

Weekly economic update

7 – 13 June 2010

Recent economic data from the Polish economy suggested that, after a slight slowdown in GDP growth at the beginning of the year, a further deceleration is possible in the second quarter (to below 3%YoY), due to, among others, temporary factors adversely affecting the activity of consumers and enterprises (early Easter, national mourning, effects of flooding). The data indicate a continued recovery in the industrial sector, driven by strong foreign demand, but activity in the domestic market (construction, retail trade) suffered from negative effects of recent unexpected events and weather anomalies. In the subsequent quarters a revival in economic activity should take place, so that the GDP growth in 2010 should be slightly above 3%YoY.

Financial markets are still characterised by uncertainty and rapid swings in moods, and investors worried about the consequences of fiscal tightening on economic growth and the possibility of spreading problems with debt to other countries (including Hungary, which had declared that the previous government had manipulated the data). The zloty and bonds weakened during the week and the euro has fallen to a new four-year low against the dollar on the wave of returning risk aversion.

This week, there are no major data releases in Poland. If the PO manages to convince the other parties (or at least PSL) that the vote on the nomination of Marek Belka for the NBP Governor could take place before the presidential election, the new head of the central bank may be appointed on Friday. If not, the reaction of financial markets should not be too negative in our view. Abroad, top events will include meetings of central banks in the euro zone and UK. The market does not expect any change in interest rates and investors' attention, as usual, will be focused on the ECB press conference, with the special interest in sovereign debt issues and the ECB's bond purchases, as well as the latest growth and inflation forecasts. Few macroeconomic data releases from the US and in some euro zone countries will provide guidance on the pace of economic recovery in recent months.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (7 June)							
11:00	PL	Tender of 52-week T-bills worth PLN1.1-1.6bn					
12:00	DE	Industrial orders	Apr	%MoM	0.2	-	5.0
TUESDAY (8 June)							
12:00	DE	Industrial orders	Apr	%MoM	0.8	-	4.0
WEDNESDAY (9 June)							
16:00	US	Wholesale inventories	Apr	%MoM	0.6	-	0.4
19:00	US	Fed's Beige Book					
THURSDAY (10 June)							
13:00	GB	BoE decision		%	0.5	-	0.5
13:45	EZ	ECB decision		%	1.0	-	1.0
14:30	US	New jobless claims	tyg.	k	448.0	-	453.0
14:30	US	Foreign trade balance	Apr	\$ bn	-41.0	-	-40.42
FRIDAY (11 June)							
Opening of FIFA World Cup 2010							
14:30	US	Retail sales	May	%MoM	0.2	-	0.4
15:55	US	Preliminary Michigan index	Jun	pts.	74.5	-	73.6

Source: BZ WBK, Reuters, Dow Jones

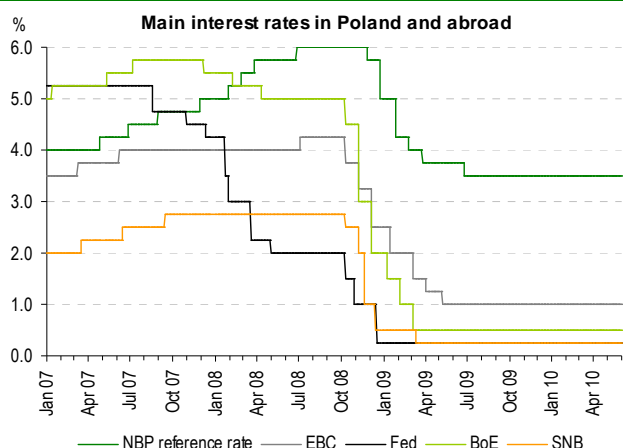
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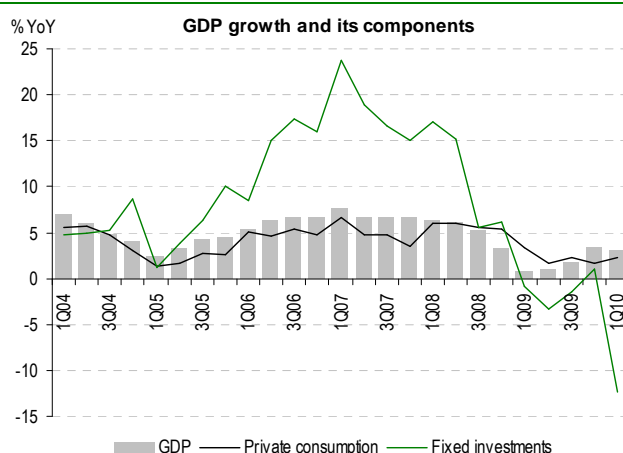
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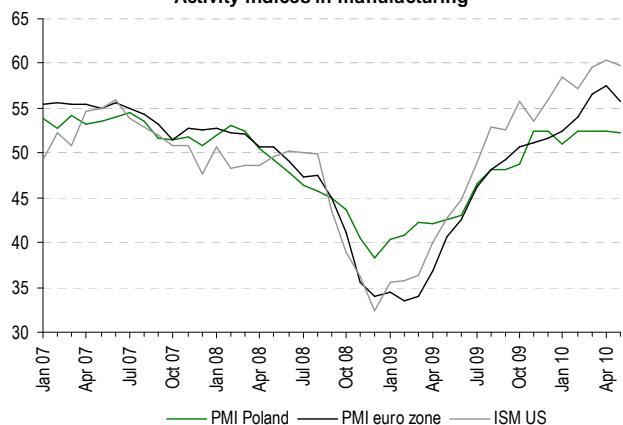
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What's hot this week – No data, ECB meeting and CEE countries in focus

- With no data releases in the domestic market, the focus will on the ECB meeting, as well as a few publications abroad. Rates in the euro zone will remain unchanged, but comment by Jean-Claude Trichet will be closely watched regarding fiscal crisis in Europe, financial markets regulations and economic recovery prospects.
- Also, events in Central and Eastern Europe may be important for the Polish market i.e. developments regarding Hungarian fiscal situation, confidence vote for government in Romania, and further talks on forming the new government in Czech Republic.
- In the next couple of days it will get clear whether Sejm will vote on Marek Belka's nomination for the position of NBP Governor. PSL is expected to take decision on Tuesday on whether it will support (together with SLD and PiS) postponement of voting after presidential election.

Economy last week – Moderate slowdown in the economy

- GDP growth decelerated slightly to 3% in 1Q10, which was roughly in line with expectations. Nevertheless, GDP breakdown brought a few surprises.
- Much deeper than expected decline in investment (by 12.4%YoY, driven most likely by heavy winter weather conditions) was offset in large part by solid performance of foreign trade and rebuilding in inventories. The two latter factors might be better than previously forecasted also in the upcoming quarters. Private consumption accelerated moderately to 2.2%YoY.
- In the second quarter GDP growth may decelerate further to below 3% as consumers and firms' activity may be under negative influence of some temporary negative effects (early Easter, national mourning, flood). We expect economic recovery to be continued in the following quarters and we still forecast GDP growth in 2010 as a whole slightly above 3%

Activity indices in manufacturing

- Polish PMI for the manufacturing sector dropped in May to 52.2 from 52.5 in April. Despite the deterioration in the main index, the data showed the maintenance of growth in industrial production at the pace seen in April. The growth rate of new orders weakened, but only in case of domestic orders, while export orders grew at the fastest pace since March 2007. In total, the report was fairly optimistic for industrial production forecasts for May.
- Ministry of Finance expects inflation to decline in May to 2.1%YoY, and to below 2% in June. According to the ministry, the forecast for May, however, is fraught with more uncertainty than usual, and the main risks are food prices, for which the ministry assumed a growth of only 0.1%MoM. In our opinion, the food prices increased more significantly (0.9%MoM), and as a result the CPI will be at 2.3%YoY.

Quote of the week – When voting on new NBP Governor?**Marek Wikiński, SLD, Rzeczpospolita, 1 June**

If the Lower House speaker decides to include in the next week's schedule the voting on this issue (to appoint NBP Governor), we will support a motion to postpone it.

Waldemar Pawlak, PSL and deputy PM, PAP, 1 June

We think that candidate for the NBP Governor position should be proposed by the country's President with strong social mandate. Even if the President of the country will be elected only in July, he can then propose the candidate of Marek Belka again. Voting would take place in July, not in autumn.

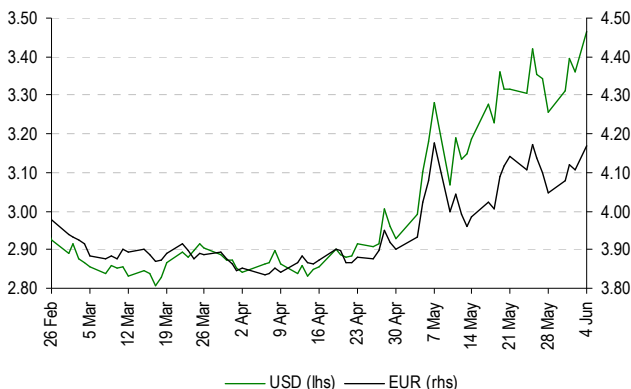
Jarosław Kaczyński, PiS, PAP, 2 June

I do not see any reason to hurry. Even from the constitutional point of view this is rather a doubtful issue. Legitimacy of NBP Governor could be even undermined. This makes no sense. Let's wait a few weeks.

Bronisław Komorowski would like the Lower House to vote on the candidature of Marek Belka already during the nearest parliamentary session (9-11 June). It is not sure, however, whether the speaker will be able to introduce this point into agenda, as comments by other parties politicians suggested they would like to postpone the voting. It is therefore quite possible that the appointment of new NBP governor will take place only after the presidential election. The Lower house's Public Finance Committee will issue the opinion on the Belka's candidature on Wednesday. If the voting takes place this week, this would be probably on Friday, 11th June.

Market monitor

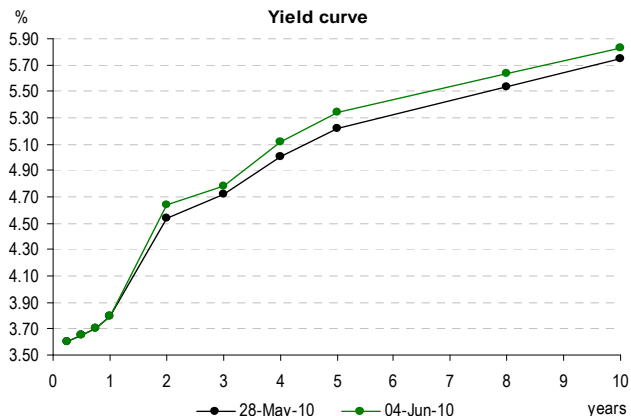
Zloty exchange rate



Significant weakening during long weekend

- Last week the Polish currency was driven purely by changes in global sentiment. Trading range against the euro was very wide from 4.057 on Monday to 4.20 on Friday. During the week the zloty lost against the euro ca. 2.3%, while forint weakened by almost 4.5% and Czech crown remained almost unchanged. Domestic data publications had no impact on the market.
- With no important local events (possible postponement in appointment of NBP governor should be neutral), sentiment will be again driven by events abroad. Besides concerns about euro zone's fiscal situation, rising worries about Hungarian fiscal position may weigh on currencies in the region. Still, 4.20 remains an important resistance level for EURPLN.

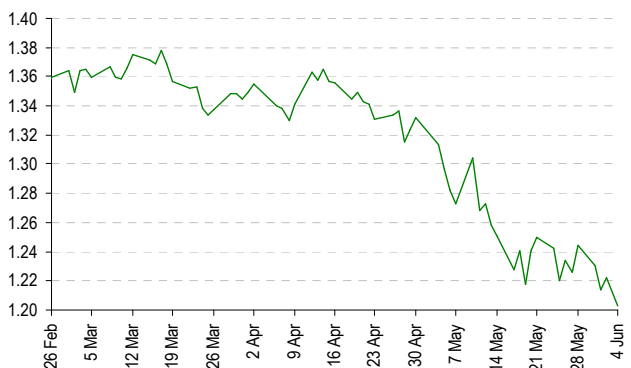
Yield curve



Weakening in bond market with low activity

- Yields of domestic bonds were roughly stable for the better part of the week with limited activity of investors – market holiday in the US and UK on Monday and later the day off in Poland. High demand for Polish papers on two-year bonds auction did not affect yields. On Friday, global risk aversion and worsening in sentiment in the region led to yields rise by 6-8 bp.
- The bond market will remain under influence of sentiment in the region, especially in the context of last week's failure of bond auction in Romania, showing limited interest of investors in the CEE. Therefore, Hungarian fiscal problems should be closely watched and in the case of further escalation of fiscal woes Polish yields may be under pressure again.

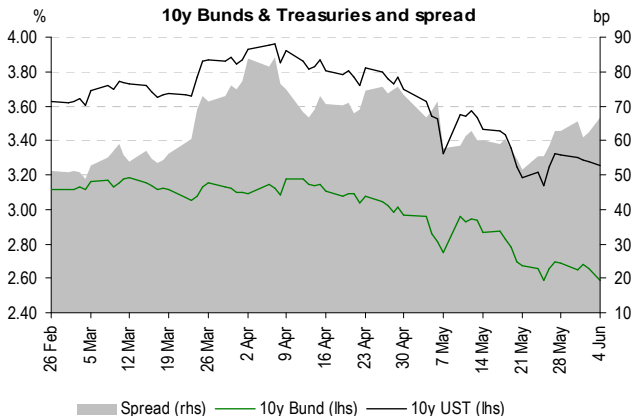
EURUSD rate



Euro hits new lows

- For the most of the week the single European currency was under pressure, approaching a few times the four-year low. Bad sentiment towards the euro was driven by worries on conditions of European banks after the release of ECB's stability report as well as on prospects of economic recovery in Europe. On Friday the euro weakened significantly breaking important levels and falling below 1.21 against the dollar and below 1.40 against CHF. The move was triggered by politicians' comments during G20 summit and by information from Hungary.
- Breaking 1.21 level may open the room for further euro depreciation. This week the most important data will be US retail sales and Michigan index. Markets will also closely watch comments by Bernanke and Trichet.

10y Bunds & Treasuries and spread



Core markets yields down

- After the moderate fall in bond yields on the core markets in the first part of the week, on Friday Bunds and Treasuries strengthened sharply after the weaker-than-expected labour market report in the US and due to significant fall in equity indices. Negative information from Hungary and worries on contagion effect of fiscal problems led to considerable increase in CDS rates for many countries, especially Hungary.
- Higher risk aversion will drive appetite for safe assets in the coming days, unless the economic data are strong enough to bring optimism back to global markets. Comments after the ECB meeting should support bonds as expectations for later rather than sooner rate hikes should be maintained.

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