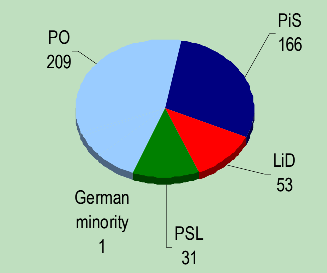
Bank Zachodni WBK

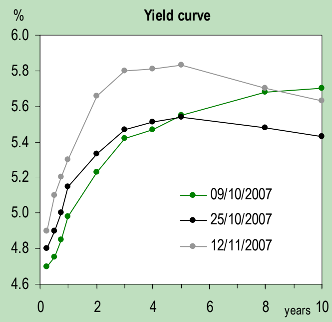
MACROscope

Polish Economy and Financial Markets

November 2007

Distribution of seats in the Sejm after election





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Change in landscape

- **Since the publication of our previous report, there has been significant change in political landscape that impacted the financial market, and primarily consisted in the zloty appreciation and yield curve inversion.** It seems that the financial market has high hopes for the new government, reforms, reduction in the budget deficit, swift entry to the eurozone. In our opinion, however, the first statements made by politicians do not justify this enthusiasm. While indeed there is a chance for some changes on the supply side of the economy (streamlined laws, deregulation etc.), there is a question mark around the reduction of direct taxes or tax wedge (even in the form adopted by the previous parliament) or reduction of deficit in a little worse economic conditions, while the entry to the eurozone is announced to happen in the years 2012-13 (like in the case of the previous government). This is why there is a question whether the market euphoria will be sustainable. It seems to us that both domestic factors and global factors (lower risk appetite) may shortly cause zloty adjustment and yields increase, especially at the short end of the yield curve that will be impacted by the liquidity situation and change in the inflation path in the following months to grow the risk of more interest rate hikes. Long-term bonds will still be influenced by the convergence play, although, it should be noted that while financial markets tend to believe the Civic Platform rather than the Law and Justice in terms of the delivery of the scenario of joining the eurozone within 5 years, there may be some obstacles on the way to delivering this objective (apart from the need to meet the required criteria). These are talks with the coalition partner, the NBP (report on benefits and costs is to be published as late as towards the end of 2008) and the European Union's side. The candidate for the position of the ministry of finance is remembered as a supporter of swift entry to the eurozone, however, it is not obvious whether the political limitations will allow him to achieve this scenario.

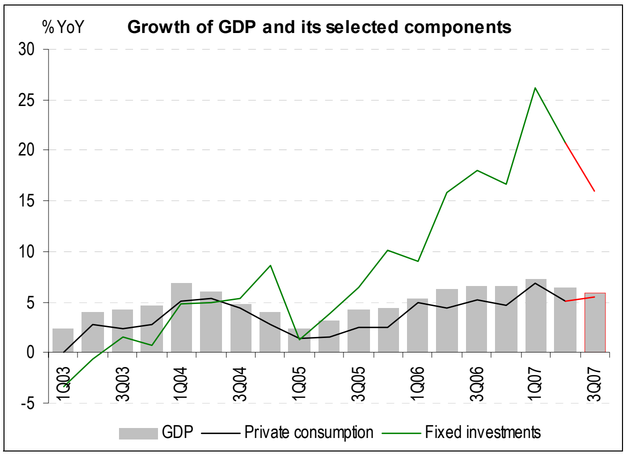
- **While the landscape in the real economy remains the same (expected economic slowdown in Q3), it has changed for short term inflation prospects.** After the positive August surprise, the inflation grew considerably in September, and in addition, the Ministry of Finance published a pessimistic forecast for October. This means that in the upcoming months the inflation may exceed the upper end of the fluctuation band around the inflation target. A month ago, market participants supported by statements made by the Monetary Policy Council were thinking whether interest rates would grow only to 5.25%, while now the scenario of the growth to 6% is being considered. Like a month ago, we are of the opinion that after the November hike, the Council will still make two hikes early in the next year and this will put an end to the hike cycle. This will be caused by reduction in economic growth indicators, stabilisation on the labour market, drop in inflation from Q2 and change in the policy pursued by the world's key central banks (lower restrictiveness).

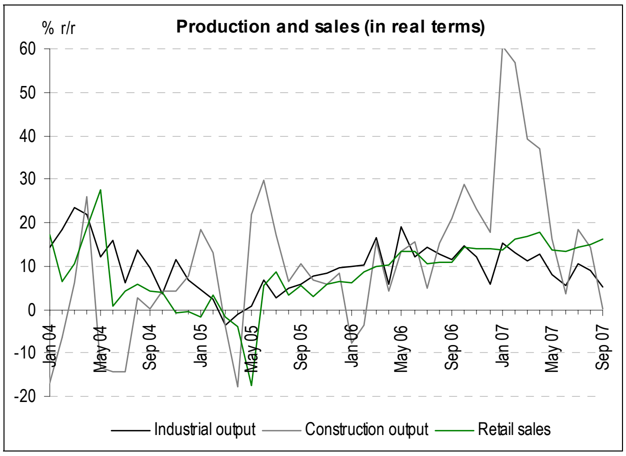
Financial market on 31 October 2007:

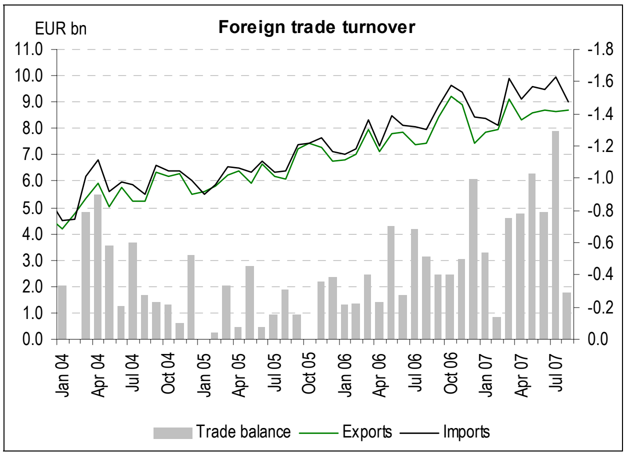
NBP deposit rate	3.25	WIBOR 3M	5.21	USDPLN	2.5155
NBP reference rate	4.75	Yield on 2-year T-bonds	5.39	EURPLN	3.6306
NBP lombard rate	6.25	Yield on 5-year T-bonds	5.61	EURUSD	1.4433

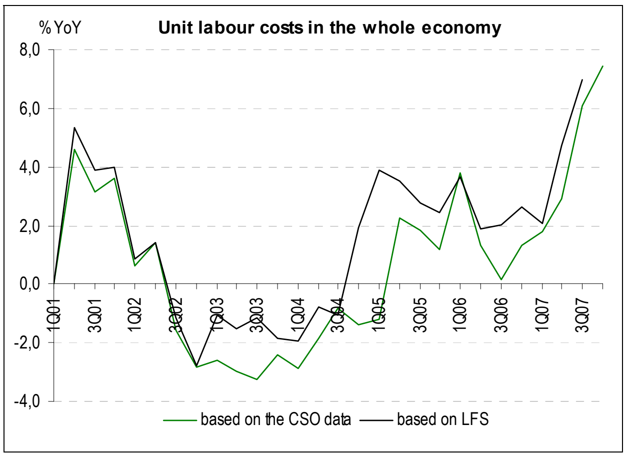
This report is based on information available until 12.11.2007

Economic update









Source: CSO, NBP, own calculations

Will GDP growth reach 6% in Q3?

- In September industrial production rose by 5.2%YoY and retail sales increased by 14.2%YoY. Retail sales growth in real terms amounted to 12.2%YoY, which was the lowest result this year.
- The picture in construction-assembly sector was even more pessimistic, as after several months of two-digit growth the production grew only by 0.2%YoY. Taking into account that September data were influenced by the lower number of working days, the seasonally adjusted indices of output growth were higher and amounted to 7.5%YoY and 5.0%YoY for the industry and construction, respectively.
- Based on the one month data it is hard to assess whether poor September's result was beginning of a trend, especially as far as construction is concerned (other signals from the economy rather do not confirm such scenario). However all monthly statistics on the real sphere of the economy were below market expectations for the second consecutive month. Although industrial output figure was above our forecast and retail sales growth was very close to our expectation, we decided to lower forecast of GDP growth for the third quarter to below 6%.
- Private consumption remains the main driver of economic growth and its role may even increase in the next couple of quarters. Sharp increase in food prices creates some risk factor, as disposable income may decrease in real terms in the short-term, for people with high propensity to consume.
- The CSO revised quarterly GDP data covering the period 1Q06-2Q07. Figures for 2006 have been revised up, but in the two quarters of 2007 economic growth has been lowered as compared to previous estimates by 0.2-0.3 pp. GDP growth rate is returning to the level close to potential growth. We maintain our forecast for 2008 at 5.5% (slightly below 6% in 2H07).

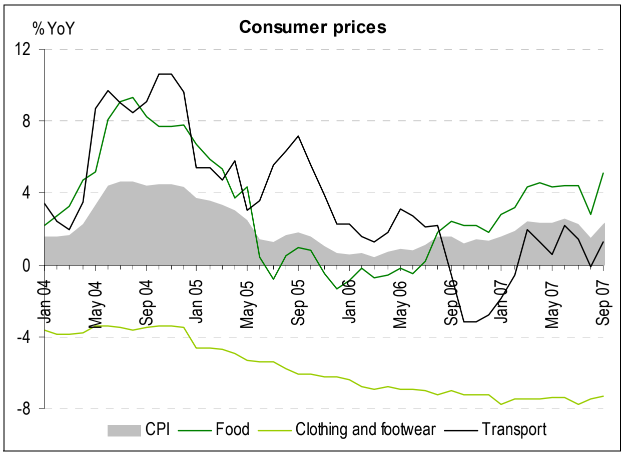
(Temporary?) improvement in external balance

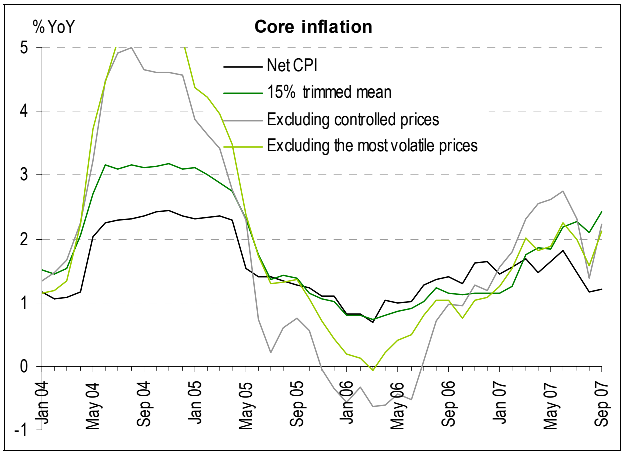
- Correction in quarterly national accounts was also visible in GDP growth breakdown. Changes were favourable from the point of view of net exports contribution (negative input down from 2.6 to 1.9 pp in 2Q07).
- August balance of payments data also brought a positive surprise. Fast exports growth (16.7%YoY) was accompanied by a slowdown in imports (12.8%YoY), which lowered the trade deficit to only €289m and C/A deficit to €637m.
- Monthly statistics are often revised and we do not change our view that current account deficit will deteriorate in the coming quarters to above 5% from below 4% currently.
- Positive factor in statistics for August was significant inflow of foreign direct investments, which exceeded €1bn again. At the same time outflow of portfolio capital amounted to almost €800m.

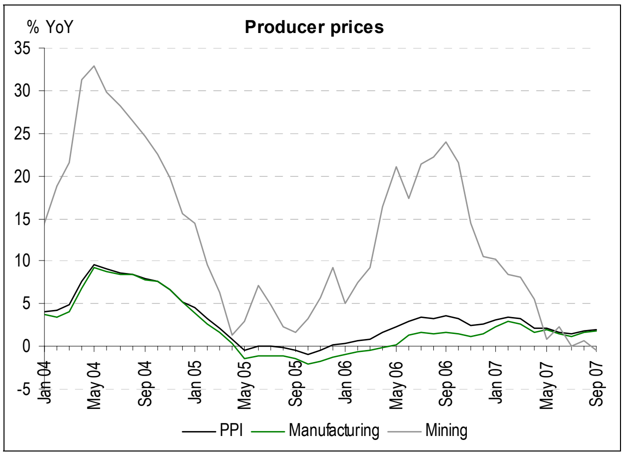
Unit labour costs accelerate further

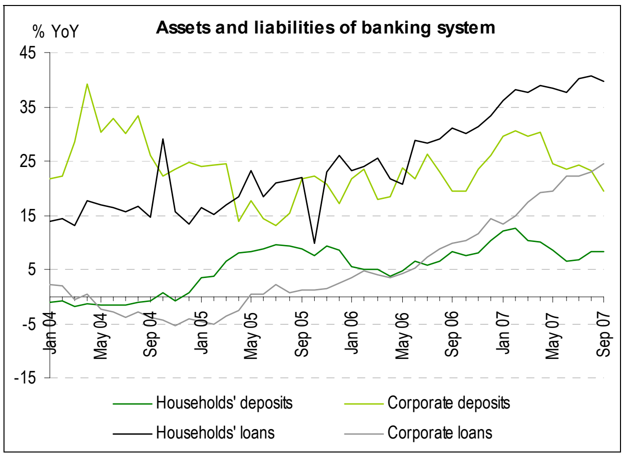
- In September the average wage growth in the corporate sector decelerated to 9.5%YoY and employment rise slowed down to 4.7%YoY (from 10.5%YoY and 4.8%YoY, respectively). The unemployment rate fell more than expected (to 11.6%).
- Wage bill in the corporate sector increased 14.7%YoY in nominal terms and 12.2% in real terms (from 15.8% and 14.1%).
- The data were below median of market forecasts, although they confirmed that the labour market conditions keep tightening. Wages in the whole economy increased by 9.7%YoY in Q3, which bodes well for consumption, but at the same time it means a rise in unit labour costs by 7.4%YoY (6.1% in Q2).
- On the other hand, lowering of average wage and employment growth rates may mean that labour market conditions will not tighten significantly in future.

Economic update









Source: CSO, NBP, own calculations

Sharp inflation increase, but not in case of net inflation

▪ After the positive inflation surprise in August, next month brought the opposite effect. Prices of consumer goods and services rose by 0.8%MoM in September, while 12M inflation rate increased to 2.3% (from 1.5%). The strong growth if food prices (2.4%MoM and 5.1%YoY) was the main factor, which contributed to inflation bounce-back. Tobacco products also rose at quite high rate (1.5%MoM). The prices of other goods and services changed in line with expectations and as a result the net inflation remained unchanged in September at the level of 1.2%YoY.

▪ While the previous comments of MPC members led to market's belief that next steps in monetary tightening process might be postponed, the September's inflation release restored concerns about more significant cumulative hikes. This was additionally fuelled by the Ministry of Finance's forecast of October's CPI inflation at the level of 3%.

▪ Though we think that CPI inflation was slightly lower in October (2.8%), latest information has changed the inflation path for the forthcoming months. According to our forecasts, inflation will reach 3.3% at the end of the year, above 3.5% in 1Q07 and above 3% on average in 2008. This will driven almost entirely by food and fuel prices development (the latter offset partly by strong zloty), as we see the net inflation not exceeding the level of 2% in this period.

▪ From the point of view of monetary policy the important questions are whether the shock on the food market is temporary and whether it may be reversed, and to what extent inflation increase creates a risk of second-round effects. In this context, the recent report on agriculture market prospects in the next 10 years prepared by OECD and FAO looks interesting. It shows that after a temporary increase prices may stabilise at higher level.

Producer prices in line with expectations

▪ In September PPI inflation increased 0.1%MoM, which was in line with our expectations. The annual growth rate of PPI was above our forecast (2.0% vs. 1.9%), which was related to the revision of data for the previous month by 0.1pp.

▪ The main factor responsible for producer price increase in September was, similarly as in previous months, growth in prices in manufacturing sector (prices up 0.1%MoM). It is noteworthy that this means a slowdown in pace of price growth in manufacturing (despite higher fuel and food prices), as they were rising 0.4%MoM on average in previous months of this year.

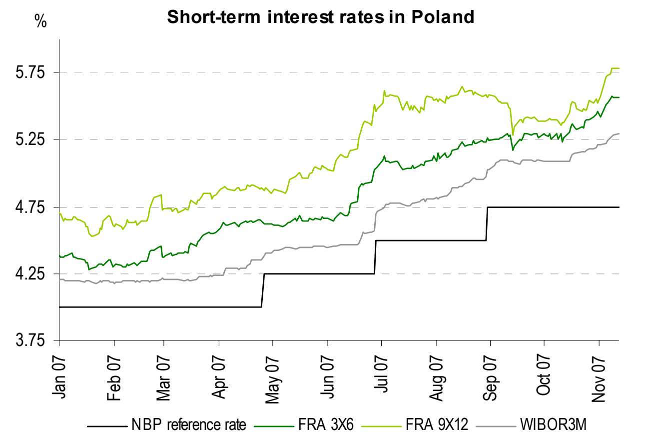
▪ Producer prices fell in the final quarter of last year (due to drop in oil prices), the effect of low statistical base will result in further acceleration of 12M PPI inflation in the remainder of this year. 12M PPI may reach 4% in December.

High credit growth maintains

▪ It seems that the scale of to-date interest rate increases and the risk of further tightening in monetary policy did not limit the demand for credit. Well, it hardly expected as regards cash loans, which show limited price elasticity, as well as in case of mortgage loans, which are to a large extent denominated in Swiss francs.

▪ In September loans rose by above 30%YoY. Households' credit growth shows a stabilisation at the level of ca. 40%YoY and there is visible acceleration in terms of credits for enterprises to 24.5%YoY from below 23% in August. The scale of increase in borrowing costs should not influence significantly economic growth in the upcoming quarters. However, we should remember that more restrictive monetary policy is accompanied by higher labour costs, higher commodities prices and stronger zloty.

Central bank watch



Selected fragments of MPC statement after October meeting
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 on food prices.

Inflation projections (% YoY)

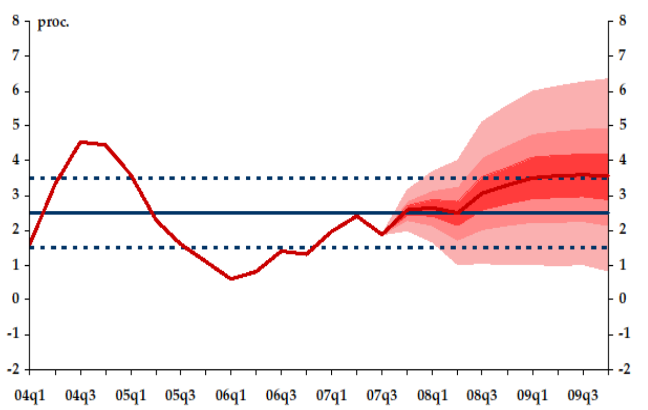
	Oct 06*	Jan 07*	Apr 07*	Jul 07	Oct 07
2007	1.9-3.8	2.1-3.8	1.3-2.6	2.2-2.5	2.2-2.3
2008	2.2-4.6	2.2-4.5	1.6-3.8	2.1-3.8	2.2-3.5
2009	-	2.4-5.2	2.1-4.6	2.1-4.3	2.5-4.6

GDP growth projections (%)

	Oct 06	Jan 07	Apr 07	Jul 07	Oct 07
2007	4.1-6.2	4.9-6.7	6.0-7.0	6.2-6.8	6.5-6.6
2008	4.5-7.0	3.6-6.4	4.0-6.3	4.3-6.7	4.4-6.2
2009	-	3.5-6.5	4.0-7.0	4.0-7.2	3.8-6.7

* concerns average inflation in the fourth quarter of a given year
Note: there is a 50% probability that the annual growth of GDP and inflation will be within the indicated ranges.

Inflation projection's fan chart and MPC's inflation target



Source: NBP, Reuters

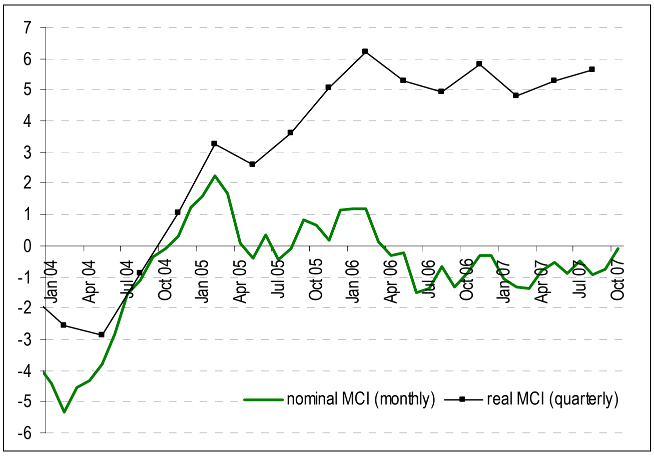
Rates unchanged in October, but more hikes to come

- The Monetary Policy Council decided to keep interest rates on hold in October, with the main reference rate at 4.75%.
- The decision was consistent with expectations of vast majority of market analysts, although the interest market has been pricing-in to some extent a possibility of rate hike already in October. Apparently, the MPC agreed that weight and number of arguments allowing to postpone a rate hike was greater that those calling for swift monetary tightening. One cannot exclude that in contrast to September, there was a motion to raise rates in October, but it did not win support.
- The official statement and the press conference have not changed expectations regarding future decisions of the MPC. The Council repeated that "the probability of inflation running above the inflation target is still higher than the probability of inflation running below the target", which de facto means restrictive monetary policy bias.
- The most important new issue was adding food prices growth as one of the inflation risk factors. The food prices were also mentioned among factors, which will be closely watched by the Council in the near future. The question arises how particular rate-setters assess persistence of the shock in the food market and the risk of its spillover on other prices.
- Despite the new projection indicates inflation increase in 2009 clearly above the target, the MPC did not decide to raise rates in October. This confirms our assessment that the MPC preferred to wait for more information (among others, concerning labour market and future fiscal policy) before tightening monetary policy further. Thus, we maintain our view that next rate hike of 25bp will take place in November and two additional hikes may take place in H1 2008.

Inflation projection up in the longer term

- The new inflation projection of the NBP presumes a slightly lower GDP growth in 2008-2009 as compared to the July projection. Despite this fact, the forecasted inflation path is slightly higher in the long term than indicated in July, though till the mid-2008 it is below the previous projection. The lowering of the inflation path till the mid-2008 as compared to the July projection was influenced most of all by a decline of the net inflation path (lower starting point in 3Q07), in part compensated by the high food prices growth. In the second part of the 2008 and in 2009 the higher inflation path as compared with the July projection was affected by higher net inflation and higher fuel inflation. Higher net inflation in the long run resulted from higher cost pressure – growing import prices and stronger than expected tightening of labour market conditions, even despite the experts' adjustments in the model slightly reduced a scale of ULC impact on price growth.
- The distribution of risks to the projection, presented in the fan chart, reflecting all uncertainty factors included in the model, is almost symmetrical, similar as in the past projections. However, after including the off-model uncertainty factors, the risk for projection is symmetrical in the short term, while in the long term is asymmetrical to the downside.
- The cut-off date of the new report was September 28. According to the NBP analysts, after the close date of the report the risks that food prices rise faster in the short term than it was showed in October projection have increased. After the September 28 there was also significant rise of fuel prices in the global markets and increase of oil prices forecasts for 2007-2008. On the other hand, according to the authors of the projection, till the close date of the report the risk of slowdown of the world economy and lower GDP growth in Poland has increased.

Restrictiveness of the Monetary Policy (Council)

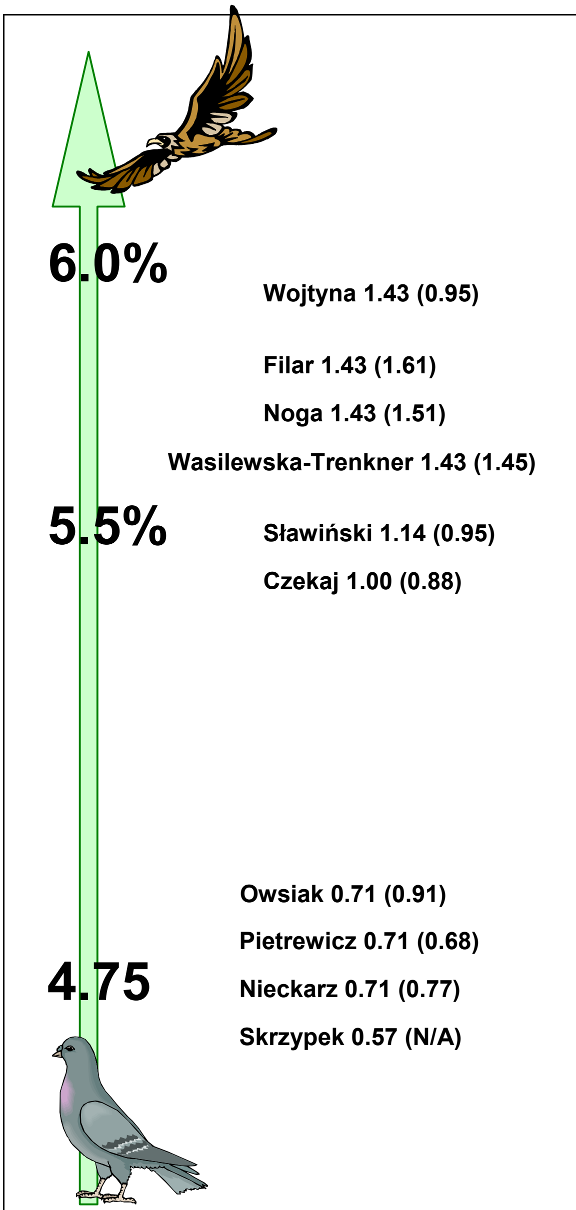


Increase in monetary policy restrictiveness in September

▪ Restrictiveness of monetary policy, measured by nominal MCI index significantly increased in October, despite no rate hike by the MPC.

▪ This was connected with both larger upward deviation of the short-term interest rates from their long-term trend, amid expectations of further rate hikes by the MPC in next months, and with significant appreciation of the zloty against the euro (in October the EURPLN rate for the first time in a few months fell below its long-term trend).

▪ Real MCI based on a quarterly basis showed increase in the restrictiveness of monetary conditions in 3Q07 as compared to the 2Q07. This was due to clear increase in short-term interest rates while the REER relative to its long-term trend weakened in 3Q07.



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.

New poles in the MPC

▪ Over the last month we have received results of votes at MPC meetings in July and August. In the new Inflation Report, published in late October, results of MPC members' voting in June, July and August were revealed, but results of the MPC vote on the 25bp rate hike in August had been earlier released in the government's monitor. Both the voting results in July and August are quite interesting. This is reflected in changes in the index of MPC members' restrictiveness, which we calculate on a monthly basis. Now, at the two opposite poles in the MPC are professor Andrzej Wojtyna and NBP governor Sławomir Skrzypek.

Wojtyna the most conservative

▪ In July the motion to raise rate by 25bp was submitted by Andrzej Wojtyna, but it was turned down by all other MPC members, even those who used to consequently support the monetary policy tightening earlier. This result, as well as a series of Andrzej Wojtyna's comments in the last months have indicated that he moved from the position of one of the moderate MPC members to the most hawkish rate-setter.

Dovish heart of the NBP governor

▪ The MPC chairman and NBP's governor Sławomir Skrzypek is at the opposite end of the Council, and given result of the MPC vote in August he is the only person who did not back any interest rate hike since the start of his term in the office. Taking into account recent comments from NBP governor on the pessimistic inflation forecast for October published by the Finance Ministry, questioning persistence of inflation acceleration and thus questioning a need for further rate hikes, it seems that also at next MPC meeting Sławomir Skrzypek will oppose monetary tightening.

…and Jan Czekaj still tips the balance

▪ Looking at results of votes at MPC meetings this year, the MPC member whose vote is crucial for balance of strength within the Council is still Jan Czekaj. Although in the recent two votes, results of which we know, he did not have to tip the balance, as there was wider majority for the made decisions, but in our opinion Czekaj will be again on the edge given likely stronger polarisation of views on policy actions within the Council in future. Currently Czekaj believes (according to his comments from an interview with PAP agency published on November 5) that "further monetary policy tightening will be needed". In his opinion, the MPC has no comfort of watching development of the economic situation in a sense that interest rates could remain unchanged for a couple of months. Probability of rate hike in November is seen by him at 55% and he added that one should not exclude next rate hikes in 2008, but this will depend on how deep the economic growth slowdown will be. "If the GDP growth decreased to around 5% or even below 5%, the monetary policy should not be tightened any more, because according to our estimates the potential GDP growth is already higher. However, one can state with large probability that we there should be no major downturn in the economy", Czekaj said.

Source: CSO, Eurostat, NBP, Reuters, own calculations

Government and politics

Distribution of seats in the parliament after election

	Sejm	Senate
PO	209	60
PiS	166	39
LiD	53	0
PSL	31	0
Others*	1	1

* One mandate in the Sejm was taken by German minority, while in the Senate there is one independent senator Włodzimierz Cimoszewicz.

Candidates for ministers in PO-PSL government

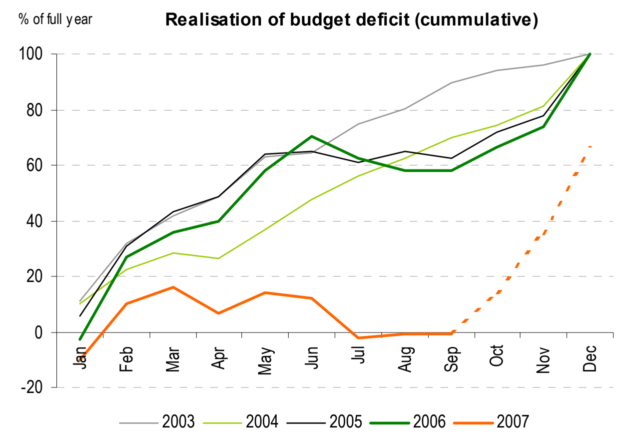
prime minister	Donald Tusk (PO)
minister of economy, deputy PM	Waldemar Pawlak (PSL)
minister of finance	Jacek Rostowski
minister of treasury	Aleksander Grad (PO)
minister of infrastructure	Cezary Garbarczyk (PO)
minister of regional development	Elżbieta Hibner (PO)
minister of internal affairs, administration	Grzegorz Schetyna (PO)
minister of foreign affairs	Radosław Sikorski (PO)
minister of national defencej	Bogdan Klich (PO)
minister of culture	Bogdan Zdrojewski (PO)
minister of education	Katarzyna Hall (PO)
minister of labour	PSL candidate
minister of agriculture	Marek Sawicki (PSL)

Biographical notes of candidates for economic ministers

Jacek Rostowski, candidate for minister of finance
Professor of economic sciences, graduated from LSE and University of London. Lecturer at foreign universities. Former economic advisor to deputy PM Leszek Balcerowicz and NBP president, ex-head of Macroeconomic Council at the Ministry of Finance. Author of numerous publications concerning EU enlargement, monetary policy, exchange rate policy and transformation of post-communist economies.

Waldemar Pawlak, candidate for minister of economy and deputy PM
PSL president, ex-Prime Minister. Graduated from mechanics division at the Warsaw University of Technology. Former president of Warsaw Commodities Exchange. Areas of interest include new technologies.

Aleksander Grad, candidate for minister of treasury
Geodesist. Since 2001 member of parliament (PO). Ex-minister of healthcare and former governor of Tarnów province. Former World Bank's associate in the area of rural areas revitalisation.



Source: BZWBK, Ministry of Finance, electoral committee

Change in political landscape after election

▪ The Civic Platform won the general election in October, receiving support of 41.5% and 209 seats in the Sejm. The Law and Justice obtained 31.1% of votes and 166 seats.

▪ PO decided to form a ruling coalition with PSL. The programme of the new government has not been presented yet. However, significant differences in the parties' programmes, particularly in economic issues, suggest it is not very likely that PO will be able to realise most of its pre-election promises. First comments of PO officials after the election suggested that one should not count too much for radical reforms.

▪ Additionally, the new government will face strong opposition in the Sejm (coalition has only slight majority of 240 votes) and it is likely that many of the proposals will meet with president's veto. Rejection of veto will require help of left-wing LiD.

What government, what economic policy?

▪ On Friday, 9 November, PO chairman Donald Tusk has been designated as the Prime Minister. Since then Tusk has 14 days to assemble the government and receive approval from the Sejm.

▪ The official line-up of the government is still unknown, but most of the candidates for ministerial posts have been revealed. The new minister of finance will be probably professor Jacek Rostowski, while Waldemar Pawlak is likely to become the deputy prime minister and the minister of economy.

▪ Rostowski as the new finance minister should meet with warm market reception, among others due to the fact that he is perceived as the advocate of fast euro zone entry and rather firm fiscal policy. However, one should remember that his field for manoeuvre will be limited by political constraints, and additionally by the fact that the supervisor of economic policies will be PSL president whose economic views are far less liberal.

▪ Most likely, the coalition with PSL will force the PO to abandon some of its proposals, among others flat tax idea. It is also hard to imagine far-reaching reforms in farmers' pension system.

▪ Among changes in fiscal policy planned by the PO there was abandoning fiscal deficit anchor in favour of a rule constraining spending growth. This could allow faster reduction in fiscal deficit in relation to GDP, especially in the period of economic expansion.

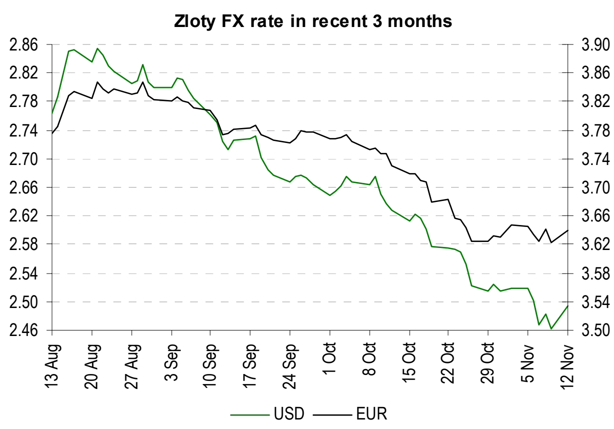
▪ The new government is likely to speed up the privatisation process of state-owned companies, which was promised, among others, by the candidate for new treasury minister Aleksander Grad. This would decrease the net borrowing needs of the state budget in the following years, being a positive factor for the debt market.

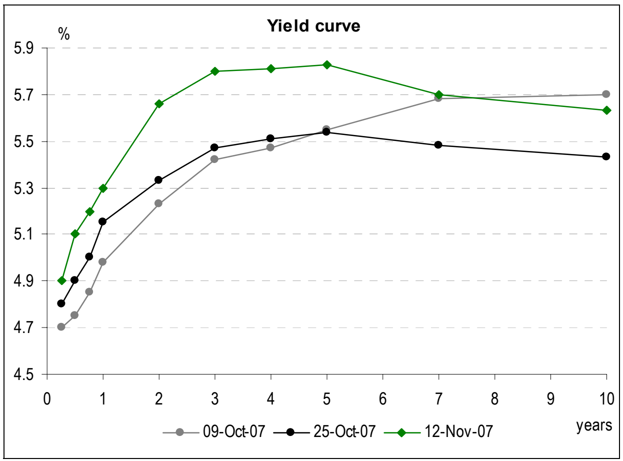
Accumulation of budget spending in the last quarter

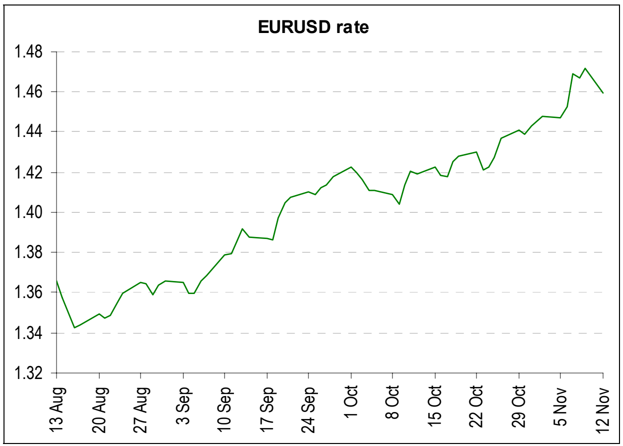
▪ After three quarters of this year, the state budget was in surplus reaching PLN197.5m. Fast rise in tax revenues was maintained, as regards income and indirect taxes, which signalled that the economy was still expanding quickly. In sum, total revenues after September reached 76.4% of annual plan.

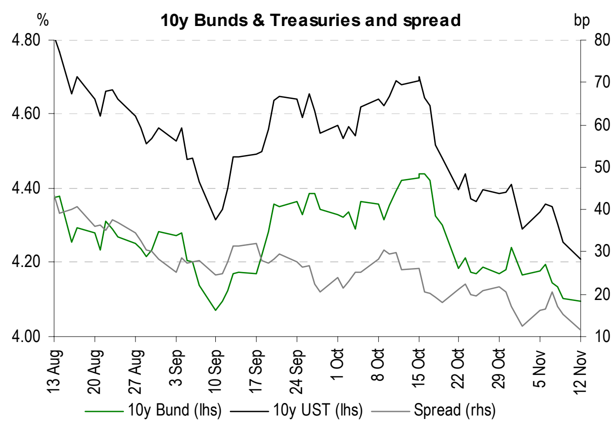
▪ Maintenance of budget surplus in September was partly due to further delays in spending some of budgetary funds. After three quarters total budget expenditure was at 67.5% of annual plan. However, next months will bring accumulation of overdue payments. This started already in October when according to FinMin's estimates the budget deficit of PLN4bn was recorded (14-15% of the level planned for 2007). It still seems likely that at the end of the year the total deficit will be close to PLN20bn (against PLN30bn planned in the budget bill).

Market monitor









Source: Reuters, BZ WBK

Zloty gains after the elections

▪ In October the zloty significantly strengthened. It received a positive impulse from investors' expectations for introducing economic reforms as well as rising probability of sooner entry to the euro zone after surprising victory of the PO in the parliamentary elections. Moreover, expectations of more interest rate hikes in Poland increased, and zloty was additionally supported by the weakening dollar. In the result the EURPLN rate approached 3.60 and after a slight correction it stabilised near 3.65. A more significant strengthening occurred against the dollar.

▪ In our view the market sentiment after the victory of PO in the elections seems to be overly optimistic, though it seems, that it may hold for some time. There may be a slight correction before the year end, however expectations of more rate hikes should keep the zloty at strong levels.

The yield curve inversion

▪ The election victory of the party perceived as market friendly as well as the behaviour of the core debt markets contributed to a significant increase in bond prices at the longer maturities. Moreover, higher than expected data on CPI, high FinMin's inflation forecast for October, and hawkish comments of the MPC members contributed to substantial 2Y bonds weakening. In the first days of November the yield curve inversed.

▪ Amid fears over long-lasting increase of food prices, CPI data moved to the foreground. The comments of the next MPC members are going to be crucial for the market. In our view bonds may slightly strengthen after the release of the CPI though in a few months time they may still weaken on maintained expectations of monetary tightening. The effect of elections at the longer end of the curve may weaken though the expectations of interest rate cuts in the US will work in the opposite direction.

The dollar weakening sees no end

▪ After another rate cut by Fed and new information about problems and losses of financial institutions connected with investments in the mortgage instruments, the rapid depreciation of the dollar in the world markets was continued. The EURUSD rate gradually set new records and reached a level slightly above 1.47 on the wave of rising expectations of more interest rate cuts in the US and decline of interest rate disparity against the euro zone. In the last few days there was a slight recovery and the EURUSD rate fell to 1.456.

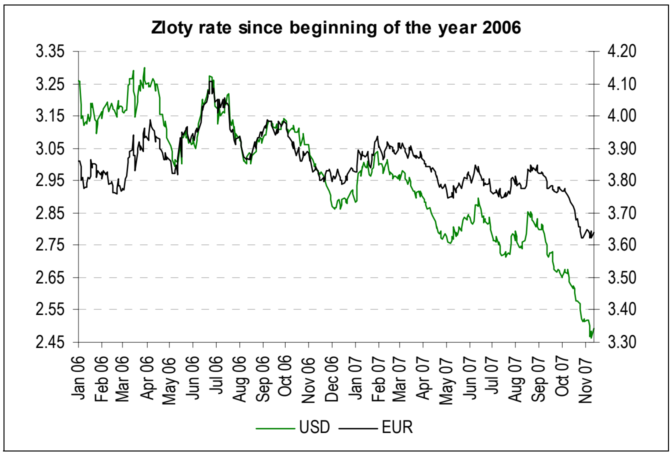
▪ In our opinion the dollar may weaken further on expectations of more monetary policy easing by the Fed. However, later on the greenback is going to recover losses incurred against the single currency. Next weeks the market may stay under influence of news on financial institutions problems and maintained uncertainty.

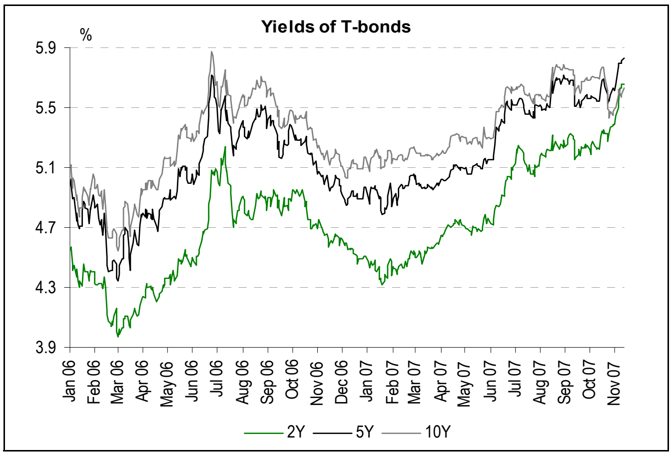
Rate cut expectations in the US strengthen debt markets

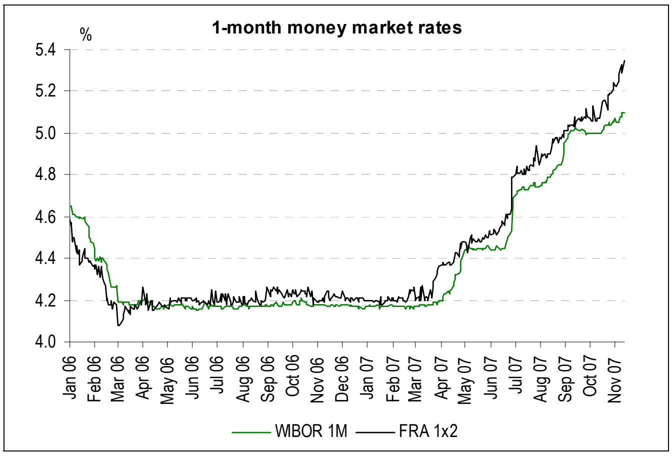
▪ The mounting fears over the performance of the US economy, expectations of more interest rate cuts in the US amid limiting fears over inflation resulted in substantial drop in yields. The moment of increased risk aversion and flight to quality also contributed to rising prices of US bonds. German bond market was additionally supported by not so hawkish comments of the ECB. The yields of 10Y Treasuries declined since the mid October from 4.64% to 4.20%, while yields of 10Y Bunds Bund from 4.36% to 4,09%.

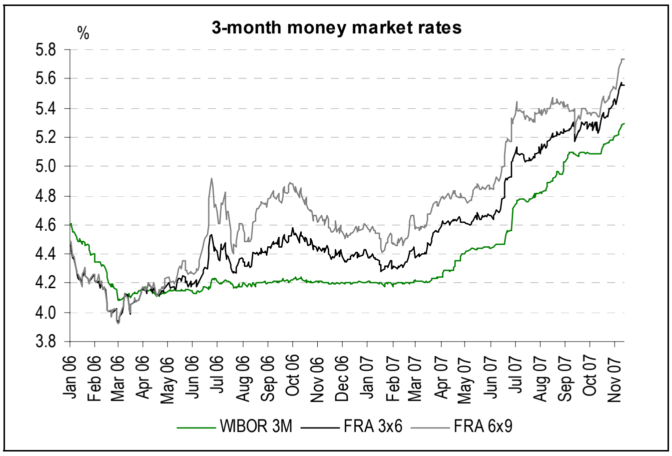
▪ We expect that Fed is going cut interest rates one more time by 25 bp in Q1 2008, while the ECB will postponed the decision to raise rates for a longer time. The investors' attention is doping to focus mainly on data determining the economic growth In the US and the bond prices will be under strong influence of next data fuelling the uncertainty in the credit markets.

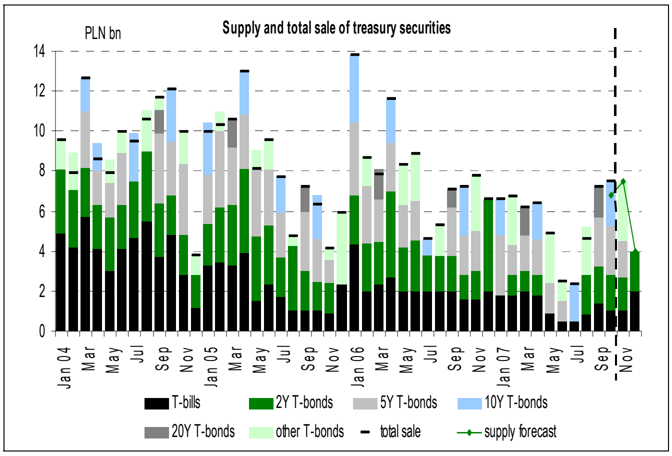
Market monitor











Treasury bill auctions (PLN m)

Date of auction	OFFER / SALE	
	52-week	Total
03.09.2007	900 / 900	900 / 900
17.09.2007	500 / 500	500 / 500
Total September	**1 400 / 1 400**	**1 400 / 1 400**
08.10.2007	500 / 500	500 / 500
22.10.2007	500 / 500	500 / 500
Total October	**1 000 / 1 000**	**1 000 / 1 000**
05.11.2007	1 000 / 1 000	1 000 / 1 000
19.11.2007	-	-
Total November*	**1 000 / 1 000**	**1 000 / 1 000**

* estimations based on Ministry of Finance preliminary information

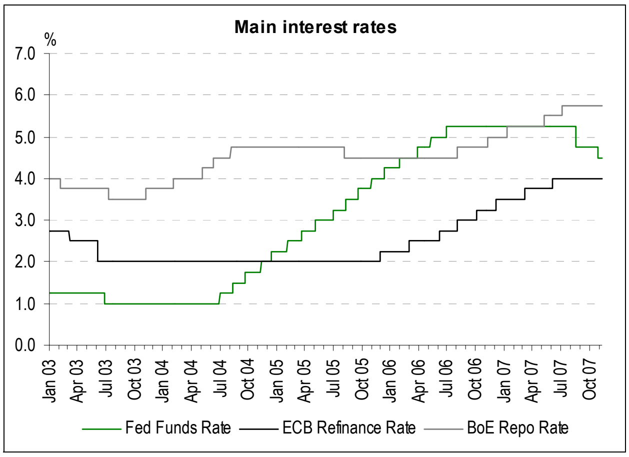
Treasury bond auctions in 2007 (PLN m)

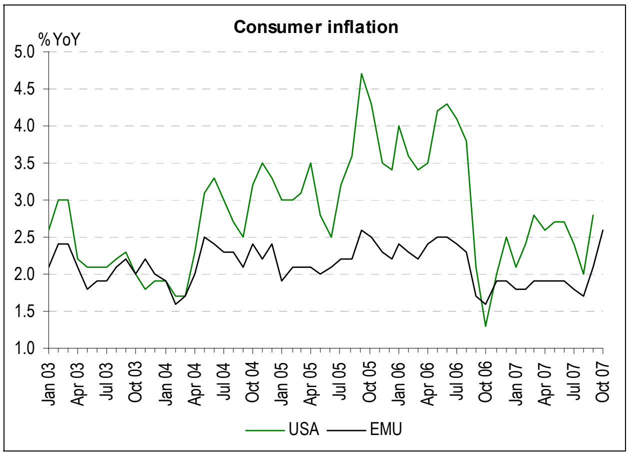
month	First auction				Second auction				Third auction			
	date	T-bonds	offer	sale	date	T-bonds	offer	sale	date	T-bonds	offer	sale
January	-	-	-	-	10.01	DS1017	1 800	1 800	17.01	PS0412	3 000	3 000
February	07.02	OK0709	1 000	1 000	14.02	WZ0118 | IZ0816	2400 | 0	2400 | 0	21.02	PS0412	1 500	1 500
March	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	2 160	2 160	17.10	PS0412	2 300	2 300
November	07.11	OK0709	1 700	1 700	14.11	WZ0118 | IZ0816	2 500 | 500	-	21.11	PS0412	1 500 | 2 500	-
December	05.12	2L	-	-		-	-	-	-	5L	-	-

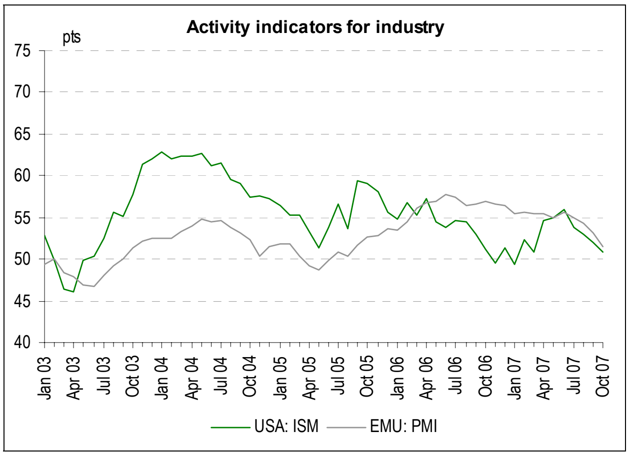
* with supplementary auction

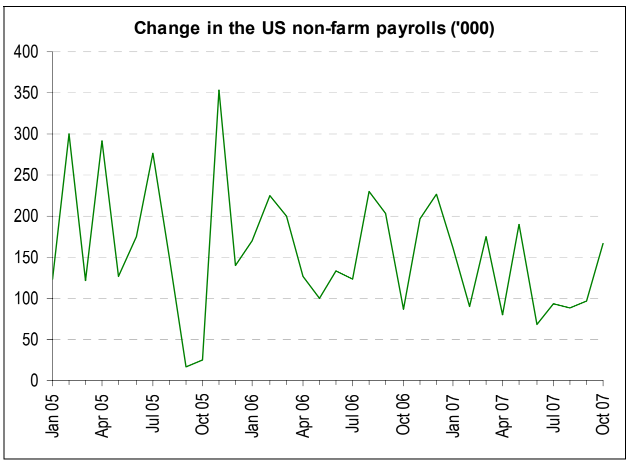
Source: Ministry of Finance, Reuters, BZ WBK

International review









Source: Reuters, ECB, Federal Reserve

Fed cuts rates again

▪ In October Fed decided to cut interest rates by 25 bp. The main rate fell to 4.50%. In the communiqué it signalled that the past interest rate cuts should help in calming down situation in the financial markets and support the US economy and it stated that the upside risk to inflation balanced the downward risk to economic growth. This may suggest that Fed may not be willing to cut rates again already in December. Further comments of Bernanke focused on the risks to economic growth.

▪ ECB left the interest rate unchanged In November. At the press conference the ECB said that, the bank is ready to counteract the present upside risks for inflation. However, Trichet added also that the ECB stays in the „wait-and-see" mode on the next data releases and the development of the situation in the financial markets amid maintained increased uncertainty.

Inflation rebounds

▪ The US inflation rose in September by 0.3%MoM (2.8%YoY) against expected 0.2%MoM, while the core CPI increased in line with forecasts by 0.2%MoM (2.1%YoY). The CPI growth resulted mainly from energy prices growth. The PPI index increased in September by 1.0%MoM against expectations of 0.9%, most of all due to rising oil prices. The core index increased by 0.1%MoM, i.e. slightly below expectations of 0.2%MoM. The core PCE index rose by 0.2%MoM and 1.8%YoY.

▪ In September the inflation in the euro zone increased in line with forecasts and early estimates to 2.1%YoY from 1.7%YoY in August. Data did not affect the markets. The flash estimates of the Eurostat of October inflation showed an acceleration of inflation measured by the HICP index to 2.6%YoY, significantly above the market expectations.

GDP growth in Q3 exceeds expectations

▪ The ISM index for the US manufacturing sector fell in October to 50.9 pts from 52.0 pts in September, which resulted among others from tighter credit conditions and slowdown in the housing market. The ISM index for the services sector appeared better than expected and amounted to 55.8 pts against a forecast of 54.0 pts, which slightly supported the view of the US economy.

▪ The PMI index for the manufacturing sector in the EMU in October was in line with the preliminary estimate and declined to 51.5 pts, the lowest level since August 2005, though it did not affect the financial markets. The main reason was weaker demand in the euro zone and the effect of single currency strengthening. On the other hand the PMI index for services sector rose to 55.8 pts from 54.2 pts in September, which was slightly above the market expectations.

▪ The US Q3 GDP growth amounted to 3.9% and was much above market expectations of 3.0% against 3.8% in Q2. The GDP growth comprised quite strong PCE growth, business investment, narrowing the trade deficit amid strong exports growth and inventories change. This result was good despite strong decline on residential investment. The GDP deflator rose by 0.7%, much below the consensus (2%). On the other hand the core PCE price index was higher than expected and amounted to 1.8% vs. forecasted 1.5%.

Quite positive data from the labour market

▪ Data from the US labour market showed much higher than expected growth in non-farm payrolls in October, i.e. by 166k vs. expected 80k. The rate of unemployment in the US remained unchanged at 4.7%. The unit labour costs fell in Q3 by 0.2% while the labour productivity increased by 4.9%.

▪ The decline of unit labour costs might slightly calm down Fed fears over inflation pressure from the labour market. Despite, data was better than expected it did not significantly improve moods.

Economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
12 November US: Market holiday	**13** ***POL: Balance of payments (Sep)*** GER: ZEW Index (Nov) EMU: Preliminary GDP (Q3) US: Pending home sales (Sep)	**14** ***PL: Auction of 10Y floating-rate and 12Y CPI linked bonds*** ***PL: CPI (Oct)*** ***PL: Money supply (Oct)*** US: PPI (Oct) US: Retail sales (Oct)	**15** EMU: Final HICP (Oct) US: CPI (Oct) US: NY Fed index (Nov) US: Philadelphia Fed index (Nov)	**16** ***PL: Wages and Employment (Oct)*** US: Net capital flows (Sep) US: Capacity utilization (Oct) US: Industrial output (Oct)
19 ***PL: Treasury bills auction***	**20** ***POL: Fianncial results of nonfinancial enterprises (Q3)*** ***PL: Industrial Output (Oct)*** ***PL: PPI (Oct)*** US: House starts (Oct)	**21** ***PL: Auction of 5Y bonds*** US: Final Michigan (Nov) US: New jobless claims US: FOMC minutes	**22** ***POL: MPC minutes (Oct)*** US: Market holiday	**23** ***PL: Business climate (Nov)*** ***PL: Core inflation (Oct)*** JP: Market holiday EMU: Preliminary manufacturing PMI (Nov) EMU: Preliminary services PMI (Nov)
26 ***PL: Retail sales (Oct)*** ***PL: Unemployment (Oct)***	**27** ***PL: MPC meeting*** GER: Ifo Index (Nov) US: Consumer confidence (Nov)	**28** ***PL: MPC meeting – decision*** EMU: M3 money supply (Oct) US: Durable goods orders (Nov) US: Home sales (Oct)	**29** ***PL: Switch auction*** US: Preliminary GDP (Q3) US: Core PCE (Q3) US: GDP deflator (Q3) US: New homes sales (Oct)	**30** ***PL: GDP (Q3)*** EMU: Economic sentiment (Nov) EMU: Preliminary HICP (Nov) EMU: Revised GDP (Q3) US: Core PCE (Oct) US: Chicago PMI (Nov)
3 December ***PL: Treasury bills auction*** EMU: Manufacturing ISM (Nov) US: Manufacturing ISM (Nov)	**4** EMU: PPI (Oct)	**5** ***PL: Auction of 2Y bonds*** EMU: Non-manufacturing PMI (Nov) US: ADP report (Nov) US: Unit labour costs & productivity (Q3) US: Non-manufacturing ISM (Nov)	**6** GB: BoE meeting – decision EMU: ECB meeting - decision US: New jobless claims	**7** US: Non-farm payrolls (Nov) US: Unemployment (Nov) US: Preliminary Michigan (Dec)
10 US: Pending home sales (Oct)	**11** GER: ZEW index (Dec) US: Wholesales inventories (Oct) US: Fed meeting – decision	**12** ***POL: Switch auction*** ***POL: Balance of payments (Oct)*** US: Import prices (Nov) US: Trade balance (Oct)	**13** ***POL: MPC minutes (Dec)*** ***POL: CPI (Nov)*** CH: SNB meeting - decision US: PPI (Nov) US: Retail Sales (Nov)	**14** ***PL: Money supply (Nov)*** EMU: Final HICP (Nov) US: CPI (Nov) US: Capacity utilization (Nov) US: Industrial output (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	26	-
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	26	-
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

Source: CSO, NBP

Economic data and forecasts

Monthly economic indicators

		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	Nov 07
Industrial production	%YoY	14.8	12.0	5.9	15.4	13.0	11.3	12.6	8.1	5.6	10.4	8.9	5.2	8.8	8.6
Retail sales [c]	%YoY	13.3	13.6	13.3	16.5	17.5	19.2	15.1	14.8	16.2	17.1	17.4	14.2	16.7	17.1
Unemployment rate	%	14.9	14.8	14.8	15.1	14.8	14.3	13.6	12.9	12.3	12.1	11.9	11.6	11.3	11.3
Gross wages [b c]	%YoY	4.7	3.1	8.5	7.8	6.4	9.1	8.4	8.9	9.3	9.3	10.5	9.5	9.5	10.2
Employment [b]	%YoY	3.6	3.8	4.1	3.8	4.3	4.5	4.4	4.4	4.6	4.7	4.8	4.7	4.7	4.5
Export (€) [d]	%YoY	23.8	21.7	10.2	15.4	13.8	15.0	16.8	9.8	10.7	17.4	16.7	10.4	13.4	11.7
Import (€) [d]	%YoY	29.3	22.6	18.2	19.6	12.2	18.5	23.8	12.9	16.6	23.5	12.8	16.3	14.3	16.2
Trade balance [d]	EURm	-404	-499	-996	-542	-141	-757	-781	-1030	-786	-1293	-289	-959	-542	-983
Current account balance [d]	EURm	-906	-993	-1290	-881	-545	-681	-740	-1524	-1343	-1436	-637	-859	-592	-1043
Current account balance [d]	% GDP	-2.8	-3.0	-3.2	-3.4	-3.2	-3.2	-3.2	-3.4	-3.7	-3.9	-3.8	-4.0	-3.9	-3.8
Budget deficit (cumulative)	PLNbn	-16.6	-18.5	-25.1	3.1	-3.0	-4.8	-2.1	-4.3	-3.7	0.6	0.3	0.2	-4.3	-10.8
Budget deficit (cumulative) [e]	% of FY plan	66.3	73.9	100.0	-10.3	10.1	16.1	6.9	14.2	12.3	-2.1	-0.9	-0.7	14.3	36.0
CPI	%YoY	1.2	1.4	1.4	1.6	1.9	2.5	2.3	2.3	2.6	2.3	1.5	2.3	2.8	3.0
PPI	%YoY	3.2	2.5	2.6	3.1	3.5	3.3	2.2	2.1	1.7	1.5	1.8	2.0	2.5	3.2
Broad money (M3)	%YoY	12.8	14.6	16.0	19.3	18.0	18.0	17.8	16.0	14.7	15.6	16.1	14.3	14.8	14.4
Deposits	%YoY	11.8	13.4	15.2	18.5	18.3	17.7	18.2	16.4	15.2	15.9	16.3	15.3	15.5	14.8
Loans	%YoY	19.5	20.7	23.4	25.0	26.5	26.8	28.4	28.6	29.2	31.4	31.1	30.9	30.0	29.2
USD/PLN	PLN	3.09	2.97	2.88	2.98	2.98	2.94	2.83	2.80	2.84	2.75	2.80	2.73	2.61	2.50
EUR/PLN	PLN	3.90	3.82	3.81	3.88	3.90	3.89	3.82	3.78	3.81	3.77	3.81	3.79	3.71	3.65
Reference rate [a]	%	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	5.00
Lombard rate [a]	%	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	6.50
WIBOR 3M	%	4.22	4.20	4.20	4.20	4.20	4.22	4.32	4.44	4.52	4.78	4.80	5.09	5.13	5.30
Yield on 52-week T-bills	%	4.35	4.29	4.20	4.14	4.07	4.23	4.36	4.43	4.42	4.70	4.80	5.01	5.04	5.25
Yield on 2-year T-bonds	%	4.84	4.65	4.54	4.41	4.46	4.55	4.71	4.70	4.93	5.14	5.23	5.25	5.30	5.60
Yield on 5-year T-bonds	%	5.24	5.01	4.91	4.90	4.97	4.98	5.07	5.11	5.40	5.50	5.61	5.60	5.59	5.80
Yield on 10-year T-bonds	%	5.39	5.18	5.10	5.16	5.18	5.18	5.27	5.28	5.52	5.60	5.68	5.69	5.64	5.65

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	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08
GDP	PLNbn	983.3	1 060.2	1 157.4	1 258.1	266.7	280.2	282.4	328.1	288.8	305.9	307.2	356.2
GDP	%YoY	3.6	6.2	6.3	5.5	7.2	6.4	5.8	5.9	4.6	5.9	5.6	5.9
Domestic demand	%YoY	2.4	7.3	7.4	7.0	7.7	8.2	6.9	7.1	5.8	7.5	7.1	7.5
Private consumption	%YoY	2.0	4.8	5.7	5.7	6.9	5.1	5.5	5.2	5.0	6.5	6.0	5.5
Fixed investments	%YoY	6.5	15.6	18.3	14.0	26.2	20.8	16.0	15.5	12.0	15.0	14.5	14.0
Industrial production	%YoY	4.0	12.5	9.6	8.2	13.0	8.5	8.1	8.7	6.2	7.7	9.7	9.0
Retail sales (real terms)	%YoY	1.5	11.9	14.5	14.4	17.4	14.1	12.8	13.6	13.1	16.9	13.7	14.0
Unemployment rate [a]	%	17.6	14.8	11.5	8.5	14.3	12.3	11.6	11.5	11.1	9.3	8.7	8.5
Gross wages (real terms) [c]	%YoY	1.2	4.2	6.4	5.1	5.9	6.5	8.1	5.9	4.6	5.0	5.0	5.6
Employment [c]	%YoY	1.9	3.2	4.5	3.9	4.2	4.5	4.8	4.5	4.2	4.0	3.7	3.6
Export (€) [b]	%YoY	17.8	20.4	13.7	13.0	14.7	12.3	14.6	13.2	13.0	13.0	13.0	13.0
Import (€) [b]	%YoY	13.4	24.0	17.1	17.3	16.8	17.5	17.5	16.7	17.0	17.0	17.0	18.0
Trade balance [b]	EURm	-2 242	-5 536	-9 676	-15 889	-1 440	-2 594	-2 541	-3 101	-2 683	-4 058	-4 040	-5 108
Current account balance [b]	EURm	-3 866	-8 787	-12 037	-18 250	-2 104	-3 610	-2 932	-3 391	-3 347	-5 074	-4 431	-5 398
Current account balance [b]	% GDP	-1.6	-3.2	-3.9	-5.3	-3.2	-3.7	-4.0	-3.9	-4.2	-4.5	-4.8	-5.3
Budget deficit (cumulative) [a]	PLNbn	-28.6	-25.1	-19.8	-28.0	-4.8	-3.7	0.2	-19.8	-	-	-	-28.0
Budget deficit (cumulative) [a]	% GDP	-2.9	-2.4	-1.7	-2.2	-	-	-	-	-	-	-	-
CPI	%YoY	2.1	1.0	2.4	3.0	2.0	2.4	2.0	3.0	3.5	3.0	3.0	2.6
CPI [a]	%YoY	0.7	1.4	3.3	2.6	2.5	2.6	2.3	3.3	3.4	2.9	2.8	2.6
PPI	%YoY	0.7	2.5	2.6	2.8	3.3	2.0	1.8	3.2	3.6	2.8	2.3	2.7
Broad money (M3) [a]	%YoY	13.1	16.0	14.0	10.7	18.0	14.7	14.3	14.0	13.1	12.8	12.3	10.7
Deposits [a]	%YoY	12.6	15.2	13.5	11.2	17.7	15.2	15.3	13.5	13.1	12.9	12.2	11.2
Loans [a]	%YoY	13.3	23.4	29.6	23.1	26.8	29.2	30.9	29.6	28.0	26.0	23.9	23.1
USD/PLN	PLN	3.23	3.10	2.77	2.59	2.97	2.82	2.76	2.53	2.47	2.54	2.65	2.68
EUR/PLN	PLN	4.02	3.90	3.79	3.63	3.89	3.80	3.79	3.66	3.60	3.64	3.67	3.63
Reference rate [a]	%	4.50	4.00	5.00	5.50	4.00	4.50	4.75	5.00	5.50	5.50	5.50	5.50
Lombard rate [a]	%	6.00	5.50	6.50	7.00	5.50	6.00	6.25	6.50	7.00	7.00	7.00	7.00
WIBOR 3M	%	5.29	4.21	4.69	5.66	4.20	4.42	4.89	5.26	5.53	5.70	5.70	5.70
Yield on 52-week T-bills	%	4.92	4.18	4.65	5.61	4.14	4.40	4.84	5.20	5.50	5.65	5.65	5.65
Yield on 2-year T-bonds	%	5.04	4.57	5.15	5.74	4.47	4.78	5.21	5.52	5.80	5.75	5.70	5.70
Yield on 5-year T-bonds	%	5.25	5.03	5.45	5.75	4.95	5.19	5.57	5.75	5.80	5.80	5.70	5.70
Yield on 10-year T-bonds	%	5.24	5.22	5.51	5.64	5.17	5.36	5.66	5.66	5.70	5.65	5.60	5.60

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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