

Weekly economic update

8 – 14 January 2007

The New Year started with a significant correction in the emerging markets, which included also Poland. The main source of the weakening was market concern about slowdown in the American economy that found reflection also in FOMC minutes from December's meeting, market anticipation of weak non-farm payroll figures, as well as negative signals for the zloty coming from the technical analysis. In the background, there was information that Sławomir Skrzypek is new President's candidate for the post of the NBP governor. As a result, the zloty fell significantly on Thursday, by almost 2% against the dollar and over 1% against the euro, braking through important technical level 3.845. Much stronger than anticipated US non-farm payrolls data slightly eased pressure on the zloty at the end of the week. Nevertheless, in our view it is quite unlikely that the EURPLN rate soon drops back below 3.845. The zloty should rather stabilize in range of 3,845-3,9. Solid economic fundamentals still support the view of strong zloty, but the potential of further correction will depend on the moves of the global players. If concerns about slowdown in US economy deepen, the correction in the emerging markets may get stronger, and EURPLN may exceed 3.90 and the next resistance level will be at around 3.95.

In the nearest days, local market player's attention will be focused on the procedure of Sławomir Skrzypek's appointment for the post of NBP governor. On Monday and Tuesday the candidate will be interviewed in the parliament and the final vote in the Sejm is planned on Wednesday. If it does not get delayed for the procedural reasons, there should be no problems with the support of the coalition parties (absolute majority is required), as the Law and Justice again can use a threat of premature elections for minor coalition partners. Judging by the progress of work on 2007 budget in the parliament one could suspect that it could be very hard to approve the budget in time, i.e. until the end of January. This implies that soon we could see a return of the same story that took place one year ago, i.e. considerations whether the President will decide to dissolve the parliament or not. In general, the most important for the zloty should be information and trends on global markets. This week the calendar of data releases abroad is rather thin, with US retail sales and ECB meeting being the most important.

Economic Calendar

Time GMT	COUNTRY	INDICATOR (importance level)	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (8 January)							
10:00	PL	Auction of PLN900m 52-week Treasury bills					
WEDNESDAY (10 January)							
10:00	PL	Auction of PLN1.5-2.5bn 10Y Treasury bonds DS1017					
13:30	US	Bilans handlowy	Nov	\$ bn	-59.7	-	-58.87
15:00	US	Wholesale inventories	Nov	%	0.4	-	0.8
THURSDAY (11 January)							
10:00	EMU	GDP	Q3	%YoY	2.7	-	2.7
12:00	GB	BoE meeting - decision		%	5.0	-	5.0
12:45	EMU	EBC meeting – decision		%	3.5	-	3.5
FRIDAY (12 January)							
13:00	PL	M3 money supply	Dec	%YoY	14.3	14.1	14.4
13:30	US	Foreign trade prices	Dec	%	0.5	-	0.2
13:30	US	Retail sales	Dec	% m/m	0.6	-	1.0

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

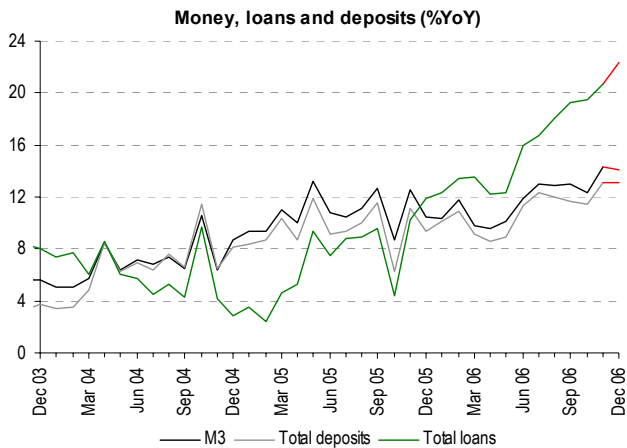
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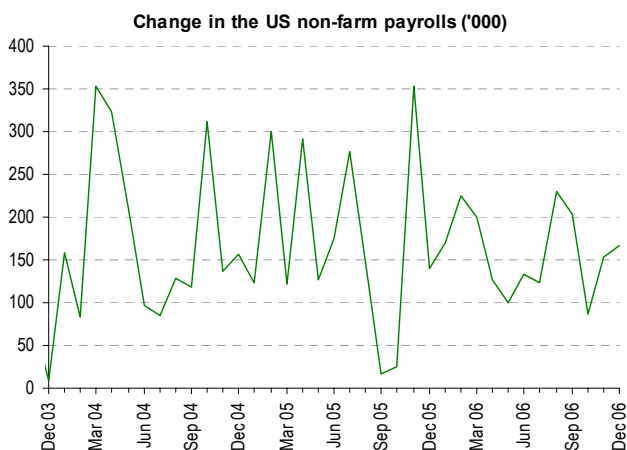
What's hot this week – Few data, change of NBP president

- The second week of the year will be as poor as regards domestic data releases as the former one. The only figures to see will concern money supply in December. Continuation of rapid growth in M3 (over 14%YoY) and loans (22%) is expected, but it will have little importance for the market.
- There will be small number of publications abroad. Still, the data from US economy may affect assessment of the economic perspectives, channelling through EUUSD exchange rate and emerging markets' currencies. Situation on global markets will remain a main driver of trends for the zloty and Polish equities.
- ECB meeting is expected to conclude without any changes in interest rates, although further monetary tightening is being anticipated further ahead.

Sławomir Skrzypek – NBP president hopeful

42-year-old Sławomir Skrzypek graduated from Silesian University of Technology in Gliwice and also holds M.A. in economics from Warsaw School of Economics. He holds an MBA from University of Wisconsin - La Crosse and diploma in Business Management from Georgetown University. Also, he was trained in asset and liability management in Polish banking system at Silesian University in Katowice. In 1993-1997 he was working in the Supreme Chamber of Control, being responsible for financial control of central and local administrations and of the banking sector. In 1997-2000 he was deputy president of the National Fund for Environmental Protection and Water Management. Since November 2002 he was deputy mayor of Warsaw, right-hand of president Lech Kaczyński, being responsible e.g. for financial policy, investments and proprietary supervision. Currently he is acting president of the state-owned PKO Bank Polski savings bank.

- Amid lack of other important events, at the start of the week the investors will be watching the procedure of NBP governor appointment. Sławomir Skrzypek's interrogation in Sejm will start on Monday.
- Sejm's vote is planned for Wednesday, 10 January (on the same day Leszek Balcerowicz ends his tenure), although it cannot be ruled out that it will be delayed e.g. due to procedural issues (it is not sure the candidate will manage to get required certificates in time).
- Coalition LPR and Samoobrona initially suggested their support of Skrzypek is not certain, but their stance should be tempered by the perspective of early election in case of coalition breakdown. Especially that the pace of work on 2007 budget suggests it will be difficult to pass budget on time, i.e. before end of January.

Economy last week – Strong US labour market

- At the very start of the New Year domestic data releases were rare and not significant for the market.
- NBP data on balance of payments in Q3 were not very much different from what was seen in monthly statistics. Current account deficit was low (€907m) and export growth was solid (20.1%YoY).
- PMI manufacturing index in Poland dropped in December to seven-months low, but remained well above 50 level, which is the mark between contraction and economic expansion. The decline was consistent with notable deceleration in industrial output growth in December predicted by us.
- US non-farm payrolls data were much stronger than predicted (167,000 in December, upward revisions in previous months, which strengthened the dollar and moderated the scale of correction in emerging markets).

Quote of the week – Monetary policy strategy unaffected?

Dariusz Filar, MPC member; Rzeczpospolita, 4 January

One should never forget that the MPC is a ten-member panel. (...) Obviously the new person may affect the internal balance of votes to some extent. But it does not imply that monetary policy will weigh on the new governor only.

Mirosław Pietrewicz, MPC member; Rzeczpospolita, 4 January

NBP governor is only one of the Council members and its chairman. I doubt whether the change will affect the MPC's policy.

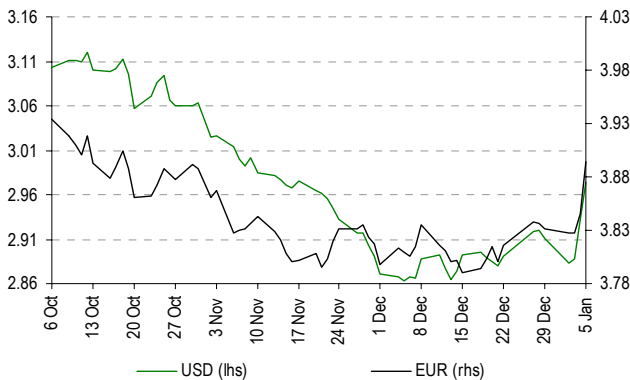
Marian Noga, MPC member; PAP, 4 January

The balance within the MPC is likely to remain unchanged – with camp opting against monetary policy tightening still prevailing.

MPC members correctly pointed out that the new NBP president will be only one out of ten interest rate setters, so one should not expect he will manage to set the tone of the Council's policy. Especially that even his predecessor was not able to do it despite very strong personality. Let's repeat one more time that if the new NBP chief starts pushing too strongly for monetary easing, it could yield opposite results, i.e. rate cut aimed at strengthening MPC credibility. Much more important will be NBP president's views on F/X policy, where his decisive power is much greater (e.g. as regards foreign exchange interventions).

Market monitor

Zloty exchange rate

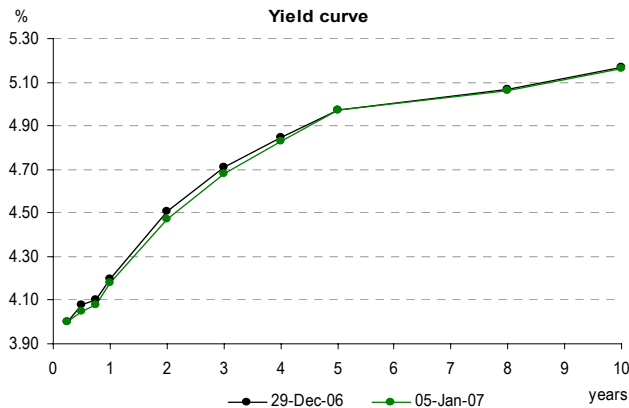


Significant zloty's sell-off

▪ Last week zloty significantly depreciated amid correction in the emerging markets. Some nervousness might have arisen with regards to the information of new nomination for the post of the NBP's president. Moreover there were some signals from technical analysis suggesting such weakening. EURPLN rate broke important level 3.845 and rose by ca. 1.5% up to 3.88, and USDPLN rate rose by 2.6% to 2.98.

▪ Strong economic fundamentals should support the zloty. We assume the potential for further zloty weakening is rather limited and after some stabilisation zloty may appreciate. US data will influence behaviour of foreign investors toward emerging markets, which will be crucial for the zloty. In our view this week the EURPLN rate may fluctuate in range of 3.81-3.91 with support at 3.845 and resistance at 3.9, while USDPLN rate in range of 2.92-3.02.

Yield curve

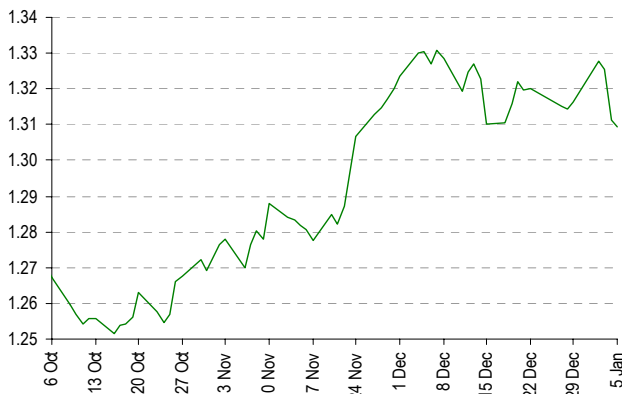


CPI forecasts support the short end of the yield curve

▪ Last week the debt market was positively influenced by the lowered CPI forecasts of the Ministry of Finance. Later sell-off in the emerging markets had an impact also on Polish bonds. In the result the yield curve steepened, as the short end of the curve was supported by the inflation forecasts.

▪ Lowered CPI forecasts support our view, that official interest rates may remain unchanged even throughout the whole 2007. The nomination of Sławomir Skrzypek for the post of the NBP's president may pose a risk for this scenario as the Monetary Policy Council may raise the interest rates by 25 bp, so as to calm down the market players. Another risk is still the tightening situation in the labour market.

EURUSD rate

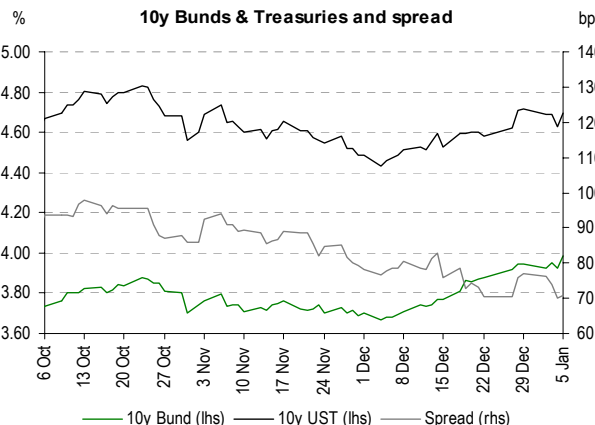


Better US data strengthen the dollar

▪ In the previous week the manufacturing ISM index in United States positively surprised the markets, what lowered the expectations of soon rate cuts in US and supported the dollar. The reports from the labour market that were released during the week (i.e. ADP) signalled a significant weakening, however Friday non-farm payrolls data were much better than expected, thus EURUSD rate fell to 1.3.

▪ The ECB's communiqué may include some hints on the scale of further rate hikes in the euro zone, which may result in a rise of EURUSD rate from today's levels. Recently released good data from US contribute to the rise of market expectations of soft landing in US. Next week the retails sales figure will be the most important for the dollar, while foreign trade figures may be also important.

10y Bunds & Treasuries and spread



Data from the labour market erased weekly bond gains

▪ After a significant rise of yields at the end of the previous year last week the US bonds market strengthened on expectations of soft labour market data. Yields of 10Y US bonds fell even below 4.6%, though much better than expected non-farm payrolls resulted in sudden rise in yields to the levels from the start of the week (4.68%). Yields of 10Y Bunds followed the US market, though rose by 3 bp since Monday to 3.98%.

▪ Presently the US retails sales data are going to be the most important with regards to the expectations of the future performance of US economy. In the euro zone the most the ECB communiqué is going to be the most important, as it may suggest the pace of further monetary policy tightening. US wholesale inventories and foreign trade prices may also have some weigh.

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