Bank Zachodni WBK

# Weekly economic update

22 – 28 February 2010

**The zloty fluctuated around the level of 4.0 per euro over the past week, in line with our suggestion from the previous report. At the same time, sentiment in global markets and the EURUSD exchange rate were subjects to significant fluctuations. Publications of the domestic economic data for January have provided a lot of surprises, but their impact on the market was negligible, since for statistical reasons it was difficult to assess on the basis of these data the actual trends in the economy.**

**The last week of March will pass on the Polish financial market under the sign of waiting for the MPC meeting and the publication of a new *Inflation Report*, containing updated projection for inflation and GDP. NBP's projection is likely to show more optimistic economic growth than the previous one. The question is whether this also implies higher (and how much?) medium-term inflation path. Data on retail sales and unemployment, published a little earlier, should not have a key impact on the behavior of investors. More important will be events abroad, including Bernanke's semi-annual address to Congress, and publication of many key economic data as next financial reports of companies for Q4.**

## Economic calendar

| Time CET | COUNTRY | INDICATOR | PERIOD | | FORECAST | | LAST VALUE |
|---|---|---|---|---|---|---|---|
| | | | | | MARKET | BZWBK | |
| | | **MONDAY (22 February)** | | | | | |
| **11:00** | **PL** | **Tender of 52-week T-bills worth PLN1.3-1.8bn** | | | | | |
| | | **TUESDAY (23 February)** | | | | | |
| **10:00** | **PL** | **Retail sales** | **Jan** | **%YoY** | **5.3** | **5.2** | **7.2** |
| **10:00** | **PL** | **Registered unemployment rate** | **Jan** | **%YoY** | | **12.8** | **11.9** |
| **10:00** | **PL** | **Business climate indicators** | **Feb** | **pts.** | **-** | **-** | **-** |
| 10:00 | DE | Ifo index | Feb | pts. | 96.1 | - | 95.8 |
| 15:00 | US | Case/Shiller index | Dec | %MoM | -3.1 | - | -5.3 |
| 16:00 | US | Consumer confidence | Feb | pts. | 55.9 | - | 55.9 |
| | | **WEDNESDAY (24 February)** | | | | | |
| | **PL** | **MPC decision** | | **%** | **3.50** | **3.50** | **3.50** |
| 8:00 | DE | GfK index | Mar | pkt. | 3.0 | - | 3.2 |
| 11:00 | EZ | Industrial orders | Dec | %YoY | 6.0 | - | -0.5 |
| 16:00 | US | New home sales | Jan | m | 0.35 | - | 0.342 |
| | | **THURSDAY (25 February)** | | | | | |
| 10:00 | EZ | M3 money supply | Jan | %YoY | 0.0 | - | -0.2 |
| 11:00 | EZ | Business climate | Feb | pts. | -1.05 | - | -1.12 |
| 14:30 | US | Durable goods orders | Jan | %MoM | 1.5 | - | 1.0 |
| 14:30 | US | Jobless claims | w/e | k | 463.0 | - | 473.0 |
| 16:00 | US | Home prices | Dec | %MoM | | - | 0.5 |
| | | **FRIDAY (26 February)** | | | | | |
| 11:00 | EZ | HICP final | Feb | %YoY | 1.0 | - | 0.9 |
| 14:30 | US | GDP | Q4 | %QoQ | 5.5 | - | 5.7 |
| 14:30 | US | GDP deflator | Q4 | %QoQ | 0.6 | - | 0.6 |
| 14:30 | US | Core PCE | Q4 | %QoQ | 1.4 | - | 1.4 |
| 15:45 | US | Chicago PMI | Feb | pts. | 59.0 | - | 61.5 |
| 15:55 | US | Final Michigan index | Feb | pts. | 74.0 | - | 74.4 |
| 16:00 | US | Home sales | Jan | m | 5.5 | - | 5.45 |

Source: BZ WBK, Parkiet, Reuters

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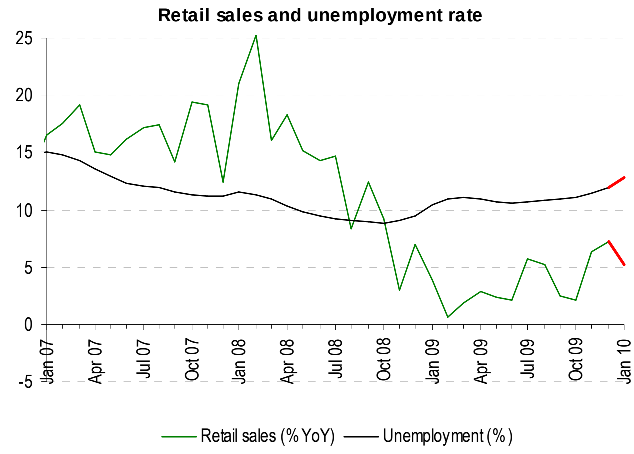
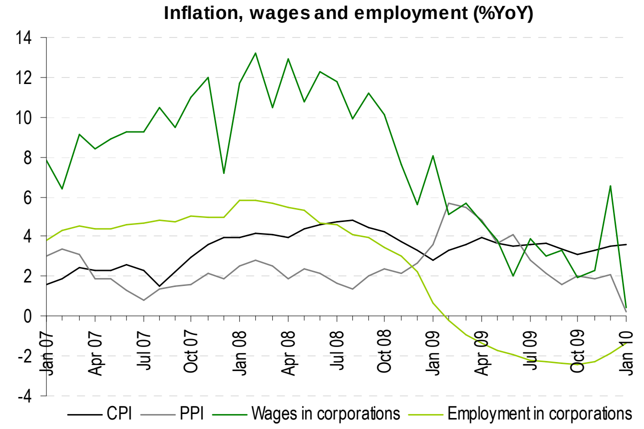
## What's hot this week – MPC meeting, inflation report, many important data abroad

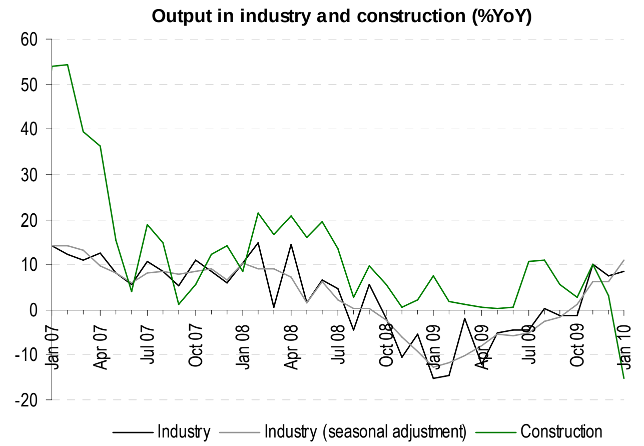



- The first meeting of the MPC in a completely new line-up will end most likely with no change in interest rates, but comments of Council members and the communiqué after the meeting may be important hints for the market about the prospects for monetary policy.
- Also important will be the results of new inflation and GDP projections made by the NBP. Publication of the full *Inflation report* will probably take place at the end of the week.
- Data on retail sales, which will appear before the MPC decision, will be in our opinion, weaker than consensus, but should not significantly affect the market. Significant increase in unemployment in January, also should not affect the mood, because it was signalled by the Ministry of Labour.
- Large number of key data releases abroad and Bernanke's speech in Congress will affect the global sentiment and appetite for risk.

## Economy last week – Data for January hard to interpret




- Much of the data for January published so far was a surprise, but it is difficult to draw clear conclusions from them about actual trends in the economy, due to statistical effects and the impact of transitory factors.
- CPI inflation was slightly higher than expected and rose in January from 3.5% to 3.6%YoY. However, this is tentative data and will be revised next month due to the change in weights basket. In the coming months inflation will fall rapidly.
- PPI growth slowed (in line with our forecast) to 0.2%YoY and will remain very low until the end of the year.
- The dynamics of employment (-1.4%YoY) was higher than forecast, while wage growth (0.5%YoY) disappointed. However, both changes resulted from the difficult to estimate one-off factors – changes in the sample of companies employing more than 9 people by the CSO and the high base effect associated with the reduction of PIT in January 2009.




- Output in industry was considerably higher than forecast and rose by 8.5%YoY (11.1% after seasonal adjustment), instead of the expected slowdown. Surprise was due, inter alia, to strong growth in production of computers and electronics (68%YoY!). It is hard to say right now whether this upturn is permanent. However, increases in other sectors were also good, suggesting a continued recovery in external demand. It is possible that a change in the sample of firms employing more than 9 people also had the impact on production growth.
- Production in construction fell in January by about 15% yoy, in line with our forecast, due to severe weather conditions which halted construction work. In February, the weather was unfavourable for construction as well, which may mean that investment growth in the first quarter this year will be weaker than assumed until recently.

## Quote of the week – How soon the MPC will be mulling rate hikes?

**Sławomir Skrzypek, NBP president, TVN CNBC, 16 Feb**

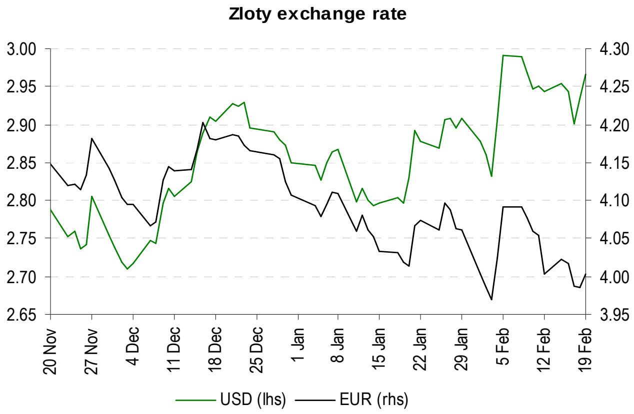
*In Q2 we expect (that inflation will be) at the lower end of allowed band. (...) Monetary policy is not a short-term policy. (...) We have a classical dilemma. On the one hand, one should slowly should start considering interest rate hikes. On the other, one should...watch the European Central Bank, why there are no rate hikes in the US.*

**Zyta Gilowska, MPC member, PAP, 16 Feb**

*I think that interest rate policy should be very cautious. The Council will be acting in conditions of very loose fiscal policy, which has to be taken into account. (...) Currently, in short-term perspective the more important issue is economic growth rather than inflation.*

President Kaczyński finally appointed new MPC members: Zyta Gilowska, Adam Glapiński and Andrzej Kaźmierczak. All three should represent the "dovish" wing in the new MPC. Even potentially the least "dovish" Gilowska said that currently more important is GDP growth than inflation. Most of MPC members expect (like us) that inflation will fall in the next few months and will reach the bottom in the summer. That is why we expect that for the better part of the year interest rates will be unchanged, especially that pace of economic revival seems to decelerate. NBP president also does not seem convinced about need of fast hikes. Although he mentioned that maybe the Council should start thinking about hikes, he added "slowly", which we think means 2-3 quarters horizon.

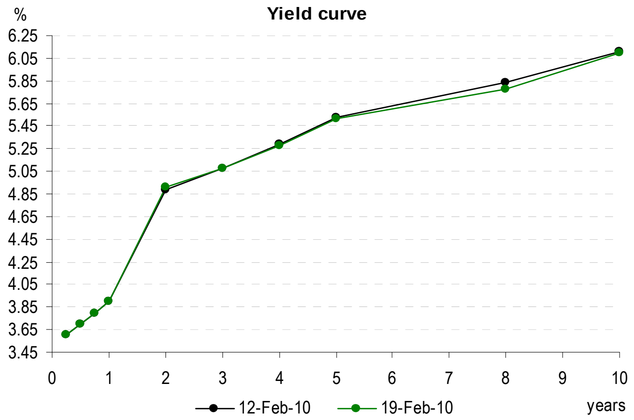
## Market monitor




### Zloty in horizontal trend around 4.0 per euro

▪ Last week the zloty fluctuated near 4.0 per euro, in line with our prediction from the previous report. Reduced fear of bankruptcy of Greece and gains in global stock markets after good results of companies and macroeconomic data from the US contributed to the strengthening of currencies in the region in the middle of the week, but at the end of the week a correction took place, inter alia, triggered by a hike in the Fed's discount rate.

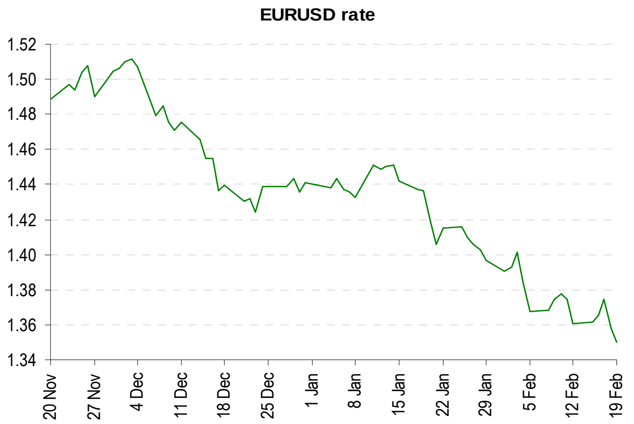
▪ As long as there is no new reason for a surge in risk aversion in global markets, the zloty should continue fluctuating near the level of 4.0 to the euro. An important support level from a technical point of view seems to be 4.06, while important resistance is at 3.96.




### Bond yields almost unchanged

▪ Activity in the domestic debt market was limited last week. The main event was the auction of 10-year bonds, the result of which was perceived as moderately good, mainly due to the relatively high demand. Bond yields hardly changed over the week.

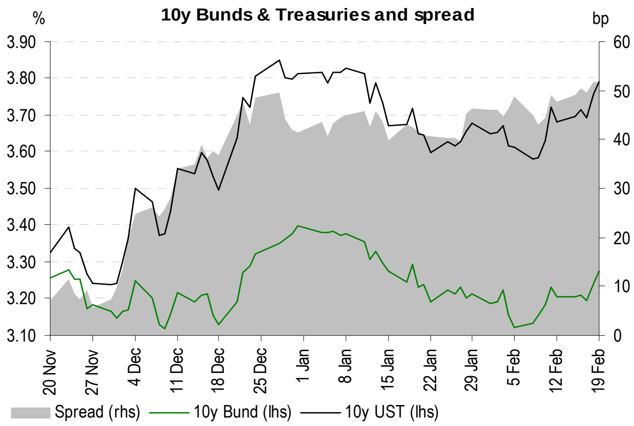
▪ This week, players on the debt market will be waiting for the outcome of the MPC meeting and the new projections of inflation and GDP by the NBP. Communiqué of the Council and comments of the new members, which may appear after the meeting, can influence expectations about future monetary policy decisions. However, we do not expect a significant rise in expectations for faster interest rate hikes this year. Thus, bond yields should remain stable in the nearest week.




### The strongest dollar in nine months

▪ Although the euro managed to slightly make up for losses in the first part of the week, among others on support plans for Greece, on Thursday and Friday the dollar strengthened again and the EURUSD exchange rate fell below 1.35, the lowest level for three quarters. This resulted from good data from the US as well as from Fed's decision to raise the discount rate, which was a step towards the withdrawal of emergency measures supplying the market with liquidity. The unexpected moment of decision provoked fears that it may mean sooner tightening of monetary policy.

▪ This week markets will focus on the speech of Ben Bernanke in Congress, and a series of key figures in the US and the euro area. Fed's chairman's comments about the pace of monetary policy may be crucial for the dollar.




### Weakness in the core debt markets,

▪ Bond yields in the core debt markets were in upward trend last week. It was driven by a moderately high risk aversion and the associated gains in the equity markets, and good macro data, which confirmed hopes for continuation of economic recovery. Upward move in the curve (especially at the short end) deepened after the Fed decision to raise the discount rate by 25 bp, which by the way also confirmed market expectations that economic recovery is under way.

▪ Bernanke's speech may be the opportunity to further explain last week's decision to hike the discount rate, and to express opinions about the prospects for economic recovery in the US and Fed's monetary policy, which will be crucial for the yield curves in the core markets.

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