

Weekly economic update

15 – 21 May 2006

After a prolonged pause, Polish market will turn again to domestic macroeconomic data this week. Last time, data released for March showed many surprises and it is possible it will be the case also this time (although a surprise could be in the opposite direction). Our forecasts of economic figures for this week are mostly quite far from consensus – we foresee lower inflation, lower industrial output and lower current account gap – thus if they prove right, it will be a positive impulse for the debt market and for the zloty. But in general, this week's data should confirm the strength and persistence of economic recovery coupled with clear improvement on the labour market, and thus materialisation of our forecasts (not to mention higher market predictions) will not be a sufficient argument to convince the Monetary Policy Council to reduce interest rates in the near term.

The week will be full of data releases abroad. US data will be tracked with special attention due to Fed's hint that they will determine next rate decisions. Thus, strong market reaction and high EURUSD volatility could be predicted.

Economic calendar

TIME GMT	REGION	INDICATOR (importance level*)	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
MONDAY (15 May)							
12:00	POL	CPI (H)	Apr	%YoY	0.6	0.4	0.4
13:00	USA	Capital net flows (H)	Mar	\$ bn	80.0	-	86.9
TUESDAY (16 May)							
9:00	GER	ZEW index (H)	May	pts	60.0	-	62.7
9:00	EMU	Industrial production (M)	Apr	%YoY	3.0	-	3.2
12:30	USA	Build permits (H)	Apr	m	2.045	-	2.094
12:30	USA	House starts (H)	Apr	m	1.95	-	1.96
12:30	USA	PPI (H)	Apr	%MoM	0.2	-	0.1
13:15	USA	Capacity use (H)	Apr	%	81.5	-	81.3
13:15	USA	Industrial production (H)	Apr	%MoM	0.5	-	0.6
WEDNESDAY (17 May)							
9:00	POL	Auction of PLN1.8-2.8bn 5Y PS0511 bonds (H)	Apr				
12:00	POL	Wages (H)	Apr	%YoY	5.3	5.8	5.4
12:00	POL	Employment (H)	Apr	%YoY	2.7	2.6	2.7
12:00	POL	Current account (M)	Mar	€ bn	-400	-165	-538
9:00	EMU	Final HICP (H)	Apr	%YoY	2.4	-	2.2
12:30	USA	CPI (H)	Apr	%MoM	0.5	-	0.4
THURSDAY (18 May)							
16:00	USA	Philadelphia Fed index (H)	May	pts	12.6	-	13.2
FRIDAY (19 May)							
12:00	POL	PPI (H)	Apr	%YoY	0.9	0.9	0.9
12:00	POL	Industrial production (H)	Apr	%YoY	9.0	3.9	16.4
6:00	JP	BOJ meeting – decision (M)	Mar	%			
9:00	EMU	Foreign trade (M)	Apr	€ bn	2.0	-	3.1

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

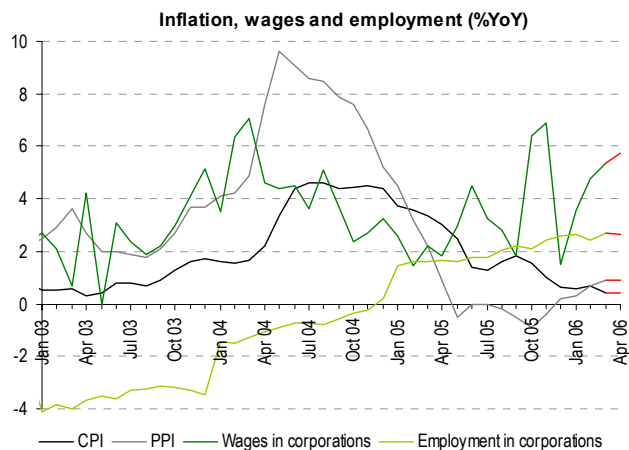
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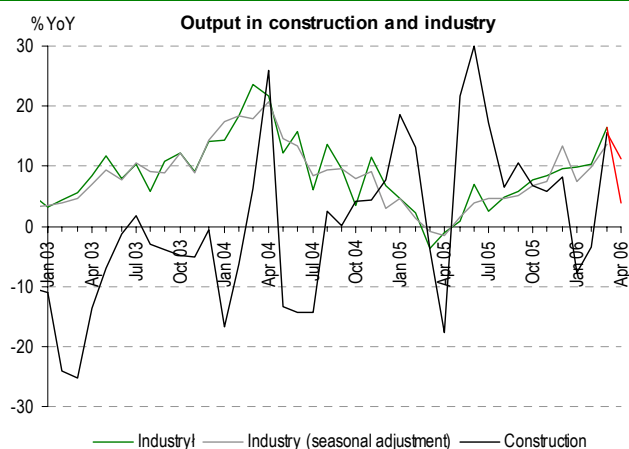
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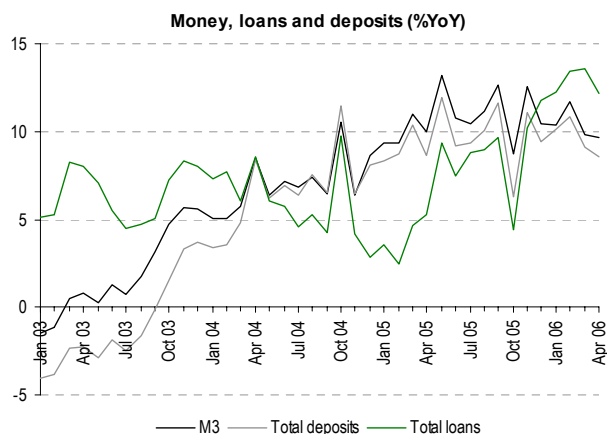
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What's hot this week – Will April data show more surprises?

- After a pause in domestic data publication, this will be a number of important data points that will appear with high significance for the debt market and for the zloty.
- The week will start with the publication of April's inflation rate. FinMin's estimate and market consensus point to a slight rise to 0.6%YoY, while we predict stable CPI at 0.4%YoY. Realisation of our forecast would be a positive signal for the debt market, although it would not change our view that the MPC will keep interest unchanged in May, watching the scale of revival in the economy and on the labour market.
- Some hint on the latter will be given on Wednesday. Employment in enterprises is likely to grow at a healthy 2.6%-2.7%YoY, and average pay rise will be strong as well (our forecast 5.8%YoY, market consensus 5.3%YoY), confirming good prospects for consumption demand.



- Balance of payments figures for March will be released also on Wednesday. Figures should be positive for the zloty, thanks to a strong advance in exports and imports (18.5% and 15.3%YoY, correspondingly) and a quite low current account balance – at €165m according to our forecast while the market anticipates ca. €400m.
- As regards industrial output growth, we see it also below market consensus – market predicts a 9%YoY rise while our forecast is ca. 4%YoY. In our view, a downturn in April will result from a lower number of working days, although data adjusted for this factor will represent a continuation of strong expansion in industry.
- The week will be full of data releases abroad. US data will be tracked with special attention due to Fed's hint that they will determine next rate decisions. Thus, a strong market reaction and high EURUSD volatility could be predicted.

Economy last week – Delay in rate hikes in US is possible

- Money supply decelerated growth from 9.8% to 9.6%YoY in April, roughly in line with our prediction. Growth in households' loans weakened from 25.4%YoY in March to 21.7%YoY in April and corporate credit slowed down slightly from 3.9% to 3.7%YoY. However, taking into account a scale of revival in economic activity, one could expect a pickup in loan growth in subsequent months.
- FOMC raised the federal funds rate by 25 bp for the 16th consecutive time to 5% maintaining the language that "some further policy firming may yet be needed", although the statement added also that "the extent and timing of any such firming will depend importantly on the evolution of the economic outlook" by which it left the door open for a pause in rate hikes in case upcoming economic data show a deceleration in economic activity.

Quote of the week – Finance minister does not plan to quit right now

Zyta Gilowska, deputy PM, minister of finance

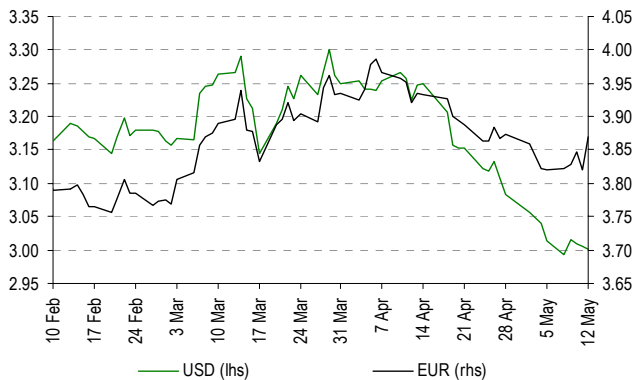
PAP, 12 May

I do not plan to run for Warsaw mayor. I have very responsible tasks, a chair of deputy Prime Minister joined with finance minister post is not a joke, especially that word "minister" means servant – I act like this and I feel like this.

From the financial market's point of view, Zyta Gilowska's presence in the government is a guarantee that the implemented economic programme will not fall into the strong influence of populist parties. It seems that one should not be afraid of finance minister's dismissal in the short term, although her earlier comments used to suggest that preparation of the 2007 budget and new public finance bill could be her last tasks in this cabinet (both projects should be completed by autumn).

Market monitor

Zloty exchange rate

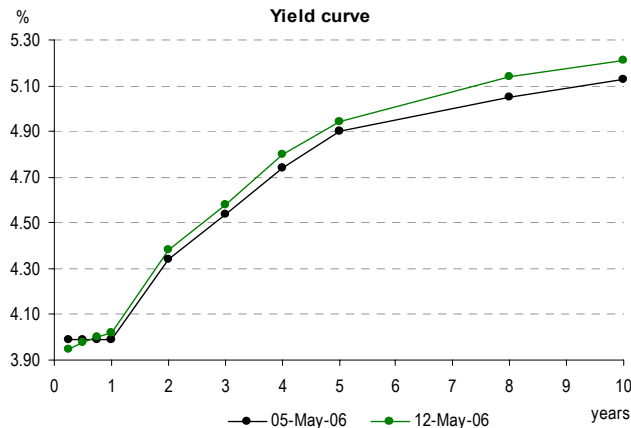


Zloty weakened by abroad and politics

▪ After slight weakening at the start of the previous week zloty gained in reaction to Zyta Gilowska comments on the positive effect of EU funds inflow on the zloty and with regards to falling dollar and increased interest of investors toward the region. At the end of the week zloty lost ground on speculation the finance minister could resign at the end of the year and weakening in the emerging markets. Thus zloty depreciated since last Friday by ca. 1.5% against the euro and remained unchanged vs. the greenback.

▪ In our opinion zloty will fluctuate near lately traded levels in range of 3.81-3.91 against the single currency and 2.95-3.05 versus the dollar and it will be dependent on the international markets situation, and most of all on expectations of Fed decision on its next meeting and investors sentiment toward the dollar.

Yield curve

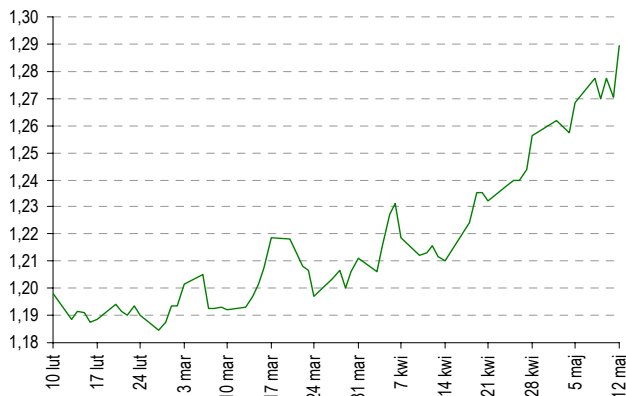


Slight changes on the debt market

▪ In reference with lack of essential data release scheduled for the past week on the domestic market Polish bonds were mainly under influence of the foreign markets. Yields slightly rose by 4-9 bp since last Friday and stronger sell-off occurred at the end of the week. Investors activity was limited through most of the previous week.

▪ With regards to increased MF's inflation forecast by the Ministry of Finance as well as in perspective of good macroeconomic data, market situation before the CPI release may be rather calm. In our view inflation may be lower than expected and yields may slightly fall, though before the wages and employment data the market there may be a correction. Further strengthening may come after PPI and industrial output data. The core markets may still negatively affect Polish debt.

Kurs euro do dolara

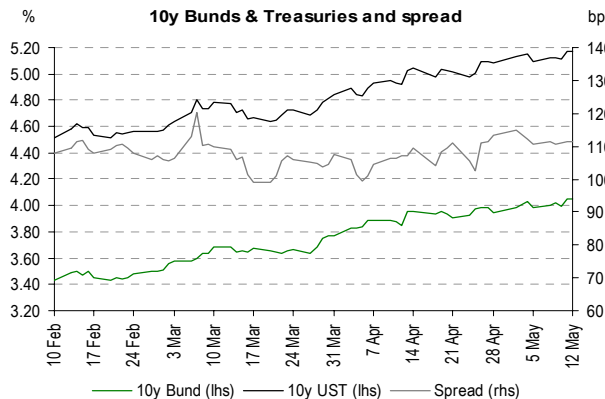


U.S. rate expectations continue to weaken the dollar

▪ At the beginning of the previous week the dollar continued to weaken against the euro, when investors awaited a "dovish" Fed's communiqué. After further weakening investors took some profits and euro slightly dipped. After rather neutral Fed's statement dollar bears speculating on a pause of interest rate hikes in U.S. gained advantage, which was supported by weak retail sales data and Michigan index. The EURUSD rate rose by ca. 1.3% in the previous week.

▪ Data on the capital inflow to U.S. may still weaken the dollar, and ZEW index work in favour of the euro. Housing markets data will be also important as they may confirm falling trend. Inflation data may be also of key importance as they may influence Fed's decision, which is highly dependent on the next data.

10y Bunds & Treasuries and spread



Further weakening on the core markets

▪ U.S. government papers weakened last week and 10Y yields rose from 5.11% to 5.16%. Yields of Treasuries fluctuated significantly, as they strengthened among others before Fed's decision and after release of import prices, and weakened before bonds auction and after Michigan index. 10Y Bund yields followed the U.S. market and rose from 4.0% to 4.05%.

▪ Next week U.S. inflation figures CPI and PPI headline and most of all core indices will be crucial for the core bonds markets amid June rate decision in United States. U.S. industrial output data and housing market data as well as ZEW index and HICP inflation in the euro zone will be also essential.

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