

# Weekly economic update

16 – 22 March 2009

Last week was marked by rising risk appetite in global markets, among others after information from major US banks (e.g. Citibank and JP Morgan) about relatively good financial results in first months of this year. Improvement in global moods and sentiment towards the CEE region was also driven by decision of the SNB to lower rates and intervene in the FX market to weaken the franc. The zloty significantly gained together with other currencies in the region and market interest rates clearly fell. In the international markets there was rise in EURUSD and weakening of the core debt market. Domestic macro data (CPI inflation rise to 3.3%YoY and narrowing of the trade gap) had no impact on the market. This week we will get next dose of local macro numbers, but changes in moods on the global markets are likely to remain the key factor.

## Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
<b>MONDAY (16 March)</b>							
<b>09:00</b>	<b>PL</b>	<b>Auction of PLN1.1-1.4bn of 26-week and PLN0.9-1.2bn of 52-week T-bills</b>					
10:00	EZ	Final HICP	Feb	%YoY	1.2	-	1.1
12:30	US	NY Fed index	Mar	pts.	-32.0	-	-34.65
13:00	US	TICS capital flows	Jan	\$bn	-	-	34.8
13:15	US	Industrial output	Feb	%MoM	-1.1	-	-1.8
13:15	US	Capacity utilisation	Feb	%	71.3	-	72.0
<b>TUESDAY (17 March)</b>							
10:00	EZ	ZEW index	Mar	pts.	-7.4	-	-5.8
12:30	US	Mouse starts	Feb	m	0.45	-	0.466
12:30	US	Building permits	Feb	m	0.50	-	0.531
12:30	US	PPI	Feb	%MoM	0.3	-	0.8
<b>13:00</b>	<b>PL</b>	<b>Average wage in enterprises</b>	<b>Feb</b>	<b>%YoY</b>	<b>5.2</b>	<b>5.7</b>	<b>8.1</b>
<b>13:00</b>	<b>PL</b>	<b>Average employment in enterprises</b>	<b>Feb</b>	<b>%YoY</b>	<b>-0.2</b>	<b>-0.2</b>	<b>0.7</b>
<b>WEDNESDAY (18 March)</b>							
12:30	US	CPI	Feb	%MoM	0.3	-	0.3
<b>13:00</b>	<b>PL</b>	<b>Industrial output</b>	<b>Feb</b>	<b>%YoY</b>	<b>-16.6</b>	<b>-15.7</b>	<b>-14.9</b>
<b>13:00</b>	<b>PL</b>	<b>Construction output</b>	<b>Feb</b>	<b>%YoY</b>	<b>0.2</b>	<b>-0.1</b>	<b>7.4</b>
<b>13:00</b>	<b>PL</b>	<b>PPI</b>	<b>Feb</b>	<b>%YoY</b>	<b>3.4</b>	<b>3.0</b>	<b>3.0</b>
18:15	US	Fed decision announcement	-	%	0-0.25	0-0.25	0-0.25
<b>THURSDAY (19 March)</b>							
-	JP	Bank of Japan decision announcement	-	%	0.1	0.1	0.1
10:00	EZ	Industrial output	Jan	%YoY	-15.5	-	-12.0
12:30	US	Initial jobless claims	w/e	'000	650.0	-	654.0
<b>13:00</b>	<b>PL</b>	<b>Minutes of MPC meeting in February</b>	<b>Feb</b>	-	-	-	-
14:00	US	Leading indicators	Feb	%MoM	-0.6	-	0.4
14:00	US	Philly Fed index	Mar	pts.	-38.0	-	-41.3
<b>FRIDAY (20 March)</b>							
<b>13:00</b>	<b>PL</b>	<b>Core inflation (CPI excluding food and energy)</b>	<b>Jan/Feb</b>	<b>%YoY</b>	<b>na/2.5*</b>	<b>2.0/2.3</b>	<b>2.8</b>
<b>13:00</b>	<b>PL</b>	<b>Business climate indicators of the stats office</b>	<b>Mar</b>	<b>pts.</b>	<b>-</b>	<b>-</b>	<b>-</b>
-	JP	Market holiday	-	-	-	-	-

Source: BZ WBK, *Parkiet* daily, Reuters \* market consensus before release of CPI data

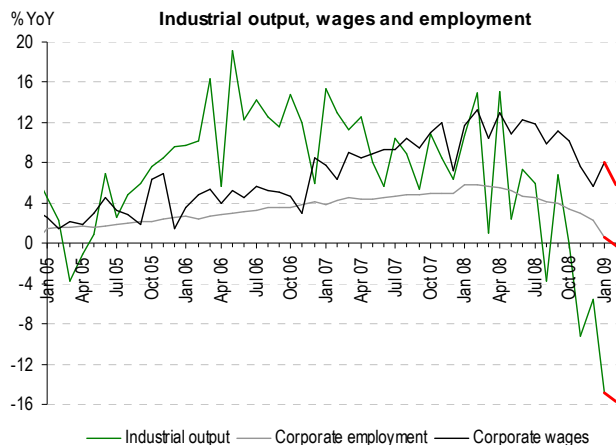
**Maciej Reluga** Chief economist (+48 22) 586 8363

**Piotr Bielski** (+48 22) 586 8333

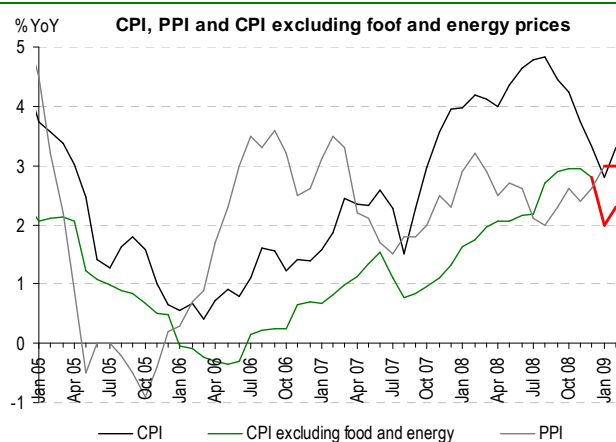
**Piotr Bujak** (+48 22) 586 8341

**Cezary Chrapek** (+48 22) 586 8342

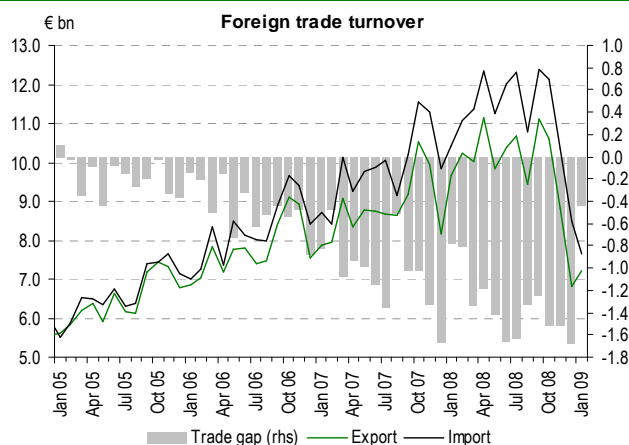
e-mail: ekonomia@bzwbk.pl

**What's hot this week** – Next dose of important domestic data

- In our view, labour market data will show further deterioration of situation and will be important argument for continuation of monetary easing.
- In case of production, we are slightly more optimistic than the market consensus, but even a result slightly better than our forecast (double digit growth in production) will be significant confirmation of economic downturn and argument in favour of further monetary easing.
- As the MPC meeting in February took place just after significant depreciation of the zloty, minutes of the meeting may show the Council's opinions about relation between interest rate changes and zloty exchange rate and between exchange rate and inflation outlook.
- Next inflation data, i.e. PPI and core inflation, will be less important for the market. Much more important will be events abroad, in particular the statement after Fed meeting.

**Economy last week** – Higher CPI inflation, lower trade deficit

- CPI inflation in February reached 3.3%YoY and proved slightly higher than our forecast consistent with market consensus (3.2%) and was lower than the FinMin's estimate of 3.4%. However, at the same time change in weights lowered CPI in January (from 3.1% to 2.8%), which means that scale of inflation acceleration was stronger than expected even by the FinMin.
- Prices of fuel and energy went up sharply in February, being the main factors fuelling CPI inflation (these factors are also responsible for higher PPI inflation in recent months). Apart from fuel market, impact of zloty depreciation on prices seems to be small and in our view after a few months of stabilisation, inflation should start descending towards the NBP target again. Core inflation fell sharply at the start of the year. Together with zloty rebound, falling inflation should encourage the MPC to continue interest rates cuts.



- The current account deficit in January was lower than expected and reached €1.1bn. The concerns over significant collapse in exports were confirmed and its scale (25.2%YoY) was slightly smaller than expected. At the same time, imports dropped more than expected (-26.6%YoY), and trade deficit was a mere €441m, the least since June 2006. This confirmed that both external and domestic demand was weakening at the start of the year. On the other hand one should expect that slump in imports should lead to fast improvement in the contribution of net exports to GDP this year.
- Monetary statistics for February confirmed a slowdown of annual M3 and deposit growth and acceleration in loan growth (although the latter is related to the FX effect and after its elimination loans growth decelerated).

**Quote of the week** – ERM2 entry no so soon**Witold Koziński, deputy NBP governor, 9 March**

As regards talks with the ECB, we are ready to start negotiations together with the FinMin. Until now we had no opportunity to hold such talks.

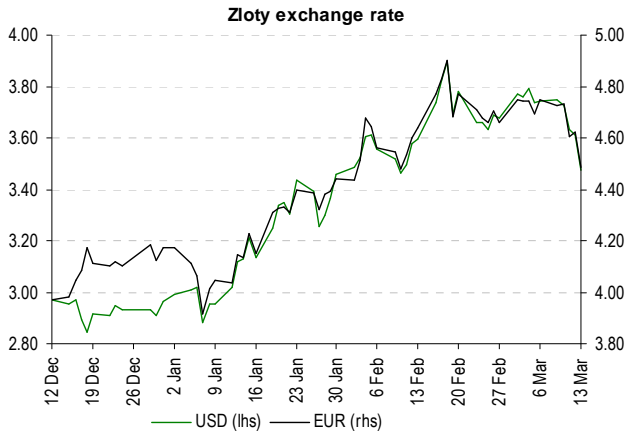
**Marek Rozkrut, head of FinMin's research dep., Reuters, 10 March**  
As regards entry to the ERM2, the current conditions may make it difficult. They may make it difficult to set a parity. There is also a risk of increased exchange rate volatility in the mechanism.

**Ludwik Kotecki, the government's proxy on euro adoption, Reuters, 11 March**

In my opinion we may realistically think about the ERM-2 when two conditions are met: when the zloty is relatively stable and there is some kind of political consensus.

Even though government officials still do not exclude entry to ERM2 in H1 2009 (which is necessary if we want to enter euro zone in 2012, in line with government's road map), there appear more and more doubts, even in their comments, that current market situation may delay the entire process. Recently, some rumours appeared that Poland has already started talks with the ECB about ERM2 entry. However it is hard to imagine such negotiations could be successful without NBP participation. Meanwhile, NBP deputy chief said that central bank was not involved in such talks. EU officials stressed recently that despite the crisis, one should not count on relaxation of Maastricht criteria or other rules of euro zone accession (e.g. shortening period of stay in the ERM2).

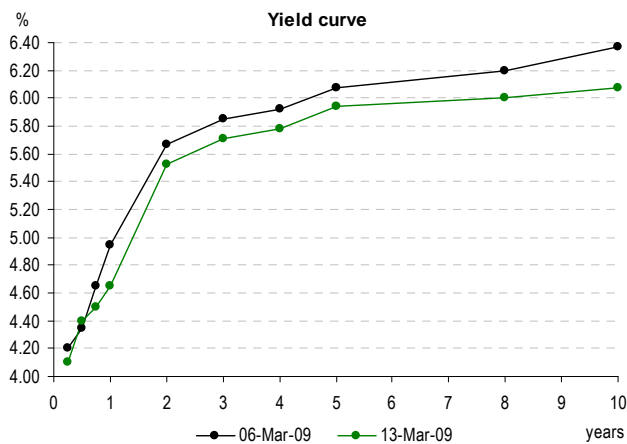
## Market monitor



## Clear strengthening of the zloty

▪ The past week brought clear strengthening of the zloty. Domestic currency was supported by the news on the Hungarian central bank intervention, lower risk aversion in the global markets as well as actions of the Swiss central bank (rate cut and decision on FX interventions). Consequently, the zloty appreciated during the week by 4.9%, together with other currencies in the region (Czech crown by 4%, Hungarian forint by 4.6%).

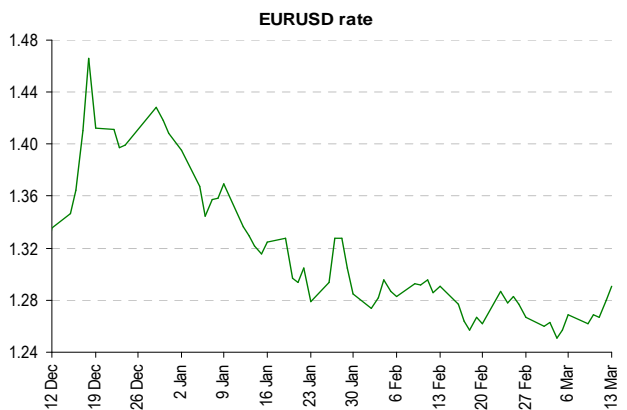
▪ In our view this week there may be a correction of the zloty strengthening due to profit taking by investors and possible reversal of positive moods in the global markets, which is going to trigger renewed wave of opening positions against currencies in the region. However, after important support levels for EURPLN were broken in the past week, we do not change our view that in the subsequent weeks the zloty should gradually appreciate.



## ...and domestic interest rates market

▪ The domestic interest rate was gradually strengthening along the zloty appreciation. There was fall in bond yields (by 13-30 bp), IRS rates (12-24 bp), FRA rates (11-22 bp) and WIBOR rates (ca. 5 bp). Along with higher risk appetite and improved sentiment towards the region, the asset swap spread narrowed and yield curve flattened (2-10 spread fell from 66 bp to 54 bp). Inflation data did not have visible influence on the domestic interest rate market.

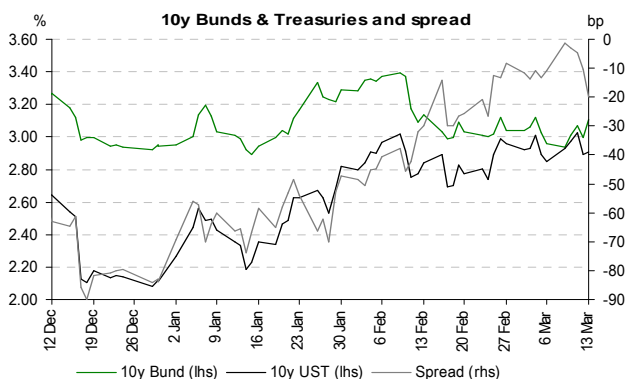
▪ This week industrial output and labour market data should be supportive for the interest rate market (in both cases our estimates are above consensus, but even materialization of our forecasts would confirm strong weakening of economic activity). On the other hand, the slight zloty correction may act in the opposite direction. Overall, we expect a stabilization of the local interest rate market this week ahead of MPC meeting next week.



## EURUSD going up

▪ At the start of the week, EURUSD was staying slightly above 1.25, amid still negative moods after quite pessimistic forecasts of the World Bank and comments from Warren Buffet. Nevertheless, after significant moods improvement in world markets and rise in risk appetite, next days were negative for the dollar. A positive factor for euro was also SNB actions that improved assessment of banking sector stability in the CEE region. At the end of the week, EURUSD rose above 1.29.

▪ At the start of this week, comments from weekend meeting of G20 finance ministers may be important for the EURUSD. Later on, key factors will be FOMC statement and changes in global risk aversion.



## Weakening in core markets

▪ Core debt markets experienced a weakening last week, connected with a fall in appetite for safe assets amid improvement in sentiment on global markets. Additional upward pressure on yields resulted from concerns about large debt supply – last week there were bond auctions in the US. At the end of the week, yields of 10Y Treasuries and Bunds reached 3.11% and 2.91% correspondingly, versus 2.96% and 2.85% in the previous week.

▪ This week, key issue for core debt market will be whether reduced risk aversion observed last week will hold. Besides, any news about quantitative easing measures in Fed communiqué may be important for the market.

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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](mailto:ekonomia@bzwbk.pl), <http://www.bzwbk.pl>



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