Bank Zachodni WBK

MACROscope

Polish Economy and Financial Markets

October 2007

Softer policy ahead?

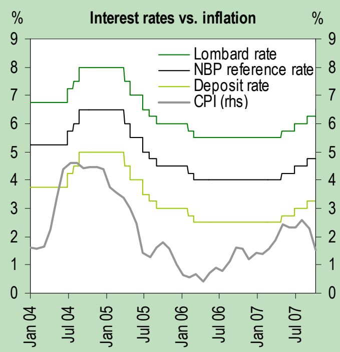
- **Since the release of our previous report, the data did not suggest significant changes in the Polish economy**. We keep our predictions for slight deceleration of GDP growth (to ca. 6% in the second half of the year), although the August inflation surprise caused a decrease in predicted inflation path. This change was one of the main factors resulting in adjustment in market expectations concerning further monetary policy decisions. It was supported by the comments of some MPC members, who suggested, among others, that strong enough signals causing another increase of the interest rates could occur at the beginning of the next year. As we have announced earlier, starting from this edition of MACROscope we will publish index of MPC members restrictiveness (apart from publishing monetary conditions indices), which should be helpful in assessment of changes in rate-setters' opinion and balance of strength in the Council. While after the August's Council meeting, the market participants' forecasts indicated the rate hike already in October, last weeks brought the change of these expectations. We stay in line with our forecast, according to which the rates will be increased in November, as in our opinion another market data, especially those from the labour market will convince the Council to such move. The extent to which the rates will be increased in the next year is a crucial question, because the Council's members suggested that it can be less than 5.5%. So far we stick to our view of two more moves by 25 bps in the first two quarters 2008.

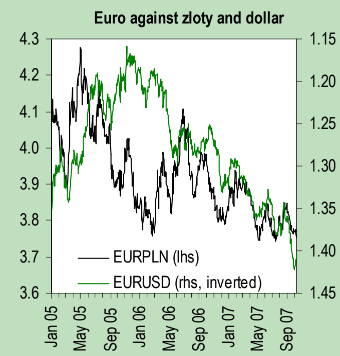
- **More crucial change of expectations appeared as the prospects of monetary policy led by the world's main central banks.** After September's Fed interest rates cut by 50 bp we expect another moves with a chance for the Fed fund rate to fall to the level of 4% in the mid-2008. It also seems that another interest rise in the euro zone, if it will happen, will be conducted not before the next year. Lower than forecasted other central banks' restrictiveness can be an important factor for the Monetary Policy Council while taking future decisions, although it is worth remembering that the monetary policy cycles had not always changed in line with the world's trends.

- **According to our last month's expectations, zloty continues appreciating trend, which is connected with lower risk aversion, as well as strong fundamentals of the Polish economy.** Zloty's strengthening was more visible in relation to US dollar that weakened to the record level against the euro. We do not change our expectations for keeping weak dollar and further zloty's appreciation till the end of this year. Decline in Polish yields that occurred in the last couple of weeks was mainly caused by the rapid inflation fall, which effect was not offset by the hawkish labour market data. We assume that another data releases (among others, indicating inflation increase) and one more interest rates increase this year will cause the yields to rise by the end of the year.

Financial market on 28 September 2007:					
NBP deposit rate	3.25	WIBOR 3M	5.10	USDPLN	2.6647
NBP reference rate	4.75	Yield on 2-year T-bonds	5.25	EURPLN	3.7775
NBP lombard rate	6.25	Yield on 5-year T-bonds	5.56	EURUSD	1.4168

This report is based on information available until 09.10.2007





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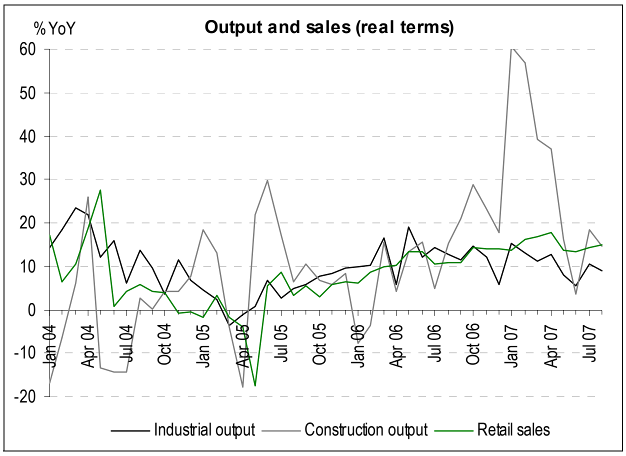
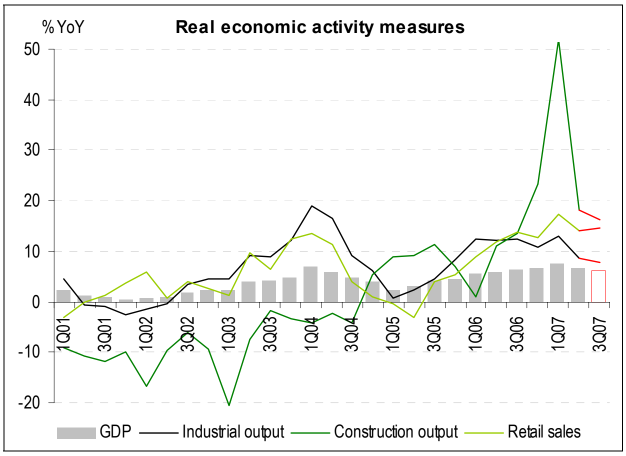
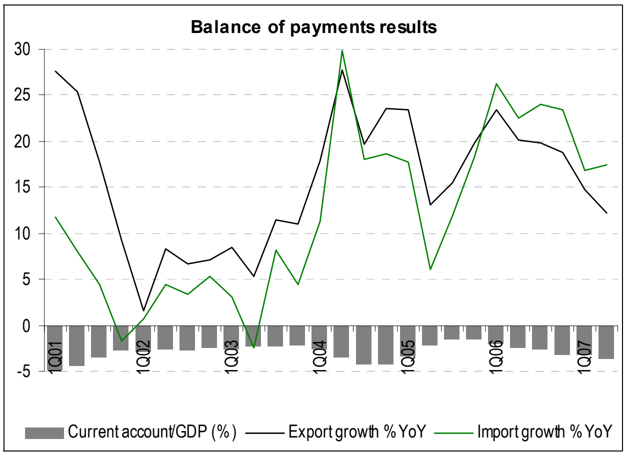
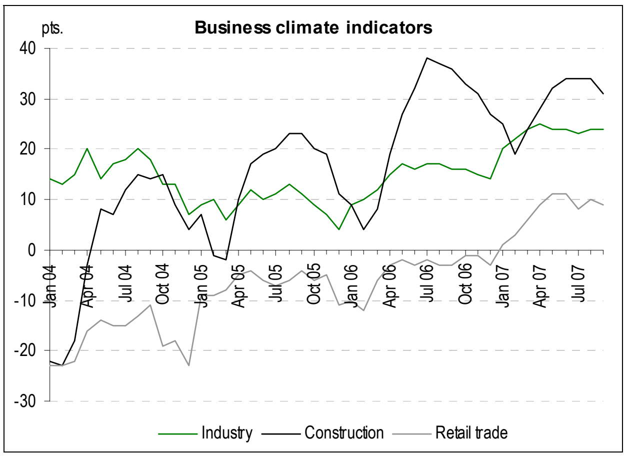
Economic update









Source: CSO, NBP, own calculations

Economic activity rises although slower

- Sold industrial output increased 9%YoY in August after 10.4% rise in July. Although the result was worse than the median prediction, the noted rise should be still treated as solid. Seasonally adjusted production growth reached 9.4%YoY and was higher than in three preceding months.
- Construction and assembly production increased in August by 14.6%YoY (16.4%YoY after seasonal adjustment).
- Although the output growth rates in industry and construction are not as high as in the first half of the year, they are at levels showing that both sectors are still in the phase of expansion. Thus, it is still too early to herald a downturn in economic growth. The pace of expansion is just getting closer to potential level.
- While expansion in industry and construction is stabilizing, the recovery in retail trade is still getting momentum. Retail sales growth in August reached 17.4% YoY in nominal terms and 16.1% in real terms, beating forecasts once again. Strong growth was maintained in all kinds of sales, which indicates that the demand growth is broad based. The main factor fuelling this growth is rapid increase in households' income (see later on).
- Generally, the latest monthly data confirmed that the pace of GDP growth in the second half of the year will not be as high as in the two first quarters, although it should be near 6%. The importance of domestic demand has been increasing gradually.
- GDP growth for 2006 has been revised up by the CSO from 6.0% to 6.2%. Domestic demand growth has been increased (with particularly strong revision in inventories rise), however the estimate concerning foreign trade balance deteriorated. We keep our prediction assuming that GDP growth in 2007 will reach 6,5% on average.

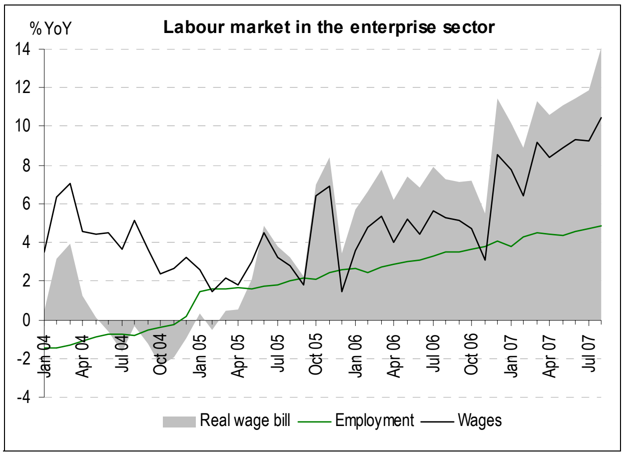
Gradual deterioration in external balance

- NBP's balance of payments data confirm gradual worsening of external balance, reflected in widening current account deficit.
- According to recently released quarterly data, after the first half of the year the cumulative 12-month current account deficit increased to 3.7% of GDP against 3.2% of GDP at the end of 2006 and 1.6% in 2005.
- In July current account deficit was high again, reaching €1.3bn, and in relation to GDP it increased to 3.8%.
- Such situation occurs although export continues fast, double-digit growth (in July above 17% YoY), because import turnover is much stronger, being supported by the vigorous domestic demand growth.

Business climate surveys herald stabilisation of growth

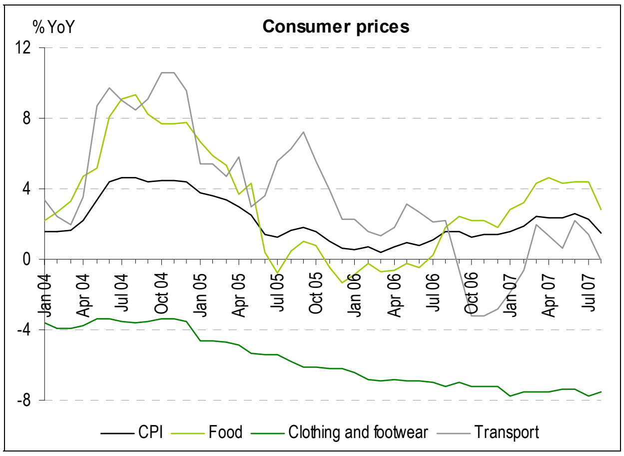
- CSO's survey on economic climate in enterprises showed optimistic assessment in most of sectors in September. In manufacturing and construction indices are stabilising at high levels. The best performance is recorded in services and retail trade where sentiment measures are the highest in 13 years.
- Ipsos' consumer confidence index slightly declined in September, but it is still one of the highest in last 10 years. Propensity to consume increased to record high level. CSO's consumer climate index was also one of the highest in history.
- The results seem to suggest stabilisation of growth rates in industry and construction and further rapid expansion in consumption demand, being fuelled by rapid improvement in households' income.

Economic update



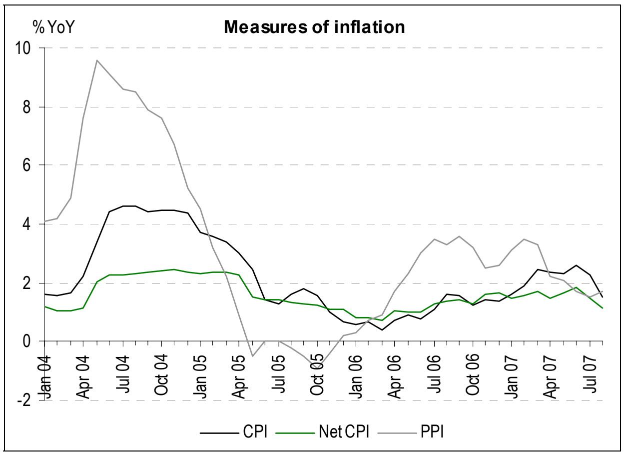
Labour market heating up

- Average pay in enterprises sector increased in August by 10.5%YoY, accelerating from 9.3% in July, while average employment rose 4.8%YoY against 4.7%YoY in the previous month. In both cases the results were above market expectations.
- The wage bill in enterprises sector rose by 15.8%YoY in nominal and 14.1% in real terms. Additionally it is worth remembering that these estimates consider gross remuneration while household's incomes are also influenced by the decline in pension premium for employees by 3 pp since July (although this year it does not affect those with the highest salaries).
- Labour market data suggest that the increase in unit labour costs can be maintained in next quarters being one of the crucial risk factors for inflation.



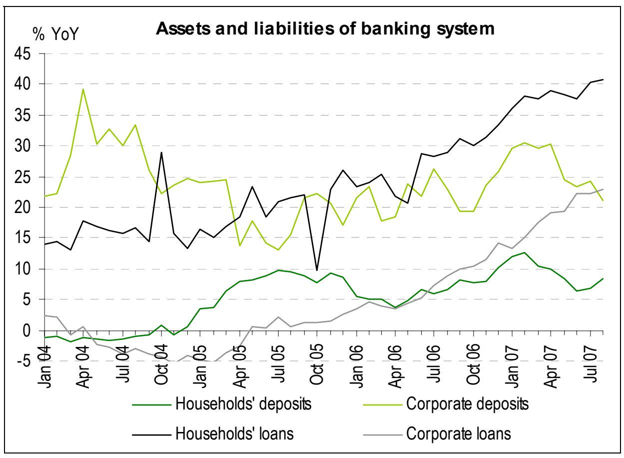
... meanwhile inflation stays low

- August inflation data were a positive surprise. The CPI growth slowed down to merely 1.5%YoY from 2.3%YoY in July. It was mainly caused by the fall in costs of internet services and prices of audiovisual equipment (prices in communication and entertainment and culture dropped by ca. 2%), although crucial were also low food and fuel prices.
- Reduction in main inflation rate was followed by a decrease in core inflation. Net inflation (excluding food and fuel prices) reached in August 1.2%YoY against 1.5% in July.
- PPI growth accelerated in August to 1.7%YoY. The rise in prices in the majority of sections suggests that the companies are trying to pass increasing costs pressure to prices, although strong competition is slowing down this process.
- Surprising scale of CPI decrease in August suggests one should reconsider inflation path in the nearest months. The impact of promotion cuts in internet fees on CPI will be probably temporary, however before it subsides the path of inflation will be probably slightly below the one earlier forecasted. In the long run however, internet fees and prices of electronic equipment should be gradually descending.
- According to the Ministry of Finance in September the CPI index increased 0.5%MoM and 2.0%YoY. It is quite high estimate, as our forecast suggests inflation acceleration to 1.8%YoY. One could suppose such significant increase in prices was caused by assumption about high food prices. It should be remembered though that in the last several months the accuracy of FinMin's inflation forecasts have decreased.
- We still predict that inflation rate will be close to the target at the end of he year, and net inflation should remain below 2% until the year-end (possibly even below 1.5%).



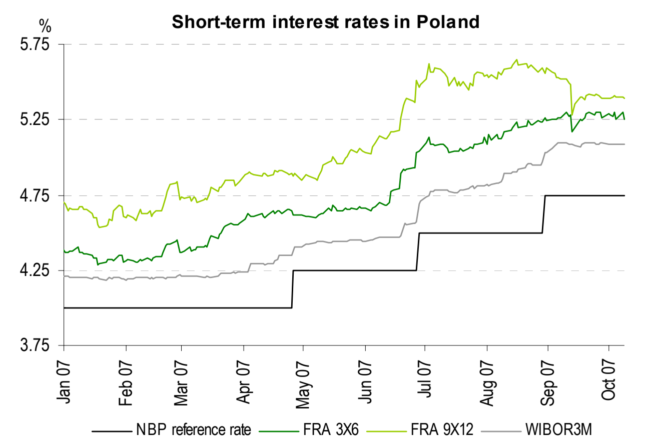
Credit growth still accelerating

- The rise in broad money supply (M3) in August stayed at the high level of 15.6%YoY. The total deposits and money in circulation increased in the same pace.
- Meanwhile, credit growth accelerated again. Households' loans increased in August by almost 41%YoY and the credits for enterprises rose by ca. 23%YoY. This is the fastest loans growth in the polish banking sector since the end of 1990s (especially after considering inflation differences).
- High demand for loans persists and does not seem to be seriously affected by recent interest rates hikes in Poland and abroad. This suggests that the domestic demand expansion will be continued in the nearest future, supporting fairly high pace of economic expansion.



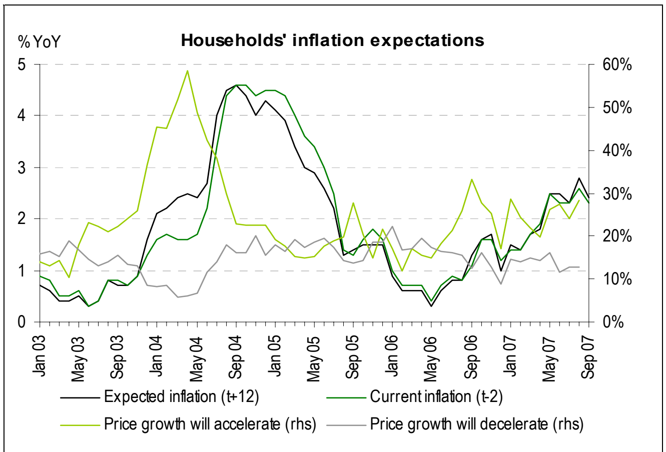
Source: CSO, NBP, own calculations

Central bank watch



Selected fragments of MPC statement after September meeting
In August the annual growth of consumer prices in Poland amounted to 1.5%. The decline in inflation observed in 2007 Q3, although deeper than previously expected, is of temporary nature. The Council assesses that in 2007 Q4 inflation will be close to the inflation target of 2.5%.
In the Council's assessment, in the medium term the probability of inflation running above the inflation target decreased to a certain degree due to the previously implemented monetary policy tightening, though it is still higher than the probability of inflation running below the target. A more comprehensive assessment of the scale of the risk of inflation overshooting the inflation target will only be possible after analysing the data released in the future.
The Council will be closely monitoring the growth and structure of domestic demand, including the degree of the expansionary fiscal policy stance, developments of the current account balance, the relation between wage and labour productivity growth, zloty exchange rate, the impact of globalisation on the economy and developments in international financial markets.

Selected fragments of Monetary Policy Guidelines for 2008
In line with practice of growing number of central banks, striving for more in-depth analysis of economic developments, the Council decided to limit, from 2008, the frequency of publications of Inflation Reports including inflation projections, from four to three times a year. Such frequency of projections will be sufficient from the point of view of medium-term character of relation between monetary policy and economic developments. In turn, additional time between preparation of consecutive Reports will enable for deepening of research carried out by the NBP and will make it possible to improve analytical tools which are necessary for effective conduct of monetary policy. (...) Reports will be published in February, June and October.
Among factors that will affect shape of monetary policy in 2008 the most important ones seem to be: labour market conditions and situation in public finance.
Despite favourable prospects for economic growth and rising labour productivity it is expected that 2008 will see further rise in unit labour costs and as a consequence strengthening of inflationary pressure.



Source: NBP, Reuters

Pause in rate hikes. For how long?

- MPC statement after the September meeting, which concluded with no rate hike, was not surprising.
- The list of factors, which according to the Council are going to limit inflation in the medium term, was extended with a "possible slowdown of the global economy". The list of factors in favour of an acceleration inflation remained unchanged.
- Deeper than expected fall in inflation in Q3 was regarded by the Council as a one-off, which suggests that this will not affect monetary policy prospects.
- Although the Council said that balance of risks to inflation had improved, the same statement appeared in July and one month later a rate hike took place. We think, however, this time the Council will defer decision on next hike longer, given that crucial information regarding labour market and fiscal policy, i.e. key areas for the MPC, will only be available in November.
- Recent comments from central bankers, including those from the hawkish camp, suggested that even conservative rate-setters have become less prone to further hikes. They said that the new inflation projection due in October will be of high importance, but according to MPC's Filar the Council may not be convinced about a need for next hike even in November, when labour market data for Q2 are available, nor in December, when GDP figures for Q3 will be published.
- In our opinion, central bankers have felt too comfortable after lower than predicted inflation data for August. Taking into account inflation acceleration expected in next months and above all persisting threats related to the tightening in labour market conditions, we think the Council will hike rates again this year.

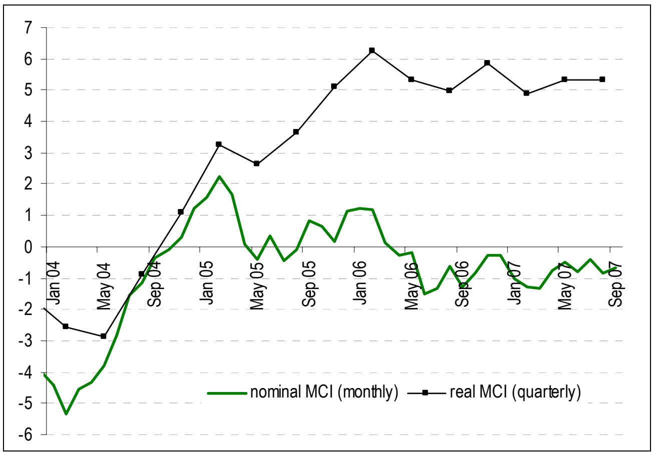
Fewer inflation projections a year

- The Monetary Policy Guidelines for the Year 2008 adopted by the MPC do not differ much from the document for the previous year as regards understanding of the inflation target and the way of its implementation.
- Meanwhile, the Council announced a change in frequency of releasing the Inflation Reports with inflation projections from four to three times a year: in February, June and October.
- The document mentioned situation in the labour market and in public finance as factors which will be of key importance for monetary policy in 2008. This is consistent with what was signaled earlier in official statements and minutes of MPC meetings. The Council expects further rise in unit labour costs, leading to strengthening in inflationary pressure, which suggests continuation of monetary tightening.

Inflation expectations follow CPI

- After a significant rise of inflationary expectations in August caused by the increase of CPI inflation in June above the central bank's target of 2.5%, September brought the weakening of inflationary expectations.
- This was in line with predictions, considering the adaptive character of households inflationary expectations in Poland (built in the construction of NBP index of inflationary expectations of households) and the inflation decline in July.
- Considering further inflation decrease in August, one may predict that the households inflationary expectations will decline in October, but later on should be gradually rising along with forecasted increase in the headline inflation rate. However, in recent months inflationary expectations have been close to the inflation target, which is a perfect situation for the MPC.

Restrictiveness of the Monetary Policy (Council)

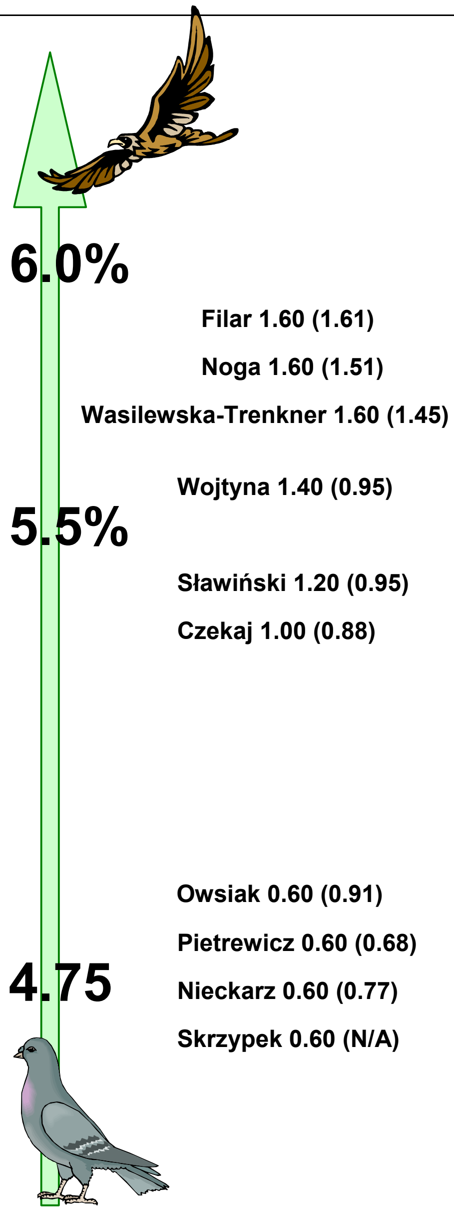


Increase in monetary policy restrictiveness in September

▪ Restrictiveness of monetary policy, measured by nominal MCI index (we described MCI indices we use in the previous edition of MACROscope) slightly increased in September.

▪ This resulted from a rise in short-term interest rates (both in absolute terms and in relation to long-term trend) after the rate hike by the MPC and from strengthening of the zloty against the euro (also both in absolute terms and versus the long-term trend).

▪ Meanwhile, real MCI hardly changed in the third quarter as compared to the second quarter of the year. This is because rise in real interest rates (both in absolute terms and relative to the long-term trend) was fully offset by weakening of the real effective exchange rate.



Note: Direction of the arrow reflects our expectations regarding direction of interest rate changes within the nearest 12 months. Values in percent indicate our **subjective** assumption as regards a preferred level of the reference rate in 12 months by a particular MPC member.

Who is who in the Monetary Policy Council?

▪ Poland's MPC, the same as collective bodies responsible for monetary policy in other countries, consist of members with different views and opinions on economic developments and the role of a central bank.

▪ Usually, three camps are distinguished in rate-setting panels. Doves and hawks are poles apart and in between them moderate rate-setters are located. Hawks are consistently more in favour of higher interest rates than doves who favour a more relaxed policy.

▪ Starting from this edition of MACROscope, we decided to launch a measure of central bankers' restrictiveness, which should be helpful in assessing, on a monthly basis, who is who in the MPC and what policy actions are likely in the future. One of reasons for that is to show how a centre of gravity in the MPC shifted after the change on the NBP governor post in January 2007 – Sławomir Skrzypek replaced Leszek Balcerowicz.

▪ The measure is based on methodology proposed by Timothy Edmonds in "The Monetary Policy Committee: theory and performance", Research Paper 99/17, February, House of Commons Library.

▪ Each recorded vote is given a 'score'. A vote for the majority view is given a score of 1. A vote for a more hawkish (less dovish) decision than the majority view has a score of 2 and a vote for a less hawkish (more dovish) decision than the majority view has a score of 0. Hence a hawk will have a number of 'twos', whereas a 'dove' will have some 'zeroes'. Average of points for all votes is the value of the index for a given MPC member. The results are used to determine the "hawk–dove" index. Numbers directly by the name are values of the index for 2007 (period since the beginning of Skrzypek's term) and numbers in parentheses are values of the index for 2004-2006 (period when current MPC members worked with former NBP governor). However, values of the index are not the only factor determining a central banker's position on the "hawk-dove" axis. We also take into account very recent comments of MPC members.

Change of the governor changes balance of strengths in the Council

▪ Sławomir Skrzypek, who replaced Leszek Balcerowicz, a radical hawk, at the beginning of 2007, proved, given a pattern of his votes, to be a dove.

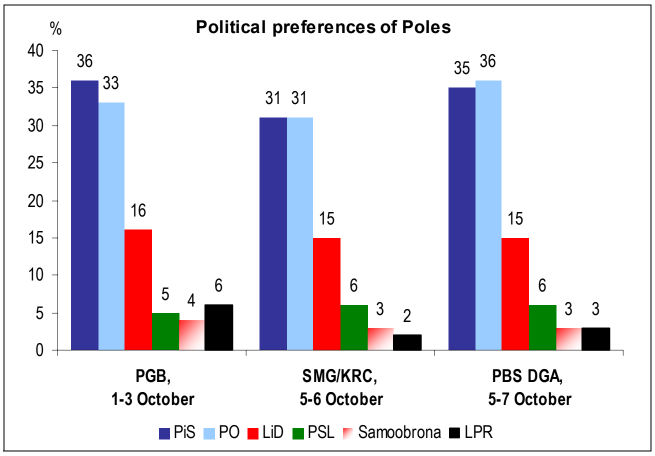
▪ However, the Council as a whole has not become more dovish, as the change at the post of the NBP governor was offset by the change in restrictiveness of other MPC members. The most apparent difference, in terms of the index calculated by us took place in case of Andrzej Wojtyna, but Andrzej Sławiński and Jan Czekaj also became more hawkish (less dovish) relative to the Council as a whole.

Jan Czekaj in the spotlight

▪ After recent changes in relative restrictiveness of MPC members, centre of gravity in the Council has shifted. As Wojtyna and Sławiński, especially the former one, approached the hawkish camp, now the key voter is Czekaj. Given this year's voting results, he was the MPC member who determined that there was no hike in March, but then there were two hikes of 25bps in April and June. That's why our view regarding scale of monetary tightening in 12M horizon is consistent with our belief what is his preferred interest rate level in such period.

Source: CSO, NBP, Reuters, own calculations

Government and politics



Election campaign at the last straight

▪ Two weeks before the parliamentary elections their result and the shape of the new political area after their completion are a great unknown.

▪ The pool's result indicate the biggest support for PO and PiS, leaving other parties far behind. However the distance between the two leaders and the winning position changes from one poll to another. It's worth remembering that the election results two years ago differed significantly from the earlier polls.

▪ Financial market expects the election results with calm and it doesn't seem that it can worsen the investor's attitude in the short term. Moreover it can last many weeks till we will know more about new government and its economic policy.

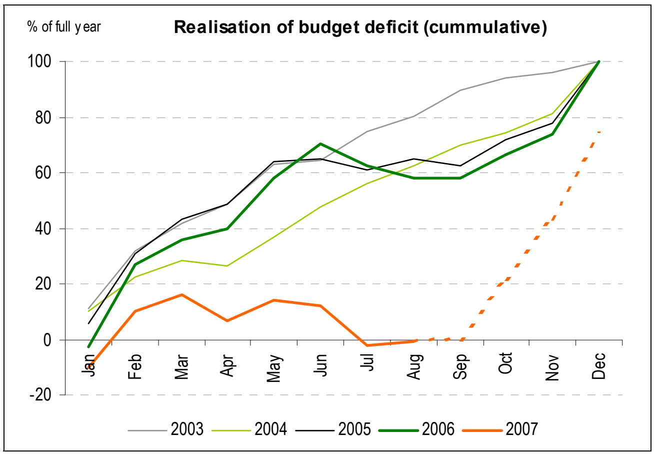
Main parameters of the 2008 budget

	3rd version	2nd version	1st version
Deficit (PLNbn)	28.6	28.1	30.0
Expenditures (PLNbn)	310.4	275.1	271.6
Revenues (PLNbn)	281.8	247.0	241.6
GDP growth (%)	5.5	5.5	5.7
Domestic demand (%)	7.2	7.2	6.8
Gross accumulation (%)	13.9	13.9	13.4
CPI (average, %)	2.3	2.3	2.3
Average gross wage (%)	5.9	5.9	6.0
Average employment (%)	2.0	2.0	2.3
USDPLN (average)	2.77	2.77	2.77
EURPLN (average)	3.74	3.74	3.74
Current account deficit (% PKB)	5.2	above 5	4.7
NBP reference rate (average, %)	5.2	5.2	4.7

Another change in the 2008 budget

▪ Despite hopes of the Ministry of Finance, the Senate did not lower family allowances. Although loss in revenues due to this fact was estimated at a few billion zlotys, it concerns to a large extent local governments. Thus, the central budget's loss does not equal the whole cost of family allowances. Moreover, the ministry assumed higher revenues from dividends. Thus, central budget deficit was increased only by PLN0.5bn. Levels of total revenues and spending were increased by the same amount in order to take into account flows of funds from the EU.

▪ Possibly, the 2008 budget will be amended once more. Civic Platform officials suggested that in case the party wins elections there may be changes in the budget aimed at reducing he deficit. They also suggested imposing some kind of a spending anchor instead of a limit on the nominal deficit as it is now.

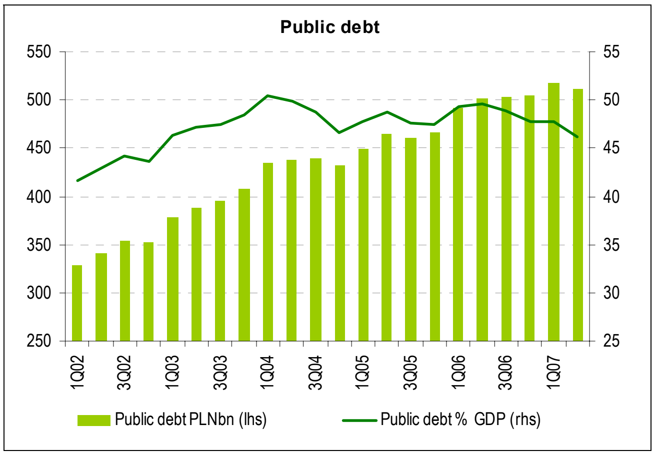


Budget results keep surprising

▪ According to The Ministry of Finance, after eight months of this year the state budget recorded a surplus of PLN275m. The expenditures were at 60.7% of the amount planned for this year and the incomes made 68.7% of whole year's plan.

▪ Latest comments of Ministry's officials suggest that after September there was a surplus in the budget again, yet only slightly lower (about PLN160m).

▪ According to the deputy finance minister Elżbieta Suchocka-Rogulska it is an effect of accumulating amount of due payments, however the delayed spending should be used until the end of year, so in the last quarter there will be acceleration in budget spending. The predicted deficit realisation in December is still at the level of PLN22-23bn (against plan at PLN30bn).



Public debt stabilizing

▪ Excellent budgets results are the effect not only of some delays in the expenditures but also of very good economic results that caused high tax incomes.

▪ As a result, the increase in the public sector debt has halted in recent quarters. At the end of June, the public debt reached PLN511bn, decreasing by about 1% in comparison to the end of the first quarter.

▪ The public debt in relation to GDP has been systematically declining since the beginning of 2006, because along with nominal debt level stabilization, there was rapid growth of nominal GDP.

▪ The relation of debt to GDP (without government's guarantees) decreased to 46.1% in June, the lowest level since 2002.

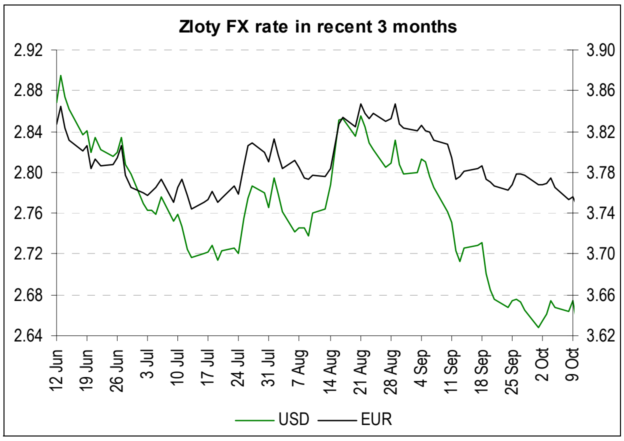
Source: BZWBK, Ministry of Finance, opinion polls

Market monitor

Zloty stronger in September

▪ After August weakening of the zloty we expected appreciation in September and such scenario fulfilled. The domestic currency strengthened against the euro as well as the dollar, which resulted among others from weakening greenback in the international markets on expectations of monetary policy easing in the US. Fed cut rates more than expected, which supported the risk appetite, and the EURPLN rate stabilised in range of 3.76-3.78. In the last days zloty broke the lower end of this range.

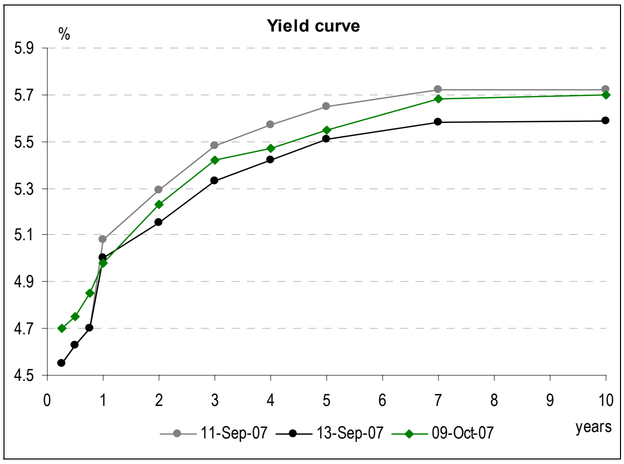
▪ In our view the zloty rate may stabilise near the currently traded levels, while the average zloty rate against the euro and the dollar in October will be lower than in September. This will be a consequence of lower risk aversion and expectations of rate cuts in the US. Possible slight dollar recovery may pose some risk, while election results might have positive effect for the zloty.



A slight gain in the fixed income market

▪ A positive effect of the August low inflation, which resulted in a deep fall in market interest rates, was only partly balanced by strong data from the labour market. The Fed's decision on interest rates temporarily supported Polish debt market, however, later on rates started rising again, while the spread against the core markets was narrowing. The negative tone of the recently released inflation forecast of the MinFin was balanced by little "hawkish" comments of the Council members. In the result yields declined since the release of our last report.

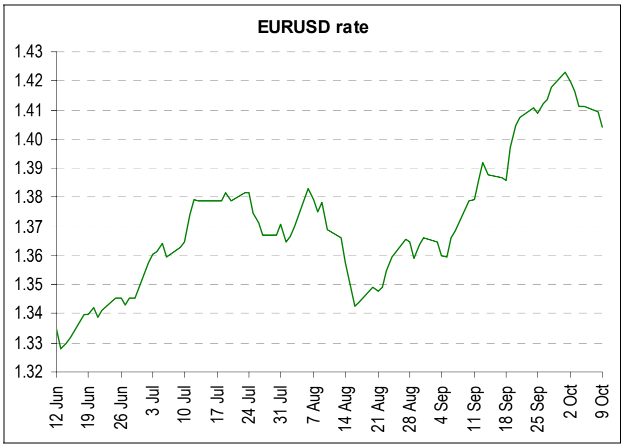
▪ Next comments of the MPC members may support the bond market, similar as inflation staying in our view at low level. Weaker data from the US and EMU may be also positive for the market, while the strong data from the domestic labour market may have a negative effect. In our view rates will be raised in November, and two more hikes will follow next year.



Significant fall of dollar in reaction to Fed rate cut

▪ After the decision of the US central bank to cut interest rates the dollar weakened strongly in reaction to further narrowing of interest rate disparity between the US and the euro zone. From day to day EURUSD rate was reaching new record high levels and when it increased above 1.42 investors started realizing their profits. Technical correction occurred and dollar recovered, which was also connected with approaching G7 meeting amid often-repeated comments about the strength of the single currency. The dollar was also supported by better than expected data from the US labour market and their revision for the previous months.

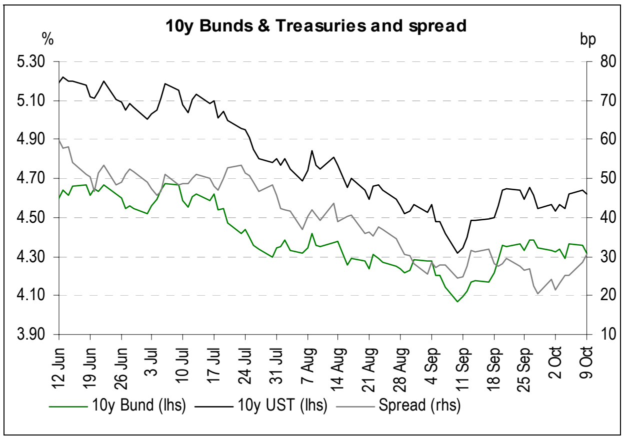
▪ We expect the dollar to stay at weak levels against euro till the end of the year on expected further interest rates cuts in the US and stable rates in the euro zone till next year's June.



Strong steepening of the US yields curve

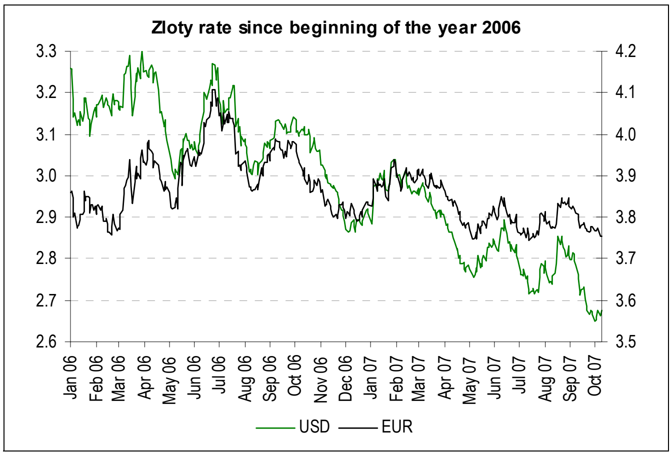
▪ Fed's decision about bigger than expected rate cut caused an increase of the inflationary concerns in the US and strong curve steepening, that was followed by German Bunds price changes, despite declining expectations for the next rate hikes. After a slight recovery yields increased again in reaction to positive data from the US labour market. The 10-year T-bonds yields rose by the middle of September from 4.34% to 4.64% and 10-year Bunds from 4.10% by 4.36%.

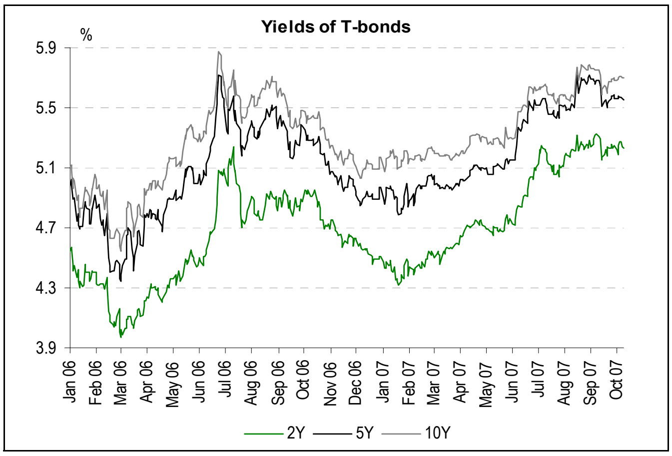
▪ In our opinion Fed will cut the interest rates one more time this year, and next one will follow in the 1Q07. We forecast that ECB will not increase rates this year and the next rises can take place in 2008. The 10-year yields may stay at higher level because of the inflation threats and on expectations of rate hikes after stabilisation of the situation in the US.

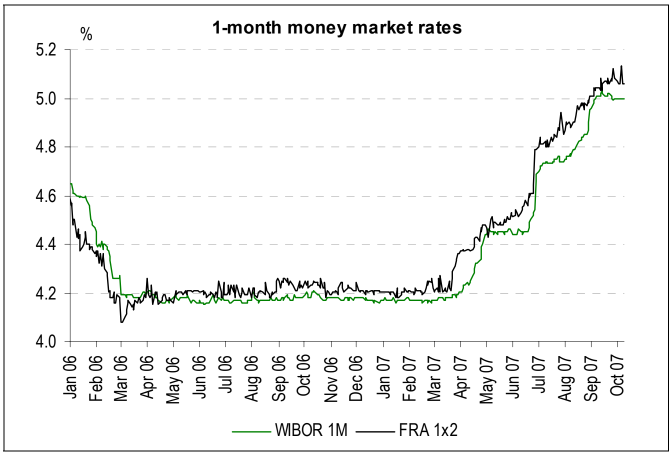


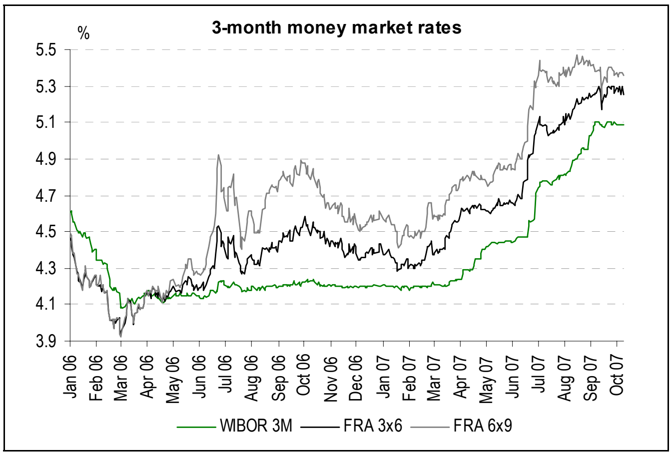
Source: Reuters, BZ WBK

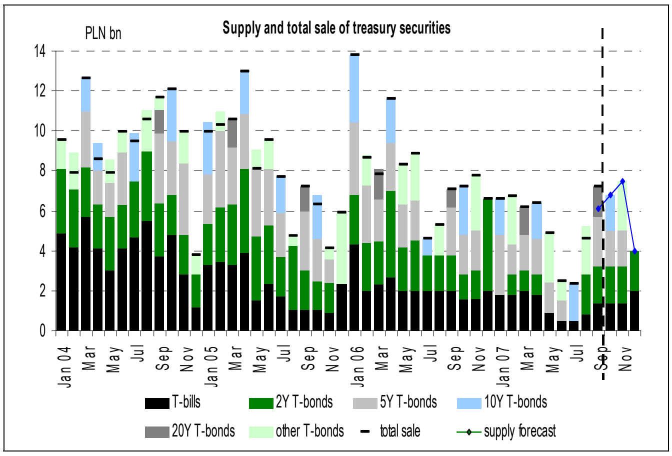
Market monitor











Treasury bill auctions (PLN m)

Date of auction	OFFER / SALE 52-week	Total
06.08.2007	800 / 800	800 / 800
20.08.2007	-	-
Total August	**800 / 800**	**800 / 800**
03.09.2007	900 / 900	900 / 900
17.09.2007	500 / 500	500 / 500
Total September	**1 400 / 1 400**	**1 400 / 1 400**
03.10.2007	500 / 500	500 / 500
17.08.2007	500- 1 000	500- 1 000
Total October*	**1 000 – 1 500**	**1 000 – 1 500**

* estimations based on Ministry of Finance preliminary information

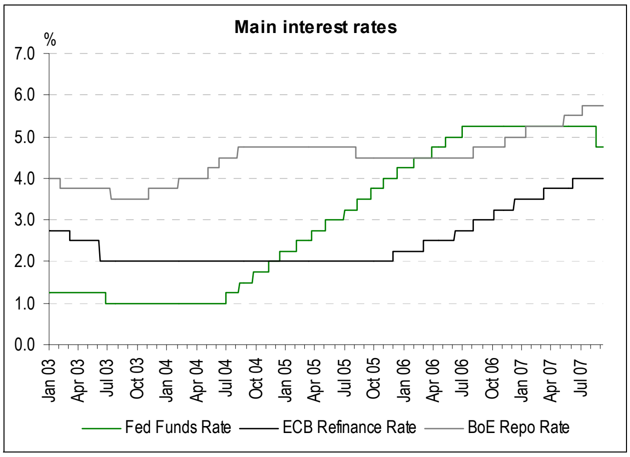
Treasury bond auctions in 2007 (PLN m)

month	First auction				Second auction				Third auction			
	date	T-bonds	offer	sale	date	T-bonds	offer	sale	date	T-bonds	offer	sale
January	-	-	-	-	10.01	DS1017	1 800	1 800	17.01	PS0412	3 000	3 000
February	07.02	OK0709	1 000	1 000	14.02	WZ0118 | IZ0816	2400 | 0	2400 | 0	21.02	PS0412	1 500	1 500
March	07.03	OK0709	1 000	1 000	14.03	WS0922	1 400	1 400	21.03	PS0412	1 800	1 800
April	04.04	OK0709	1 000	1 000	11.04	DS1017	1 800	1 800	18.04	PS0412	1 800	1 800
May	-	-	-	-	09.05	WZ0118 | IZ0816	2000 | 500	2000 | 498	16.05	PS0412	1 500	1 500
June	06.06	-	-	-	13.06	WS0437	1 000	1 000	20.06	PS0412	1 000	1 002
July	04.07	-	-	-	11.07	DS1017	1 800	1 800	-	-	-	-
August	01.08	OK0709	2 000	1 400	08.08	WZ0118 | IZ0816	2 400 | 0	2 400 | 0	-	-	-	-
September	05.09	OK0709	1 800	1 800	12.09	WS0922	1 500	1 500	19.09	PS0412	2 500	2 500
October	03.10	OK0709	1 800	1 800	10.10	DS1017	1 800	-	17.10	PS0412	1 500- 2 500	-
November	07.11	2L	-	-	14.11	10L WIBOR | 12L CPI	-	-	21.11	5L	-	-
December	05.12	2L	-	-	-	-	-	-	-	5L	-	-

* with supplementary auction

Source: Ministry of Finance, Reuters, BZ WBK

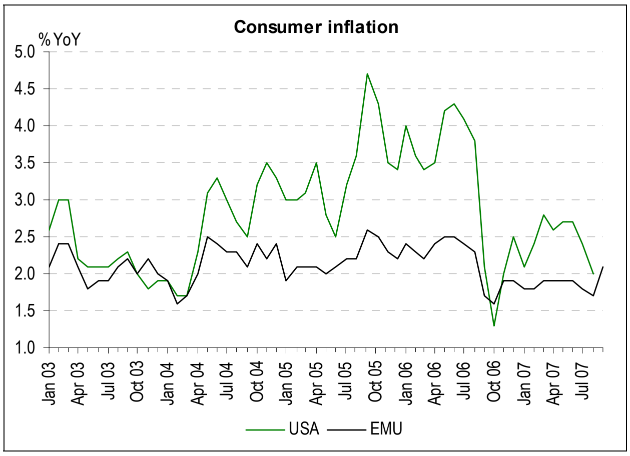
International review



Fed baldly cuts rates, another ECB pause

▪ Fed cut rates by 50 bps, which was a deeper move than the market expected. It was justified in the official communiqué that the decision was taken to mitigate the adverse effects for the real economy sector, that should appear as the result of disruptions on the financial markets and to sustain the moderate economic growth. At the same time the bank noted that some risk for inflation remained.

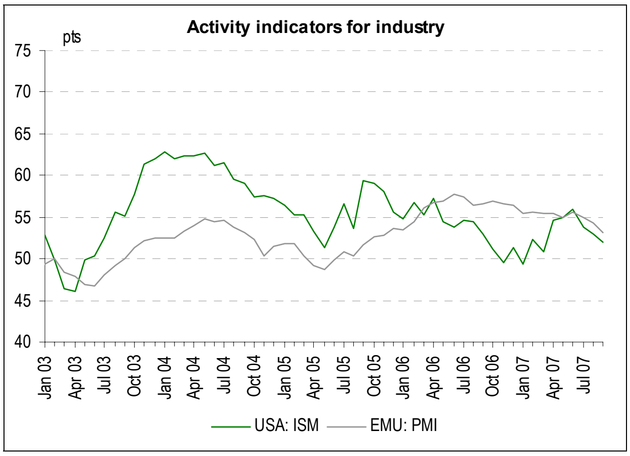
▪ ECB left main interest rate at the level of 4.0% and resigned from saying that the monetary policy in EMU stayed on the accommodative side. Bank kept the opinion that the main concern is a care for the price stability, however there are more data needed before taking another decision changing rates amid upside risks to inflation and downside risks for economic growth. ECB's president added that some moves helping financial markets in normal functioning are needed.



Inflation still outside Fed's comfort zone

▪ Released data about US inflation in August showed a decline in CPI by 0.1%MoM against expected no change, on falling oil prices. Core inflation increase was in line with the forecasts and reached 0.2%MoM. In annual terms indices fell to 2.0% and 2.1% respectively. The core PCE index rose in September by 0.1%MoM below the market consensus and in annual terms it declined to 1.8%. PPI in August decreased by 1.4%MoM (+2.2%YoY) against expected fall by 0.2%MoM, mainly because of food and energy prices. Core PPI index increased by 0.2%MoM (2.2%YoY) against expectations of 0.1%MoM.

▪ HICP inflation in the euro zone in August was at 1.7%YoY, while in September it accelerated according to Eurostat estimates to 2.1%YoY as a result of higher oil prices. It was above the ECB's target level for the first time in 13 months.

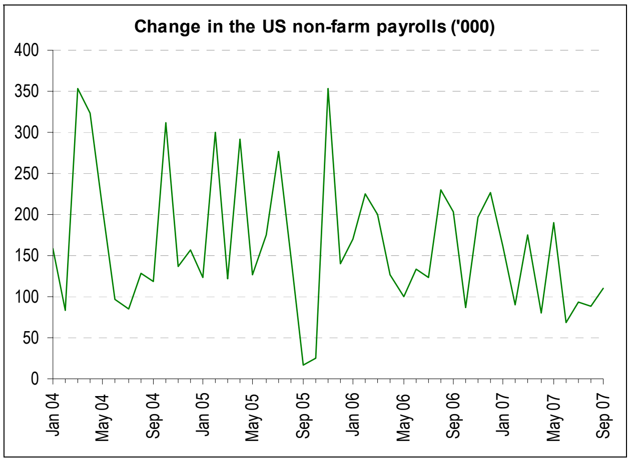


Activity indices slightly lower

▪ ISM index for the US industry sector fell in September to 52.0 points from 52.9 in August, what was slightly below the market expectations, although there was an increase in employment index. The economic activity in the US services sector reflected in the ISM index rose in September, although a little weaker than in August and as compared with expectations. ISM index reached 54.8 points amid the increase in employment and price index that balanced the negative effects of the headline index decline.

▪ The euro zone manufacturing PMI index reached in September 53.2 pts (the lowest level in 2 years) against 54.3 pts in the previous month. The PMI index for the services sector in the euro zone fell in September to slightly smaller extent than was expected, to 54.2 pts from 58.0 pts in August, though it was still the largest fall in monthly terms in the last 9 months (the deepest decline of German index). This was influenced by a moment of the economic cycle, tightening of conditions in the credit markets as well as strong euro.

▪ According to final data GDP for Q2 in the US increased by 3.8% (against 4.0% according to previous estimates and forecast 3.9%) The revision concerned first of all net export. Import seemed higher than expected.



Source: Reuters, ECB, Federal Reserve

Decrease in employment for the first time in 4 years

▪ Non-farm employment data showed an increase by 110,000 against expected 100,000 however data for the previous 2 months were upwardly revised, for August from a decline by 4,000 to rise by 89,000 and in July from 83,000 to 93,000. Unemployment rate in September reached 4.7% against 4.6% in August, which was in line with market analytics expectations.

▪ Weak August data and revision for the past 2 months were the arguments that enabled Fed significant rate cut. Better data slightly improved the market moods on the US economy.

Economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
8 October ***PL: Treasury bills auction*** US: Market holiday	**9** US" FOMC protocol	**10** ***PL: Auction of 10Y bonds*** US: Wholesales inventories (Aug)	**11** EMU: GDP (2Q) US: Import prices (Sep) US: Trade balance (Aug)	**12** ***PL: Money supply (Sep)*** US: PPI (Sep) US: Retail sales (Sep) US: Preliminary Michigan (Oct)
15 ***PL: CPI (Sep)*** ***PL: Wages and Employment (Sep)*** ***POL: Balance of payments (Aug)*** US: NY Fed index (Oct)	**16** GER: ZEW Index (Oct) EMU: Final HICP (Sep) US: Net capital flows (Aug) US: Capacity utilization (Sep) US: Industrial output (Sep)	**17** ***PL: Auction of 5Y bonds*** US: CPI (Sep) US: Home sales (Sep)	**18** ***PL: Industrial Output (Sep)*** ***PL: PPI (Sep)*** US: Philadelphia Fed index (Sep) US: New jobless claims	**19**
22 ***PL: Treasury bills auction*** ***PL: Core inflation (Aug)***	**23** ***PL: Business climate (Oct)*** ***PL: Retail sales (Sep)*** ***PL: Unemployment (Sep)***	**24** ***PL: Switch auction*** EMU: NTC Manufacturing PMI (Oct) EMU: NTC Services PMI (Oct) US: Home sales (Sep)	**25** ***PL: MPC's minutes*** GER: Ifo Index (Sep) US: Durable goods (Sep) US: New jobless claims US: New homes sales (Sep)	**26** EMU: M3 money supply (Oct) US: Final Michigan (Oct)
29	**30** ***PL: MPC meeting*** US: Consumer confidence (Oct)	**31** ***PL: MPC meeting – decision*** JP: BOJ meeting – report after decision EMU: Economic sentiment (Oct) EMU: Preliminary HICP (Oct) US: Preliminary GDP (Q3) US: Core PCE (Q3) US: GDP deflator (Q3) US: ADP report (Oct) US: Chicago PMI (Oct) US: Fed meeting – decision	**1 November** ***PL: All Saints' Day*** US: Core PCE (Sep) US: New jobless claims US: Manufacturing ISM (Oct) US: Pending home sales (Sep)	**2** EMU: Manufacturing ISM (Oct) US: Non-farm payrolls (Oct) US: Unemployment (Oct) US Factory orders (Sep)
5 ***POL: Treasury bills auction*** US: Non-manufacturing ISM (Oct)	**6** EMU: Non-manufacturing PMI (Oct) EMU: Retail Sales (Sep)	**7** ***POL: Auction of 2Y bonds*** US: Unit labour costs & productivity (Q3) US: Wholesales inventories (Sep)	**8** GB: BoE meeting – decision EMU: ECB meeting - decision US: New jobless claims	**9** US: Import prices (Oct) US: Trade balance (Sep) US: Preliminary Michigan (Nov)

Source: CSO, NBP, Finance Ministry, Reuters

MPC meetings and data release calendar for 2007

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
MPC meeting	30-31	27-28	27-28	24-25	29-30	26-27	24-25	28-29	25-26	30-31	27-28	18-19
MPC minutes	-	-	-	-	24	21	19	23	20	25	22	13
GDP*	-	-	2	-	31	-	-	30	-	-	30	-
CPI	15	15[a]	14[b]	13	15	13	13	14	13	15	14	13
Core inflation	22		23[b]	23	23	22	23	23	24	22	23	21
PPI	19	19	19	20	21	20	19	20	19	18	20	19
Industrial output	19	19	19	20	21	20	19	20	19	18	20	19
Retail sales	29	23	23	25	25	26	24	24	25	23	-	-
Gross wages, employment	16	15	15	17	17	19	16	16	17	15	16	17
Unemployment	29	23	23	25	25	26	24	24	25	23	-	-
Foreign trade	about 50 working days after reported period											
Balance of payments*	2	-	30	-	-	29	-	-	28	-	-	-
Balance of payments	16[c]	12	14	13	18	15	13	13	12	15	13	12
Money supply	12	14	14	13	14	14	13	14	14	12	14	14
NBP balance sheet	5	7	7	6	7	6	6	7	7	5	7	7
Business climate indices	23	22	22	23	23	22	23	23	24	23	23	21

* quarterly data, [a] preliminary data, January, [b] January and February, [c] November 2006, [d] January, [e] February

Source: CSO, NBP

Economic data and forecasts

Monthly economic indicators

		Sep 06	Oct 06	Nov 06	Dec 06	Jan 07	Feb 07	Mar 07	Apr 07	May 07	Jun 07	Jul 07	Aug 07	Sep 07	Oct 07
Industrial production	%YoY	11.6	14.8	12.0	5.9	15.4	13.0	11.3	12.6	8.1	5.6	10.4	9.0	4.2	9.1
Retail sales [c]	%YoY	14.5	13.3	13.6	13.3	16.5	17.5	19.2	15.1	14.8	16.2	17.1	17.4	14.5	17.2
Unemployment rate	%	15.2	14.9	14.8	14.9	15.1	14.9	14.4	13.7	13.0	12.4	12.2	12.0	11.7	11.5
Gross wages [b,c]	%YoY	5.1	4.7	3.1	8.5	7.8	6.4	9.1	8.4	8.9	9.3	9.3	10.5	10.6	10.3
Employment [b]	%YoY	3.5	3.6	3.8	4.1	3.8	4.3	4.5	4.4	4.4	4.6	4.7	4.8	4.9	4.9
Export (€) [d]	%YoY	16.9	23.8	21.7	10.2	15.4	13.8	15.0	16.8	9.8	10.7	17.4	13.6	10.3	9.3
Import (€) [d]	%YoY	19.9	29.3	22.6	18.2	19.6	12.2	18.5	23.8	12.9	16.6	23.3	18.4	14.3	15.5
Trade balance [d]	EURm	-399	-404	-499	-996	-542	-141	-757	-781	-1030	-786	-1278	-967	-795	-1038
Current account balance [d]	EURm	-25	-906	-993	-1290	-881	-545	-681	-740	-1524	-1343	-1300	-977	-545	-973
Current account balance [d]	% GDP	-2.6	-2.8	-3.0	-3.2	-3.4	-3.2	-3.2	-3.2	-3.4	-3.7	-3.8	-3.8	-4.0	-4.0
Budget deficit (cumulative)	PLNbn	-14.5	-16.6	-18.5	-25.1	3.1	-3.0	-4.8	-2.1	-4.3	-3.7	0.6	0.3	0.1	-6.4
Budget deficit (cumulative) [e]	% of FY plan	57.8	66.3	73.9	100.0	-10.3	10.1	16.1	6.9	14.2	12.3	-2.1	-0.9	-0.4	21.3
CPI	%YoY	1.6	1.2	1.4	1.4	1.6	1.9	2.5	2.3	2.3	2.6	2.3	1.5	1.8	2.1
PPI	%YoY	3.6	3.2	2.5	2.6	3.1	3.5	3.3	2.2	2.1	1.7	1.5	1.7	1.9	2.4
Broad money (M3)	%YoY	13.4	12.8	14.6	16.0	19.3	18.0	18.0	17.8	16.0	14.7	15.6	15.6	15.0	15.7
Deposits	%YoY	12.1	11.8	13.4	15.2	18.5	18.3	17.7	18.2	16.4	15.2	15.9	15.6	14.7	14.6
Loans	%YoY	19.2	19.5	20.7	23.4	25.0	26.5	26.8	28.4	28.6	29.2	31.4	31.1	30.3	30.0
USD/PLN	PLN	3.12	3.09	2.97	2.88	2.98	2.98	2.94	2.83	2.80	2.84	2.75	2.80	2.73	2.67
EUR/PLN	PLN	3.97	3.90	3.82	3.81	3.88	3.90	3.89	3.82	3.78	3.81	3.77	3.81	3.79	3.76
Reference rate [a]	%	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.25	4.25	4.50	4.50	4.75	4.75	4.75
Lombard rate [a]	%	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.75	5.75	6.00	6.00	6.25	6.25	6.25
WIBOR 3M	%	4.21	4.22	4.20	4.20	4.20	4.20	4.22	4.32	4.44	4.52	4.78	4.80	5.09	5.05
Yield on 52-week T-bills	%	4.44	4.35	4.29	4.20	4.14	4.07	4.23	4.36	4.43	4.42	4.70	4.80	5.01	5.00
Yield on 2-year T-bonds	%	4.87	4.84	4.65	4.54	4.41	4.46	4.55	4.71	4.70	4.93	5.14	5.23	5.25	5.25
Yield on 5-year T-bonds	%	5.31	5.24	5.01	4.91	4.90	4.97	4.98	5.07	5.11	5.40	5.50	5.61	5.60	5.60
Yield on 10-year T-bonds	%	5.48	5.39	5.18	5.10	5.16	5.18	5.18	5.27	5.28	5.52	5.60	5.68	5.69	5.70

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates

[a] at the end of period [b] in corporate sector [c] in nominal terms [d] balance of payments data on transaction basis [e] 2006 - % of Dec, 2007 - % of plan

Quarterly and annual economic indicators

		2005	2006	2007	2008	1Q06	2Q06	3Q06	4Q06	1Q07	2Q07	3Q07	4Q07
GDP	PLNbn	983.3	1 060.2	1 155.5	1 248.9	242.4	253.9	261.4	300.1	267.1	279.6	282.8	326.1
GDP	%YoY	3.6	6.2	6.5	5.5	5.5	6.0	6.3	6.6	7.4	6.7	6.1	6.1
Domestic demand	%YoY	2.4	7.3	8.0	7.2	5.3	5.4	6.9	8.6	8.6	9.3	7.1	7.2
Private consumption	%YoY	2.0	4.8	5.7	5.9	5.4	4.8	5.6	5.1	6.9	5.1	5.4	5.4
Fixed investments	%YoY	6.5	15.6	19.0	14.0	7.6	14.5	19.3	19.3	29.6	22.3	16.0	15.5
Industrial production	%YoY	4.0	12.5	9.6	8.7	12.4	12.1	12.3	10.8	13.0	8.5	7.9	8.9
Retail sales (real terms)	%YoY	1.5	11.9	15.2	14.9	9.0	11.8	13.8	12.6	17.4	14.1	14.7	14.4
Unemployment rate [a]	%	17.6	14.9	11.5	8.5	17.8	16.0	15.2	14.9	14.4	12.4	11.7	11.5
Gross wages (real terms) [c]	%YoY	1.2	4.2	6.9	6.0	4.3	3.9	4.1	4.5	5.9	6.5	8.1	7.4
Employment [c]	%YoY	1.9	3.2	4.6	4.0	2.6	3.0	3.4	3.8	4.2	4.5	4.8	4.7
Export (€) [b]	%YoY	17.8	20.4	12.5	13.0	23.4	20.1	19.8	18.8	14.7	12.3	13.6	9.7
Import (€) [b]	%YoY	13.4	24.0	17.0	17.3	26.2	22.5	24.0	23.4	16.8	17.5	18.5	15.5
Trade balance [b]	EURm	-2 242	-5 536	-10 759	-17 107	-845	-1 199	-1 599	-1 893	-1 440	-2 594	-3 040	-3 685
Current account balance [b]	EURm	-3 866	-8 787	-12 181	-18 529	-1 972	-2 025	-1 602	-3 188	-2 104	-3 610	-2 822	-3 645
Current account balance [b]	% GDP	-1.6	-3.2	-4.0	-5.5	-2.0	-2.5	-2.6	-3.2	-3.2	-3.7	-4.0	-4.0
Budget deficit (cumulative) [a]	PLNbn	-28.6	-25.1	-21.9	-28.0	-9.0	-17.7	-14.5	-25.1	-4.8	-3.7	0.1	-21.9
Budget deficit (cumulative) [a]	% GDP	-2.9	-2.4	-1.9	-2.2	-	-	-	-	-	-	-	-
CPI	%YoY	2.1	1.0	2.2	2.6	0.6	0.8	1.4	1.3	2.0	2.4	1.9	2.4
CPI [a]	%YoY	0.7	1.4	2.7	2.6	0.4	0.8	1.6	1.4	2.5	2.6	1.8	2.7
PPI	%YoY	0.7	2.5	2.5	2.8	0.9	3.0	3.6	2.6	3.3	2.0	1.7	3.1
Broad money (M3) [a]	%YoY	13.1	16.0	12.8	11.9	10.9	12.2	13.4	16.0	18.0	14.7	15.0	12.8
Deposits [a]	%YoY	12.6	15.2	10.5	9.9	10.3	11.9	12.1	15.2	17.7	15.2	14.7	10.5
Loans [a]	%YoY	13.3	23.4	29.6	23.1	13.6	16.0	19.2	23.4	26.8	29.2	30.3	29.6
USD/PLN	PLN	3.23	3.10	2.80	2.67	3.19	3.14	3.10	2.98	2.97	2.82	2.76	2.65
EUR/PLN	PLN	4.02	3.90	3.80	3.68	3.83	3.95	3.96	3.85	3.89	3.80	3.79	3.74
Reference rate [a]	%	4.50	4.00	5.00	5.50	4.00	4.00	4.00	4.00	4.00	4.50	4.75	5.00
Lombard rate [a]	%	6.00	5.50	6.50	7.00	5.50	5.50	5.50	5.50	5.50	6.00	6.25	6.50
WIBOR 3M	%	5.29	4.21	4.65	5.56	4.29	4.15	4.20	4.20	4.20	4.42	4.89	5.07
Yield on 52-week T-bills	%	4.92	4.18	4.62	5.40	4.02	4.06	4.37	4.28	4.14	4.40	4.84	5.10
Yield on 2-year T-bonds	%	5.04	4.57	4.95	5.40	4.23	4.49	4.89	4.67	4.47	4.78	5.21	5.33
Yield on 5-year T-bonds	%	5.25	5.03	5.35	5.70	4.67	5.04	5.36	5.05	4.95	5.19	5.57	5.68
Yield on 10-year T-bonds	%	5.24	5.22	5.48	5.90	4.83	5.27	5.55	5.22	5.17	5.36	5.66	5.75

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates

[a] at the end of period; [b] balance of payments data on transaction basis [c] in corporate sector

This analysis is based on information available until 09.10.2007 has been prepared by:

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