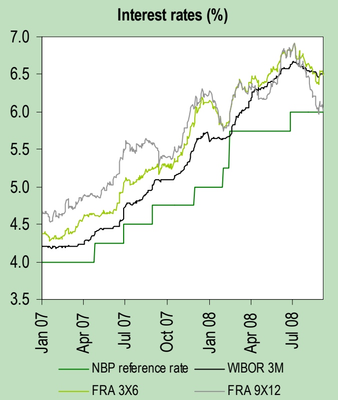
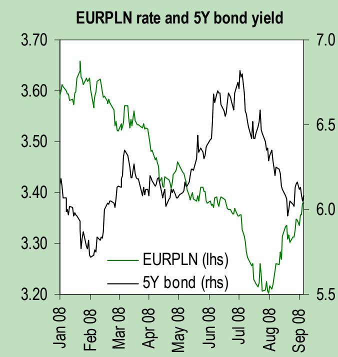
Bank Zachodni WBK

# MACROscope

Polish Economy and Financial Markets

September 2008

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# The Olympian Calm

- **The Monetary Policy Council keeps Olympian calm and still awaits further economic information and even though some of the Council members would like to raise the interest rate already now, the majority of the Council is still not in favour of such a decision.** Is there a chance that the motion on the interest rates increase gets the green light during the next months? We still believe so. Nonetheless, changes in the economic outlook for the euro zone and the significant decrease in oil price (the possibility that EBC will cut the rates in 2009) make it more likely that we will rather face one rise, potentially in October, after the new inflation and GDP projections are published. The key question today is how strong the economic slowdown will be and how it will impact the medium-term inflation outlook. Despite the fact that GDP in the second quarter was higher than expected, we still forecast that the GDP growth will be slightly below 5% in the second half of the year and 4.5% next year. The chance of the MPC cutting the interest rates next year, which is priced-in by the market, may become reality if the global risk factors for the GDP growth on the medium-term get stronger. So far, the inflation rate in Poland is twice as high as the inflation target, the core inflation indicators see the upward trends, the salary growth maintains at the very high level and the unit labour costs grew by ca. 10% in the second quarter.
- **It is quite hard to keep calm observing the situation on the Polish foreign exchange market. Though in line with our projections presented last month, we have been witnessing the continued correction, the scale of zloty weakening exceeded our expectations.** Last month our projection concerning the EURPLN rate as at the year-end (3.30) seemed too conservative to some people, but now we receive comments that it seems to be too low. We do not believe something very unusual has been happening on the Polish FX market if we take account of the situation in the global markets. For example, the difference between the lowest and the highest EURPLN rate in the holiday season was slightly above 5%, whereas in the case of EURUSD rate it was more than 11%. This year, the volatility of the zloty rate was on average lower than for other currencies in the Region, namely the Czech crown and the Hungarian forint. This month, we witnessed a significant swing of the market sentiments but it is worth noting that at the beginning of July, the rate was quite as similar as at the end of August. At present, after the FX rate has overreacted in one direction, it is going back in the other one.
- **Taking into consideration the substantial uncertainty as to the basic macroeconomic factors and the difficulty in making projections for the worldwide and the Polish economies, at the beginning of the report we propose a more casual *Special Focus*.** Is there any connection between the economic and sport results? Many analyses say yes and we attempt to show how we can assess the results of individual Olympic teams at the Beijing Olympic Games in this respect.

| Financial market on 29 August 2008: | | | | | |
|---|---|---|---|---|---|
| NBP deposit rate | 4.50 | WIBOR 3M | 6.50 | USDPLN | 2.2691 |
| NBP reference rate | 6.00 | Yield on 2-year T-bonds | 6.31 | EURPLN | 3.3460 |
| NBP lombard rate | 7.50 | Yield on 5-year T-bonds | 6.16 | EURUSD | 1.4746 |

This report is based on information available until 05.09.2008

# Special focus

## Do results in sport depend on economy?

As everybody knows, economists are tasked with projecting what will happen in the economy and on financial markets. Interestingly, complex statistical tools used for projections are also handy for forecasting the outcome of sport events. In the June's MACROscope published before EURO2008, we attempted to show how economic performance determines a chance to win in the tournament. Let me only remind that in this context the results of the Polish football team came as no surprise. The Spanish football team was one of the favourites to win the cup while the performance of Russian and Turkish players could take viewers by surprise.

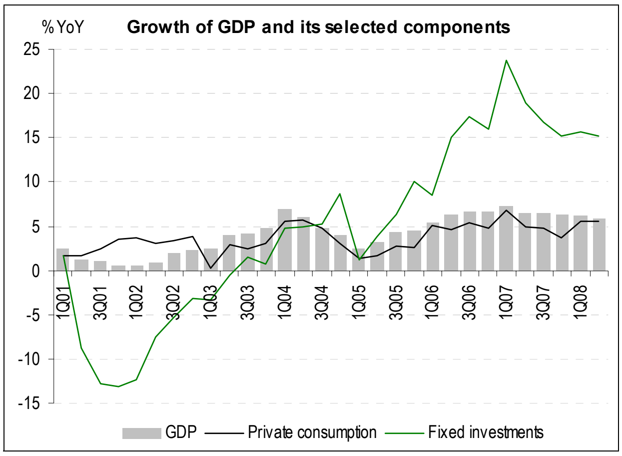
For many years now medal projections have been made in the run-up to the Olympic Games. Amongst those reports, forecasts made by economists play a crucial role. There is even a kind of competition who will produce more adequate projections of results at the games: PricewaterhouseCoopers, professor Andrew Bernard from Dartmouth University or professor Daniel Johnson from Colorado College? The last two have co-authored scientific papers in which they attempted to show what economic and political factors impact a country's sporting prowess at the Games.

Intuitively, it seems that the first factor which determines the amount of medals is the country's population. Apart from the parity for the number of contenders per country, it is population which determines the number of athletes representing a country. The second factor is economic wealth measured most frequently as national income per capita. These two factors may have a significant concurrent impact – rich big players (the US, Great Britain, Germany, France). Sometimes, one factor is so strong that it more than offsets the weakness of the other element – large Chinese population is more important than the wealth of some (even large) European states. In this context, poor results of athletes from India or Indonesia are puzzling. There are also examples of countries which achieve similar results taking advantage of only one of the above factors – populous but poor Ethiopia picked up as many medals in Beijing as small yet rich Denmark. Interestingly, there is often the effect of specialisation in small countries. For example, in the last Beijing 2008 Games, Ireland picked up all its 3 medals in boxing, Jamaica won all its 11 medals in short-distance running, Kenya and Ethiopia finished up winning 14 and 7 medals in long-distance running, respectively. Australia claimed 20 (out of 46) in swimming. Let me mention a result of Iceland, not very nice for us – one medal in handball.

One of analysis prepared by economists even tried to find relationship between the country's climate (not economic, but weather) and the number of medals during the Olympics. Colder nations outperform their competitors, even in Summer Games, which is probably to a large extent connected with the fact that they are richer. In the Winter Games the amount of medals depends more on per capita income, while in the Summer Games the population is more important. We could pick a few more important statistics elements which influence a haul of medals in the Games. Firstly, the so-called 'host effect' which definitely boosts performance. This is proven not only by Chinese athletes in Beijing, but also by only four medals won by Greeks in Beijing compared to 16 in Athens. Besides, some research shows that former Soviet Union republics can also boast better results than it is suggested by other factors. Although according to the research by professor Bernard, this element existed only until the Sydney Games, a one-party system in China can also be conducive to better results. According to PWC, "sport it seems is one area where a planned economy can succeed".

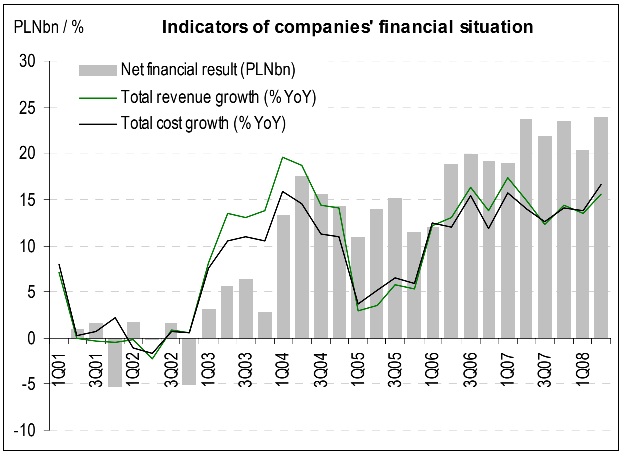
Given the above factors, the brilliant performance of China should not come as a surprise. This is also the case with the US with the greatest haul of medals and Russia being third in the medals table. These countries were destined to sports success at the Games, due to available resources. The results of the US and China were better and of Russia worse than projected. Great Britain exceeded projections despite visible economic downturn. Perhaps this time "the host effect" turned on earlier. Since we attempt to explain the correlation between the number of medals and economic and political factors, then why we should analyse European states separately? We can joke that this is the euro zone that should be at the top of the medals table (166 medals), not to mention the EU as a whole (280 medals), although if athletes from the EU had contended as one nation, then the EU could not have send so many representatives. As regards Poland's results, the best projection was made by professor Bernard (nine medals and fewer than four gold medals) while others were more optimistic (PWC - fourteen medals, professor Johnson – twenty four medals, of which 6 gold). Averaging out, given Poland's economic potential, we should have expected at least 15 medals.

# Economic update




### Second quarter: still solid economic growth...

- Economic slowdown in Q2 2008 was smaller than predicted. GDP growth reached 5.8% versus 6.1% in Q1. Interestingly, gross value added growth accelerated to 6.1% from 5.5% in Q1, while seasonally adjusted GDP growth reached 1.5%QoQ after 1.4% recorded in Q1.
- Good performance of the economy was largely due to high growth in private consumption (5.6%YoY) and investment (15.2%YoY), amid lower than forecast negative impact of net exports (-0.6 pct. pts. contribution versus -0.4 in Q1). Public consumption also had negative impact on economic growth as it fell 1.2%YoY.
- According to Eurostat, GDP growth in Poland reached 6.1% in Q2, versus 6.2% in Q1 2008.

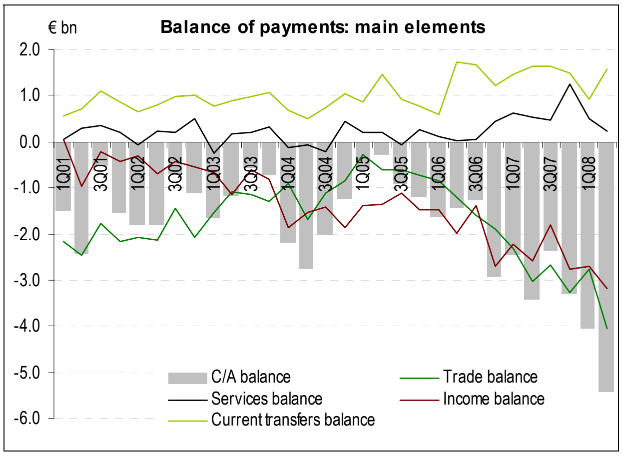



### ... companies' profits still rising (though slower)

- Solid economic growth was reflected in financial results of enterprises that improved once again in Q2. However, the rate of improvement has clearly decelerated as compared to previous quarters.
- Revenue growth remained high (over 15%YoY), however cost growth was even faster, triggering slight deterioration in financial parameters, among others a decline in gross and net profitability, increase in cost ratio, and fall in liquidity.
- Ratio of exporting companies declined in the first half of the year to 48.2% from 48.8% last year. A share of exporters with profits also declined, although main financial parameters of this group still remained better than average for all surveyed companies.


### ... amid accelerating labour costs growth

- Job growth in Q2 was not as impressive as at the start of the year. Average employment in the national economy rose 3.7%YoY, while the number of employed according to Labour Force Survey increased 3.5%YoY. However, labour market tensions did not weaken. Gross wage growth accelerated again, reaching 11.6%YoY in Q2 (12% in enterprises sector).
- In effect, amid a slight deceleration in economic growth, unit labour costs growth gained momentum, reaching 9.2%YoY in Q2 (estimate based on GDP growth and LFS employment data), against 8.5%YoY in Q1.
- Labour productivity growth accelerated slightly to 2.2%YoY from 1.5% in Q1. While in industry and construction productivity maintains rapid growth (ca. 4% and 9%YoY, respectively), in services it dropped once again in Q2.

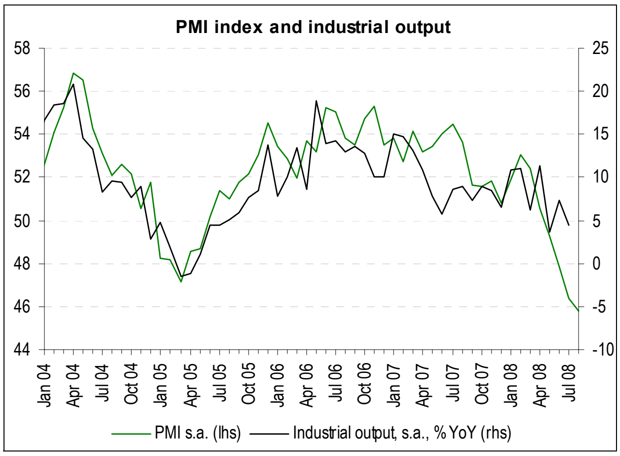


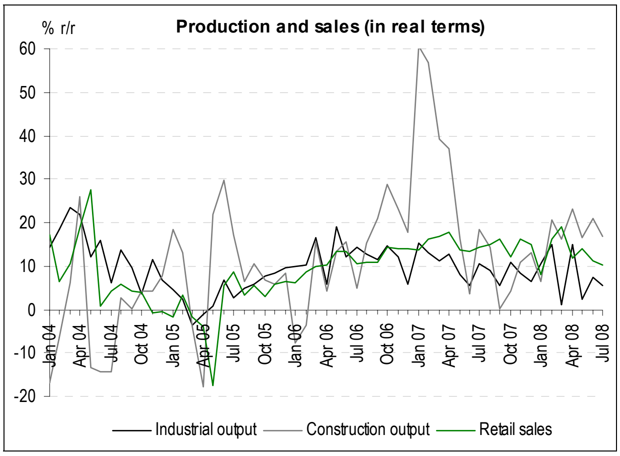

### ... and widening external imbalance

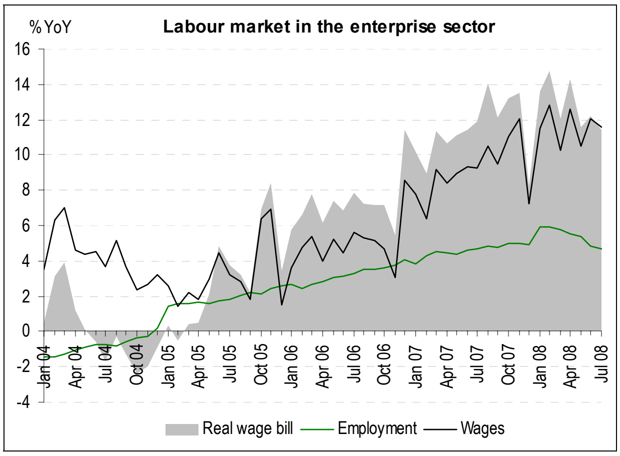
- Despite persistently high export growth (16%YoY in June and 20.4% average in Q2), there was a rise in trade deficit in the second quarter due to clear import acceleration (20.2%YoY in June, ca. 22% in Q2).
- At the same time, there was a clear deterioration observed in income balance (due to high dividend payments abroad) and services balance.
- Cumulated 12-month current account deficit increased to 4.5% of GDP at the end of the second quarter and according to our forecasts it will probably exceed 5% by year-end.
- The coverage of C/A deficit by foreign direct investments has been gradually falling. However, the ratio including both FDI inflow and funds from the EU, is still at safe level of ca. 100%.

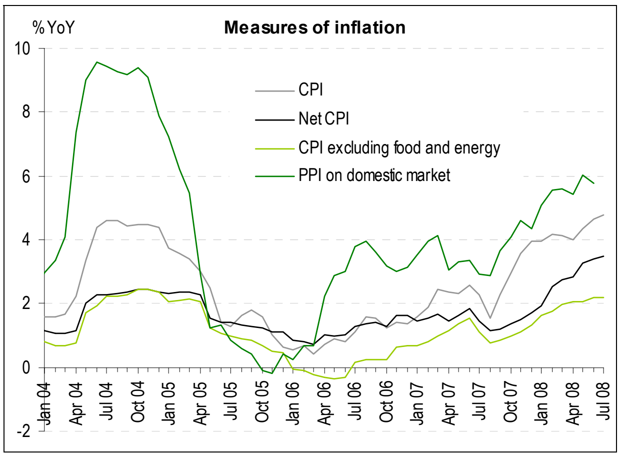
Source: CSO, own calculations

# Economic update




Source: CSO, NBP, own calculations

## How deep economic slowdown in H2?

- Although economic growth in Q2 was better than forecast, the slowdown in the economy is a fact for more than a year. The key question right now is about a scale of this process in the quarters ahead. There are more and more concerns that the second half of the year may see stronger deterioration in economic activity.
- Business climate indicators are showing worsening moods of entrepreneurs and consumers and signal a drop in new orders. The PMI index for Poland recorded particularly deep collapse in July and August.
- In our view, continuation of loan growth, predicted acceleration of EU funds inflow, falling commodities prices abroad and zloty weakening still give arguments to predict a moderate economic slowdown. GDP growth should be only slightly below 5% in H2.

## Weaker industry, robust growth in trade and construction

- Industrial output growth in July reached 5.6%YoY (4.4% in seasonally adjusted terms), confirming that economic activity has been weakening in Q3. Output growth may fall to nearly zero in August, which is suggested by lower number of working days and deep slump in PMI.
- Slightly better result was recorded in construction, where production rose almost as fast as in the first year-half (ca. 17%YoY). This suggests that investment growth remains quite robust. The question is whether falling profitability will convince managers to revise their investment plans later this year.
- Retail sales growth in July reached 14.3%YoY (10.1%YoY in real terms) and remained in double digits in almost all sections apart from sales of food and motor vehicles. Consumers' demand has been growing mainly due to high income growth.

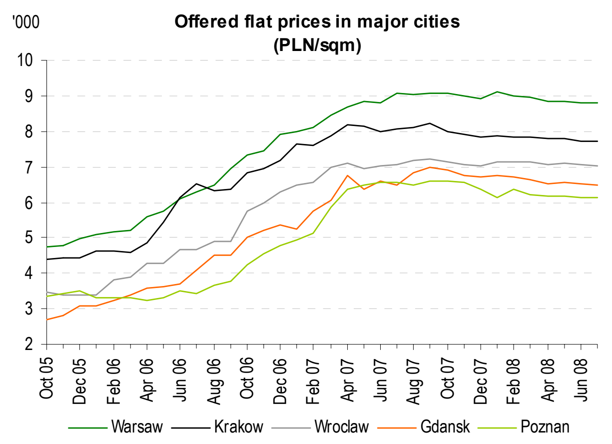
## Wage growth still fast despite weaker labour demand

- Despite gradual economic slowdown taking place, wage pressure remains at elevated level. Wage growth in enterprises sector reached 11.6%YoY in July, slowing only slightly from 12%YoY in June.
- After two months of employment stabilisation, July saw 0.2%MoM increase (4.7%YoY). However, in manufacturing average employment fell third time in a row, which seems to reflect increasing problems of exporters in the face of worsening economic climate abroad and strong zloty.
- Wage growth in enterprises sector increased 16.8%YoY in July (11.5% in real terms), slower than in June and in H1. Nevertheless, households' revenues keep growing fast, supported among others by accelerating growth in social benefits (over 11%YoY in June-July).

## Inflation closer and closer to 5%

- CPI growth accelerated in July to 4.8%YoY, the highest level in seven years, which was caused mainly by higher annual growth of prices of fuel, energy and food. There is a clear difference between behaviour of prices of goods and services. The former have been falling in many cases, while the latter are growing at accelerating pace.
- Core inflation excluding prices of food and energy remained at 2.2%, while net inflation increased from 3.4% to 3.5% in July. One should expect that in August both indicators will go up sharply and CPI growth is likely to exceed 5%YoY.
- PPI growth reached only 2.3%YoY in July (in manufacturing merely 1%YoY). However, it was affected by zloty appreciation, reducing export prices. PPI on the domestic market stays high, reflecting mounting cost pressure for producers.

# Housing market update

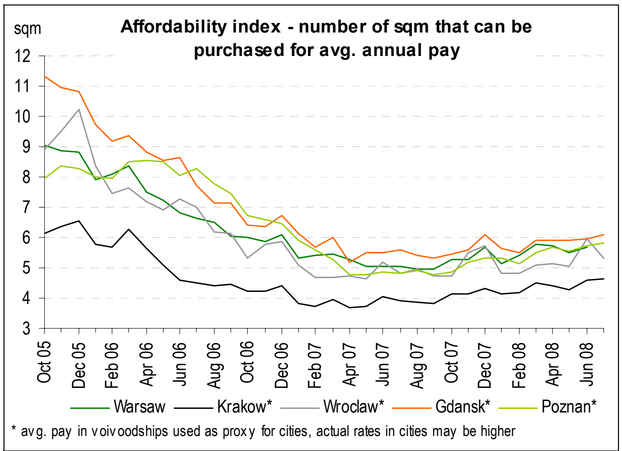



## House prices little changed

▪ Situation on housing market has been little changed for a couple of months. Average house prices in big towns remain stable or are slightly falling, while in smaller cities they are slowly rising, catching up with the leaders.

▪ According to szybko.pl, the biggest drop of average offered flat prices since July 2007 until July 2008 was recorded in Poznań (-6.2%), Kraków (-4.4%) and Warsaw (-3%). Prices in Wrocław and Gdańsk remained almost unchanged.

▪ One has to bear in mind that average prices are not the perfect measure of situation in the housing market. The biggest fall in prices and customers' demand concerns dwellings of low standard in blocks of flats. Meanwhile, prices of luxurious apartments have been quite stable.

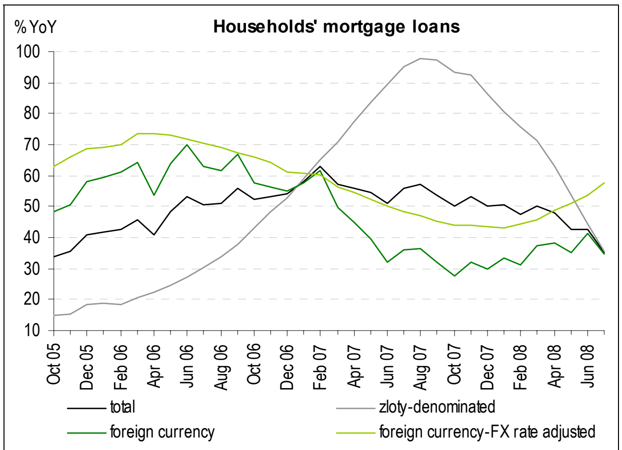



## House affordability growing, not if financed with PLN loan

▪ Likewise in previous months, robust wage growth in July and stabilisation of house prices caused improvement in relation between average salary and house cost. Over the last year, the number of square meters that one could buy for average annual pay increased by ca. 20% in Poznań and Kraków, and by ca. 10% in Gdańsk and Wrocław.

▪ This factor, as well as persisting structural shortage of flats that we have mentioned many times should prevent house prices in Poland from falling in medium run.

▪ On the other hand, a factor that may constrain flats affordability is an increase in domestic interest rates and potential tightening of loan policies by commercial banks.

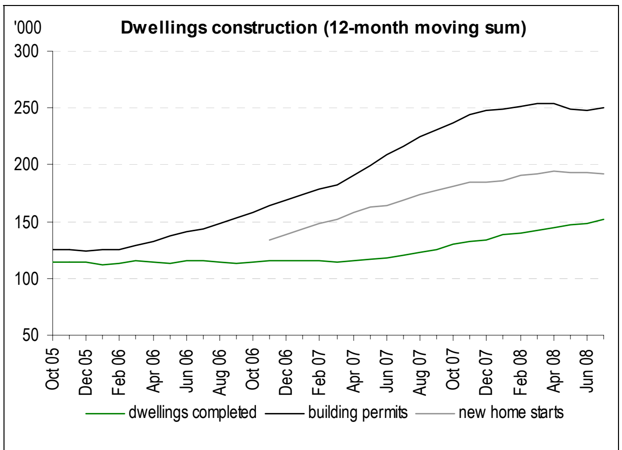



## Demand for mortgage loans still strong

▪ Difference in interest rates between mortgage loans in PLN and CHF has been growing, which shifts households' demand towards foreign currency housing loans.

▪ NBP data showed little decline in households' mortgage debt in July. Nevertheless, it was heavily affected by rapid zloty appreciation (by more than 6% versus Swiss franc in July), which lowered value of outstanding foreign currency debt. We will see this effect in reverse in data for August, when the zloty erased previous gains.

▪ According to our estimate, mortgage loans adjusted for impact of zloty appreciation increased in July by record PLN6bn versus June. Annual (adjusted) growth rate of households' mortgage loans reached 49% against 50.2%YoY in June.




## Supply of new homes rising

▪ In July there were 14,500 new houses completed in Poland, 26% more than one year before. Almost half of this number represented houses for sale or for hiring. During the last 12 months the number of new house completions reached 151,600. These are mainly effects of investments started in the last two years.

▪ The number of new building permits is gradually stabilising – in July it reached ca. 24,000 (up 9.1%YoY), while in the last 12 months it amounted to ca. 250,000. At the same time, the number of new home starts increased by over 192,000.

▪ Developers have been reporting problems with sale of new investments. The problems are amplified by the fact that large part of new houses probably enters the secondary market immediately after completion.

Source: CSO, NBP, szybko.pl, own calculations

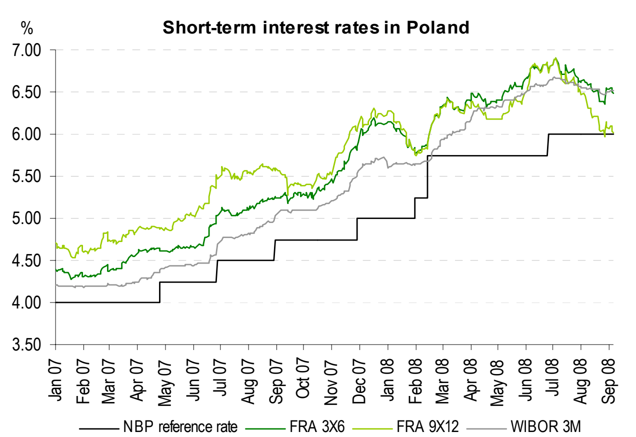
# Central bank watch

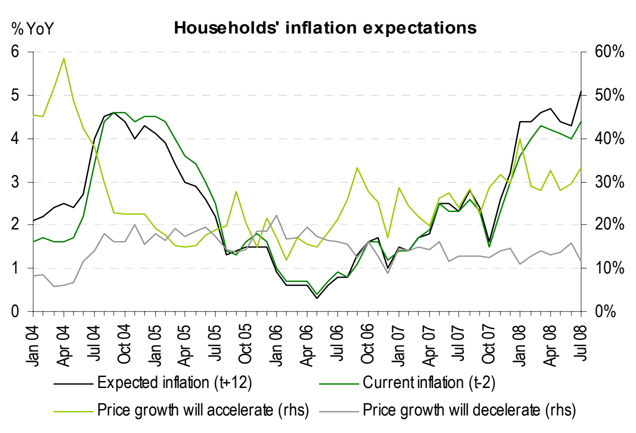
**Key fragments of the MPC statements as compared to July**

~~The latest data on the United States and the euro area point to further deterioration of the outlook for growth in these economies.~~ **Both the national accounts data and other information concerning economic activity in the euro area indicate stronger than expected decline in GDP growth in that region. In the United States, despite favourable data for 2008 Q2, subsequent quarters are expected to see a decline in the economic activity.** At the same time, many countries ~~have recorded a rise in both the current and the forecast~~ **continue to record increased** inflation. ~~In the past few months~~ **Recently**, oil prices in the world markets have ~~increased strongly, while displaying high volatility~~ **decreased markedly, albeit remaining at a relatively high level**. ~~Uncertainty persists as to the scale in which the decline in activity in the external environment may affect the Polish economy.~~

In the Council's assessment, in the coming quarters the pressure on wage increases will probably persist, though the gradually slowing economic growth**, weakening labour demand and deteriorating financial results of enterprises** should be easing the wage pressure and, consequently, also the inflationary pressure. Increased inflation in the coming quarters will, to a large extent, result from the growth of administered prices and also from the food and fuel price growth **previously** observed in the world economy and affecting the Polish market. **Future inflation may also be increased by rising prices of some services, which to some extent may result from the growth of energy prices.** Persistently increased inflation creates a risk of inflation expectations remaining at an elevated level and, consequently, feeds the risk of second-round effects. ~~Moreover, the rise in prices of energy may be gradually passing through to prices of other goods and services.~~

~~In the medium term inflationary pressure may be curbed by still good financial results of enterprises and continuously high investment growth conducive to productivity growth.~~ In the medium term, easing of the inflationary pressure may be supported by the **considerable** slowdown in the global economy and, consequently, also by a decline in economic growth in Poland. The inflationary pressure may still be eased by the import of goods from low-cost countries. The previous increases of the NBP's interest rates as well as the zloty appreciation observed **in the previous period** ~~over the past quarters, which in the recent period has most probably outpaced the appreciation of the equilibrium exchange rate~~ will also contribute to lowering inflation.




Źródło: NBP, Reuters

### Waiting until October

▪ As we expected, despite keeping rates on hold in August, the Council kept the informal restrictive bias, did not rule out monetary policy tightening, and claimed that a more comprehensive assessment of inflation outlook will be possible after analysing the data released in the near future.

▪ We still think that the next decision of the MPC will be a rate hike. However, given indications of economic slowdown abroad (particularly in the euro zone) and concerns about weakening of economic growth in Poland, now it seems that this will be a single rate hike of 25bp.

▪ Expected by us increase in CPI inflation to ca. 5%, in net inflation to around 4% and in the CPI excluding food and energy prices to above 2.5% as well as still two-digit growth in average wages, could be an impulse to deliver a rate hike already in September.

▪ On the other hand, however, economic activity indicators for August (industrial output, retail sales, exports) will be probably quite weak, among others due to an effect of lower number of working days, which will surely not help to persuade those rate-setters who are afraid of serious economic slowdown in 2H08 that more rates hikes are needed.

▪ Therefore, it seems to us that majority of MPC member will decide to wait with a change in monetary policy parameters until October, when the new inflation projection is published. If results of the new projection will confirm the scenario of moderate economic slowdown (and not serious economic downturn) and slow return of inflation to the target, one should expect 25bp rate hike in October.

### Markets expected more dovish statement again

▪ MPC's decision in August did not surprise and did not affect market rates. However, the official statement and press conference of the MPC did significantly influence the market and soon after rates in the money market increased by almost 10bp while bonds weakened. Apparently, some market players counted on cancellation of the restrictive bias.

▪ In July, negative reaction of interest rate market took place as well, although the statement was more dovish. Then, 'dovishwards' changes were more clear, and as a result the weakening in the bond market was slighter and short-time.

▪ We think, that the statement will be also relatively hawkish in September, leaving a room for another hike. It seems that chance of rate hike in September is bigger that it was in July-August.

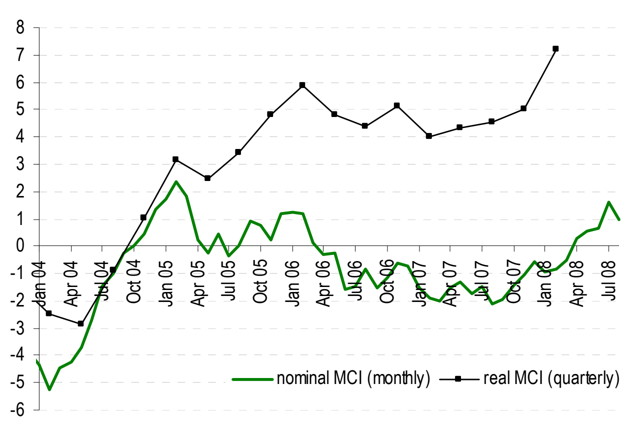
### Inflation expectations still very high

▪ Not until some time could we say, whether according to what MPC says "maintenance of increased inflation brings the risk of preservation of inflation expectation at the higher level". So far, the observation of monthly data on expectations could not fill one with the optimism.

▪ However, although the current inflation increased, inflation expectations stabilised at the level of 5.1% in July, but the structure of answers is still quite negative in future inflation's point of view.

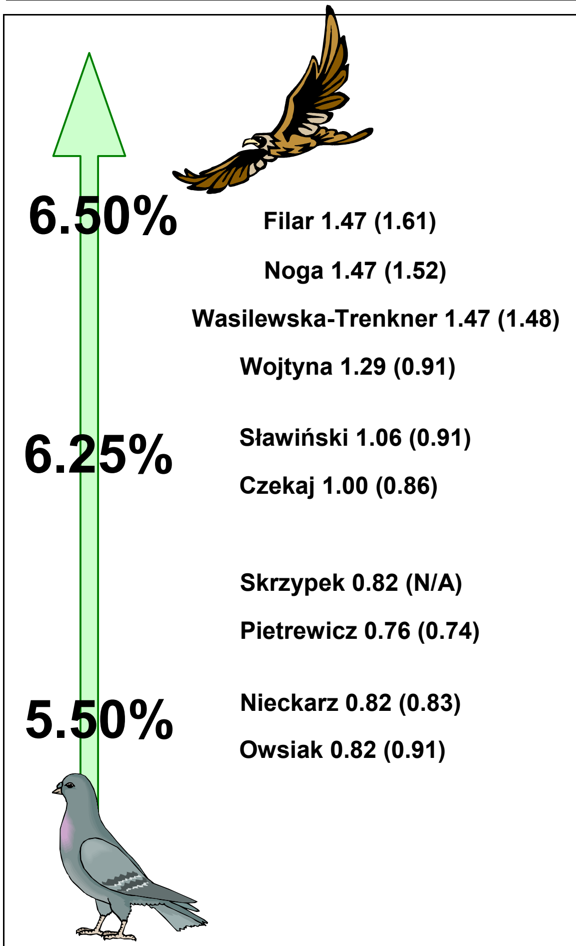
▪ The percentage of respondents expecting that prices will rise faster than now increased to 33.1%. Moreover, the percentage of people claiming that prices will rise as fast as now is still at a high level of 47.1%. The sum of these two answers (above 80%) is the highest since May 2004.

# Restrictiveness of the Monetary Policy (Council)




**MCI slightly down in August, more in September**

- After growth recorded at the beginning of the year, index of monetary policy restrictiveness saw slight drop in August.
- Despite the lack of changes in monetary policy parameters, money market rates dropped slightly and we expect their stabilisation in September.
- The weakening of the zloty was an additional factor responsible for the fall in MCI. Although, the zloty's rate was in August still stronger than equilibrium rate, this gap was smaller than that one in July. As we take in our calculations average month rates into account, affection of this factor will be even more clear in September, pointing at the slighter help from the foreign exchange market for Monetary Policy Council in its fight against the inflation.




Index is between 0 and 2. 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. Average of points for all votes is the value of the index for a given MPC member.

Numbers directly by the name are values of the index for period since the beginning of Sławomir Skrzypek's term as NBP governor and numbers in parentheses are values of the index for 2004-2006.

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.

**No change in restrictiveness but lower target rates**

As we wrote in the last month, it seemed that decision on rate hike was made unanimously in June. Confirmation of these expectations means, that our restrictiveness ranking of MPC members remained unchanged again. It will not happen until we include results from voting for the hike by 25bp in July (and probably in August either). On the basis of MPC member's comments, it seems however that data from the economy (rather world than Polish) affected the target rates perceived by them in 12 months. Even if they do not announce it directly, waiting for next data hawks would like to hike rates in a lower degree than previously, while doves start talking about the prospects of rate cuts.

**Hawks talk about one-two hikes**

In the last month, we wrote that Halina Wasilewska-Trenker said about the necessity of at least two rate hikes. Publications of another economic data however apparently decreased their scale. Though one should admit that Wasilewska-Trenkner's comments have been changeable recently. Before the publication of data for July, she said that it would not go without the hike, but "I'm less sure about that than a month ago, while the key reason of my hesitation is that what is happening in the oil and commodities market". Since that time, oil prices have dropped, and after GDP data we heard from her, that such a data are the ammunition for the hikes. Answering the question whether a single hike by 50bp is possible Halina Wasilewska-Trenker replied: "I could not rule that out". All in all, the best summary is that in her opinion one more hike is inevitable in this year. Dariusz Filar, Marian Noga and Andrzej Wojtyna gave comments in a similar tone, as they saw no reasons to delay hikes or even showed willingness to hike rates twice (Filar). Probably, they voted for a hike in August and will support such a motion in September.

**Doves want to wait and then cut.**

In the comments of MPC members at the opposite side of the restrictiveness index, opportunities for rate cuts have been appearing. Stanislaw Nieckarz said, that a period of at least stabilization of rates is necessary, while next year may bring opportunities for cuts. Stanislaw Owsiak could hardly imagine hikes if inflation and GDP growth started to decrease as deep scale of it might even require rate cuts (in 2009). Miroslaw Pietrewicz says rather about the stabilization, while NBP President Sławomir Skrzypek about the necessity of observing the situation in Poland and in the world.

**Czekaj and Sławiński: further hikes cannot be excluded**

As it is known, prof. Jan Czekaj and prof. Andrzej Sławiński are the key members to gain a majority in MPC. Financial markets should listen attentively to their opinions. Since the publication of the last report, we have dealt with their some comments, which one can consider as consistent with the statement of MPC, not ruling out further rate hikes dependent on the publications of next data.

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

# Government and politics

**Comments of government officials on the zloty strength:**

**Katarzyna Zajdel-Kurowska, deputy finance minister (TVN CNBC, 3 September):** We have been working on the scenario between 4.6 and 5.0% GDP growth in 2009 (..). In 2009, the mean year rate of the zloty against the euro may be similar to this currently observed.

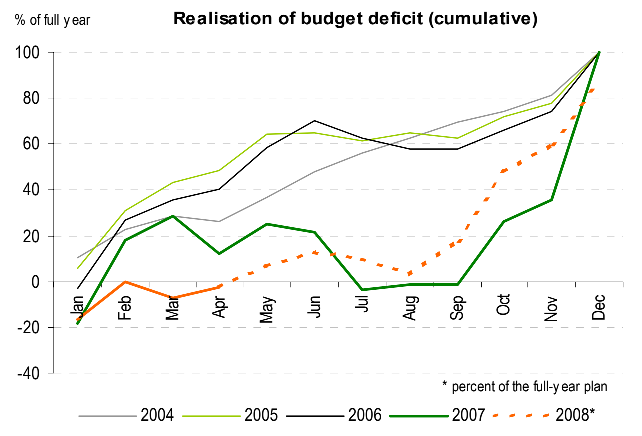
**Katarzyna Zajdel-Kurowska, deputy finance minister (Reuters, 1 September):** The balance of inflation risks has improved towards lower inflation. Taking the situation in the food and fuels markets into consideration, we see no need to change the forecast. It is realistic, taking also administrative prices into consideration. (…) In our assessment of the situation, the balance of risks is towards the lower GDP growth than we announced, but FinMin have not yet made a final decision on the dynamics and the structure. GDP might be lower than previously assumed 5%. Friday data from CSO on GDP structure affects the delay of such a forecast. (…) works on the macro assumption and the income side should be finished in this week.

## GDP forecast lower, inflation forecast unchanged

▪ A month ago we wrote that revision of the macroeconomic budgetary assumptions might took place at the turn of August and September. The Ministry of Finance claimed that work would be finished until 5 September, which was the cut-off date of this report. Possibly, the ministry was waiting for the approval of the government.

▪ According to *Rzeczpospolita* daily, FinMin revised GDP forecast to 4.8% from 5.0%. It would be a move in a good direction, though still not significantly enough to consider the forecast as conservative.

▪ At the same time, the ministry maintains optimistic estimate of annual average CPI inflation below 3%. Should inflation dropped to that level, accompanied by lower GDP growth, planned high budget incomes might be at risk.




## This year's budget exceedingly good

▪ The budget gap reached PLN2.7bln after July, which means that monthly surplus was noted. Moreover, according to the ministry, the budget gap was lower than PLN1bln after August.

▪ That means, that the budget gap is significantly below the value forecasted by FinMin some time ago. It is a result of unrealised expenditures (a dozen or so PLNbn), which is mainly driven by the use of EU funds below the plan. At the same time, incomes rise at a slower rate than assumed in the Budget Act (below 10%YoY against planned 19.5%). To some extent it was caused by lower flow of EU funds, however incomes from indirect taxes are also below the plan (9.3% in July against planned 12.7%).

▪ FinMin assumes, that budget gap will be at PLN20-24bn at the end of the year. We believe it will be closer to PLN24bn.

**Main aims of new act on public finances**

**1.** The strengthening and improvement of transparency of public finance sector (restriction in legal and organisational forms in the sector)

**2.** Introduction of Multi-year Financial Plan of the State and multi-year financial forecast in local governments units

**3.** Introduction of solutions in the area of task budget

**4.** Assumption of stable solutions, which help in conducting rational financial management in the state budget and budgets of local governments units.

**5.** Proposals of new regulations improving and strengthening the system of internal audit.

**6.** Strengthening of precautionary levels in the state budget and budgets of local governments units.

**7.** Introduction of changes in the management of EU funds and other funds from foreign non-returnable sources.

## New act on public finance sector

▪ The draft of Act on Public Finance stipulates changes in three main areas: change of precautionary measures concerning the level of public debt in relation to GDP introduction of the Multi-year Financial Plan (MFP), and changes in organisation of public finance sector.

▪ MFP will be prepared with four-year horizon, for both central government and local governments, and authorities would be obliged to set deficit for the next year at the level assumed in the MFP (except for particularly justified cases).

▪ In case of sector organisation, changes concern among others liquidation of subsidiary budgetary units and funds, introduction of task budget and strengthening the system of internal audit.

**If the public debt to GDP ratio exceeds:**

**1.** 47% but lower than 52% - in the draft of the Budget Act adopted by the government for the new budget year, budget gap cannot be higher than one resulting from the Budget Act for the current budget year,

**2.** 52% but lower than 55% - the government adopts the draft of the Budget Act, in which level of the difference between incomes and expenditures guarantees that the public debt to GDP ratio forecasted for the end of the budget year (which is concerned by the draft) will be lower than ratio announced until 31 May for the previous budget year. Moreover the draft of the Budget Act does not assume expenditures on new investments with unit values exceeding PLN500bn and period of realisation exceeding two years.

**3.** 55% but lower than 60% - the draft of the Budget Act does not assume any rise in the wages for workers in the state budget sector, expenditures on new investments, and restrain the indexation of retirements and pensions to the level of the growth of consumer goods and services prices for the previous budget year. It also imposes a ban on giving loans and credits from the state budget.

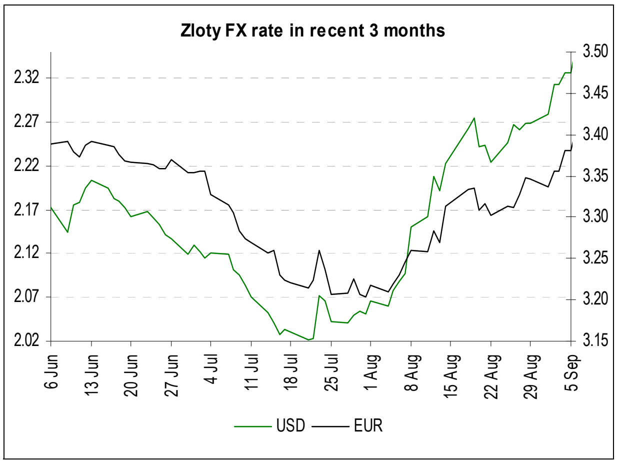
Source: Ministry of Finance, PAP, Reuters, own calculations

## New precautionary levels for the public debt

▪ The draft introduces two new precautionary levels at 47% and 52% instead of 50%. Should the level of 55% be exceeded, the government additionally checkups multi-year expenditures and investments. The last, constitutional fourth level (60%) requires restructuring plan, the lack of budget gap and lack guarantees for local governments.

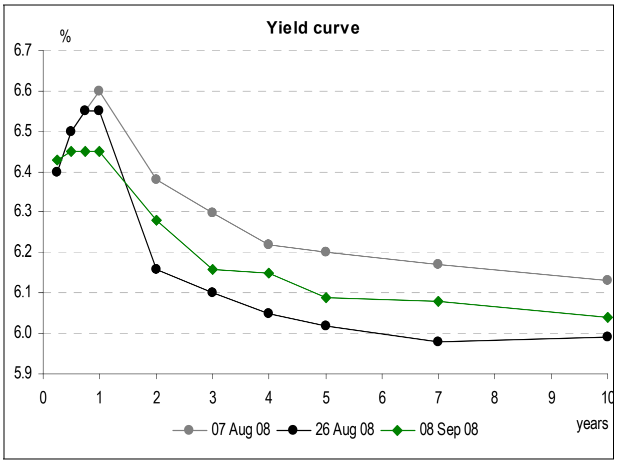
▪ Above mentioned changes are to increase Poland's credibility and reduce costs of public debt servicing (PLN500m in the first year and more later on). While such a scale of savings is hard to verify, we positively assess proposed changes and gradual tightening of restrictions for government after breaching consecutive thresholds. Increase in rationality of funds management, credibility, transparency and predictability of fiscal policy are positive as well.

# Market monitor



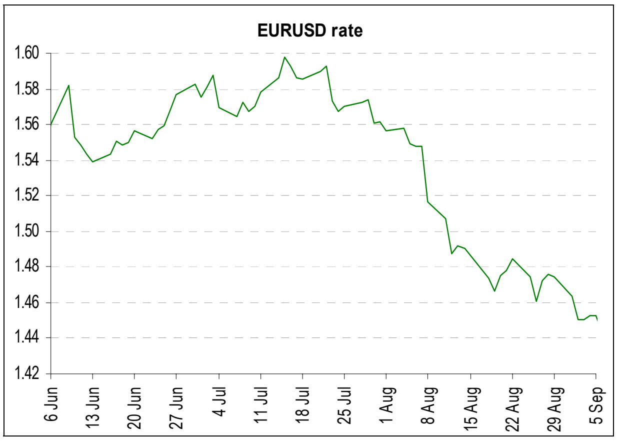

## Wave of zloty sell-off

- After reaching the record 3.20 level against the euro the zloty began weakening at the start of August and this tendency was fuelled at the start of September, when the EURPLN rate was approaching 3.50 and USDPLN was close to 2.50. The dollar appreciation against the euro was one of the main reasons, and this contributed to the weakening of the currencies in the region, including the zloty. The EURPLN rise since the start of August was the largest (ca. 9%) and the longest in two years.
- We perceive the current situation in the FX market was temporary. The prospects of the Polish economy did not change significantly in the last month and the zloty move is a correction after an excessive appreciation in July. This correction might have activated stop-losses additionally adding to market volatility. In our view the zloty should start recovering, though this can be restrained by any further dollar gains vs. the euro.



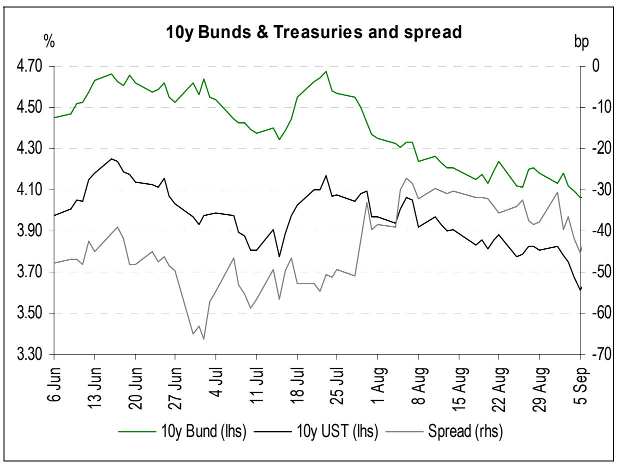

## Debt market continues to strengthen

- Last month in the domestic debt market yields fell by 10-15 bp across the curve with higher price increase at the longer end. The strengthening was driven by the situation in the core debt markets, on which a substantial strengthening was recorded. Other factors contributing to price increases included comments of the MPC members of softer tone, initial August inflation estimates of the FinMin and industrial output data that contributed to price gains.
- Taking into account our base scenario for next moves of the MPC we do not expect further substantial bond price increases. Amid considerations on economic growth prospects the activity indicators may be crucial for the market (possible fall of industrial output on annual basis). Inflation data will also be against market strengthening. The situation in core markets will be essential as well as foreign data, which gain in importance for the MPC.




## Abrupt dollar recovery

- In the last weeks further drop in oil prices was recorded even to ca. 100$ per barrel due to falling concerns over the negative effects of the Gustav hurricane and over deterioration of EU-Russia relations on Georgia conflict. This factor as well as higher fears over more significant economic slowdown also other economies other than US, resulted in heavy dollar recovery. Since the mid-July the EURUSD fell by 12.5%, and since mid-August by 8%.
- The dollar recovery came sooner than we thought. We maintain our view that in longer-term the dollar should gain in strength against the euro, though at slower pace (to 1.40 at the end of this year). In the nearest weeks there may be some correction of the EURUSD rate to the upside with possible return to 1.45, which is an important resistance level.

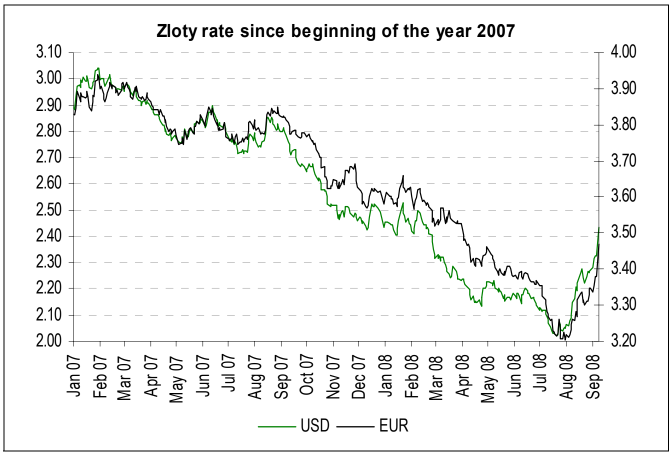


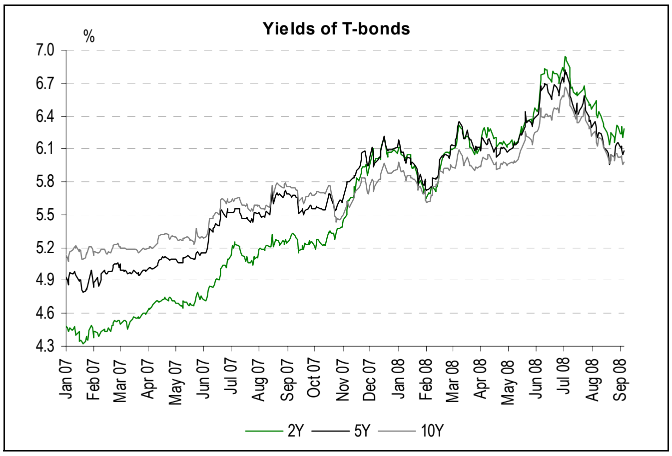

## Yields fall in the core debt markets

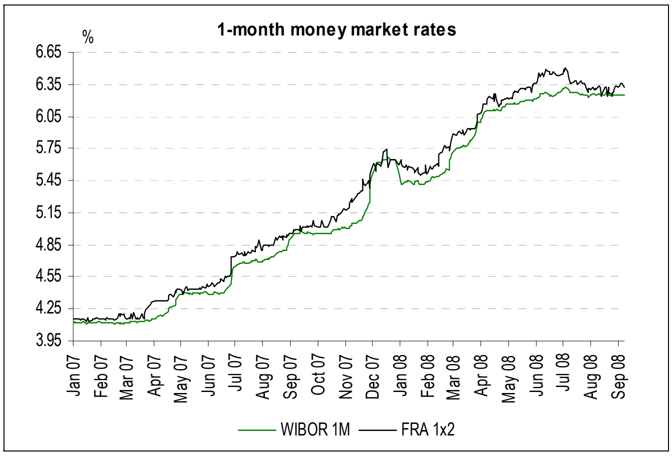
- Substantial strengthening was observed in the core debt markets. Yields of 10Y US Treasuries fell by 30 bp to 3.74%, and of Bunds by 25 bp to 4.07%. Bonds gains were fuelled by oil prices drops, which positively affected the inflation prospects, weak data from the US (among others from the labour market), negative news from the financial sector and declines in stock markets as well as weak figures from the euro zone (Ifo, lowered EMU's GDP forecasts).
- If inflation falls substantially influenced by lowering oil prices, then substantial economic growth weakening in the euro zone may result in some rate cuts by the ECB. Such prospect may result in further gradual decline of interest rates in the euro zone. In the United States the official interest rates may stay unchanged even till the end of the 2009, which should result in price rise also in the short term. The markets behaviour may be largely influenced by the developments of the situation in the oil market.

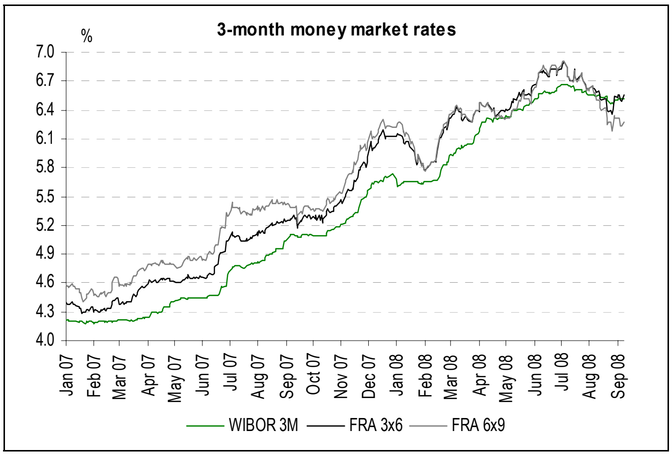
Source: Reuters, BZ WBK

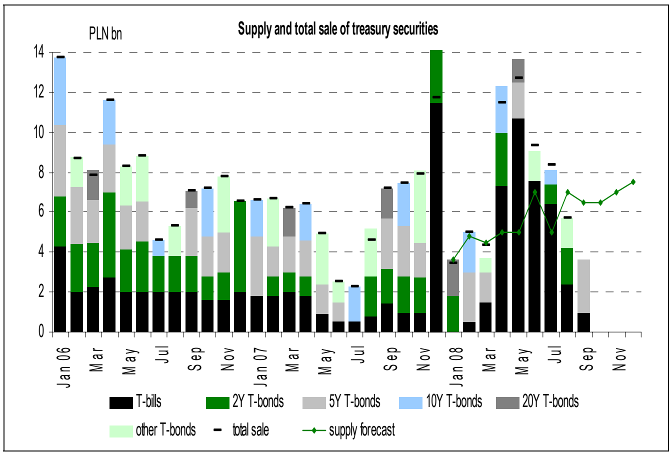
# Market monitor




**Treasury bill auctions (PLN m)**

| Date of auction | 52W | 26W | 13W | 5W | 3W | 2D |
|---|---|---|---|---|---|---|
| | | | (OFFER)*/SALE | | | |
| **09.06.2008** | 1400/1320 | - | 1400/1577 | - | - | - |
| **16.06.2008** | 1400/1443 | - | 1400/1449 | - | - | - |
| **07.07.2008** | 1200/965 | - | 500/709 | - | - | - |
| **14.07.2008** | 1200/1298 | - | 500/629 | - | - | - |
| **21.07.2008** | - | 1000/1000 | 500/500 | - | - | - |
| **28.07.2008** | - | 1000/1023 | 500/526 | - | - | - |
| **04.08.2008** | 1200/1200 | 1200/1200 | - | - | - | - |
| **11.08.2008** | 700/700 | 700/700 | - | - | - | - |
| **18.08.2008** | 500/500 | 500/500 | - | - | - | - |
| **01.09.2008** | 500/500 | 500/502 | - | - | - | - |
| **08.09.2008** | 500/500 | 500/500 | - | - | - | - |
| **15.09.2008** | (0-2000) | (0-2000) | - | - | - | - |
| **13.10.2008** | (0-2000) | (0-2000) | - | - | - | - |

** based on data of the Ministry of Finance*

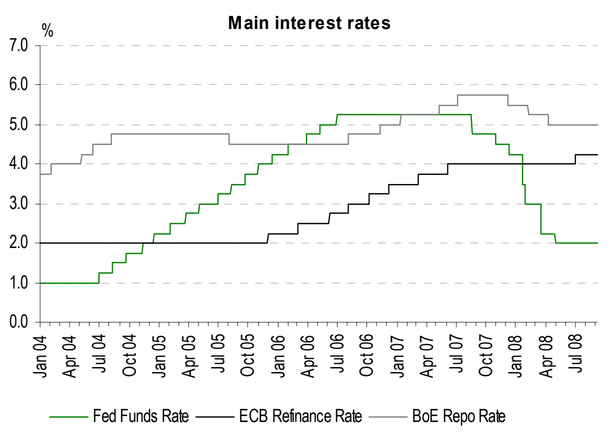
**Treasury bond auctions in 2008 (PLN m)**

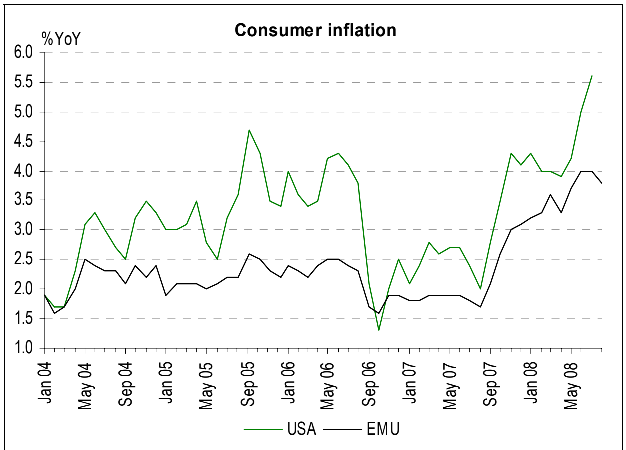
| month | First auction | | | | Second auction | | | | Switch auction | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | date | T-bonds | offer | sale | date | T-bonds | Offer | sale | date | T-bonds | sale |
| **January** | 02.01 | OK0710 | 1 800 | 1 655 | 09.01 | WS0922 | 1 800 | 1 800 | 16.01 | PS0413 / IZ0816 / WS0922 | 524 / 766 / 431 |
| **February** | 06.02 | PS0413 | 2 500 | 2 500 | 13.02 | DS1017 | 2 000 | 2 000 | 20.02 | WZ0816 / WZ1118 | 855 / 914 |
| **March** | 05.03 | PS0413 | 1 500 | 1 500 | 12.03 | WS0437 | 700 | 700 | 19.03 | PS0413/WZ0118/WS0922 | 1632/ 340 /369 |
| **April** | 02.04 | OK0710 | 2 700 | 2 700 | 09.04 | DS1017 | 2 300 | 1 208 | 16.04 | PS0413/DS1017 | 3399/2804 |
| **May** | 07.05 | PS0413 | 1 800 | 1 800 | 14.05 | WS0922 | 1 200 | 714 | 21.26 | OK0710/PS0413/DS1017 | 0/0/0 |
| **June** | 04.06 | IZ0816/WZ0118 | 500/1000 | 505/719 | - | - | - | - | 11.06 | no switch auction organised | |
| **July** | 02.07 | OK0710 | 1000 | 1000 | 09.07 | DS1017 | 700 | 705 | 23.07 | PS0413 | 1558 |
| **August** | 06.08 | OK0710 | 1 800 | 1 830 | 13.08 | WZ0118\|IZ0823 | 1 000 \| 500 | 1 000 \| 451 | 22.08 | DS1017 | 1244 |
| **September** | 03.09 | PS0413 | 2 640 | 2 640 | 10.09 | WS0429 | 1 000 | - | - | - | - |
| **October** | 01.10 | 5Y | - | - | 08.10 | 10Y | - | - | - | - | - |
| **November** | 05.11 | 5Y | - | - | 12.11 | 12YCPI\|10Yfloat | - | - | - | - | - |
| **December** | 03.12 | 2Y | - | - | - | - | - | - | - | - | - |

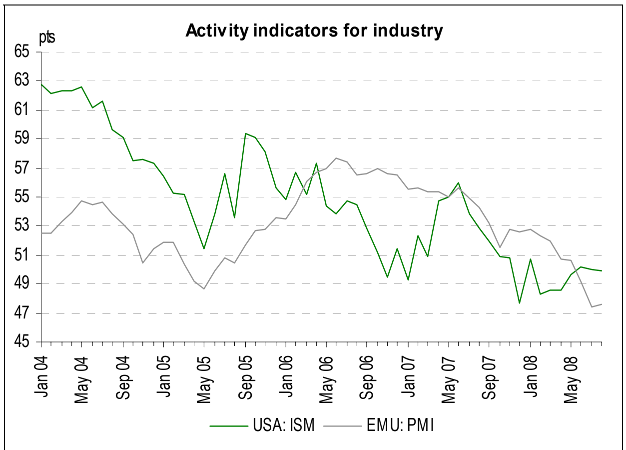
* with supplementary auction

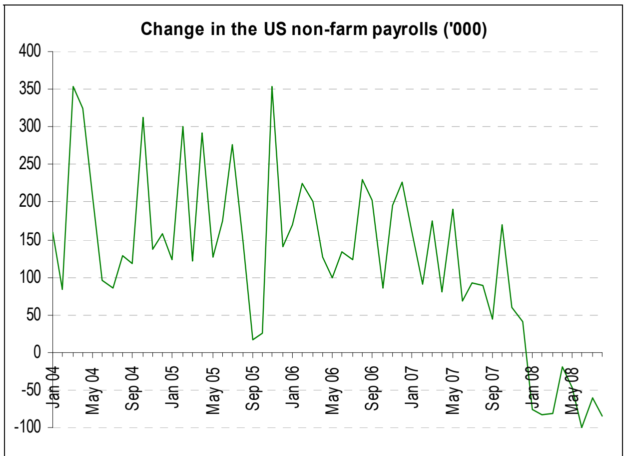
Source: Ministry of Finance, Reuters, BZ WBK

# International review




Source: Reuters, ECB, Federal Reserve

**Interest rates in the US and EMU unchanged**

▪ According to the minutes of the FOMC meeting on August 5, the US central bankers "generally anticipated that the next policy move would likely be a tightening". It was stated in the document that a part of the Fed members expressed concerns that the net inflation would not return to average levels, unless the monetary policy is tightened faster as compared to market expectations. Fed emphasised that everything will depend on the development of the situation in the financial markets and in the economy.

▪ As expected, the ECB left interest rates unchanged (reference rate at 4.25%). The tone of J.C. Trichet comments suggested little chances for rate cuts in the EMU in the nearest time. He underscored that a main objective of the ECB is maintaining price stability and preventing second round effects that may arise from persistently elevated inflation, particularly in the face of existing wage pressure.

**Drop in inflation in EMU, increase in the US**

▪ Final inflation data on HICP inflation in the euro zone for July showed slightly lower growth (4.0%YoY) than preliminary estimates (4.1%YoY). Core inflation remained at the level of 2.5%. According to preliminary forecasts for August inflation slowed down to 3.8%YoY, which could have been due to the significant drop in oil prices. PPI index rose by 1.1%MoM (9.0%YoY). However, ECB raised its inflation forecasts for 2008 and 2009 to 3.5%YoY and 2.6% from 3.4% and 2.4%.

▪ CPI in the US increased by 0.8%MoM (5.6%YoY) in July against market forecast of 0.4%. Core inflation was as expected at 0.3%MoM. PPI increased by 1.2%MoM (9.8%YoY – highest level in 27 years) against expectations at the level of 0.6%. Core PPI was also higher than forecasted (0.2%MoM) and noted rise by 0.7%MoM (3.5%YoY – highest in 17 years). The data confirmed rising cost pressure in the US economy.

**Weaker GDP forecasts in the EMU**

▪ According to Fed's Beige Book, the weakening of economic activity and maintaining price pressure was noted in most regions of the US in the last month. US ISM for industrial sector was only slightly worse than expected at 50pts and reached 49.9pts. The highest monthly drop in paid price index has been noted since October 2006. US ISM index of services activity rose to 50.6pts in August from 49.5pts from July. US GDP data for the second quarter were revised significantly upwards to 3.3%.

▪ Retail sales in Germany in July were weaker than forecasted (drop by 1.5%MoM against forecasts at –0.3%MoM). PMI in the industry for the euro zone increased to 47.6pts in August against 47.4pts in July, which is still close to 5 year lows. Components of the index pointed at the increase in the stock of finished goods index to the highest level since 1997. Data for services sector in the euro zone showed another contraction in activity though PMI index was higher than forecast and amounted to 48.5pts. Data on economic growth published by Eurostat confirmed the drop of GDP by 0.2%QoQ in the second quarter. In September ECB lowered its forecasts of economic growth to 1.4YoY and 1.2% from 1.8% and 1.5% in 2008 and 2009, respectively.

**Data from the US labour market disappointed**

▪ Data from the American labour market showed drop in non-farm payrolls by 85k in August against the expectations at -75k. Moreover data from two previous months were revised downwards by ca. 60'000. On the other hand. At the same time, unemployment rate increased to 6.1% against expected lack of changes from the level of 5.7%. Data from labour market in the US reflected worsening of the activity in the US economy.

# Economic calendar

| Monday | Tuesday | Wednesday | Thursday | Friday |
|---|---|---|---|---|
| **8**<br>***PL: Auction of Treasury Bills*** | **9**<br>US: Pending home sales (Jul)<br>US: Wholesale inventories (Jul) | **10**<br>***PL: Auction of 20Y bonds*** | **11**<br>US: Import prices (Aug)<br>US: Trade balance (Jul) | **12**<br>***PL: Balance of payments (Aug)***<br>***PL: Money supply (Aug)***<br>EZ: Industrial production (Jul)<br>US: PPI (Aug)<br>US: Retail sales (Aug)<br>US: Preliminary Michigan (Sep) |
| **15**<br>***PL: Auction of Treasury Bills***<br>***PL: CPI (Aug)***<br>***PL: Wages and employment (Aug)***<br>US: NY Fed index (Sep)<br>US: Capacity utilisation (Aug)<br>US: Industrial production (Aug) | **16**<br>DE: ZEW index (Sep)<br>EZ: Final HICP (Aug)<br>US: CPI (Aug)<br>US: Capital flows report (Jul)<br>US: Fed meeting - decision | **17**<br>US: House starts (Aug)<br>US: Build permits (Aug) | **18**<br>***PL: Industrial production (Aug)***<br>***PL: PPI (Aug)***<br>***PL: MPC minutes (Aug)***<br>JP: BoJ meeting – decision<br>CH: SNB meeting – decision<br>US: Leading indicators (Aug)<br>US: Philadelphia Fed index (Sep) | **19** |
| **22**<br>***PL: Core inflation (Aug)*** | **23**<br>***PL: Business climate (Sep)***<br>***PL: MPC meeting***<br>JP: Market holiday<br>EZ: Flash PMI – manufacturing sector (Aug)<br>EZ: Flash PMI – services sector (Aug) | **24**<br>***PL: MPC meeting – decision***<br>DE: Ifo index (Sep)<br>US: Home sales (Aug) | **25**<br>DE: Gfk index (Oct)<br>EZ: M3 money supply (Aug)<br>US: Durable goods orders (Aug)<br>US: New home sales (Aug) | **26**<br>***PL: Retail sales (Aug)***<br>***PL: Unemployment (Aug)***<br>US: Final GDP (Q2)<br>US: Core PCE (Q2)<br>US: GDP deflator (Q2)<br>US: Final Michigan (Sep) |
| **29**<br>EZ: Sentiment index (Sep)<br>US: Core PCE (Jul)<br>EZ: Flash HICP (Sep) | **30**<br>***PL: Balance of payments (Q2)***<br>US: Case/Shiller house price index<br>US: Chicago PMI (Sep)<br>US: Consumer confidence (Sep) | **1**<br>***PL: Auction of 5Y bonds***<br>EZ: PMI – manufacturing sector (Sep)<br>US: ADP report (Sep)<br>US: ISM – manufacturing sector (Sep) | **2**<br>EZ: PPI (Aug)<br>EZ: ECB decision<br>US: Factory orders (Aug) | **3**<br>EZ: PMI – services sector (Sep)<br>EZ: Retail sales (Aug)<br>US: Non-farm payrolls (Sep)<br>US: Unemployment (Sep)<br>US: ISM – services sector (Sep) |
| **6** | **7**<br>US: FOMC minutes | **8**<br>***PL: Auction of 10Y bonds***<br>JP: BoJ meeting- decision<br>EZ: Revised GDP (Q2)<br>US: Pending home sales (Aug) | **9**<br>GB: BoE meeting – decision<br>US: Wholesale inventories (Aug) | **10**<br>US: Import prices (Sep)<br>US: Trade balance (Aug) |

*Source: CSO, NBP, Finance Ministry, Reuters*

**MPC meetings and data release calendar for 2008**

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

* quarterly data, [a] preliminary data for January, [b] January and February, [c] November 2007

*Source: CSO, NBP*

# Economic data and forecasts

### Monthly economic indicators

| | | Aug 07 | Sep 07 | Oct 07 | Nov 07 | Dec 07 | Jan 08 | Feb 08 | Mar 08 | Apr 08 | May 08 | Jun 07 | Jul 08 | Aug 08 | Sep 08 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Industrial production | %YoY | 8.9 | 5.4 | 10.8 | 8.5 | 6.4 | 10.7 | 15.0 | 1.0 | 15.1 | 2.4 | 7.3 | 5.6 | 0.0 | 8.2 |
| Retail sales [c] | %YoY | 17.4 | 14.2 | 19.4 | 19.2 | 12.4 | 20.9 | 23.8 | 15.7 | 17.6 | 14.9 | 14.2 | 14.3 | 12.0 | 16.1 |
| Unemployment rate | % | 11.9 | 11.6 | 11.3 | 11.2 | 11.4 | 11.7 | 11.5 | 11.1 | 10.5 | 10.0 | 9.6 | 9.4 | 9.3 | 9.2 |
| Gross wages [b c] | %YoY | 10.5 | 9.5 | 11.0 | 12.0 | 7.2 | 11.5 | 12.8 | 10.2 | 12.6 | 10.5 | 12.0 | 11.6 | 11.0 | 12.9 |
| Employment [b] | %YoY | 4.8 | 4.7 | 5.0 | 5.0 | 4.9 | 5.9 | 5.9 | 5.8 | 5.6 | 5.4 | 4.8 | 4.7 | 4.4 | 4.3 |
| Export (€) [d] | %YoY | 14.9 | 8.2 | 13.5 | 13.1 | 8.7 | 23.2 | 30.2 | 12.0 | 33.9 | 12.0 | 16.1 | 13.5 | 5.1 | 15.9 |
| Import (€) [d] | %YoY | 13.4 | 13.7 | 17.7 | 15.4 | 15.4 | 18.7 | 32.5 | 13.9 | 31.8 | 14.2 | 20.2 | 15.2 | 17.4 | 19.1 |
| Trade balance [d] | EURm | -472 | -917 | -859 | -783 | -1645 | -535 | -840 | -1402 | -1075 | -1280 | -1706 | -1643 | -1615 | -1381 |
| Current account balance [d] | EURm | -576 | -546 | -1183 | -67 | -2061 | -962 | -1347 | -1738 | -1455 | -1673 | -2292 | -1693 | -1915 | -1406 |
| Current account balance [d] | % GDP | -3.6 | -3.8 | -3.8 | -3.5 | -3.7 | -3.7 | -3.8 | -4.1 | -4.2 | -4.3 | -4.5 | -4.5 | -4.8 | -5.0 |
| Budget deficit (cumulative) | PLNbn | 0.3 | 0.2 | -4.4 | -6.0 | -16.9 | 4.4 | 0.0 | 1.9 | 0.6 | -1.9 | -3.5 | -2.7 | -0.9 | -4.8 |
| Budget deficit (cumulative) [e] | % of FY plan | -1.6 | -1.2 | 26.2 | 35.5 | 100.0 | -16.4 | -0.1 | -6.9 | -2.2 | 6.8 | 12.8 | 9.9 | 3.2 | 17.8 |
| CPI | %YoY | 1.5 | 2.3 | 3.0 | 3.6 | 4.0 | 4.0 | 4.2 | 4.1 | 4.0 | 4.4 | 4.6 | 4.8 | 5.1 | 4.7 |
| PPI | %YoY | 1.8 | 1.8 | 2.0 | 2.5 | 2.3 | 2.9 | 3.2 | 2.9 | 2.5 | 2.7 | 2.6 | 2.3 | 2.1 | 2.2 |
| Broad money (M3) | %YoY | 16.1 | 14.4 | 13.8 | 13.6 | 13.4 | 12.9 | 13.5 | 13.6 | 15.0 | 15.1 | 16.3 | 16.5 | 16.0 | 16.4 |
| Deposits | %YoY | 16.3 | 15.4 | 15.2 | 15.1 | 14.5 | 14.3 | 14.7 | 15.3 | 16.7 | 17.4 | 18.5 | 19.3 | 18.7 | 18.3 |
| Loans | %YoY | 31.1 | 31.0 | 30.6 | 30.1 | 30.0 | 30.3 | 29.5 | 29.7 | 28.3 | 27.6 | 27.7 | 25.2 | 25.0 | 24.9 |
| USD/PLN | PLN | 2.80 | 2.73 | 2.61 | 2.49 | 2.47 | 2.46 | 2.43 | 2.28 | 2.19 | 2.19 | 2.17 | 2.07 | 2.19 | 2.35 |
| EUR/PLN | PLN | 3.81 | 3.79 | 3.71 | 3.66 | 3.60 | 3.61 | 3.58 | 3.54 | 3.45 | 3.40 | 3.37 | 3.26 | 3.29 | 3.39 |
| Reference rate [a] | % | 4.75 | 4.75 | 4.75 | 5.00 | 5.00 | 5.25 | 5.50 | 5.75 | 5.75 | 5.75 | 6.00 | 6.00 | 6.00 | 6.00 |
| Lombard rate [a] | % | 6.25 | 6.25 | 6.25 | 6.50 | 6.50 | 6.75 | 7.00 | 7.25 | 7.25 | 7.25 | 7.50 | 7.50 | 7.50 | 7.50 |
| WIBOR 3M | % | 4.80 | 5.09 | 5.13 | 5.36 | 5.67 | 5.64 | 5.74 | 6.03 | 6.29 | 6.41 | 6.58 | 6.62 | 6.52 | 6.50 |
| Yield on 52-week T-bills | % | 4.80 | 5.01 | 5.04 | 5.30 | 5.78 | 5.75 | 5.66 | 6.09 | 6.10 | 6.10 | 6.63 | 6.70 | 6.60 | 6.50 |
| Yield on 2-year T-bonds | % | 5.23 | 5.25 | 5.30 | 5.77 | 6.06 | 5.92 | 5.90 | 6.17 | 6.20 | 6.27 | 6.73 | 6.66 | 6.32 | 6.30 |
| Yield on 5-year T-bonds | % | 5.61 | 5.60 | 5.59 | 5.90 | 6.07 | 5.94 | 5.93 | 6.20 | 6.12 | 6.25 | 6.62 | 6.53 | 6.15 | 6.10 |
| Yield on 10-year T-bonds | % | 5.68 | 5.69 | 5.64 | 5.70 | 5.85 | 5.81 | 5.82 | 5.98 | 5.98 | 6.10 | 6.41 | 6.43 | 6.10 | 6.05 |

*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

| | | 2006 | 2007 | 2008 | 2009 | 1Q07 | 2Q07 | 3Q07 | 4Q07 | 1Q08 | 2Q08 | 3Q08 | 4Q08 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| GDP | PLNbn | 1 060.0 | 1 167.8 | 1 280.1 | 1 387.3 | 267.7 | 281.5 | 288.5 | 330.1 | 294.1 | 308.5 | 316.9 | 360.7 |
| GDP | %YoY | 6.2 | 6.6 | 5.3 | 4.5 | 7.3 | 6.5 | 6.5 | 6.4 | 6.1 | 5.8 | 4.8 | 4.8 |
| Domestic demand | %YoY | 7.3 | 8.3 | 6.4 | 6.3 | 9.3 | 9.2 | 8.4 | 6.5 | 6.3 | 6.2 | 6.5 | 6.7 |
| Private consumption | %YoY | 5.0 | 5.0 | 5.5 | 5.5 | 6.8 | 4.9 | 4.8 | 3.6 | 5.6 | 5.6 | 5.5 | 5.5 |
| Fixed investments | %YoY | 14.9 | 17.6 | 13.2 | 11.4 | 23.8 | 19.0 | 16.7 | 15.2 | 15.7 | 15.2 | 13.5 | 11.0 |
| Industrial production | %YoY | 12.5 | 9.7 | 6.7 | 6.1 | 13.0 | 8.5 | 8.1 | 9.6 | 8.5 | 8.5 | 4.6 | 5.0 |
| Retail sales (real terms) | %YoY | 11.9 | 14.0 | 11.8 | 11.8 | 17.4 | 14.1 | 12.8 | 12.2 | 16.0 | 11.1 | 9.8 | 10.5 |
| Unemployment rate [a] | % | 14.8 | 11.4 | 9.5 | 8.0 | 14.3 | 12.3 | 11.6 | 11.4 | 11.1 | 9.6 | 9.2 | 9.5 |
| Gross wages (real terms) [c] | %YoY | 4.2 | 6.7 | 6.6 | 4.9 | 5.9 | 6.5 | 8.1 | 6.5 | 7.2 | 7.7 | 6.6 | 5.5 |
| Employment [c] | %YoY | 3.2 | 4.6 | 4.8 | 2.6 | 4.2 | 4.5 | 4.8 | 5.0 | 5.9 | 5.2 | 4.5 | 3.8 |
| Export (€) [b] | %YoY | 20.4 | 12.8 | 15.0 | 6.0 | 13.4 | 12.7 | 13.1 | 12.0 | 21.3 | 20.4 | 11.6 | 8.0 |
| Import (€) [b] | %YoY | 24.0 | 17.9 | 18.0 | 11.0 | 19.5 | 19.7 | 16.6 | 16.2 | 21.1 | 21.9 | 17.3 | 12.5 |
| Trade balance [b] | EURm | -5 539 | -11 311 | -16 444 | -24 336 | -2 322 | -3 029 | -2 684 | -3 276 | -2 769 | -4 061 | -4 639 | -4 975 |
| Current account balance [b] | EURm | -7 283 | -11 577 | -20 197 | -28 489 | -2 468 | -3 434 | -2 376 | -3 299 | -4 038 | -5 420 | -5 014 | -5 725 |
| Current account balance [b] | % GDP | -2.7 | -3.8 | -5.4 | -6.9 | -2.9 | -3.5 | -3.8 | -3.7 | -4.1 | -4.5 | -5.0 | -5.4 |
| Budget deficit (cumulative) [a] | PLNbn | -25.1 | -16.9 | -23.6 | -18.2 | -4.8 | -3.7 | 0.2 | -16.9 | 1.9 | -3.5 | -4.8 | -23.6 |
| Budget deficit (cumulative) [a] | % GDP | -2.4 | -1.4 | -1.8 | -1.3 | - | - | - | - | - | - | - | - |
| CPI | %YoY | 1.0 | 2.5 | 4.4 | 3.7 | 2.0 | 2.4 | 2.0 | 3.5 | 4.1 | 4.3 | 4.9 | 4.2 |
| CPI [a] | %YoY | 1.4 | 4.0 | 4.1 | 3.6 | 2.5 | 2.6 | 2.3 | 4.0 | 4.1 | 4.6 | 4.7 | 4.1 |
| PPI | %YoY | 2.5 | 2.3 | 2.7 | 3.2 | 3.3 | 2.0 | 1.7 | 2.3 | 3.0 | 2.6 | 2.2 | 3.1 |
| Broad money (M3) [a] | %YoY | 16.0 | 13.4 | 13.9 | 10.5 | 18.0 | 14.7 | 14.4 | 13.4 | 13.6 | 16.3 | 16.4 | 13.9 |
| Deposits [a] | %YoY | 15.2 | 14.5 | 15.0 | 10.0 | 17.7 | 15.2 | 15.4 | 14.5 | 15.3 | 18.5 | 18.3 | 15.0 |
| Loans [a] | %YoY | 23.4 | 30.0 | 21.1 | 13.8 | 26.8 | 29.2 | 31.0 | 30.0 | 29.7 | 27.7 | 24.9 | 21.1 |
| USD/PLN | PLN | 3.10 | 2.77 | 2.28 | 2.39 | 2.97 | 2.82 | 2.76 | 2.52 | 2.39 | 2.18 | 2.21 | 2.36 |
| EUR/PLN | PLN | 3.90 | 3.78 | 3.41 | 3.34 | 3.89 | 3.80 | 3.79 | 3.65 | 3.58 | 3.41 | 3.31 | 3.34 |
| Reference rate [a] | % | 4.00 | 5.00 | 6.25 | 6.25 | 4.00 | 4.50 | 4.75 | 5.00 | 5.75 | 6.00 | 6.00 | 6.25 |
| Lombard rate [a] | % | 5.50 | 6.50 | 7.75 | 7.75 | 5.50 | 6.00 | 6.25 | 6.50 | 7.25 | 7.50 | 7.50 | 7.75 |
| WIBOR 3M | % | 4.21 | 4.73 | 6.36 | 6.52 | 4.20 | 4.42 | 4.89 | 5.39 | 5.80 | 6.43 | 6.55 | 6.68 |
| Yield on 52-week T-bills | % | 4.18 | 4.69 | 6.25 | 6.20 | 4.14 | 4.40 | 4.84 | 5.37 | 5.84 | 6.28 | 6.60 | 6.30 |
| Yield on 2-year T-bonds | % | 4.57 | 5.23 | 6.28 | 6.14 | 4.47 | 4.78 | 5.21 | 5.71 | 5.99 | 6.40 | 6.43 | 6.30 |
| Yield on 5-year T-bonds | % | 5.03 | 5.52 | 6.20 | 6.10 | 4.95 | 5.19 | 5.57 | 5.85 | 6.02 | 6.33 | 6.26 | 6.20 |
| Yield on 10-year T-bonds | % | 5.22 | 5.56 | 6.08 | 6.03 | 5.17 | 5.36 | 5.66 | 5.73 | 5.87 | 6.16 | 6.19 | 6.10 |

*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

Bank Zachodni WBK

This analysis is based on information available until 05.09.2008 has been prepared by:

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