

Weekly economic update

29 June – 5 July 2009

Last week's decisions of central banks in Poland and in the US were consistent with expectations. The Fed left interest rates unchanged, underscoring that they may remain exceptionally low for extended period. The Monetary Policy Council cut main interest rates by 25 bp, maintaining easing bias, which suggests that was not the last cut in a cycle. However, comments of MPC members hinted that the next move is unlikely in July. For sure, new economic data will be important for the Council, including a pace of inflation decline. This week we will see the Ministry of Finance's view on inflation in June, which may affect market expectations. In our view CPI growth slowed down in June below 3.5%, however not substantially, due to strong rise in fuel prices in recent weeks.

Amid limited number of domestic publications, this week the market will be following moods in global markets, which will be under influence of numerous data about business climate, US labour market, as well as ECB decision.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD	FORECAST			LAST VALUE
				MARKET	BZWBK		
MONDAY (29 June)							
11:00	PL	Auction PLN0.8-1.0bn of 52-week Treasury Bills					
11:00	EZ	Economic sentiment	Jun	pts.	70.8	-	69.3
11:00	EZ	Consumer sentiment	Jun	pts.	-30.0	-	-31.0
TUESDAY (30 June)							
10:00	EZ	M3 money supply	May	%YoY	4.6	-	4.9
11:00	EZ	Flash HICP	Jun	%YoY	-0.2	-	0.0
14:00	PL	Current account balance	Q1	€ bn	-	-0.08	-5.12
15:00	US	Case/Shiller index	Apr	%YoY	-18.9	-	-18.7
15:45	US	Chicago PMI	May	pts.	39.0	-	34.9
16:00	US	Consumer confidence	Jun	pts.	55.2	-	54.9
WEDNESDAY (1 July)							
9:00	PL	PMI – manufacturing		pts.	-	43.7	42.5
9:58	EZ	PMI – manufacturing	Jun	pts.	42.4	-	40.7
11:00	PL	Auction of bonds OK and/or PS					
14:15	US	ADP report	Jun	k	-375.0	-	-532.0
16:00	US	Pending home sales	May	%	0.8	-	6.7
16:00	US	ISM – manufacturing	Jun	pts.	44.5	-	42.8
THURSDAY (2 July)							
11:00	EZ	PPI	May	%YoY	-5.6	-	-4.6
13:45	EZ	EBC decision		%	1.0	-	1.0
14:30	US	New jobless claims	w/e	k	615.0	-	627.0
14:30	US	Non-farm payrolls	Jun	k	-355.0	-	-345.0
14:30	US	Unemployment rate	Jun	%	9.6	-	9.4
16:00	US	Factory orders	May	%MoM	0.8	-	0.7
FRIDAY (3 July)							
	US	Market holiday			-	-	-
9:58	EZ	PMI – services	Jun	pts.	44.5	-	44.8
11:00	EZ	Retail sales	May	%YoY	-2.7	-	-2.3

Source: BZ WBK, Parkiet daily, Reuters;

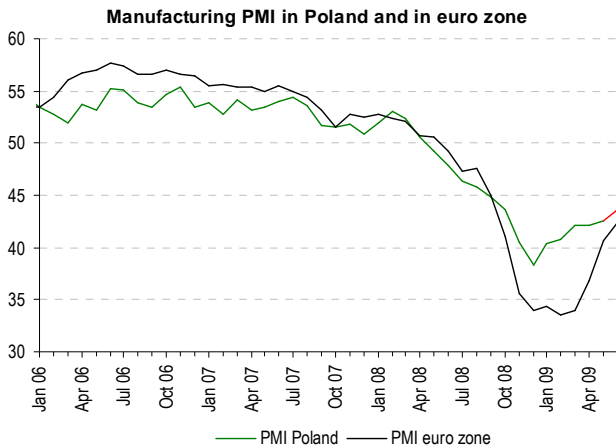
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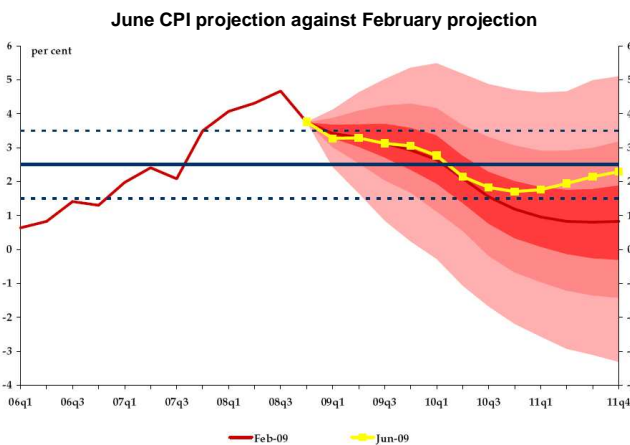
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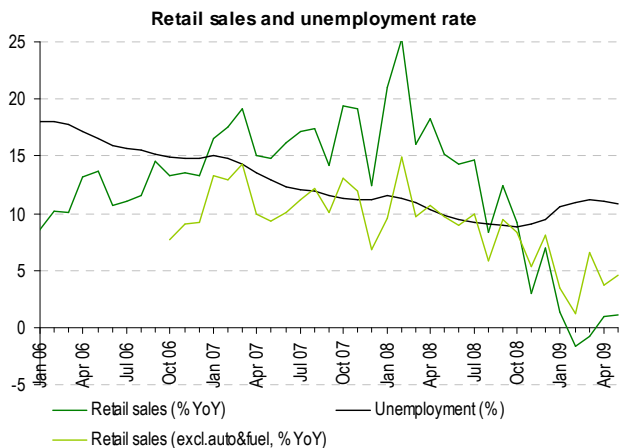
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What's hot this week – Markets under impact of events abroad

- This week will be predominated by data releases abroad, including numerous activity indicators in the US and euro zone, and US labour market data, that will verify market expectations concerning pace of recovery from recession.
- Also, ECB meeting will be in focus of attention with rates widely expected to remain unchanged.
- In Poland, the release of FinMin's inflation forecast for June will be in the foreground, as well as PMI manufacturing index. After CPI data release for May, the deputy finance minister said he expected inflation fall in June to 3.0%. In our view the decline will be smaller due to significant fuel price hikes in recent weeks (we predict CPI at 3.4%YoY).
- After three months of stabilisation, PMI index should go up this time, following improvement of moods in the euro zone and rest of the world.

Economy last week – Central banks and data did not surprise

- In line with our expectations, the MPC cut interest rates by 25bps (reference rate to 3.50%) and kept easing bias in monetary policy as the new NBP projection showed lower GDP path and inflation still below the target in the medium-term, although above the path in the February's projection.
- In NBP analysts' view, balance of risks shows that in the projection horizon there is higher risk of inflation going above projection and GDP lower than predicted by central path.
- The government informed that budget amendment will lift deficit to PLN27bn. Revenue shortfall due to lower GDP growth (0.2%) will amount to PLN37bn. Apart from earlier savings of PLN19.7bn and deficit increase by PLN9bn this will be covered by additional spending cuts in ministries by PLN3bn and higher inflow from dividends by PLN5bn. Finance minister did not rule out a tax hike in 2010-2011.



- Retail sales data for May proved close to expectations and showed slight increase to 1.1%YoY from 1% in April. Official data confirmed tentative estimates indicating a fall in the registered unemployment rate to 10.8% in May. However, in annual terms the unemployment rise accelerated. In our view, sales will be falling in following months due to deteriorating situation in the labour market.
- Core inflation excluding food and energy prices was slightly higher than expected and reached 2.8%YoY in May, but the other 3 measures fell and overall assessment of inflation outlook has not changed.
- The CSO's business climate indicators rose in June on a monthly basis in industry and construction and fell in retail trade. Consumer confidence indicators in June continued a rebound seen since April, but are still at very low levels.

Quote of the week – Possible further rate cuts, but rather not in July

Jan Czekaj, MPC member, PAP, Reuters, 25 June

There is a room for rate cuts – whether it will be used, I don't know. (...) Undoubtedly the room is decreasing. It will depend on how we will assess economic situation.

Mirosław Pietrewicz, MPC member, Reuters, 25 June

I think that in the nearest month there will be too little time to make further changes, i.e. cuts. (...) I think that more changes, i.e. cuts are possible, but I cannot say it on behalf of the entire MPC.

Marian Noga, MPC member, PAP, 25 June

I would not rule out one more rate cut, to 3.25%.

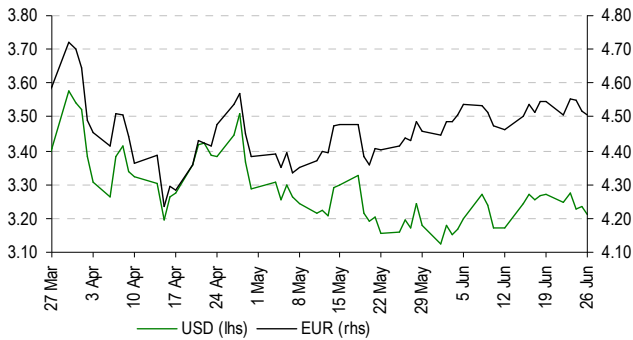
Andrzej Sławiński, MPC member, TVN CNBC, 25 June

If there are more changes in interest rates, I would not expect substantial ones, as real interest rates are already low in Poland.

On one hand, recently we saw hawks who did not rule out another cut, although were quite reserved about it, and on the other hand there were doves suggesting that there is little room left for monetary easing and the next rate cut is not likely in July. Crucial for the vote Jan Czekaj stressed that important information will be GDP data for Q2, which will be known only after the MPC meeting in August. It suggests that the next rate cut could take place in September. In turn, dovish Mirosław Pietrewicz said that in his opinion one month is not enough to make decision about another reduction in rates, which similar as comments from Czekaj suggests that one should rather not count on a rate cut in July. In our view much will depend on the next data due for release over the next month, including the scale of inflation drop in June.

Market monitor

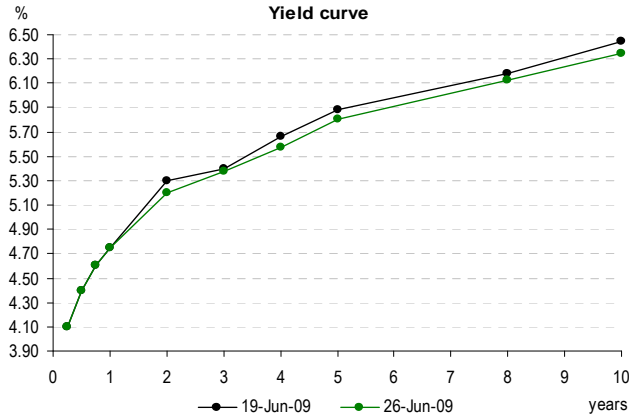
Zloty exchange rate



No clear trend in the currency market

- Zloty exchange rate was quite stable in the past week, remaining in range 4.50-4.56 for most of the time. Reaction to domestic events and data releases was limited, more important were changes in risk aversion abroad. At the end of week, the EURPLN rate was almost at the same level as at close on previous Friday, similarly as Hungarian forint and Czech crown.
- Amid small number of domestic events, this week the currency will be following moods in global markets, which in turn will be influenced by numerous data releases in the US and euro zone. Still undecided IMF's help for Latvia may prevent currencies in the region from more significant strengthening. EURPLN should remain in 4.40-4.60 range.

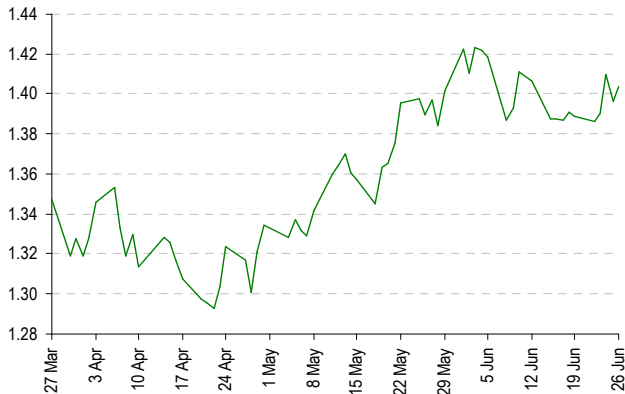
Yield curve



Yields fell at the end of the week

- Yields of Polish bonds remained stable for almost entire week, and did not react neither to government's announcement about budget amendment, macroeconomic data releases, nor to MPC decision. Only on Friday the market strengthened, being affected by news from the Ministry of Finance about zero supply of long-term bonds during summer holidays and cancelling switching auctions. Asset swap spreads narrowed substantially as well.
- The most important information for bond market in the near term will be FinMin's inflation forecast, which may change market expectations about next MPC decisions. It will be released just before Wednesday's bond auction, which will gauge sentiment in the market, however it seems there should be no problem with investors' demand.

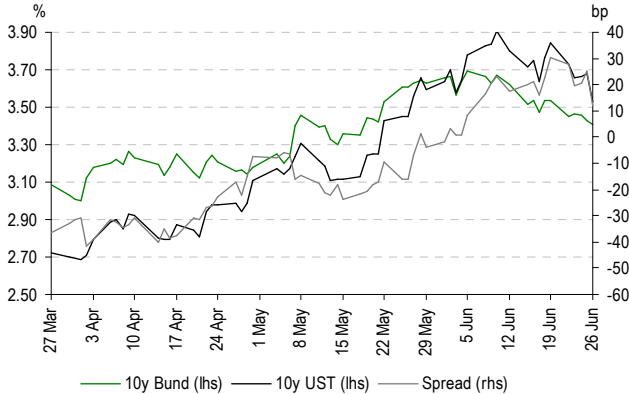
EURUSD rate



Dollar under pressure

- Dollar exchange rate was fluctuating last week in range 1.30-1.41, reflecting changes in global risk aversion under influence of incoming economic data and information. A negative factor for the dollar was repeating calls from China about a need to diversify foreign exchange reserves and to establish alternative world reserve currency.
- The list of data releases that may affect the market this week is quite long. Key for market assessment of economic outlook will be data from American labour market, and numerous indicators of economic climate in the US and euro zone. On Friday, there is market holiday in the US (Independence Day), so market activity will be lower towards the end of the week.

10y Bunds & Treasuries and spread



Yields lower in core debt markets

- There was significant strengthening in the core debt markets due to heightened risk aversion, falling stocks and well-received bond auctions in the US. Yields of 10Y Treasuries and Bunds decreased by 31 and 13 bps, respectively, as compared to the previous Friday, falling to the lowest levels in 4 weeks. The core debt gains took place despite majority of macro data releases in the US were better-than-expected.
- Similar as in case of the FX market, this week the key focus of attention for the core debt markets will be the US non-farm payrolls report and leading indicators of economic activity. Markets will also watch the ECB President's press conference and his assessment of economic outlook and further plans regarding quantitative easing of monetary policy.

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