

Weekly economic update

4 – 10 July 2011

Since the beginning of the previous week a quite positive mood has predominated the market. The hopes that the Greek parliament will approve the 5-year austerity plan contributed to substantial gains in the stock markets and to strengthening of the euro against the dollar. When the austerity plan was finally approved, the stocks gained even more considerable, but reaction of the EURUSD proved to be moderate. With some delay, the increasing risk appetite supported the zloty, which gained also after release of the balance of payments data. The domestic debt gained due to positive information from Greece as well as thanks of plans to limit the supply of treasury papers in the remainder of the year. The released macro data did not draw much attention.

The weekend decision of the Eurogroup concerning the bailout for Greece should be only a formality in face of Greek approval of austerity plan. On Monday the US investors are having a market holiday, but this should not limit the volatility substantially. On Wednesday the MPC is to make its decision on interest rates. The decision and communiqué should not change the expectations about upcoming policy actions, but the new inflation projection can deliver some hints on this issue. On the other hand, the global market will await the tone of the ECB's communiqué. One month ago the bank suggested that the rates will be hiked in July, but did not give much hints about further decisions. That is why the communiqué can substantially affect the EURUSD rate. At the end of the week important US labour market data are due for release. The figures will show if the May reading was only a temporary lull or a result of slowdown in US economy. In our view the EURPLN rate will hover in the range of 3.94-4.00 and the global sentiment will be of crucial importance for the trading. We expect a stabilisation on domestic debt market, although the new inflation projection may prove to be important.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (4 July)							
EZ	10:30	Sentix index	Jul	pts	1.2	-	3.5
EZ	11:00	PPI	May	% YoY	6.3	-	6.7
US		Banking holiday					
TUESDAY (5 July)							
EZ	9:58	PMI – services	Jun	pts	54.2	-	56.0
EZ	11:00	Retail sales	May	% YoY	-0.4	-	1.1
US	16:00	Industrial orders	May	% MoM	1.0	-	-1.2
WEDNESDAY (6 July)							
PL		MPC decision		%	4.50	4.50	4.50
DE	12:00	Industrial orders	May	% MoM	-0.7	-	2.8
US	16:00	ISM – services	Jun	pts	54.1	-	53.6
THURSDAY (7 July)							
PL	11:00	Bonds switching auction					
DE	12:00	Industrial output	May	% MoM	0.5	-	-0.6
GB	13:00	BoE decision		%	0.50	-	0.50
EZ	13:45	EBC decision		%	1.50	-	1.25
US	14:15	ADP report	Jun	k	60	-	38
US	14:30	Initial jobless claims	week	k	421	-	428
FRIDAY (8 July)							
DE	8:00	Exports	May	% MoM	1.5	-	-5.5
US	14:30	Non-farm payrolls	Jun	k	90	-	54
US	14:30	Unemployment rate	Jun	%	9.0	-	9.1

Source: BZ WBK, Parkiet, Reuters

Maciej Reluga Chief economist (+48 22) 586 8363

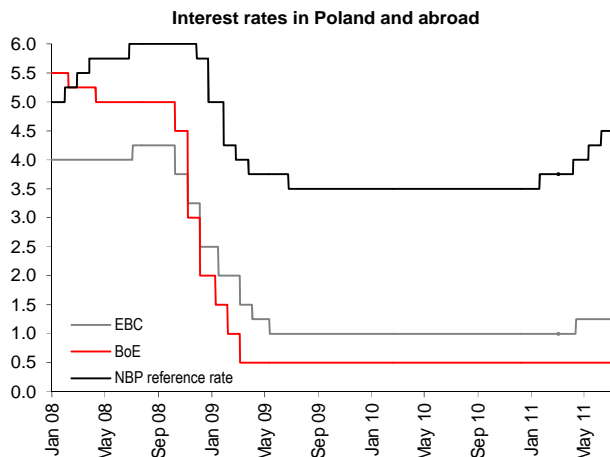
e-mail: ekonomia@bzwbk.pl

Piotr Bielski (+48 22) 586 8333

Marcin Sulewski (+48 22) 586 8342

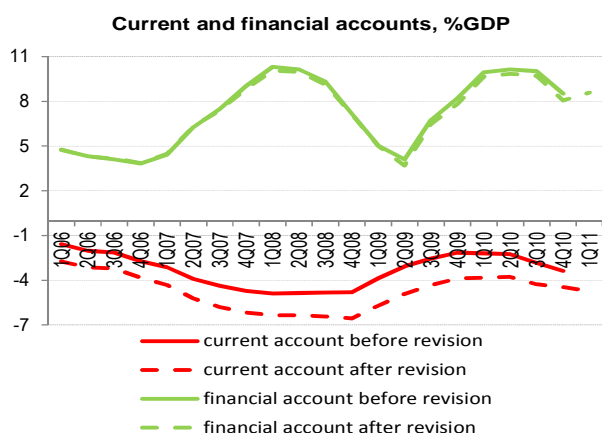
Piotr Bujak (+48 22) 586 8341

Marcin Luzziński (+48 22) 586 8362

What's hot this week – Meeting of the MPC and ECB, US data

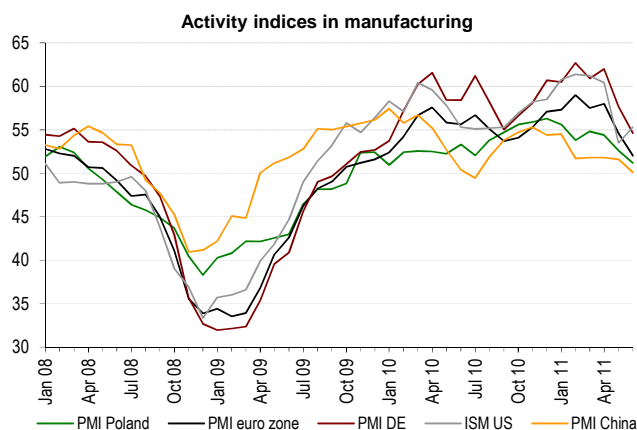
■ The main issue this week in Poland will be the MPC decision. In face of clear message that the MPC members want to assess the results of previous interest rates hikes, we expect, similarly as the market, that the rates will be kept on hold this week. The communiqué may confirm a pause in hiking cycle, but it should not affect the market. One day later the ECB is to release its decision. The interest rate is anticipated to increase to 1.50%, but more important will be the suggestions about further steps of the monetary policy. The tone of the communiqué can affect the EURUSD rate and the interest rate market.

■ At the end of the week monthly data from US labour market are due for release. In the previous month this reading disappointed and the June figures can indicate if the substantial drop of new payrolls in May was only temporary or persistent, due to slowdown in economy.

Last week in the economy – Balance of payments revision not that scary, PMI below expectations

■ Revision of balance of payments data for 2004-2010 brought widening of the C/A gap in different years on the scale ranging from 1.1% to 1.8% of GDP, i.e. in line with our predictions and less than some market participants feared. The NBP stated that the thorough examination has identified four categories with substantial impact on the errors and omissions: import of used cars from the EU, some transfers comprised in the current account, repurchase agreements and external assets of the nonfinancial sector.

■ Deficit for 2010 widened to 4.5% from 3.4% of GDP, while market expected 4.7% according to the Reuters survey. We stick to our view that – despite some fears – the revision of BoP data will not have a substantial impact on the GDP.



■ PMI in manufacturing was worse than our and market's expectations (51.8 and 52.3, respectively) and dropped to 51.2, the lowest level since 2010. A plunge below the neutral level of 50.0 was recorded by new orders subindex and especially by the new export orders, which is in line with global tendencies (to some extent due to earthquake in Japan). The increase of output slowed down again, the cost pressure picked down as well, but the increase of employment remained above average. Our forecast of industrial output is below market expectations, similarly as in case of PMI.

■ In June the inflation expectations amounted to 4.2% (the CPI known during the survey was 4.5%YoY). The share of respondents expecting an acceleration of inflation decreased, while share of respondents expecting a stabilisation or slowdown increased.

Quote of the week – It can turn out that interest rate hikes are necessary**Marek Belka, NBP governor, Reuters, 28th June**

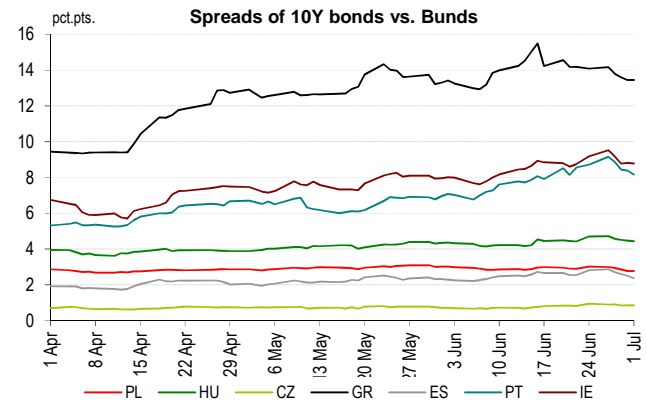
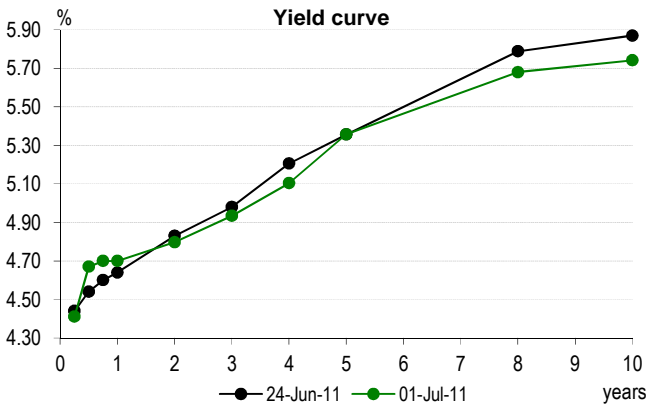
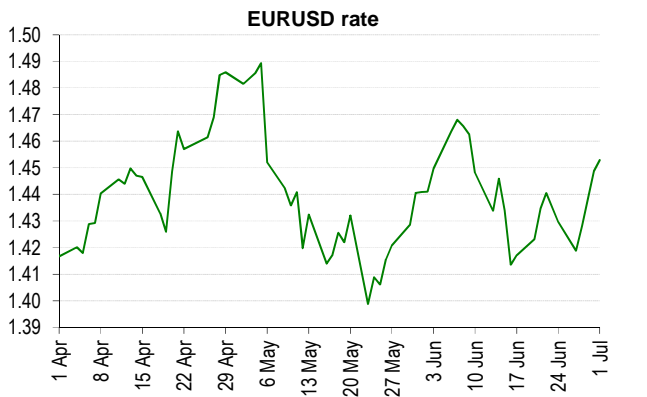
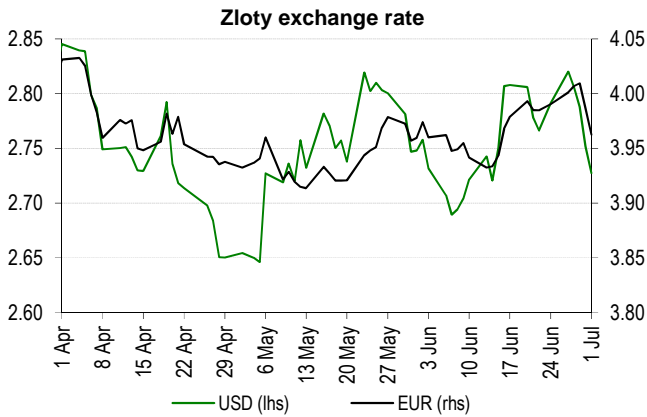
I am not afraid of inflation (...), we were conscious that it can increase. Now we can see that the food and oil markets' situation is stabilising or even reverting. If something [inflation] jumps too high, it has to fall.

Jerzy Hausner, NBP governor, Reuters, 27th June

Inflation should stop increasing and more or less after a year it should come to level close to our target, i.e. 2.5 per cent. Of course the MPC Council cannot affect the world's oil or food prices. (...) If the manufacturers judge that the increases of commodity prices are not temporary but persistent, they will probably raise the prices. (...) So we should not herald an end of hiking cycle, as it can turn out that we should continue to do our job.

One week ahead of the MPC meeting, statements of its members did not change our forecast that the interest rates will be kept on hold in July. As regards the future, we share the view of NBP governor Marek Belka, who expects that the inflation will soon decrease slightly. Still, the annual annual will remain above 4.5% until the end of the year (and will be close to 5% by the end of 2011), which – in our view – is enough to make MPC Council hike one more time by 25bp. This will happen probably in the autumn.

Market monitor



After appreciation we expect stabilization of zloty...

▪ Since the start of the week the zloty was lagging behind other currencies and assets gaining thanks to return of risk-on sentiment. For the first two days of the week EURPLN continued the upward trend and USDPLN was hovering at elevated level. Also the Czech crown and the Hungarian forint did not took advantage of relatively positive moods in the global markets. Only approval of the austerity plan by the Greek government positively affected the CEE currencies, and the zloty was additionally strengthened by revised balance of payments data. At the end of the week the zloty was near 3.96, nearly PLN0.06 below the weekly high. We expect that this week EURPLN will remain in the range of 3.94-4.00 and the key factor driving the domestic currency will be developments in the global markets.

▪ EURUSD was rising clearly throughout the week on hopes that the Greek parliament will pass the 5-year austerity plan. Additionally, the euro was positively affected by comments from ECB President confirming expectations for a rate hike in July. During the week EURUSD rose to 1.45 from 1.41 (briefly reaching 1.455). Announcement of the payment of next tranche of funding for Greece seems to be a done deal and the market will focus more on possible news regarding new aid package for Athens. Any hints from the ECB on next policy actions will be crucial as well. In the first part of this week the euro may be loosing, because many positive news on the debt crisis has already been priced in. Upward potential for EURUSD may be also constrained by uncertainty regarding the ECB rhetoric. All in all, although potential for rise in EURUSD is limited, we also do not expect a significant drop, below the resistance at 1.42.

... and yields of bonds

▪ The domestic yield curve flattened over the past week due to visible appreciation of long term bonds. One of the factors supporting that securities was deputy minister of finance, Dominik Radziwiłł saying that in Q3 the ministry will probably not issue T-bills and supply of bonds will be limited to only one auction a month. Plans of supply for Q3 showed the FinMin will sell DS1021 bonds (and not DS1020 that is presently a benchmark for 10Y tenor) what dragged yields of that security down. Apart from that, window dressing and decision of Greek parliament had positive impact on the market. We expect that this week yields will remain stable. The risk factor for that scenario may be new NBP's inflation projection. If it does not show CPI lowering of CPI path, expectations for an interest rate hike may be strengthened. Then yields on the short end may rise.

▪ Yields on the core fixed income markets were rising on hopes for positive news from Greece. As the austerity measures were accepted, upward trend was continued. Still, the scale of move was not too big, what means investors are still aware that details on their participation in the next bailout package is due to be discussed. At the end of the week yields of the 10Y Bunds and Treasuries reached 3.03% and 3.17% respectively.

▪ Spreads versus 10Y Bunds narrowed – mainly due to falling yields of bonds of countries from euro zone's periphery – amid positive news from Greece. Greek bonds that gained most.

This publication has been prepared by Bank Zachodni WBK S.A. for information purposes only. It is not an offer or solicitation for the purchase or sale of any financial instrument. Information presented in the publication is not an investment advice. All reasonable care has been taken to ensure that the information contained herein is not untrue or misleading. But no representation is made as to its accuracy or completeness. No reliance should be placed on it and no liability is accepted for any loss arising from reliance on it. Forecasts or data related to the past do not guarantee future prices of financial instruments or financial results. Bank Zachodni WBK S.A., its affiliates and any of its or their officers may be interested in any transactions, securities or commodities referred to herein. Bank Zachodni WBK S.A. or its affiliates may perform services for or solicit business from any company referred to herein. This publication is not intended for the use of private investors. Clients should contact analysts at and execute transactions through a Bank Zachodni WBK S.A. entity in their home jurisdiction unless governing law permits otherwise. Copyright and database rights protection exists in this publication. Additional information is available on request. Please contact Bank Zachodni WBK S.A. Treasury Division, Economic Analysis Unit, ul. Marszałkowska 142, 00-061 Warsaw, Poland, phone (+48 22) 586 83 63, email ekonomia@bzwbk.pl, <http://www.bzwbk.pl>