Bank Zachodni WBK

Weekly economic update

15 – 21 March 2010

After a fairly short-lived and not very strong correction (EURPLN up to 3.912), which scope was limited by another wave of risk appetite in global markets after the Friday publication of better than expected data on production in the euro area and retail sales in the US, the zloty has regained some ground, but in our opinion it is still overbought, which poses a risk of weakening. The direction of move will be determined by changes in global sentiment, which will be affected this week by lots of events abroad, including meeting of the Fed and the numerous publications in the US.

Set of data from the Polish economy, which will be released this week, will help clarify whether and to what extent a surprise, which appeared in publications for January were momentary disturbances. We expect to see the results, which should not substantially change the picture of the economic situation. It is possible that there will be more comments of the MPC members seeking to steer market expectations about the prospects for monetary policy and exchange rate.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
		MONDAY (15 March)					
11:00	**PL**	**Tender of 52-week T-bills worth PLN0.7-1.0bn**					
13:30	US	NY Fed INDEX	Mar	pts.	22.0	-	24.91
14:00	**PL**	**CPI**	**Feb**	**%YoY**	**3.0**	**3.0**	**3.6**
14:00	US	Capital flows	Jan	$ bn	-	-	-
14:15	US	Capacity use	Feb	%	72.6	-	72.6
14:15	US	Industrial production	Feb	%MoM	0.1	-	0.9
		TUESDAY (16 March)					
11:00	DE	ZEW index	Mar	pts.	43.1	-	45.1
11:00	EZ	HICP final	Feb	%YoY	0.9	-	1.0
13:30	US	New home starts	Feb	mln	0.58	-	0.591
13:30	US	Building permits	Feb	mln	0.61	-	0.622
13:30	US	Import prices	Feb	%MoM	0.0	-	1.4
14:00	**PL**	**Wages in enterprises sector**	**Feb**	**%YoY**	**2.6**	**2.1**	**0.5**
14:00	**PL**	**Employment in enterprises sector**	**Feb**	**%YoY**	**-1.0**	**-1.0**	**-1.4**
19:15	US	FOMC decision		%	0-0.25	-	0-0.25
		WEDNESDAY (17 March)					
11:00	**PL**	**Auction of WZ0121 bonds**					
13:30	US	PPI	Feb	%MoM	-0.2	-	1.4
14:00	**PL**	**Industrial production**	**Feb**	**%YoY**	**8.6**	**7.0**	**8.5**
14:00	**PL**	**Construction output**	**Feb**	**%YoY**	**-12.0**	**-11.1**	**-15.3**
14:00	**PL**	**PPI**	**Feb**	**%YoY**	**-2.1**	**-2.0**	**0.2**
		THURSDAY (18 March)					
	JP	BoJ decision		%	0.1	-	0.1
13:30	US	CPI	Feb	%MoM	0.1	-	0.2
13:30	US	New jobless claims	w/e	k	455.0	-	462.0
14:00	**PL**	**MPC minutes**	**Feb**	**-**	**-**	**-**	**-**
14:00	US	Leading indicators	Feb	%	0.2	-	0.3
14:00	US	Philadelphia Fed index	Mar	pts.	18.0	-	17.6

Source: BZ WBK, Dow Jones, Parkiet, Reuters

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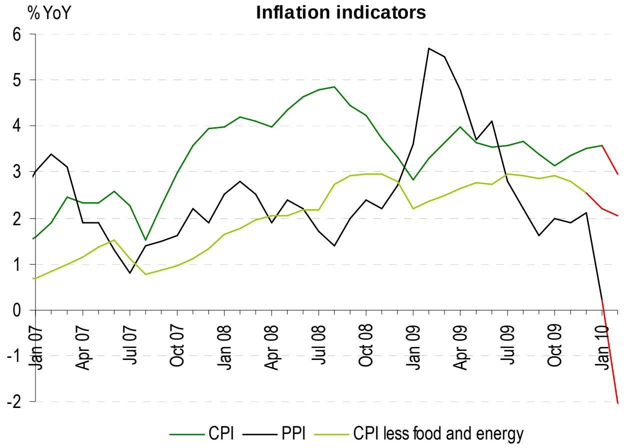
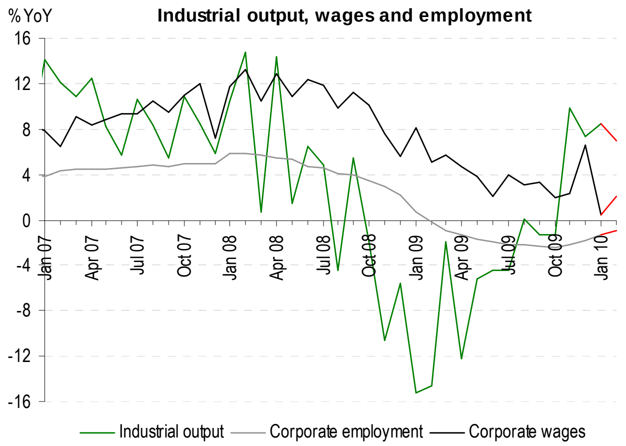
What's hot this week – Next set of information from the economy

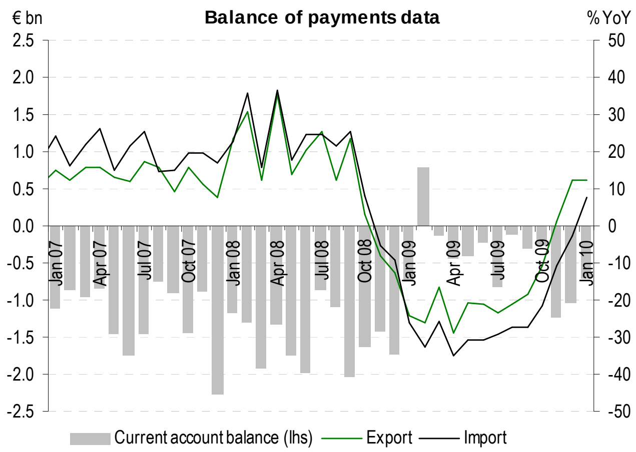


- This month the CSO will release the updated weights in the CPI basket, which will be used for computing inflation figures for February and revision of January figure.
- We are not able to say what will be the influence of the change in the basket weights on inflation. Assuming they will be neutral, we forecast the annual CPI growth rate declined in February to 3.0%YoY, among others due to much smaller as compared to previous year price increases in housing utilities, energy and fuel. FinMin's forecasts and market consensus are at the same level
- In February there was probably a deep decline of the PPI index, where the high base effect connected with strong increase in fuel and commodity prices a year ago was much stronger. In our view producer prices fell by 2%YoY (which is similar to the market consensus).



- In our view the wage growth drop in the corporate sector, which occurred in January was temporary and resulted from the effect of unusually high base. In February the annual growth rate in wages should return to 2.1%.
- We forecast that in February the employment remained at January level, which means slowdown in annual rate of labour shedding to -1%YoY.
- Although the industrial output growth remained relatively high in February, in our view it decelerated, as we assume that the surprising increase in January at least temporarily resulted from one-off order. The market consensus assumes maintaining of growth rate at January level.
- The construction sector will most probably record another month of double-digit drop in output, as the weather conditions still did not support the activity. Any delays should be made up for in the next months.

Economy last week – Rebound in foreign trade, slightly better in credit market



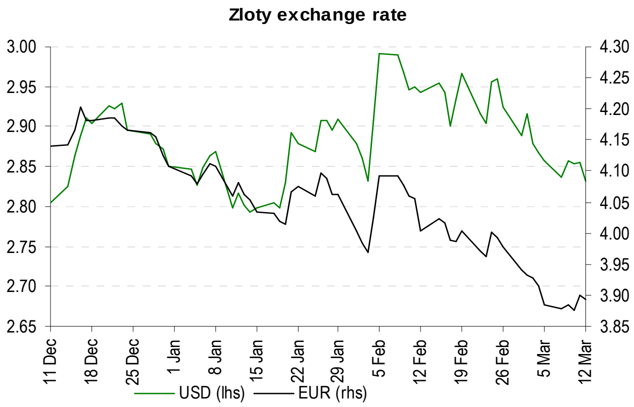
- The current account deficit in January was at €710m, more than we expected. Export growth (12.3%YoY) was solid, though slightly lower than we assumed, and import growth (7.6% r/r) was in line with our forecast. Apparently the economic recovery abroad (which is reflected in record high data on industrial output in the euro zone for January) supports the rebound in Polish foreign trade from the bottom.
- In January the inflow of portfolio investments to Poland was at record high level of €4.7bn (partly due to eurobond issue worth €3bn), and FDI inflow was at high €1.3bn.
- Money supply growth slowed down in February to 5.1%YoY from 6.3% in January. After elimination of FX effect the corporate and household loans rose by 0.5%MoM, while deceleration in their annual growth rates stopped. This seems to confirm a gradual reversal of trend in the credit market.

Quote of the week – MPC would not like the zloty to strengthen too much

Sławomir Skrzypek, NBP president, PAP, 10 Mar
Currently all fundamentals of our economy point to stable zloty. (...) There is a series of risk factors, which may lower the inflation path. The FX rate belongs to such factors.
Andrzej Rzońca, MPC member, PAP, 11 Mar
The main threat for the GDP growth is too fast zloty appreciation. The zloty should not strengthen faster than is indicated by fundamentals, not faster than currencies of other countries in the region.
Andrzej Bratkowski, MPC member, PAP, 9 Mar
I assess the probability of a rate hike this year for ca. 30%. I would like to emphasise that we are facing great deal of uncertainty.
Jan Winiecki, MPC member, PAP, 12 Mar
When we say that this (second slump) may not be excluded, than we should be very cautious while considering rate hikes.

As we expected a week ago the "hawkish" rhetoric of the central bankers was tempered by the zloty appreciation. NBP president corrected the tone of his comments, stating that the strong zloty would lower the future inflation and the current strengthening of the Polish currency departs from fundamentals. What is important, MPC members from the "hawkish" camp joined the discussion, and they clearly tried to lower the market expectations for rate hikes and weaken the pressure on the zloty. In our view more active approach of the central bank to the zloty exchange rate and attempts of counteracting its excessive appreciation are right. We still expect first rate hike only in Q4, though a change in the bias to restrictive is possible more or less in the middle of the year.

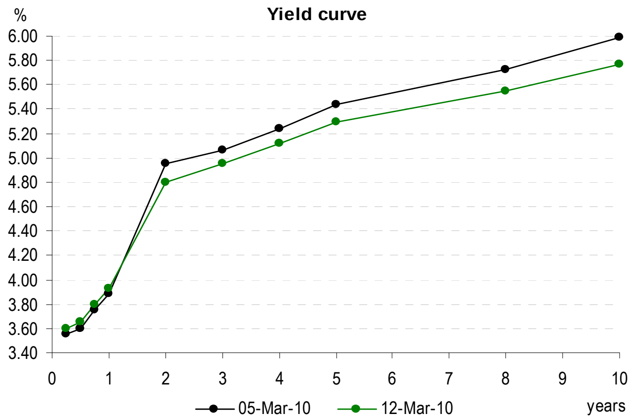
Market monitor



Global sentiment again supporting the zloty

▪ After a strong opening of the week, in the following days there has been a correction of the zloty awaited by us, although its scope was reduced by a strong increase in risk appetite on Friday. EURPLN reached the peak point of 3.912, influenced by statements of the central bankers cooling down expectations for rate hike and mentioning readiness for FX intervention. Positive data from the euro zone and the USA at the end of the week, however, neutralized the impact of domestic factors.

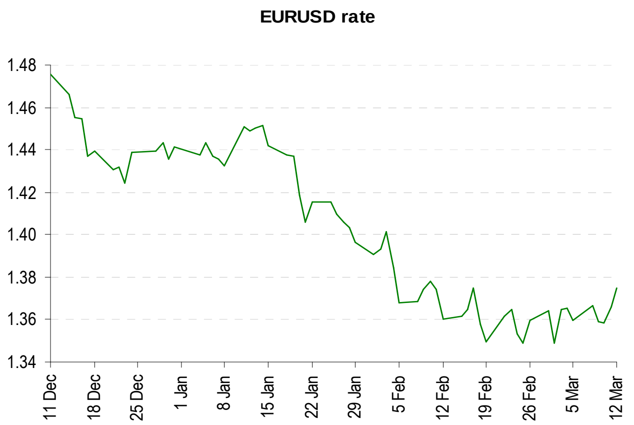
▪ We believe that the zloty continues to be overbought, which suggests that any not so positive information from the economy or a deterioration in sentiment abroad may be an excuse for a correction. Resistance band for EURPLN remains at 3.95-3.97, and support at 3.85-3.87.



Clear strengthening of the domestic bonds

▪ There were many factors supporting the domestic bond market last week, including dovish comments of the MPC members, very good auction results of 2Y bonds, as well as further evidence that the supply of treasury bonds this year may be significantly lower than planned (the successful issuance of bonds in CHF, progress in privatization). In addition, and at the end of the week there was another wave of rise in appetite for risk. As a result, the yield curve shifted down by as much as 15-20 bp.

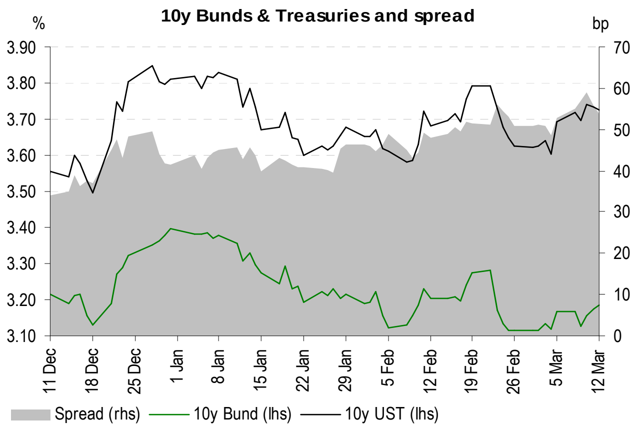
▪ Publication of domestic data this week should be rather neutral for the debt market. Probably a change in sentiment abroad would have greater impact on the yield curve. Important factors will include outcome of the Fed meeting, after which the market will be waiting for hint, whether rates will actually remain at historically low "for a long time."



Dollar remains strong, despite some depreciation

▪ After stabilization for the better part of the week, the euro managed to bounce up slightly against the dollar due to data on industrial production in the euro zone published on Friday, which growth was the highest in 20 years. However, the US currency remains at a fairly strong levels.

▪ In the next few days the market will be dominated by information from the US – a large number of publications of data and the FOMC meeting. In the euro area only the German ZEW index and final HICP inflation data are worth attention. If the indicators of the US economy do not spoil the faith in the economic recovery, which was supported on Friday by better than forecast retail sales data, the dollar could strengthen again.



Risk appetite up, core debt markets down

▪ Positive sentiment on global stock markets and high appetite for risk were not conducive for core debt markets. Weakening during the week was also caused by expectation for the bond auctions in the US with a large supply. Auction results were actually very good though, causing a rebound. Overall, yields on 10-year Treasuries and Bunds increased during the past week by 2-3 bp, reaching on Friday respectively 3.73% and 3.19%.

▪ In addition to data publications, key factor for trends in the core debt markets this week will be the Fed meeting. Markets will be anxious to see if the policy committee retains the “extended period” phrase in its post meeting statement, despite recent signs of economic rebound.

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