

Weekly economic update

15 – 21 September 2008

The end of last week was dominated by a discussion about PM Tusk's declaration that the government would like Poland to enter the euro zone in 2011. Though we believe that chances for this scenario are insignificant, but strong government's declaration might mean that 2012-13 would become more likely than subsequent dates. On Tuesday, government is about to meet with MPC, and surely accession to the euro zone as well as budget for 2009 will be one of the main points on the agenda. So far according to NBP the government has not consulted this issue with the central bank. It is worth to observe the comments of both sides after the meeting. Some MPC members (Filar, Wojtyna) have already suggested that faster path to the euro would require more restrictive monetary policy.

This week, the key attention of the domestic market will be focused on new data from August. While the publication at the start of the week (CPI above 5%, high wage growth) should strengthen expectations of hikes, Thursday data on low output growth and PPI might neutralize that effect. Abroad, the list of publications will be abundant as well. All eyes will be on the FOMC meeting on Tuesday evening. The attention will be focused also on numerous data on economic activity in the US and American house market. and on inflation indicators as well.

Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (15 September)							
9:00	PL	Auction of Treasury Bills					
12:00	PL	CPI	Aug	%YoY	5.0	5.1	4.8
12:00	PL	Wages in enterprises sector	Aug	%YoY	11.0	11.0	11.6
12:00	PL	Employment in enterprises sector	Aug	%YoY	4.5	4.4	4.7
12:30	US	NY Fed Index	Sep	pts	3.5	-	2.77
13:15	US	Capacity utilisation	Aug	%	79.7	-	79.9
13:15	US	Industrial production	Aug	%MoM	-0.2	-	0.2
TUESDAY (16 September)							
9:00	DE	ZEW index	Sep	%	-54.0	-	-55.5
9:00	EZ	Final HICP	Aug	%YoY	3.8	-	4.0
12:30	US	CPI	Aug	%YoY	5.6	-	5.6
13:00	US	Capital flows report	Jul	b		-	51.1
18:15	US	Fed meeting - decision	-	%	2.0	-	2.0
WEDNESDAY (17 September)							
12:30	US	House starts	Aug	m	0.96	-	0.965
12:30	US	Build permits	Aug	m	0.93	-	0.937
THURSDAY (18 September)							
12:00	PL	Industrial production	Aug	%	0.3	0.0	5.6
12:00	PL	PPI	Aug	%	2.1	2.1	2.3
	PL	MPC minutes	Aug	-	-	-	-
	JP	BoJ meeting – decision	-	%	0.5	-	0.5
12:00	CH	SNB meeting – decision	-	%	2.75	-	2.75
12:30	US	Jobless claims	w/e	k	-	-	
14:00	US	Leading indicators	Aug	%	-0.2	-	-0.7
14:00	US	Philadelphia Fed index	Sep	pts	-10	-	-12.7

Source: BZ WBK, Reuters, Parkiet

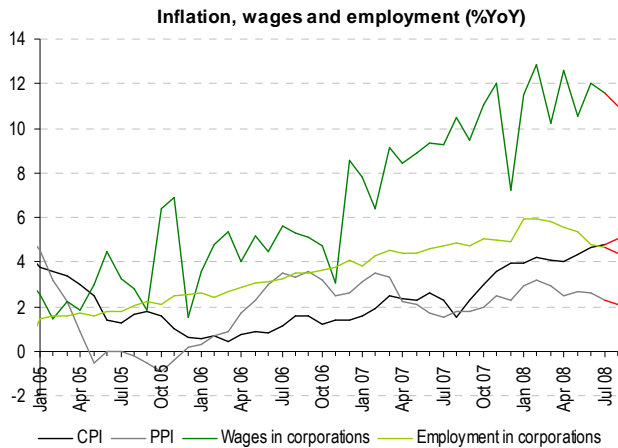
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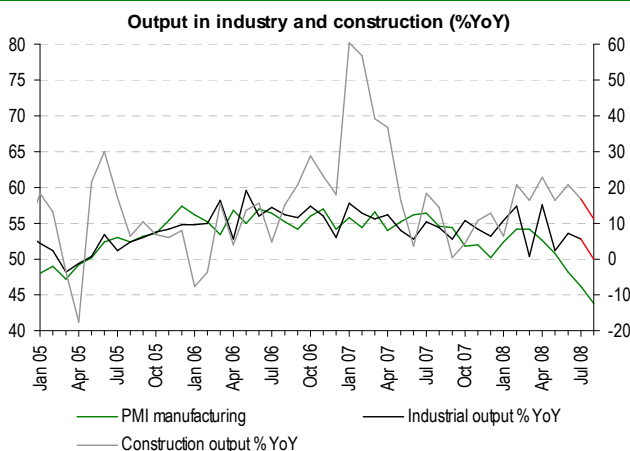
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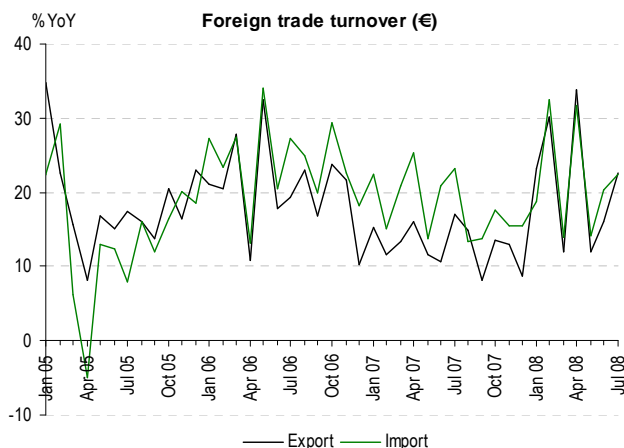
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What's hot this week – High inflation and earnings plus low production

- Key focus at the start of this week will be on data about CPI, earnings and employment for August, which may be crucial for the nearest MPC's decisions.
- We expect increase in inflation slightly above 5% in August, despite significant drop in oil prices, which will be supported by smaller deflation of food prices than in the previous year. Structure of prices forecasted by us will cause rise in net inflation to ca. 4% and new core inflation measure (without prices of food and energy) to ca. 2.8% in August. Market consensus sees CPI at 5%.
- Increase in earnings and employment in enterprise sector should slow down slightly (wages to 11%, employment to 4.4%YoY), maintaining however at level high enough that MPC will not stop being afraid of second round effect. Likely, MPC members will refer to the new data in the comments after their publications.



- Another set of domestic data will be published on Thursday. We predict that growth in industrial production was close to zero in August, which is pointed by lower number of working days (2 days) than in previous year and sharp drop in PMI. Construction output slowed down either, though in our opinion its growth maintained at quite good level (ca. 11%YoY).
- Slowdown in PPI growth to 2.1%YoY is expected among others due to commodities getting cheaper. PPI in the local market will probably stay significantly above.
- MPC minutes from the meeting in August will rather not influence the market as usual. One can expect a confirmation, that once again MPC voted on rate hike. However, this time poor data and forecasts from the euro zone deterred the Council from such decision.

Economy last week – Export still strong, demand for loans growing

- Growth of exports unexpectedly accelerated to almost 23%YoY in July, outpacing imports (ca. 20%YoY). Other elements of balance of payments improved as well (among others big surplus in transfers thanks to EU funds), and as result current account deficit dropped to €1.2bln. 12-month gap to GDP ratio slightly fell to 4.4%.
- In next months one should expect worsening of the export results, though cumulated impact of net international trade on GDP growth in Q3 might be less negative than we previously thought.
- No signs of downturn were also seen in loans market, as their growth accelerated to 26.3% in August. Growth of money supply and households' deposits slightly slowed down against July, however they still maintained at high levels.

Quote of the week – Euro zone entry in 2011 not very likely

Donald Tusk, Premier, PAP, 10 September

It is first time I am saying that my government will pursue to access the euro zone in 2011. It will be hard though possible to be realized.

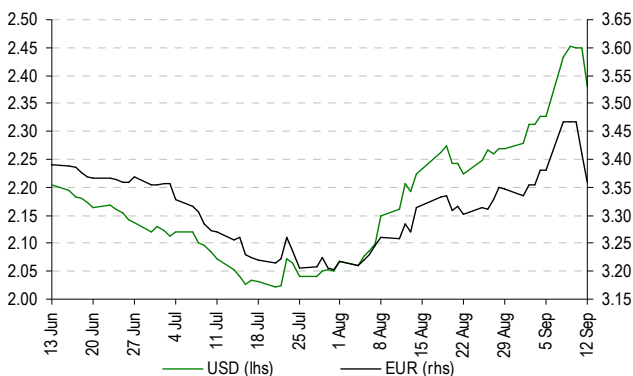
Jacek Rostowski, finance minister, Dziennik, 12 September

Prime Minister presented ambitious aspirations of the government once again. The budget draft is the expression of these aspirations. By decreasing budget gap of the state by 0.8% of GDP against the plan of previous government for 2008 and saving up PLN11.3bln on development priorities from general increase in expenditures at PLN14.2bln, the government created conditions to aim a goal which is quick accession to the euro zone. In the nearest time the government will start working on the schedule and strategy in that issue.

It seems not very likely that we succeed to access the euro zone in 2011. It would be hard to comply with economic criteria, before the end of 2010. Necessity of 2-year stay in ERM2 would be important restriction as well. To comply with the rate exchange criterion Poland would have to enter ERM2 practically in the nearest months. Previous declarations suggested that in the condition of persistent inflation and market turmoil it would rather not happen. According to finance minister the government only plans to start work on the schedule and strategy of accession to the euro zone, which suggests it will need more time to decide on ERM2. Possible changes in the constitution may be another problem as there could be no support for them in the parliament. However, strong declaration of the government means rising chances on the accession in 2012 or at least not much later.

Market monitor

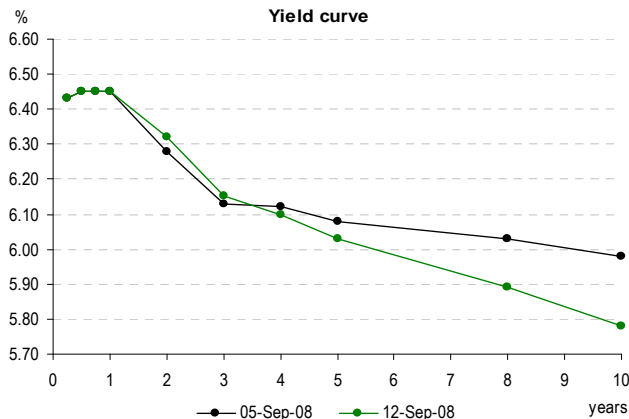
Zloty exchange rate



Tusk's comments triggered zloty rebound

- The week started with zloty correction in a scale that exceeded our expectations, and the EURPLN temporarily rose above 3.49. But in line with our intuition such rapid zloty weakening was an overreaction and the exchange rate quickly returned to our band. It seems it was not because the market believed in euro zone entry in 2011 but because the market was oversold and it needed a trigger for a rebound.
- This week the zloty will be influenced by local data, next comments from the NBP and government regarding euro zone, and the EURUSD performance amid a large number of key data releases abroad. We think that amid a correction of dollar versus euro the zloty may gain and we lower range for EURPLN to 3.32-3.42 and for USDPLN to 2.32-2.42.

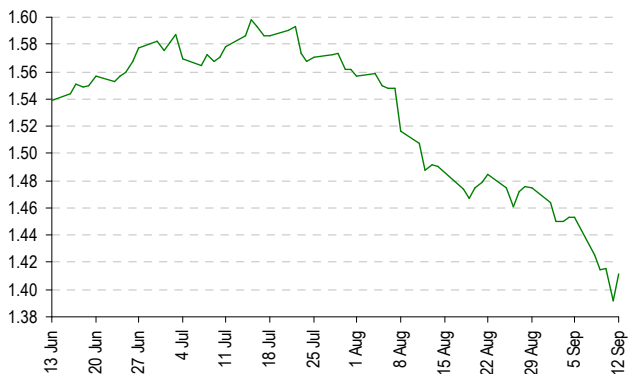
Yield curve



Euro promise strengthened long-term bonds

- Debt market activity was small in the first part of the week. After PM Tusk's comment about euro zone, short-term interest rates increased slightly, discounting a risk of more tight monetary policy, while long-term bonds strengthened due to a convergence play.
- At the start of the week, we expect to see negative information for interest rate market that may push yields higher. However, industrial output data will be weak enough to trigger a rebound later on. Comments of the government and the MPC that would increase (or not) credibility of euro adoption plan may affect slope of the yield curve.

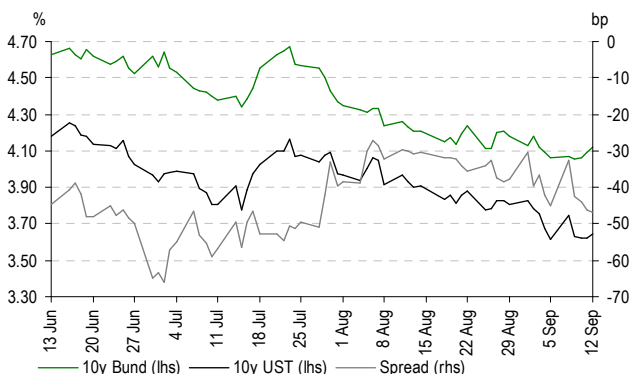
EURUSD rate



Dollar very strong despite weak data

- Almost all week the dollar was gaining strength against euro, ignoring not too good data from the US economy (among others, high trade deficit) and banking sector concerns. After falling below 1.40 on Thursday, the EURUSD rebounded on Friday, assisted by next weak data (PPI and retail sales in the US below forecasts). Despite this move, the dollar strengthened versus euro by almost 3% over the week.
- This week, key event for the dollar may be the FOMC decision and the accompanying statement. Data about inflation and economic activity in the euro zone and US may be also important. We assume that next weak readings from the US economy will allow for dollar weakening against euro.

10y Bunds & Treasuries and spread



Growing market uncertainty good for bonds

- Yields on core debt markets were fluctuating last week with a tendency towards strengthening, amid growing risk aversion and stock market declines. However in sum their level did not change significantly as compared to last Friday.
- Sentiment on core debt markets this week will be determined by the outcome of Fed meeting on Tuesday and numerous data releases in the US and euro zone. On Thursday, we will see decisions of central banks in Japan and Switzerland, both expected to leave main interest rates on hold.

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