Bank Zachodni WBK

Weekly economic update

14 – 20 March 2011

After short stabilization at the beginning of the week the risk aversion started to rise gradually. Initially, it was due to the fact that market focused on PIIGS countries (after Moody's downgrades of Greece and Spain) and persisting unrest in Libya. The bad news cumulated in the second part of the week when data from China showed a deficit in foreign trade, acceleration of inflation triggered worries over stronger monetary tightening, and on Friday the tsunami hit Tokyo.

This week a lot of domestic data will be published in Poland, which will be in our view a support for the zloty, however the key factor for the domestic currency will be external factors. Abroad the focus of attention will be on the US data (real estate market, CPI, industrial output) and - most of all - on the FOMC statement, which will be awaited by investors.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		MONDAY (14 March)					
11:00	**PL**	**Tender of 51-week T-bills worth PLN0.6-1.1bn**					
11:00	EZ	Industrial output	Jan	%MoM	0.3	-	-0.1
14:00	**PL**	**Current account**	**Jan**	**€m**	**-1380**	**-1395**	**-1573**
14:00	**PL**	**Exports**	**Jan**	**€m**	**10063**	**10305**	**9771**
14:00	**PL**	**Imports**	**Jan**	**€m**	**10651**	**10850**	**10877**
14:00	**PL**	**Money supply**	**Feb**	**%YoY**	**8.5**	**8.7**	**8.1**
		TUESDAY (15 March)					
11:00	DE	ZEW Index	Mar	pts	16.0	-	15.7
13:30	US	Import prices	Feb	%MoM	0.9	-	1.5
13:30	US	NY Fed Index	Mar	pts	16.10	-	15.43
14:00	**PL**	**CPI**	**Feb**	**%YoY**	**3.9**	**3.9**	**3.8**
19:15	US	Fed decision		%	0.0-0.25	-	0.0-0.25
		WEDNESDAY (16 March)					
11:00	EZ	HICP	Feb	%YoY	2.4	-	2.4
13:30	US	House starts	Feb	m	578	-	596
13:30	US	Building permits	Feb	m	570	-	560
14:00	**PL**	**Wages**	**Feb**	**%YoY**	**4.9**	**4.8**	**5.0**
14:00	**PL**	**Employment**	**Feb**	**%YoY**	**4.0**	**4.1**	**3.8**
		THURSDAY (17 March)					
13:30	US	Core CPI	Feb	%MoM	0.1	-	0.2
13:30	US	Initial jobless claims	week	k	388	-	397
14:00	**PL**	**MPC minutes**					
14:00	**PL**	**Industrial output**	**Feb**	**%YoY**	**9.9**	**11.2**	**10.3**
14:00	**PL**	**Construction output**	**Feb**	**%YoY**	**16.6**	**19.5**	**11.2**
14:00	**PL**	**PPI**	**Feb**	**%YoY**	**6.7**	**6.6**	**6.2**
14:15	US	Industrial output	Feb	%MoM	0.6	-	-0.1
14:15	US	Capacity utilization rate	Feb	%	76.5	-	76.1
15:00	US	Philly Fed Index	Mar	pts	29.5	-	35.9
		FRIDAY (18 March)					
11:00	EZ	Trade balance	Jan	€bn	-13.0	-	-0.5

Source: BZ WBK, Bloomberg, Parkiet, Reuters

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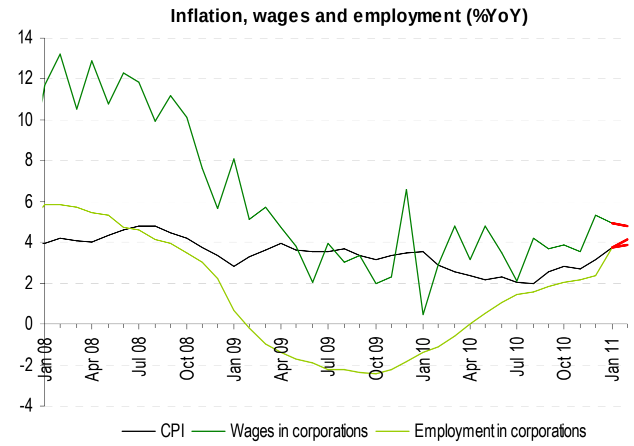
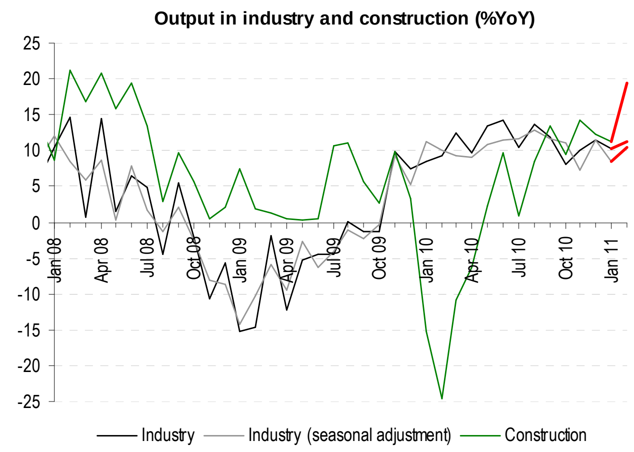
What's hot this week – Rich set of domestic data



▪ We expect that in February wage growth slowed down, but that does not change the fact that wage pressure persists and together with further acceleration of CPI is increasing the risk of second round effects. The data on inflation will be based on new CPI basket thus January's data may be revised. We expect further rise of employment (0.2%MoM) at average pace as in 2010, but slower than in January (when the data was disturbed by change of sample).

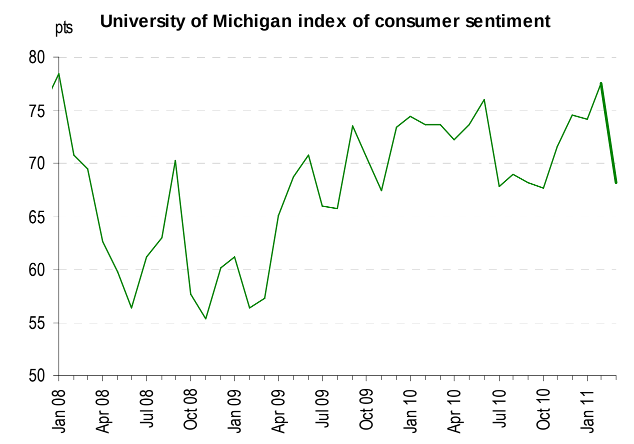
▪ Given the recent data from abroad, Polish data on foreign trade may be interesting. After seasonal drop of trade turnover in January we expect a visible rebound. Still, data released by the CSO show risk for our forecast, as presented slower pace of trade growth, particularly weaker imports. If that data is confirmed, lower trade deficit may provide some support for the zloty.



▪ In contrast to what is anticipated by the market we expect that in February the industrial output accelerated. Though PMI index for Polish manufacturing declined unexpectedly in February, we are convinced that strong performance of euro zone's and German PMI are pretty optimistic signals for domestic manufacturing sector. Additionally, the CSO's economic index indicated positive tendencies in February's industrial output.

▪ In January we have not seen a recovery in the construction and assembly output that was anticipated by us and the market consensus. Nevertheless, we predict that even lower base effect in February supported the annual rate of growth and construction output has surged. The data will show whether common expectations for recovery in investments is Q1 2011 is justified.

Economy last week – Better sales, worse consumer sentiment in the US



▪ Flash estimates of Michigan index in March clearly disappointed. The data showed a decline to 68.2pts from 77.5pts in February versus market expectations at 76.5pts. If final data confirm that estimates than the index would have plunged to the lowest level since October 2010. Still, the scale of drop is not worrying and the index obviously stayed in the upward trend.

▪ The February's retail sales in the US advanced by 1%MoM, most in four months and after excluding autos by 0.7%. The sales was surely positively affected by improvement of situation on the US labour market reflected by data on non-farm payrolls (biggest gain of workplaces since May 201) and drop of the unemployment rate to 8.9% (lowest level since April 2009).

Quote of the week – Interest rate in April is possible, but not certain

Adam Glapiński, MPC member, Reuters, 8 Mar

I think two to three rate increases this year (including the one in January) should be sufficient to avoid second-round effects. I suppose in April an increase is probable but it is definitely not certain.

Andrzej Kaźmierczak, MPC member, Reuters 10 Mar

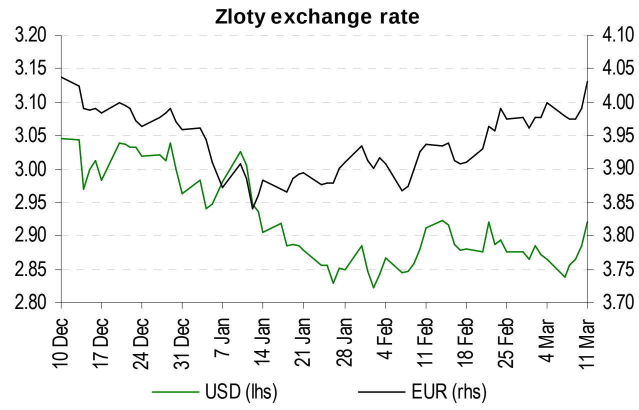
I think that if inflation tops 4 percent, a decision [to raise rates] would be straightforward. Then, a process of increasing wage demand starts and, along with this, a whole chain of second-round-effects. We need to influence inflation expectations and not only hope that external factors will fade.

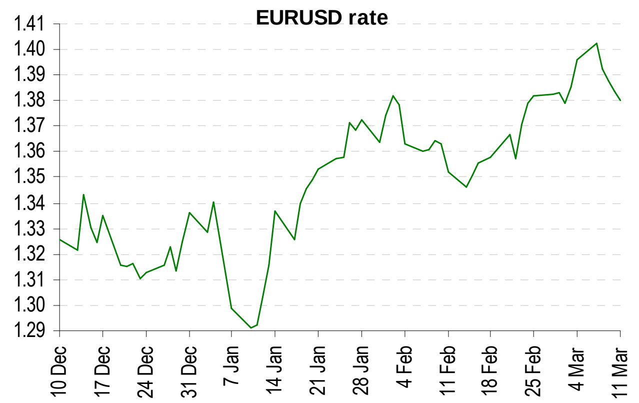
Andrzej Bratkowski, MPC member, Reuters 10 Mar

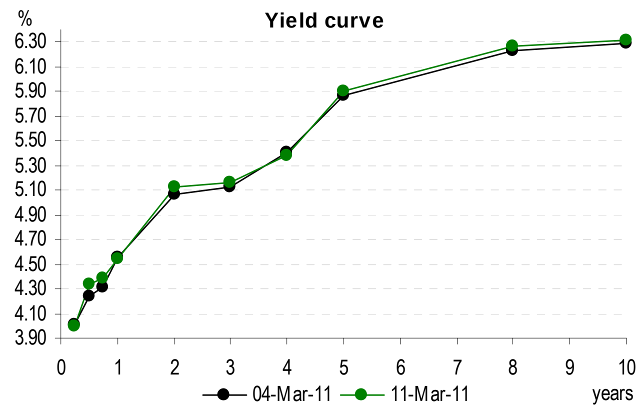
The economy could use two rate hikes, of a total of 50 basis points, in the Q2. This could allow for stable rates for a few months afterwards.

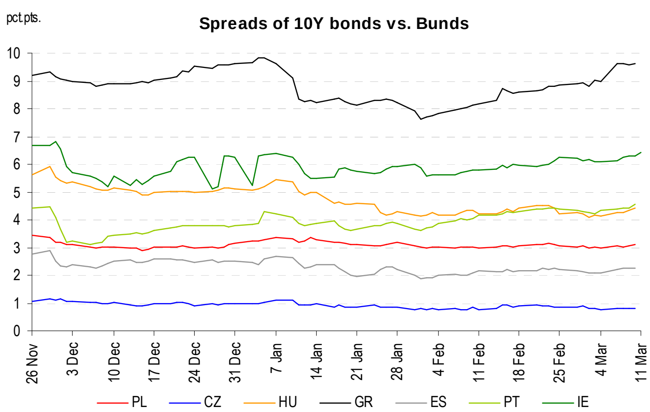
Recent comments of MPC members have increased, in our view, probability of rate hike at the April meeting. Particularly important are the remarks of Glapiński and Kaźmierczak, who used to vote against rate hikes at the last four meetings in 2010. As regards the latter member, who (along with Chojna-Duch) is considered to be the most dovish member of the Council, he seems to be slowly adopting a more hawkish bias, while Glapiński has already voted for the rate hike by 50 bps in August 2010. The results of recent votes indicate that there is only one vote missing to raise interest rates. Perhaps this week even Kaźmierczak will get arguments for a rate hike, if inflation surprises up again. Besides, the argument for the doves to change their mind on the rate hikes could be tightening of the ECB's rhetorics.

Market monitor









Small support from macro data

▪ Last week only the first two days saw some attempts of the EURPLN to get lower. In the next days, there was a sharp rise in risk aversion, triggered by social unrest in Libya, downgrade of ratings for Greece and Spain, data from China, and tsunami in Japan. Consequently, the EURPLN broke through the resistance at 3.99 and rose to 4.04, the highest level since December 2010, while USDPLN reached levels last seen in February. Data on inflation released in Czech Republic and Hungary were lower than expected and had no impact on the markets. On Friday, there was slight rebound and the EURPLN dd not manage to stay above the resistance 4.0325 for longer. Thanks to increasing EURUSD the zloty strengthened to 4.02 versus euro. We expect that this week a publication of numerous data from Poland will turn investors' attention to the interest rate outlook and will prevent the zloty from more significant depreciation. Still, the factors that may hamper global moods are valid, so we do not expect the zloty to appreciate neither. Next resistance for the EURPLN is 4.03 and 4.05, the support is at 3.99.

▪ The EURUSD continued a drop after a rebound from 1.40 that took place last Friday. Increasing fears about PIIGS countries (reinforced by Moody's decisions) and a general rise in global risk aversion have caused that during the week the rate fell to the lower limit of the band we had suggested last week, i.e. 1.375. Expectations for ECB rate hikes clearly receded to the background. At the end of the week the rate bounced back from 1.375 and this week this rebound may be continued amid expectation for dovish statement after the Fed meeeting. The support is at 1.365, the resistance 1.40.

Domestic yield curve little changed after data

▪ On the domestic debt market yields in the middle and at the long end of the curve have not changed over the week. At the short end there was a rise, but dovish Glapiński's comment halted this move. This week we will see a large portion of data that may deliver significant hints as regards monetary policy outlook. In our view, the data for February will be moderately hawkish, confirming inflationary trends in the economy. Thus, we do not expect the data to change a scale of rate hikes priced-in by the market. At the long end the changes will depend on sentiment in the global markets.

▪ Yields at core debt markets were steadily falling during the last week. A rise in demand for risky assets was supported by persisting high risk aversion. Yields of German bonds fell to the lowest level since the start of March, and yields of Treasuries were the lowest since end-January.

▪ Focusing foreign investors' attention on euro zone's peripheral debt markets resulted in a sharp rise in spreads of PIIGS bonds versus 10-year Bunds. To some extent this was caused by decreasing yields of German Bunds, but widening of Greek spread by 50 bp was mainly a result of growth in yields of Greek bonds from 12.3% to 12.8%. Twice smaller growth took place in case of bonds of Ireland, Portugal, and Spain. On Wednesday Portugal will hold a tender of one year T-bills, and on Thursday Spain will hold auction of bonds.

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