarter of this year.



- The scale of wage growth in October exceeded the most upbeat expectations and reached 6.4%YoY. As it may prove a one-off, the same as earlier slowdown in wage growth in September (to 1.8%YoY), so fat it is difficult to draw serious conclusions from the data. However, looking at average growth in average wages in the last two months (4.1%YoY), it seems that one may talk about a start of some positive tendency.
- Employment in grew 2.1%YoY, continuing rise in labour demand along with economic expansion.
- Strong wage growth together with solid rise in employment translated into clear improvement in wage bill. It grew 8.6%YoY in nominal terms and 7%YoY in real terms, the strongest in many years. It bodes well for consumption demand prospects, although wage bill growth in th nearest months may weaken.

Quote of the week – Rate cuts still possible, but under some conditions

Jan Czekaj, MPC member; ISB, 17 November

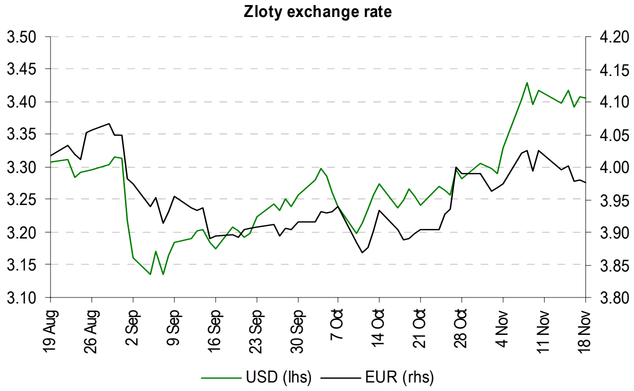
If GDP growth in 3Q05 reaches 3.5%, it would be neutral for monetary policy.

Andrzej Wojtyna, MPC member; ISB, 17 November

If it turns out that data on economic growth does not show clear acceleration exceeding 3% coupled with stronger rebound in investment, it would increase room for manoeuvre (with rates).

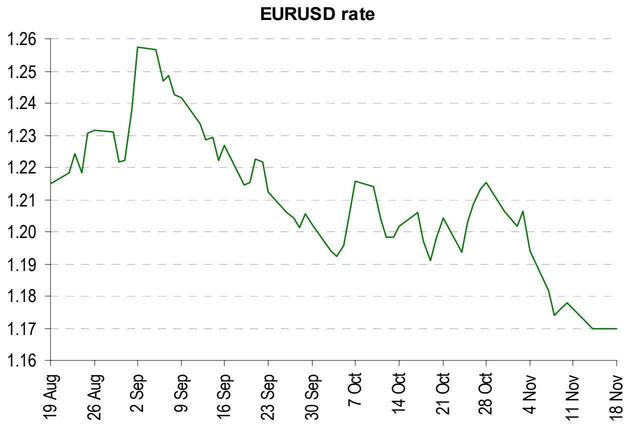
Comments of MPC members from the last week suggests that they still see some room for rate cuts. The decision on rates will heavily depend on GDP data for 3Q05. If the pace of economic growth does not exceed clearly 3% (e.g. does not reach 3.5% indicated by Czekaj as neutral for monetary policy), it may induce some central bankers to vote for another rate cut. Some role may be played also by fiscal plans.

Market monitor



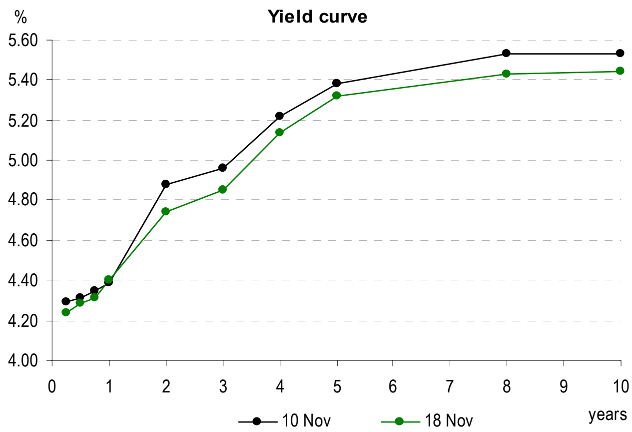
Zloty stronger on political stabilization

- FX market calmed down on successful confidence voting and zloty was gradually strengthening either against euro or the dollar, which among other was effect of MinFin declaration on adopting conservative macroeconomic assumptions to 2006 budget draft. Higher volatility of USDPLN resulted from EURUSD moves. Economic data in Poland did not significantly influence zloty. Polish currency gained 0.4% against the greenback and 1.25% against single currency within last week.
- This week we forecast EURPLN to trade in range 3.95-4.05 and USDPLN between 3.33-3.43.



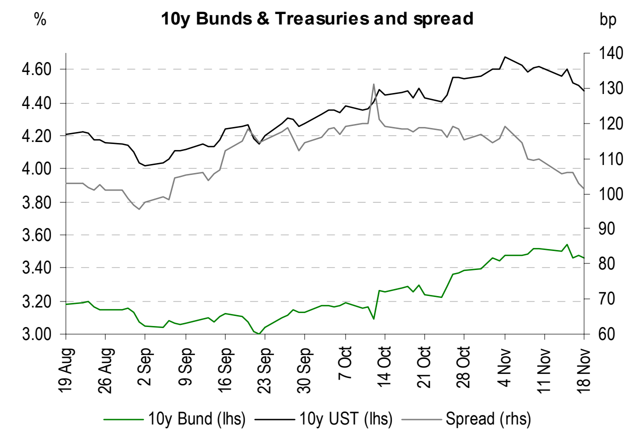
Dollar 2-year high

- Last week dollar kept on strengthening against euro down to 1.1648, close to 2-year high, in reaction to Ben Bernanke's comments on paying attention to curbing inflation and on U.S. data (higher retail sales and net capital flow). Euro partly recovered its losses on following mixed figures from U.S. and ECB's chairman Jean Claude-Trichet's statement on readiness towards rate increase in EMU.
- Consumer sentiment Michigan index, business sentiment Ifo index, statements of ECB and Fed as well as FOMC minutes will be the most important news for the greenback and may result in correction and dollar weakening. At the end of the week there is Thanksgiving Day in U.S. which will effect in lower activity.



Fixed income market gradual gains

- In the past week debt market strengthened as political situation stabilized and yields on core markets dropped. Bonds prices rose on MPC members statements on need of talks with government on euro adoption date and still possible rate cut. Inflation data as well as surprisingly low demand on tender resulted in temporary correction. Yields rose as well on higher than expected wages and industrial production figures.
- This week net inflation, retail sales as well as situation on core bond markets will be the most essential for Polish debt. Market should stabilize awaiting 3Q GDP data and budget next week.



U.S. yields and Bunds-Treasuries spread drop

- Last week U.S. data had mixed overtone. CPI, PPI and retail sales were lower than expected, though core PPI was below and core CPI along forecast. Yields of U.S. 10-year bonds hit 4.45, a Bunds 3.42 on large net capital flow in USA. Some figures suggested economic growth slowdown and curbing inflation, which weakened expectations on speedier rates hikes in United States. The end of the week brought Trichet's comments on readiness of soon rate increase and correction on U.S. market which caused further spread decline down to 101bp.
- The market will be sensitive on consumer sentiment Michigan index and business climate Ifo index as well as FOMC minutes form November meeting.

Additional information is available on request. Please contact Bank Zachodni WBK S.A. Treasury Division, Economic Analysis Unit, ul. Marszałkowska 142, 00-061 Warsaw, Poland, phone (+48 22) 586 83 63, email ekonomia@bzwbk.pl, http://www.bzwbk.pl