Bank Zachodni WBK

Weekly economic update

11 – 17 May 2009

Updated forecasts of the European Commission were pessimistic. Nevertheless, even though predictions concerning economic growth in Poland have been trimmed substantially (much below market consensus), they are still among the highest in the EU in 2009 and in 2010 expected GDP growth in Poland is the highest in the community. The Ministry of Finance was sceptical about Commission's estimates, although later on it released a conservative forecast of GDP growth and inflation for 2010. On Wednesday, the EC will make decision on opening the excessive deficit procedure against Poland and will publish a special report. In a situation when the level of fiscal criterion will be exceeded by the majority of EU member states, a significance of this factor is not too high and it is hard to expect sanctions from the Commission.

Quite low risk aversion in international markets and IMF's decision about granting the FCL to Poland contributed to zloty strengthening. There was a slight correction in the debt market. Results of stress tests for US financial institutions had positive impact on investors' sentiment. The ECB decision had smaller impact on market fluctuations last week.

This week, the most important factor for interest rate market will be inflation data. Further growth in CPI will most likely contribute to another pause in monetary easing in Poland. If inflation does not fall in May below the upper end of fluctuations band around target, also a rate cut in June would be under threat, however in such situation the June NBP projections would be crucial. Its importance and aversion towards negative real interest rates have been emphasised in MPC members' comments. We predict further fall in money supply growth and a return of current account balance below zero. Abroad, we will see flash Q1 GDP data in the euro zone and retail sales and production data in the US, which will be important in the context of rebound in economic activity and sentiment.

Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		MONDAY (11 May)					
9:00	**PL**	**Auction of PLN600-800m 52-week T-bills**					
		TUESDAY (12 May)					
12:30	US	Trade balance	Mar	bn	-29.0	-	-33.08
		WEDNESDAY (13 May)					
9:00	**PL**	**Auction of PLN2-3bn of 2Y bonds OK0711**					
9:00	EZ	Industrial output	Mar	%YoY	-17.6	-	-18.4
12:30	US	Retail sales	Mar	%MoM	-0.1	-	-1.2
		THURSDAY (14 May)					
12:00	**PL**	**CPI**	**Apr**	**%YoY**	**3.8**	**3.8***	**3.6**
12:00	**PL**	**Money supply**	**Apr**	**%YoY**	**16.6**	**16.1**	**17.6**
12:30	US	New jobless claims	w/e	k	610	-	601
12:30	US	PPI	Apr	%MoM	0.2	-	-1.2
		FRIDAY (15 May)					
12:00	**PL**	**Current account balance**	**Mar**	**€ m**	**-460**	**-483**	**525**
9:00	EZ	Flash GDP	Q1	%YoY	-4.0	-	-1.5
9:00	EZ	Final HICP	Apr	%YoY	0.6	-	1.2
12:30	US	CPI	Mar	%MoM	0.0	-	-0.1
13:15	US	Industrial output	Apr	%MoM	-0.6	-	-1.5
13:55	US	Preliminary Michigan	May	pts	66.4	-	65.1

Source: BZ WBK, Parkiet daily, Reuters * Forecast updated from 3.6%YoY after the release of the FinMin inflation forecast

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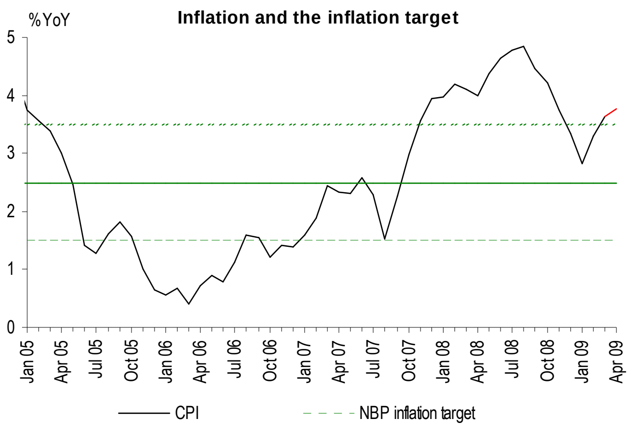
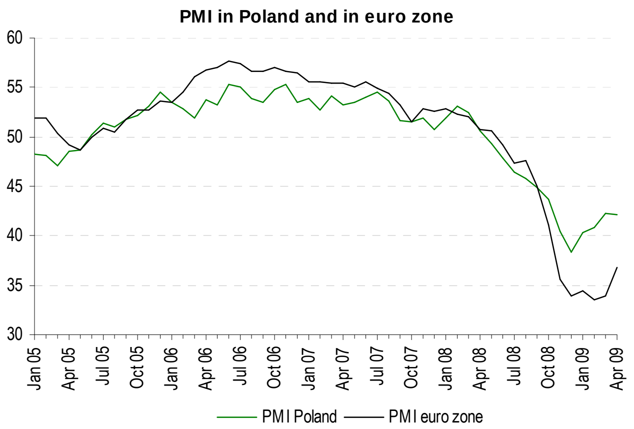
What's hot this week – New set of data



- This week the CSO will release CPI data for April. The forecast by Ministry of Finance showed 3.9%YoY (0.6%MoM), which was above market consensus at 3.8%. The expected rise in CPI index is driven by high food prices growth. According to Marek Rozkrut, director of research department in FinMin, monthly growth in food prices was lower than recorded in March (2%), but there was acceleration in annual terms.
- Balance of payments will show current account deficit with lower surplus in net transfers (mainly as a result of lower inflow of money from the EU) and moderate increase in trade balance. We forecast annual decrease in both exports and imports at lower scale than consensus, at 16% and 25%, respectively.
- We expect further deceleration in broad money M3, as well as slowdown in credit growth in the economy.

Economy last week – PMI negatively surprised, forecasts of FinMin and European Commission



- After three consecutive months of increase in Polish PMI index, in April we saw an unexpected (though moderate) fall to 42.1 from 42.2. It was below our forecast (43.9) and market consensus (43.2). We do not change our forecast of industrial production growth in April at 9.9%YoY.
- The government presented information on the macroeconomic assumptions, which will be a basis in preparation of budget for 2010. the Ministry of Finance forecasts GDP growth at 0.5-1.3% and average CPI inflation at 1.5-1.9%. Forecast on economic growth may be perceived as conservative (below market consensus), which is justified by high uncertainty connected with medium-term forecasting. This is the first time since a couple of years that the ministry is not overly optimistic
- Finance minister informed that budget amendment will take place In July, though deficit increase was not decided.
- The Ministry of Finance said European Commission's forecasts were wrong - regarding GDP growth prospects, some factors in forecast of private consumption and public investments were not taken into account.
- As a consequence, finance minister did not agree with forecasts presented by the Commission as regards general government deficit this year (6.6% of GDP). In ministry's view the highest possible deficit is 4.6% of GDP and public debt slightly below 50% of GDP. The Commission's forecast points to public debt increase to 53.6% in 2009 and ca. 60% in 2010.
- The ministry also emphasised that the CE did not take into account fact of debt safety thresholds in the Public Finance Act.
- When making comparison to fiscal position in other countries one should also take into account pension reform not adopted by most of countries within UE (deficit higher by ca. 2% of GDP).

	GDP %YoY		CPI %YoY	
	2009	2010	2009	2010
CE	-1.4	0.8	2.6*	1.9*
IMF	-0.7	1.3	2.1	2.6
FinMin	0.5-1.0	0.5-1.3	1.9	1.5-1.9
market**	0.8	1.8	2.8	

** HICP inflation*

*** median of market forecasts according to Reuters survey from April*

Quote of the week – Negative real interest rate would not be advisable

Andrzej Sławiński, MPC member, TVN CNBC, 7 May

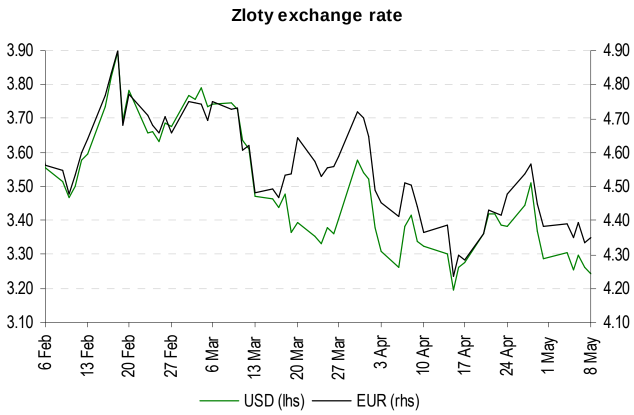
Enterprises take into account that recession in Europe will be relatively long, so I rather do not see factors, which could lead to increase in inflation beside the temporary period we are in at the moment. As macroeconomists we may convince each other that this is only a temporary period [of inflation rise], but for households, and in economics psychological factors are also important, a negative interest rate would be negatively perceived.

Mirosław Pietrewicz, MPC member, PAP, 4 May

I think that only after the inflation projection in June one may state with higher probability what should be our actions in next months. Without data on GDP growth for Q1 and information concerning predictions for 2009 and 2010 one cannot say how many steps is needed in direction of rate cuts.

Next comments from MPC members indicate that interest rates in May will be kept on hold due to central bankers' reluctance to have negative real interest rates and likely inflation rise in April to above the current level of the NBP reference rate. However, according to rate-setters, the inflation increase is temporary. The key factor for next decisions on rate cuts will be the new inflation projection in June, which will show how much room the MPC has for manoeuvre. It is crucial that even the most dovish member of the Council is ready to wait for the projection. On the other hand, taking into account expectations of hawkish Halina Wasilewska-Trenkner concerning GDP growth this year (0-1%) and in Q1 alone (0.7%YoY), one cannot exclude that she will vote for rate cuts in the next months, the same as she did sometimes in the past (e.g. in February).

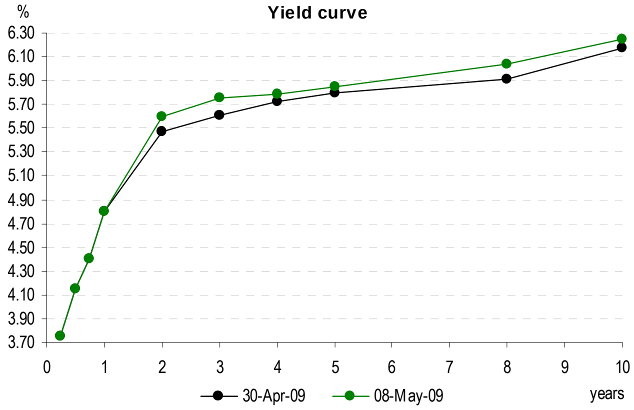
Market monitor



EURPLN was testing 4.30

▪ During the week, the zloty was exceptionally stable and fluctuated in range 4.29-4.415. Moods in international markets were quite good. Zloty strengthening was supported among others by IMF's decision on granting FCL of the amount $20bn. Also, Fitch and Moody's published positive opinions about Poland. Zloty was testing level 4.30 that we had indicated but was unable to break it for longer.

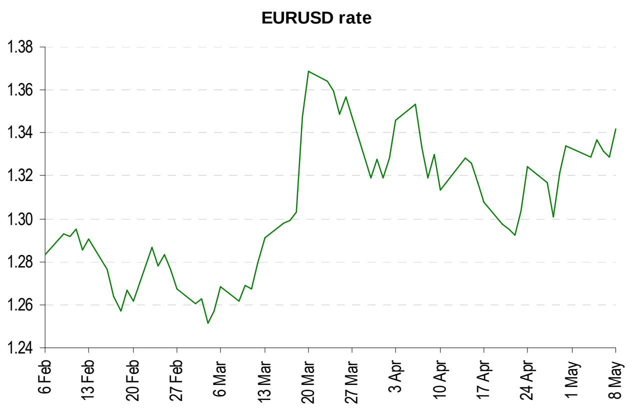
▪ Domestic data will have limited impact on the zloty. In our view the level 4.30 versus euro may be tested again this week and it cannot be ruled out that it will be broken if positive moods abroad maintain. Then, the EURPLN would go towards 4.20. The support levels for the EURPLN will be 4.41 and 4.51.



Increase in market rates

▪ Lower than predicted PMI index and higher FinMin's inflation forecast had little impact on markets. The debt market was in weakening trend, which could have been triggered by a delaying expectations for rate cuts and repercussions of higher general government deficit in 2008 and its forecasts for 2009 and weaker hopes for fast euro zone entry. Debt weakened also before the switch auction. The yield curve became flatter as the short end lost more substantially. IRS rates rose more than bond yields.

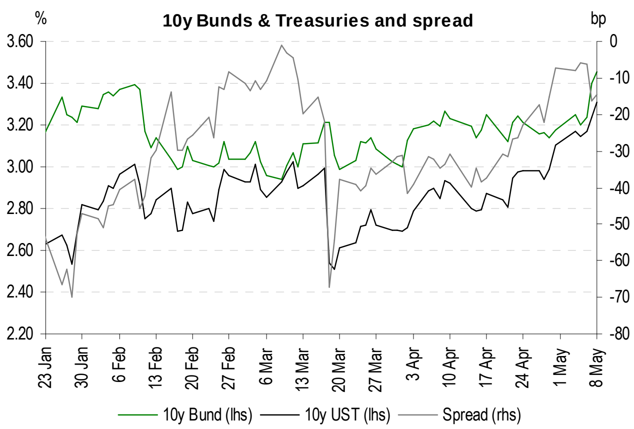
▪ Upward trend in market interest rates may be continued also this week. A negative factor for the market will be publication of inflation data and its predicted significant growth. Also, results of bond auction will be important for the market.



Several factors supportive for euro

▪ Positive moods in the global markets led to strengthening of the euro to the dollar in the past week, driving EURUSD up to 1.35. Rise in risk appetite was related to release of next better-than-expected earnings reports for Q1, stronger-than-expected macro figures from the US and the euro zone (PMI, industrial orders in Germany, ISM, US labour market data) and results of stress-tests for major US banks. ECB decision to cut rates and buy covered bonds had little impact on EURUSD.

▪ This week the key factors for risk appetite and performance of EURUSD will be the US data on retail sales and industrial production, and Michigan index. The euro may be under negative influence of the euro zone's data on GDP growth in Q1.



Yields sharply up in core debt markets

▪ There was a significant weakening in core debt markets due to fall in risk aversion and gains in stock markets. Results of stress tests for US financial results reduced concerns about bankruptcy or nationalisation of major banks. Better than predicted data from the labour market and financial results of companies for Q1 also supported market moods. Yields of 10Y Treasuries and Bunds increased to 3.31% and 3.45% from 3.11% and 3.18% last Friday.

▪ Amid maintaining positive moods abroad, bond prices in the US and Germany may remain high due to building expectations for stabilisation of economic situation. A hint for those expectations will be data released in the US and euro zone about production and sales. Inflationary data will recede to the background.

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