

# Weekly economic update

17 – 23 November 2008

The Polish financial market still remains mainly under influence of changes in moods in the global markets. At the start of the week there was an increase in risk aversion amid small liquidity during the long weekend, which led to clear weakening of the zloty and domestic bonds, though in the second part of the week there was a partial recovery, which was supported by bounce back in the world stock markets ahead of the weekend G20 meeting. The domestic data on inflation and balance of payments released in the past week were in line with market expectations and did not have influence on the zloty and local bond prices as well as on our expectations of monetary policy prospects – we still expect a fall of NBP interest rates by 100 bp next year.

This week we will get next domestic data (output, wages, employment, business climate indicators), which will allow to better assess the scale of weakening of the Polish economy (and also the probability of possibly sooner and deeper interest rate cuts by the MPC), though they will not fully reflect the effects of intensification of the global crisis. The Polish market will be still be mostly under influence of changes in the moods in the global markets and the moods will depend on reaction to results of G20 meeting and many data releases abroad scheduled for this week.

## Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
<b>MONDAY (17 November)</b>							
10:00	PL	<b>Tender of 0.5-1.2bn 13-week and 0.5-1.2bn 52-week treasury bills</b>					
13:30	US	Empire State index	Nov	pts	-26.0	-	-24.62
14:15	US	Capacity utilisation	Oct	%	76.4	-	76.4
14:15	US	Industrial production	Oct	%	0.2	-	-2.8
<b>TUESDAY (18 November)</b>							
13:00	PL	<b>Average wage in enterprises</b>	Oct	%YoY	<b>9.6</b>	<b>8.8</b>	<b>10.9</b>
13:00	PL	<b>Employment in enterprises</b>	Oct	%YoY	<b>3.7</b>	<b>3.7</b>	<b>4.1</b>
13:30	US	PPI	Oct	%MoM	-2.0	-	-0.4
14:00	US	TICS capital inflows	Sep	\$bn	50.0	-	14.0
<b>WEDNESDAY (19 November)</b>							
13:30	US	CPI	Oct	%MoM	-0.5	-	0.0
13:30	US	House starts	Oct	m	0.8	-	0.817
13:30	US	House permits	Oct	m	0.78	-	0.805
19:00	US	Minutes of FOMC meeting in October	-	-	-	-	-
<b>THURSDAY (20 November)</b>							
13:00	PL	<b>Net inflation</b>	Oct	%YoY	<b>4.3</b>	<b>4.3</b>	<b>4.3</b>
13:00	PL	<b>Industrial production</b>	Oct	%YoY	<b>1.2</b>	<b>-0.4</b>	<b>7.0</b>
13:00	PL	<b>PPI</b>	Oct	%YoY	<b>2.4</b>	<b>2.5</b>	<b>2.1</b>
13:00	PL	<b>Minutes of MPC meeting in October</b>	-	-	-	-	-
13:30	US	Initial jobless claims	w/e	'000	508.0	-	516.0
15:00	US	Leading indicators	Oct	%	-0.6	-	0.3
15:00	US	Philadelphia Fed index	Nov	pts	-35.0	-	-37.5
<b>FRIDAY (21 November)</b>							
09:00	EZ	Flash PMI manufacturing	Nov	pts	40.5	-	41.1
09:00	EZ	Flash PMI services	Nov	pts	45.0	-	45.8
13:00	PL	<b>Business climate indicators</b>	Nov	-	-	-	-

Source: BZ WBK, Parkiet Reuters;

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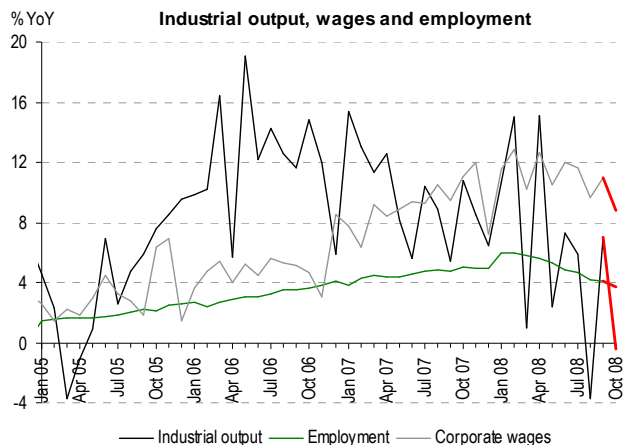
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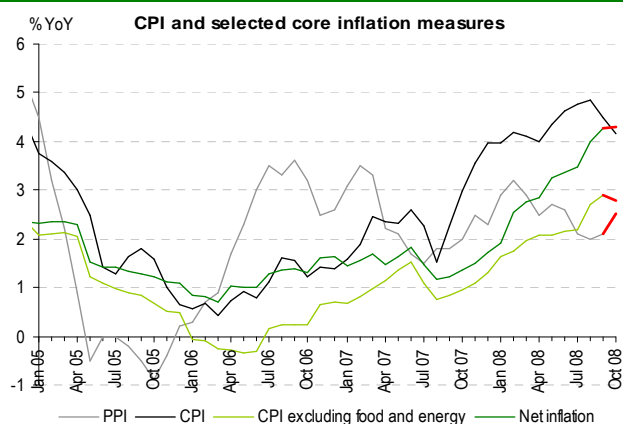
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## What's hot this week – Many data releases in Poland and abroad

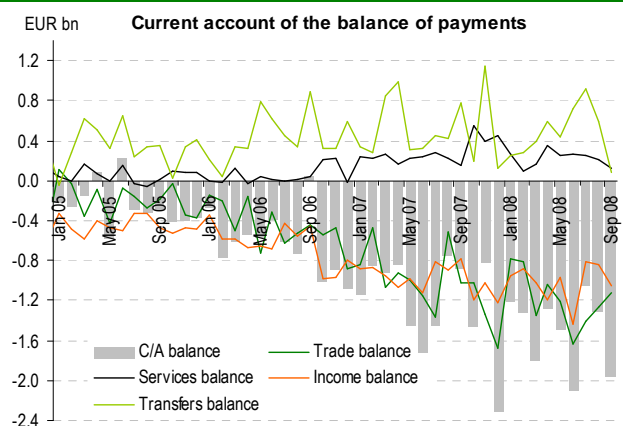


- This week is going to bring another portion of important information on domestic economy. Wages, employment, and output statistics for October will not let to fully assess the influence of global crisis on economic activity and labour market in Poland (a few more months will be necessary), though they will be an important hint, especially in connection with business climate indicators for November. Inflation numbers (net inflation and PPI) will be in the background.
- *Minutes* of the MPC meeting in October, amid fast pace of events in the economy, may be out-of-date and not useful for assessment of monetary policy prospects.
- Polish market will still be mostly under influence of changes in moods in the global markets and they will depend on reaction to G20 meeting this weekend and many data releases abroad scheduled for this week.

## Economy last week – Domestic data overshadowed by events in the global markets



- October CPI rose by 0.4%MoM and 4.2%YoY, which means a decline of annual inflation rate from 4.5% in September. The inflation fall was an effect of deceleration in annual growth of fuel prices (to 1.9% from 3.7%) and prices of food and non-alcohol beverages (to 4% from 5.1%) while price growth in other CPI components remained unchanged or slightly increased.
- Our present estimates of net inflation are in line with earlier market expectations. In October it probably remained at a level close to recorded in September (4.3%YoY). The new core inflation measure, i.e. CPI excluding food prices probably fell to 2.8%YoY from 2.9%YoY.
- Fuel and food prices will act toward lowering CPI inflation, though in our view its decline below 3.5% (the upper end of allowed band) will not happen before the end of Q1 in 2009.



- Balance of payments for September showed a continuation in widening of external imbalance of the Polish economy. Although exports rose stronger than imports (22.5%YoY and 21.2%YoY, respectively), trade deficit was higher than a year ago. Moreover, there was narrowing in surpluses in services and transfers accounts, while gap in income widened. A positive sign was a high inflow of FDI (above €1bn), though we expect it will decline next year lowering share of long-term capital (FDI and EU funds) in financing the C/A gap. After September it covered 87% of 12M C/A deficit (versus 96% after August).
- In October the money supply growth accelerated due to increase of cash growth rate amid slight fall of deposits growth (mainly due to decline of corporate deposits). The credit growth clearly increased – the FX changes effect.

## Quote of the week – Rates on hold until first months of 2009

### Dariusz Filar, MPC member, Reuters, 13 November

However taking into account the core inflation indices, which better reflects the inflationary pressures, than with high probability we may assume that the interest rates should stay unchanged till the end of Q109. In my view at the end of Q1 when we will have new inflation projection from February and when the CSO will review the inflation basket, this will be a good moment for deep reflection on interest rates level. But I don't rule out rate cuts next year. This would depend on economic growth.

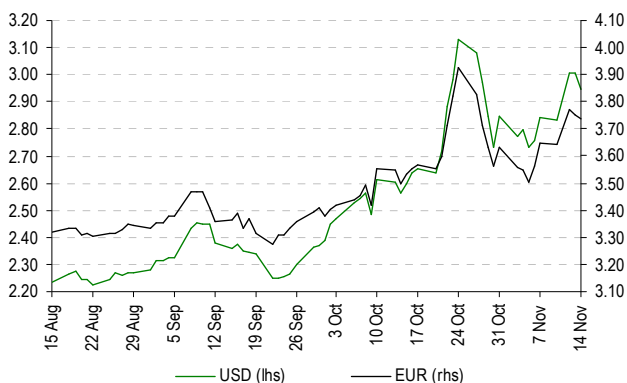
### Marian Noga, MPC member, Reuters, 13 November

In my opinion the decisions should be such that the rates should stay on hold for now. Real reference rate should equal the inflation target (2.5%). If we have 4.2% (inflation) today, the NBP reference rate is at 6%, the real reference rate is at 1.8%. If it gets to 2.5%, than we may think of interest rate cuts. (...) With this amount of data (preliminary estimates of GDP growth in 4Q08) it will be easier to take decision to lower interest rates, though not earlier than in January-February.

A relatively slow fall of CPI inflation amid still high level of core inflation is together with a zloty weakening one of the arguments of the "hawkish" camp of the MPC against swift rate cuts. According to hawkish rate-setters, D. Filar and M. Noga, interest rate cuts should not start before the end of the this year. Moreover, it is worth to note that also Stanislaw Niecekarsz from the "dovish" MPC camp said that conditions to cut interest rates will not appear before end of 2008. This is why we hold our expectations that the MPC will start the monetary policy easing cycle no sooner than towards the end of Q1 2009. On the other hand, continues downside revisions of the economic growth forecasts for global economy and Poland and deep interest rate cuts abroad (in many cases deeper than expected), pose risk of earlier and stronger MPC reaction. First decision in this direction may be a change of informal bias in the monetary policy to "easing" from "neutral" already at MPC meeting in November.

Market monitor

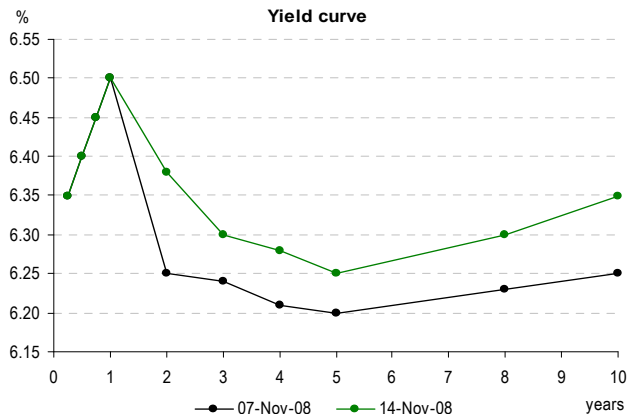
Zloty exchange rate



Higher risk aversion weakens the zloty....

- At the start of the week, amid limited liquidity during the long weekend and simultaneous rise in risk aversion in global markets, the zloty weakened significantly, going temporarily above 3.85 versus euro. In the remaining part of the week there was a partial rebound, especially on Friday, when stock market recovered.
- This week the zloty will remain mainly under influence of changing mood in international markets. Start of the week may see improvement of moods after conclusion of G20 summit and possible announcement of new actions supporting world economy. Resistance level for the EURPLN that we indicated last week, i.e. 3.75, has been broken and it may repeat also this week. Market volatility will probably remain high and we expect the EURPLN will fluctuate in a wide range of 3.60-3.80.

Yield curve



...and causes rise in domestic yields

- Likewise the zloty, domestic bonds also lost ground at the start of the week amid higher risk aversion abroad. In the second part of the week, there was partial rebound amid decreasing risk aversion. In sum, during the entire week the yield curve moved up. Local inflation data, consistent with expectations, did not have impact on the domestic interest rate market, neither did comments from MPC members.
- This week, Polish bonds prices will depend on change in moods in foreign markets (possible strengthening after G20 meeting) and local data releases. According to our forecasts, data about wages and employment should be positive for the local interest rate market.

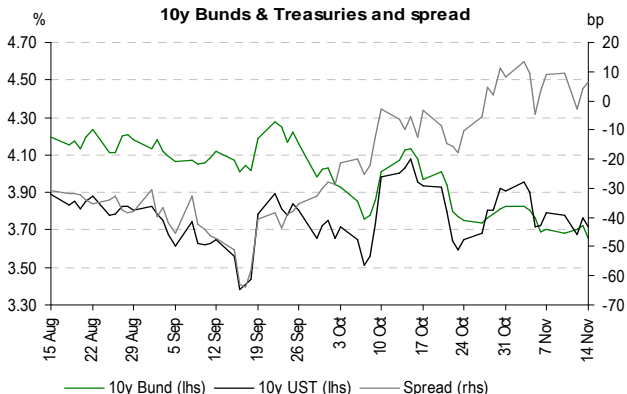
EURUSD rate



EURUSD going down

- During last week the dollar slightly gained versus euro, mainly on Tuesday due to culmination of risk aversion wave. In effect, at some point the EURUSD was at a mere 1.24. At the end of the week, together with limitation of risk aversion in world markets there was a rebound and dollar weakened. At the end of the week it was slightly stronger versus euro than last week.
- At the beginning of this week EURUSD rate performance will depend on the result of G20 summit. Strong declarations of counteracting effects of the crisis may curb risk aversion, which would be negative for the dollar. Besides, important for EURUSD will be data releases in the US and euro zone, and FOMC minutes.

10y Bunds & Treasuries and spread



Strengthening in core debt markets

- In line with rising risk aversion in global markets, core market bonds enjoyed increased interest last week. On the other hand, a negative factor for core debt markets were concerns about market effect of large supply of US debt at auctions during the week. In sum, impact of elevated risk aversion proved to be stronger, which resulted in fall in 10Y Treasuries and Bunds to 3.72% and 3.66% at the end of the week, down by 7 and 4 bp over a week.
- This week may bring some weakening in the core debt markets if a decline in risk aversion initiated at the end of last week continues. However, fresh data from the economy may lead to increase in risk aversion and positively affect the core debt markets.

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