

Weekly economic update

5 – 11 June 2006

Last week's information from domestic economy had limited impact on financial market behaviour. GDP growth in the first quarter reached 5.2%YoY, which was close to predictions and confirmed that economy is on expansionary path. Strong rise in domestic demand, and in particular in private consumption, had slightly bearish overtone for fixed income market, however Polish bond yields were quite stable throughout the week. The MPC's decision to leave interest rates on hold was also not surprising for the market. The only new element was a warning against higher wages in public sector, which in our opinion is still only a conditional risk factor. We maintain our opinion that Polish official rates will remain stable until year-end and possibly also in 2007.

In the coming week, there will be completely no economic data releases in Poland. Also, no important events that could drive market sentiment are in the agenda. In the second half of the week the Sejm will debate on the opposition's motion to dismiss Sejm speaker Marek Jurek. However, given ruling coalition's majority support in the parliament there should be no problem with rejecting this motion, so its impact on market moods should be scarce. In such situation, Polish market will remain vulnerable to news and trends abroad. In the euro zone and United States some more economic figures will be released, e.g. non-manufacturing activity indices and trade balance data. Key event of the week will be the ECB meeting. The question raised by international market players is not whether the bank will hike interest rates or not, but rather whether it will be 25 or 50 bp. The scale of the ECB move and a tone of statement issued after the meeting could have significant impact on EURUSD development and sentiment on core debt market at the end of the week.

Economic calendar

Time GMT	COUNTRY	INDICATOR (importance level*)	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
MONDAY (5 June)							
9:00	POL	Auction of PLN1.0bn 52-week T-bills (M)					
	GER	Market holiday					
14:00	USA	Non-manufacturing ISM (H)	May	pts	60.1	-	63.0
TUESDAY (6 June)							
8:00	EMU	Non-manufacturing PMI (H)	May	pts	58.5	-	58.3
WEDNESDAY (7 June)							
9:00	POL	Auction of PLN1.8-2.3bn of 2Y OK0808 bonds (H)					
9:00	EMU	Retail sales (M)	Apr	%	2.3	-	-0.2
THURSDAY (8 June)							
11:00	GB	BoE meeting – decision (H)	May	%	4.5	-	4.5
11:45	EMU	ECB meeting – decision (H)	May	%	2.75	-	2.5
14:00	USA	Wholesale inventories (H)	Apr	%	0.5	-	0.2
FRIDAY (9 June)							
12:30	USA	Import prices (H)	May	%	0.7	-	2.1
12:30	USA	Trade balance (H)	Apr	\$ bn	-65.0	-	-62.0

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

Maciej Reluga Chief economist (+48 22) 586 8363

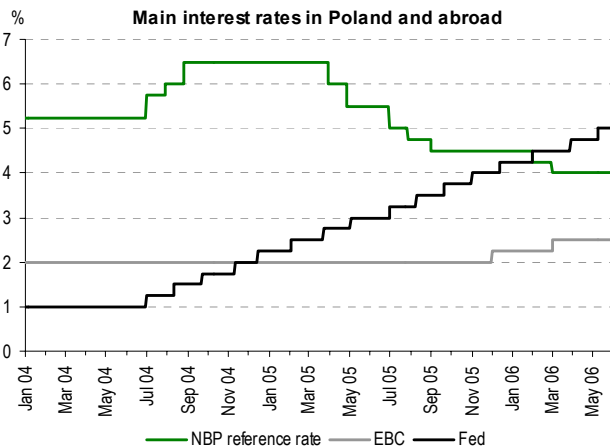
Piotr Bielski (+48 22) 586 8333

Piotr Bujak (+48 22) 586 8341

Cezary Chrapek (+48 22) 586 8342

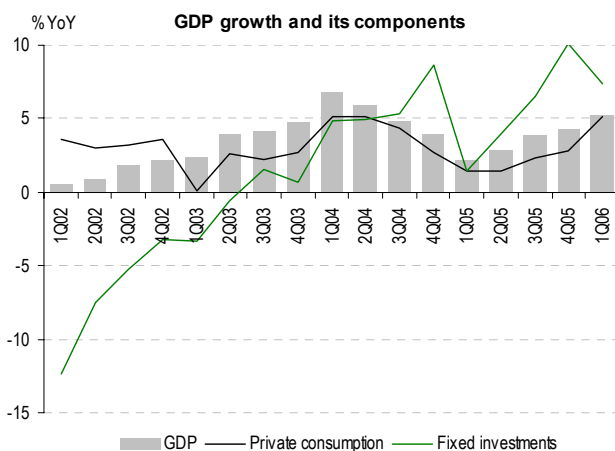
e-mail: ekonomia@bzwbk.pl

What's hot this week – Another week under influence of foreign markets

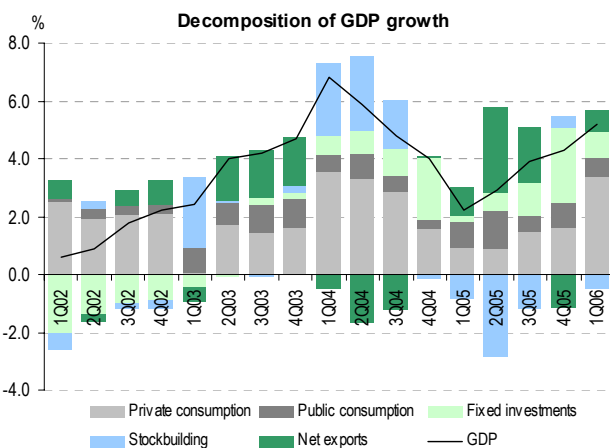


- This week there will be again no significant events or data releases on the domestic market that could have significant impact on investors' moods. Vote on Sejm speaker's dismissal at the end of week is unlikely to be successful and thus should not be important as well.
- Thus, market attention will be turned to information from abroad once again. In the U.S. and euro zone a couple of macroeconomic indices will appear (e.g. activity in services sector, trade balance) that could affect EURUSD exchange rate and expectations re rate hikes by Fed.
- EBC meeting could be important as well. The question that investors ask is not whether the bank will hike rates or not, but whether this will be 25 or 50 bp. Also, the statement after the meeting will be important as it could include some hints regarding future monetary policy movements.

Economy last week – Solid economic growth, interest rates unchanged



- GDP growth in Q1 2006 reached 5.2%, domestic demand increased 4.5% while net export added 0.7 percentage point to the overall growth rate.
- Investment growth reached 7.4%, which was below our forecast (ca. 10%), but still not a bad result. In turn, consumption growth was better than expected, at 5.1%.
- Q1 data suggest that this year's domestic demand could rise stronger than previously assumed (5.2% rather than 4.8%) amid stronger growth in private consumption (4.5% instead of 4%). We do not change our prediction for investment growth in 2006 (slightly above 9%) and total GDP growth (slightly above 5%), but share of net export could be a bit lower than we predicted.
- A downward risk for GDP growth in 2Q06 stems from lower number of working days than in 2Q05.



- Amid clearly accelerating economic growth, MPC decision to leave main interest rate unchanged at record-low 4.0% came as no surprise.
- The most important sentence of the MPC statement read "the balance of risk for future inflation has not changed significantly since the Council's last meeting, yet a risk factor related to wage pressures in the budget sector has appeared".
- It should be noted that a Council's warning against possible consequences of wage hikes is conditional and should not be treated as a strong signal of rising chances for rate hikes in near term. Therefore, we maintain our view that Poland's official rates will remain unchanged until the end of this year and possibly also in 2007.

Quote of the week – Is Ministry of Finance right again on CPI?

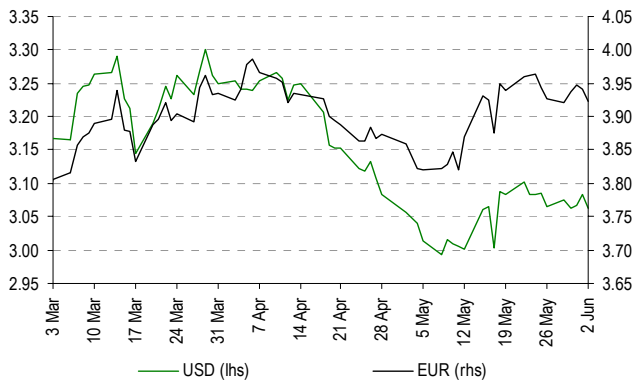
Ministry of Finance; www.mf.gov.pl, 1 June

The Ministry of Finance estimates that index of consumer prices in May (previous month = 100) was at 100.5. It implies that annual growth rate of consumer prices in this particular month could reach 100.9.

This is the second straight month when the ministry presents inflation prediction more pessimistic than market consensus. It should not be ignored given the fact that their previous forecast did materialise. It seems that a risk of deflation in the summer period moves away. On the other hand, a pace of inflation pickup is still moderate and CPI is not expected to return to 2.5% target earlier than in a few quarters time. This confirms our view that interest rates in Poland should remain stable for some time.

Market monitor

Zloty exchange rate

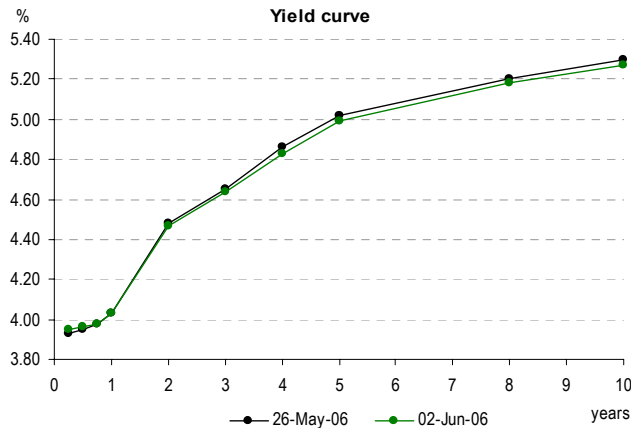


Quite calm on the FX market

▪ The start of the week was quite calm with regards to the long weekend on the main financial markets and zloty slightly weakened. Later Polish currency was supported by good GDP for the first quarter and weaker data from the U.S. economy, which contributed to strengthening of emerging markets currencies. During the week zloty appreciated against the euro by 0,2% and by 2% versus the dollar.

▪ This week the zloty could be affected by ECB decision and the communiqué influencing the interest rate expectations in the euro zone, as well as activity data and the trade balance influencing the EURUSD rate. In our opinion Polish currency will still fluctuate in range 3.88-3.98 to the euro and 2.97-3.07 against the dollar.

Yield curve

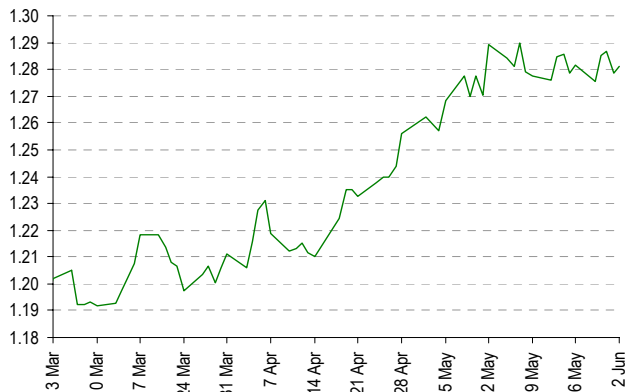


Moderate fluctuations of bond prices

▪ Yields of Polish bonds are fluctuating slightly below mid-May levels after the release of CPI and reacting mainly on the situation in the core markets. Bond prices remained almost unchanged as compared to the previous Friday. The MPC did not change the interest rates as expected and the communiqué was neutral for the markets.

▪ In the coming week there is going to be no important data in the domestic market and the Polish debt prices will trade in a quite tight range. The bond auction may show the sentiment of investors to our market. Debt may be still sensitive to the situation on the core bond markets, especially with reference to the decision meeting of the European Central Bank.

EURUSD rate

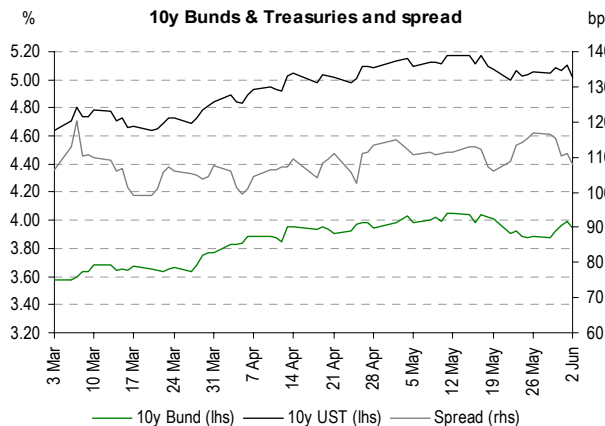


Significant dollar's fall

▪ The EURUSD rate was quite stable at the beginning of the week with regards to the Memorial Day in U.S. and market holiday in U.K. After the return of investors to the market the dollar started to weaken, though after the release of the "hawkish" FOMC statement from the May meeting the EURUSD rate fell substantially. The greenback's weakening occurred after the weaker than expected ISM index and non-farm payrolls data. During the week the EURUSD rose by 1.7%

▪ The relation of euro to the dollar will be still determined in the next week by interest rate expectations in U.S. (ISM and wholesale inventories), as well as in the euro zone (ECB's communiqué). Amid decreased expectations of further rate hikes in U.S. the trade deficit data are going to be important.

10y Bunds & Treasuries and spread



Weaker after FOMC minutes - stronger after payrolls

▪ The beginning of the week was featured by low activity on the core bond markets due to long weekend. Yields of 10Y Treasuries rose significantly (up to 5.13%), when the Fed's minutes suggested increased inflation pressures. However ISM index and non-farm payrolls contributed to a correction to 5.03%. Yields of 10Y Bunds returned from 3.88 to 3.94%.

▪ Next week the ECB is going to take decision on the interest rates level in the euro zone (expected hike by 25 bp), although the ECB's communiqué, which may include suggestions to the target levels and the pace of further monetary policy tightening. We forecast that ECB is going to increase the rates by 25 bp every quarter. Moreover the activity indices and the U.S. wholesale inventories may be important as well.

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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>



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