Bank Zachodni WBK

Weekly economic update

2 – 8 June 2008

Local macro data released last week and outcome of the MPC meeting had no direct impact on the zloty and the interest rate market. However, the domestic currency strengthened on the wave of appreciation of currencies in the region after the parity rate of the Slovak crown was revalued. Local bonds were under negative influence of clear increase in yields on the core debt markets and information from the Moody's agency that Poland was placed on the list of countries with moderate risk of rating's downgrade in case of economic slowdown. Hawkish comments from rate-setters after the MPC meeting also played a role. Even the dovish Stanisław Owsiak said that after strong GDP data there is growing probability of a rate hike in June.

This week no data releases are scheduled locally, but on Monday the FinMin will release its forecast of CPI inflation for May. Our prediction points to an increase to 4.4% from 4% rise in April. This will be the only relevant event in the Polish financial market, as the ministry will not organise auction of 5Y bonds scheduled earlier for Wednesday. Many events are due abroad with the key focus of attention to be on the ECB meeting and the US non-farm payrolls report. After the EURPLN dropped below the important level of 3.38, this week the domestic currency may remain at strong levels before the correction expected by us later in the year.

Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
		MONDAY (2 June)					
08:00	EZ	PMI manufacturing	May	pts	50.5	-	50.7
14:00	US	ISM manufacturing	May	pts	48.5	-	48.6
		TUESDAY (3 June)					
09:00	EZ	Revised	Q1	%YoY	2.2	-	2.2
09:00	EZ	PPI	Apr	%YoY	6.1	-	5.7
14:00	US	Factory orders	Apr	%	-0.1	-	1.3
		WEDNESDAY (4 June)					
09:00	**PL**	**Auction of 10Y floated bonds and 12Y inflation-indexed bonds**					
08:00	EZ	PMI services	May	pts	50.6	-	52.0
09:00	EZ	Retail sales	Apr	%YoY	-0.6	-	-1.6
12:15	US	ADP employment report	May	'000	-30.0	-	10.0
12:30	US	Labour productivity	Q1	%	2.5	-	2.2
12:30	US	Unit labour costs	Q1	%	2.0	-	2.2
14:00	US	ISM services	May	pts	50.9	-	52.0
		THURSDAY (5 June)					
11:00	GB	Bank of England decides on rates	Jun	%	5.0	5.0	5.0
11:45	EZ	ECB decides on rates	Jun	%	4.0	4.0	4.0
12:30	US	Initial jobless claims	w/e	'000	370.0	-	372.0
		FRIDAY (6 June)					
12:30	US	Non-farm payrolls	May	'000	-53.0	-	-20.0
12:30	US	Unemployment rate	May	%	5.1	-	5.0
14:00	US	Wholesale inventories	Apr	%	0.5	-	-0.1

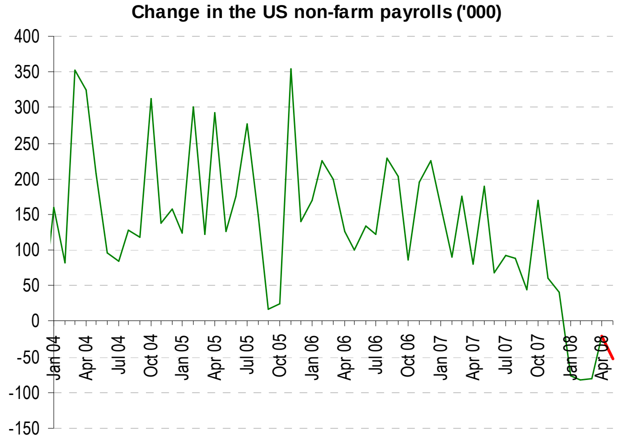
Source: BZ WBK, Parkiet, Reuters, PAP

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 – FinMin's inflation forecast and US data



▪ This week, the main event on local financial market will be the release of FinMin's inflation forecast for May.

▪ A significant increase in inflation from 4% in April is expected, among others due to a hike in natural gas prices that took place at the end of April. We predict CPI growth by 4.4%YoY. It is hard to say what will be FinMin's forecast, but it is likely to show a significant increase.

▪ Publicaiton of the FinMin's forecast will be the only important event in the domestic market, as the FinMin will not organise earlier planned auction of 5Y bonds on Wednesday. The reason for that it unfavourable situation in the debt market.

▪ Much attention will be drawn by numerous events abroad with particular focus on the ECB meeting on Thursday and the US non-farm payrolls report due on Friday.

Economy last week – MPC without sunrise, GDP growth above forecasts

Selected fragments of the MPC statement after April meeting

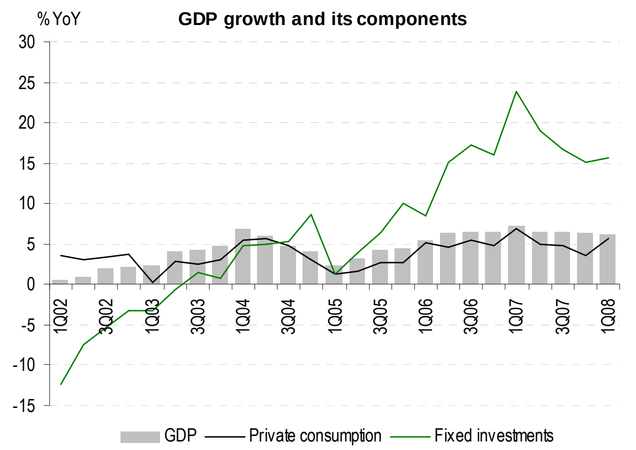
Increased inflation in the months to come will, to a large extent, result from the growth of administered prices and also from the food and fuel price growth observed in the world economy and affecting the Polish market. This creates a risk of inflation expectations remaining at a elevated level and, consequently, feeds the risk of the so-called second-round effects. **Moreover, the rise in prices of energy and food may be gradually passing through to other prices, particularly to prices of some services.**

The MPC assessed the probability of inflation overshooting the inflation target in the medium term to be higher than the probability of inflation running below the target. The MPC does not rule out that bringing inflation down to the target in the medium term would require further monetary policy tightening. In view of the persisting uncertainty as to the global growth outlook and the prospects of the Polish economy, the MPC assessed that a more comprehensive assessment of inflation outlook will be possible after analysing the data released in the near future and after considering the June inflation projection. The MPC will strive to bring inflation down to the target in the medium term.

▪ The MPC kept interest rates unchanged for the second straight month, but similarly as in April the statement left no doubts that we are still in monetary tightening cycle and the doors to rate hike in June are open.

▪ Hawkish arguments used so far were supplemented by one more – a risk of transmission of high energy prices and food prices to other prices. List of arguments for a pause in monetary tightening remained unchanged.

▪ By saying that probability of inflation staying above the target is still higher than inflation going below the target, the Council maintained a hawkish bias in monetary policy. According to the MPC, more precise assessment of inflation prospects will be possible after learning new data and new inflation projection. It confirms our expectations for a rate hike in June with a risk of one more hike later during the year.



▪ GDP growth in Q1 reached 6.1% amid private consumption growth by 5.6% and investment growth 15.7%. Export growth reached 13.7%YoY, being the highest for 1.5 years. Despite better than predicted data for Q1, we predict a slowdown in GDP growth in the remaining quarters due to decelerating investment growth and lower exports amid weakening business climate abroad. In the second half of the year, GDP growth may be below 5%.

▪ Retail sales data for April were lower than predicted, confirming some slowdown in GDP growth.

▪ On the basis of CSO data for Q1 and GDP figures, we estimate that growth in unit labour costs accelerated in Q1 to over 8%YoY. However, slower growth in employment and weaker drop in unemployment in April do not call for radical actions by the MPC.

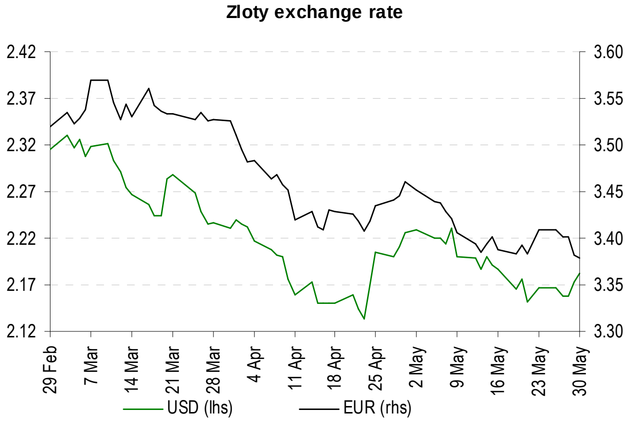
Quote of the week – Government mulling a reduction in excise tax for fuels

Donald Tusk, Prime Minister, PAP, 29 May

I predict the first meeting already today. We have to answer responsibly, after thorough analysis, to what extent producers' margins, to what extent prices at producer level, are affecting those high prices of fuel in Poland. I will talk to minister Rostowski and minister Pawlak, and also to heads of the biggest oil companies in Poland, to consider in what way we can effectively counter this threat of expensive fuels. This is a serious matter, I need to know how much money will it cost the budget and whether it will indeed cause a reduction in retail fuel prices.

Government officials, recently even the PM, are mulling over a possibility of reduction in excise tax for fuels, in order to reduce their prices. The minister of finance has strongly denied such possibility until recently. Deputy finance minister Jacek Kapica argued that excise tax for oil is below the EU required minimum, and realisation of excise revenues planned for this year is rather low (however, the latter argument is offset by the fact that total budget revenues this year may be higher than planned). Even in the government decides to cut excise tax slightly, which will reduce inflation path in the short run, it seems it will not have impact on the MPC's view on medium-term inflation prospects and in effect will have no effect on monetary policy decisions.

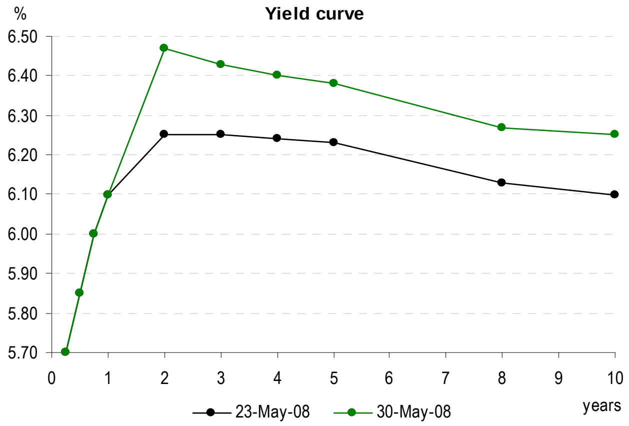
Market monitor



Zloty stronger driven by Slovak crown

▪ Some losses recorded by the Polish currency a week before started to be regained already on Monday, though it took place with limited market activity amid holiday in the US and the UK. The next two days saw stable currency market, but a significant strengthening was observed on Thursday. This was driven by a significant revaluation of the Slovak crown parity (by 17.6%) and other currencies in the region followed. Overall, the EURPLN rate approached the level of 3.37, while USDPLN rose from below 2.17 a week ago to ca. 2.18 amid significant dollar appreciation on global markets.

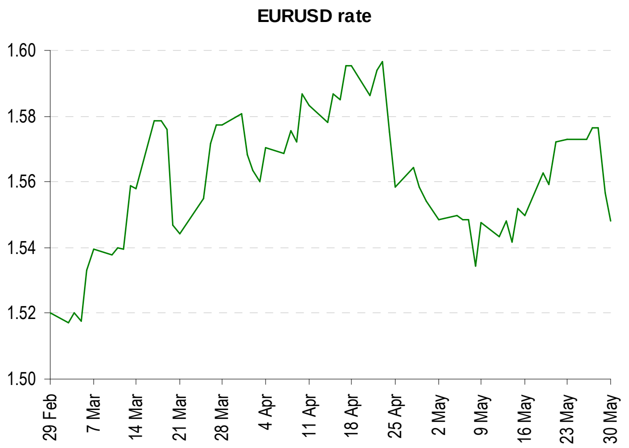
▪ As the EURPLN rate broke quite significant resistance level at 3.38 it is possible the zloty will test the record-minimum levels. That is why we maintain the expected trading range at 3.35-3.45 and at the same time we increase the range for USDPLN to 2.12-2.22.



Domestic yield curve up again

▪ Negative moods on the bond market maintained and further increase in yields took place across the curve. This was connected again with negative sentiment towards bonds on international markets, while the message from the MPC statement together with rate-setters' comments showed altogether that we remain in the tightening cycle. Additionally, Moody's rating agency included Poland on the list of countries with a moderate risk of rating downgrade, which negatively affected the market.

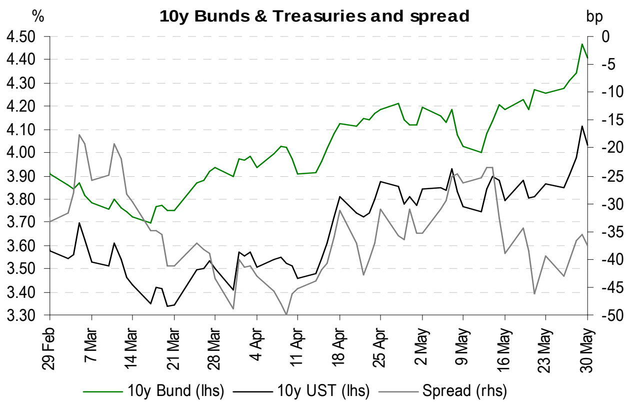
▪ At the beginning of week the pressure on Polish yields may be maintained due to the publication of the Ministry of Finance inflation forecast (significant rise in CPI expected). Some support for the market may be connected with the cancelling of five-year bond auction.



Dollar recovery

▪ The American currency recovered in the last couple of days after some losses recorded in the previous week. Excluding Monday, which was holiday on the US market with stable EURUSD, the reminder of the week showed stronger greenback. This was accompanied by a correction in the oil price. The dollar was supported by the revision of US GDP data for Q1, as well as by hawkish comments by Fed representatives.

▪ This week the focus will be on Friday's US non-farm payrolls report. However, earlier during the week a number of economic data will be released in both US and the euro zone. Also, the outcome of the ECB meeting as well as press conference will be important, and may give some support for the single European currency amid some hawkish comments expected.



Moods on fixed income market still negative

▪ Fears on global inflation outlook maintained, which connected with strong economic data in the US (mostly as regards economic growth in Q1) and hawkish comments from EBC and Fed representatives, led to further rise in yields on the core debt markets. At the end of the week yields of 10Y Treasuries and Bunds amounted to 4.03% and 4.41%, as compared to 3.85% and 4.28% a week ago.

▪ This week, similarly as in the case of EURUSD, the US labour market report will be the key for core debt markets. The expected deepening of employment reduction may give some support for bonds. However, European market might be negatively affected by the hawkish rhetoric after EBC 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