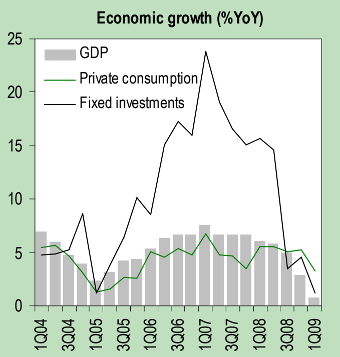
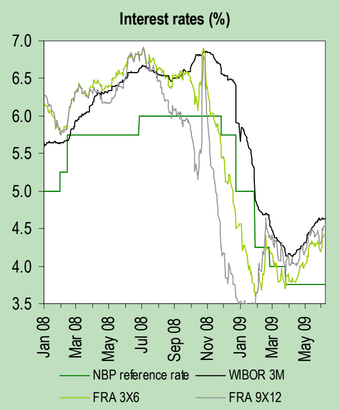
Bank Zachodni WBK

MACROscope

Polish Economy and Financial Markets

June 2009





In this issue:

Maciej Reluga
Chief economist
+48 22 586 8363

Piotr Bielski
+48 22 586 8333

Piotr Bujak
+48 22 586 8341

Cezary Chrapek
+48 22 586 8342

Email: ekonomia@bzwbk.pl

Looking for the bottom

- **GDP growth in Q1 was more or less as we expected and despite positive surprises in investments and consumption we uphold the view that the economic slowdown will continue in Q2 and Q3.** In this period, activity indicators are likely to deteriorate further, but they also may signal some stabilisation of business climate. Our projection for 0.5% GDP growth throughout the year (revised downward after changes in the projection for the euro zone to -5%) shows that slowdown to the region of 0% in Q2-Q3 will be followed by slight acceleration of up to ca. 1% at the turn of 2009. It would mean that the economic cycle would reach the bottom approximately in the middle of this year and then a moderate recovery will be a consequence of a similar trend among key trade partners (and keener competition following PLN depreciation).
- **In our view, revival in investments will happen much later and we expect their decline in the upcoming quarters.** In this month's *Special Focus*, we give a special coverage to investments.
- **As regards inflation, a reverse trend is visible and it seems that this year's inflation peak is behind us.** While effects of growth in energy prices at the beginning of the year and in food prices will be still reflected in 12-month CPI, a medium-term downward trend should persist. In other words, it will take many months to see the bottom of inflation rate in Poland largely due to plunge in economic demand.
- **In effect, we expect the Monetary Policy Council to respond and further reduce interest rates.** The Council's decision in June will primarily depend on new NBP's projection for inflation and GDP. A previous projection published in February justified lower interest rates (a slow economic growth pace and low inflation) and since then the economy has declined and inflation has risen only due to external factors. In our view, it is too early to adopt a neutral bias in the monetary policy as suggested by some of the Council members, which would mean a possibility of approaching to the bottom in this cycle of interest rate reductions. Although even with the neutral bias further reductions would be possible, then the risk of our scenario which predicts a reference rate fall to 3% would increase.
- **Developments on the financial market were roughly in line with our expectations in the previous month.** The zloty weakened with an important band of resistance in the region of 4.50, however, the resistance was broken down as a result of concerns that the Latvian lat would be devalued. Also yields of government's treasuries initially grew, but began to decrease in the middle of May.

Financial market on 29 May 2009:

NBP deposit rate	2.25	WIBOR 3M	4.62	USDPLN	3.1812
NBP reference rate	3.75	Yield on 2-year T-bonds	5.46	EURPLN	4.4588
NBP lombard rate	5.25	Yield on 5-year T-bonds	5.78	EURUSD	1.4016

This report is based on information available until 08.06.2009

Special focus

Uncertain investments

The domestic GDP data for Q1 came in as a positive surprise. In fact, the GDP growth was not much of a surprise, but the breakdown of the growth was (see the *Polish Economy* section for more details). Gross fixed investments were one of the most surprising element of the GDP as they recorded a growth of 1.2%YoY instead of the widely expected decline. In this edition of MACROscope we take a closer look at this element of the national accounts, its behaviour over the past quarters, and attempt to estimate the equation of the aggregate gross fixed investments.

Fixed investments tend to surprise

The performance of fixed investments was much surprising not only in Q1 2009, but also in the last quarters of the previous year. First, the growth of investments decelerated in Q3 more notably than expected, to 3.5%YoY from ca. 15%YoY in the first two quarters of 2008. The investment data from the biggest enterprises (employing more than 49 people) even pointed to the nominal fall in investments in the period from July to September, that is before the global crisis intensified. One could reasonably expect that the next quarters could bring all but deterioration. However, then came the positively surprising data for Q4 2008 as the growth of investments reached 4.6%YoY.

Gross fixed investments are known to be a very volatile element of the GDP. The definition provided by the Central Statistical Office (GUS) says that these are the expenditures that increase the value of fixed assets and which are spent on property, machinery and equipment, intangible assets and maintenance of fixed assets. Gross fixed investments are one of those categories of the national accounts which carry the highest degree of uncertainty[1]. This particularly refers to capital expenditures in the sector of enterprises employing fewer than 50 people and in the household sector. Data for the investments made by the enterprises employing from 10 to 50 people are gathered only twice a year (for Q2 and Q4), while no data are gathered for the fixed investments made by the legal persons with fewer than 10 employees. For such entities only rough estimates are made based on the analysis of expenses of the businesses with 10 to 15 employees and results of the business activity surveys conducted among the businesses with fewer than 10 employees (for the past two years). Estimates for the natural persons who employ fewer than 10 people are prepared in an analogous way and they are reflected in the calculation of household investments. What is more, statistical research of the stats office regarding fixed investments is troubled by the inability to define precisely whether a particular expense is to be treated as an investment or current use. Enterprises may classify their expenses differently in different periods, depending on what classification is more favourable tax-wise at the particular point in time. Moreover, many investments take place in the grey economy, which size is estimated only once a year, which additionally increases uncertainty around the investment estimates, particularly the quarterly ones. The large participation of the grey economy in the gross fixed investments, notwithstanding other factors, shows the importance of expert estimates (rather than hard data) in measurements of the investment activity.

Table 1. Share of grey economy in GDP and its main components in 2000-2006

	GDP	Gross fixed investments	Private consumption in households sector
2000	14.5%	18.6%	3.3%
2001	14.4%	16.9%	3.3%
2002	13.3%	19.3%	4.4%
2003	13.6%	18.7%	4.5%
2004	12.7%	18.8%	4.6%
2005	13.7%	20.3%	4.6%
2006	13.7%	19.3%	4.8%

Source: „National Accounts by Institutional Sectors and Sub-Sectors 2000-2006", Central Statistical Office, Warsaw, July 2008

Additional concerns about the quality of investment data arise from the vague procedures relating to the "balancing" of GDP from the production side (gross added value) with the GDP estimates from the demand side (consumption, accumulation, net exports). In practice, estimates in both approaches are different and there are discrepancies, which have to be eliminated. As a part of such procedure, there may be arbitrary changes in estimates of fixed investments. Another factor which adds to the uncertainty of estimates of real value of different categories of the national accounts, and investments in particular, is the low precision of the deflators (price indices). Deflators are imprecise in relation to many elements of the gross fixed investments, e.g. machinery & equipment, transport equipment, building and structures, as they are characterised by a significant internal assortment variability.

What affects aggregated investments?

Empirical researches for many countries show that it is difficult to explain and predict the variability of the aggregate investment. For instance, while developing the

[1] Other estimates which are deemed highly uncertain include the income from self-employment, change in inventories and the size of the grey economy.

original design of the ECMOD model used by NBP to prepare projections for inflation and GDP in the years 2005-2008, it was noted that estimation of the investment equation is extremely difficult and the estimation of cointegrating relation (i.e. estimation of the long-run relationship between variables) was abandoned and replaced by the theoretical relationship corresponding to the overall depiction of the supply side in the model[2]. One of the reasons for the difficulties in estimating the aggregated investments is the fact that this is a highly heterogeneous category of national accounts. In such a case, data aggregation gives rise to the risk of neutralisation of the effects occurring at the lower level of aggregation, particularly when these effects have different directions[3].

Our econometric analysis confirms that the estimation of the equation of aggregated investments in the Polish economy is very difficult. To some degree this might be connected with the above-mentioned issues concerning the quality and uncertainty of data on the gross fixed investments. After the unsuccessful attempts at estimation of the cointegrating relation, we decided to estimate the simple equation, which is possibly best-fitted to the available data and which precisely describes the behaviour of investments in the short-term.

Our calculations started with assessing what factors really determine the investment activity in the Polish economy. Theoretical models tend to focus on the expected return on investment and the cost of capital. For this reason, the real interest rate is proposed as a factor that is key to determining the investment activity. Additionally, noting that the investment activity may be restrained by not so much the cost of capital, but availability of capital, the investment activity analysis should check the effect of such variables as bank credit and inflow of foreign capital. However, it seems that in practice the issue of the return on capital as well as the cost and availability of capital might be dominated by the expectations of businesses regarding their future sales. For this reason, our analysis takes into account the element of expectations and moods reflected in such variables as total revenues of enterprises, overall business climate indicator published by stats office, the PMI index and WIG20 index. The first variable allows us to capture both the current demand for products and the adaptive expectations regarding the future demand, as well as the financial health of companies, which has a decisive impact on funding investments from own funds and affects the possibility of gaining external finance. Sales revenues may be a better measure of the outlook for demand and financial position than the net profit as sales revenues are not influenced by any temporary adjustments in the business operation costs. When assessing investment activity, it is also important to take into account the level of uncertainty around the economic environment, with CPI being the common uncertainty measure here. A factor we also looked at is the real effective exchange rate. This factor affects the enterprises' assessment of profitability of the investments into the foreign sales, but only at the assumption that a change in the exchange rate is considered as permanent by enterprises. Also, the analysis considers the use of production capacity which defines the needs of enterprises with regard to expand their production potential. On top of that, we took account of the global cost shock, i.e. the changes in the relative price level abroad and locally determined by the relation between the oil prices and the prices of domestic goods and services. The variables used in estimation of the investment equation also include the dummy variable to account for the effect of the substantial reduction in the personal income tax in January 2004 and Poland's EU accession in May 2004 as these two events might have significantly affected profitability of different investment projects. Definitions of the variables used in the our analysis and details of our estimates are presented in the *Technical Appendix.*

What matters is revenues and the capacity utilisation

In our econometric analysis we designed equations using different variables described above as the potential determinants of the investment activity in Poland. When assessing the statistical properties of the particular equations and testing forecasts *ex post*, we identified the equation which seems to best reflect the mechanisms currently affecting aggregate investment in the Polish economy.

Our equation relates gross fixed investments to total business revenues and the degree of utilisation of production capacity in the industry. The estimated parameters of such equation show that a 1pp increase/decrease in the annual growth of total revenues of enterprises increases/reduces the real growth of gross fixed investments by 0.86pp, while 1pp annual increase/decrease in production capacity in the industry reduces the real growth of gross fixed investments by 0.23pp.

Obviously, when assessing these elasticises one should note that the precision and reliability of their estimation is limited due to the lack of knowledge about the cointegrating relation of the variables and the low number of observations on which the equation was estimated. Also,

[2] The condition for optimisation of enterprises' profits in the Cobb-Douglas production function.

[3] For more discussion on this issue, please see for example *Aggregate investment*, Ricardo J. Caballero, NBER Working Paper 6264, November 1997.

the equation was estimated using the data from the period before the global crisis intensified (until Q3 2008). One may expect that with the growth of the overall uncertainty about the further development of the crisis in next quarters, the parameters of the estimated investment function changed significantly (although the estimations made for a sample extended by one and two quarters seem not to confirm this), and perhaps a change will be needed to the specification of the estimated investment function. For example, assuming that the meltdown in the credit markets lies at the core of the current global crisis, bank credit and/or inflow of foreign capital might prove to be more relevant factors in explaining the changes in investment activity. Econometric verification of this hypothesis will require a certain number of new observations of variables.

Noting all the concerns about the estimated investment equation and the fact that a significant revision of data might undermine reliability of the equation, one may decide that currently the equation seems to be a fairly good tool for short-term projections of gross fixed investments. This is suggested by the fact that the ex post projections prepared based on this equation quite accurately show the extent of the real investments growth deceleration in the second half of 2008 (although they overrate this growth for Q3 2008 and underrate it in Q4 2008), while the projection for the investments growth in Q1 2009 at 0.6%YoY is very close to the data officially published by stats office (1.2%YoY).

The projection for Q2, reflecting the already published official data on the use of production capacity in Q2 (decrease to 69.2%, i.e. by 10.9pp on the year) and the assumed decelerated growth of total revenues of enterprises in this period (to 0%YoY), points to the moderate real decrease in gross fixed investments by 1.7%YoY. Assuming that the growth of revenues of businesses will lower to –5%, the forecasted decrease in investments in Q2 is 4.3%YoY.

Why the worst has not come to worst?

The progress of the investment activity slowdown to date and the projection for Q2 this year prepared on the basis of our estimated equation indicate that despite the rapid deceleration of the global economy, the growth of gross fixed investments has not fallen significantly.

Trying to explain this phenomenon, one must note that gross fixed investments are a highly heterogeneous category. In other words, the analysis of investment activity may be supported by the breakdown of gross fixed investments into the following six types of investment expenditures: agriculture, forestry, fisheries and aquaculture, machinery and equipment, transport equipment, housing construction, other construction and other investments. Data in such a structure are published by Eurostat for a period starting in Q1 2004.

Table 2. Structure of nominal gross fixed investments in Poland

Share in %	2004	2005	2006	2007	2008
Agriculture, forestry, fisheries and aquaculture	0.1	0.3	0.0	0.2	0.1
Metal products and machinery	29.6	30.0	29.6	29.2	28.8
Transport equipment	9.8	9.6	10.2	10.3	10.3
Construction work: housing	14.4	14.9	14.2	13.7	14.2
Construction work: other constructions	42.4	42.2	42.4	42.9	42.5
Other products	3.8	3.2	3.6	3.8	4.0

Source: Eurostat, own calculations

Table 3. Nominal growth rate of gross fixed investments with breakdown by types

Growth rate in %YoY	1Q08	2Q08	3Q08	4Q08
Total gross fixed investments	17.8	18.7	6.1	5.3
Agriculture, forestry, fisheries and aquaculture	10.0	3.9	3.1	-0.6
Metal products and machinery	14.3	18.7	3.9	1.2
Transport equipment	27.8	18.7	-2.1	3.1
Construction work: housing	21.8	27.3	9.5	1.1
Construction work: other constructions	12.9	16.5	7.5	8.9
Other products	59.8	5.9	18.3	6.3

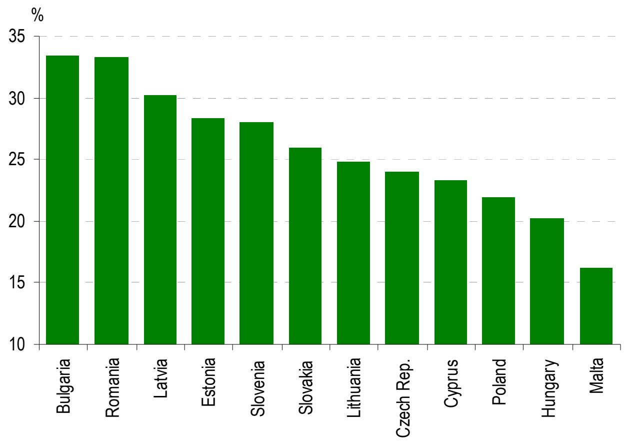
Source: Eurostat, own calculations

The data contained in the tables above show that outlays on other construction has decisively the highest share in total fixed investment over the last years. At the same time, the growth of this type of investments has been slowing over the recent quarters to a relatively small degree, which is connected with the long cycle of realisation of such investments. The relatively moderate deceleration of investments growth in the category of other construction also results from the fact that this item includes structural investments which value increases as a result of the use of EU funds. All in all, it seems that the relatively moderate lowering of investment outlays growth in the category of other construction, with its large share in total fixed investment, explains to a large extent quite slow descent of the total fixed investment growth rate.

At the same time, looking at data in tables 2 and 3 it should be noted that the significant reduction in the investment activity largely took place already in Q3 2008, i.e. before intensification of the global financial and economic crisis. Out of the 4 main types of investments (in terms of weight in total investments), this particularly relates to the spending on machinery and equipment, and transport equipment. The significant weakening of the investment activity in those areas already in Q3 2008 may be traced back to the first half of 2008 which saw a significant reduction in business revenues and decreased utilisation of production capacity and to the third quarter of 2008 when exports growth slowed down and availability of bank financing was restricted. In effect, the scale of the necessary reduction in the investment activity in the next quarters may be relatively lower, although this does not mean that we will not see negative growth rates of gross fixed investment.

Coming back to aggregate gross fixed investments, one should note the relatively low investment-to-GDP ratio in Poland. In 2008, out of the twelve new EU member states, only Malta and Hungary recorded a lower investment ratio than Poland (see the chart below). This might imply that the scale of the cyclical overinvestment in Poland is probably relatively low, so the extent of investment activity reduction during the crisis should be moderate and smaller than in other economies of the region.

Chart 1. Investment ratio in new EU member states in 2008



Source: Eurostat, own calculations

The growing role of EU funds

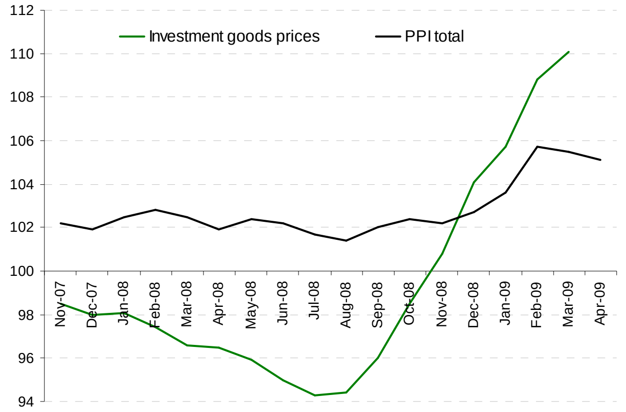
When considering the outlook for the investment activity in Poland, note should be taken of the growing significance of the EU funds. Based on the available data on the EU funding as part of the capital balance of payments (this category is a good proxy for the part of the EU funds which is put towards fixed investments), one may estimate that the relation of the EU funds used for investments to the GDP, together with its domestic co-financing, increased from 0.7% in 2004 (which was the first year of Poland's EU membership) to 1.7% in 2008. In the global crisis, EU funds are a buffer which mitigates the negative effect of the crisis on the overall investment activity in the Polish economy connected with the reduced inflow of foreign direct investments (we assume ca. 50% drop in FDIs inflow this year to nearly €5.5bn) and the lower availability of other sources of investment funding in the context of the deteriorating financial situation of enterprises and the difficulties in obtaining bank financing. According to our estimates, this year the value of the EU funds earmarked for investments with domestic co-financing may be increased to ca. 2.2% of GDP. This will be the case only with full utilisation of the advance payments from Brussels, i.e. EUR6bn (9.5% of the value of EU funds budgeted for 2007-2013). As a result, also taking into account the domestic co-financing of the EU projects, the real growth rate of investments this year will be by nearly 3pp higher and the real GDP growth rate will be nearly 0.6pp higher. In 2010, the inflow of the EU funds may add more than 5pp to the growth rate of fixed investments and ca. 1pp to GDP growth. These estimates to some degree depend on the EURPLN rate as its fluctuations affect changes in the contracted projects co-funded by the EU. The weak zloty increases the zloty-value of the EU funds.

Investments on the obstacles course

The above positive scenario of how the EU funds may impact the investment activity in Poland is by far uncertain. There is a substantial uncertainty around the advance funding of EU projects (through advance payments), a mechanism extended this year to reduce the dependence of investments on the now hard-to-obtain bank financing. However, according to the Regional Development Ministry many institutions responsible for management of the EU funds have not put any arrangements in place as of now to facilitate the use of EU advance payments. For example, out of all the voivodships, which manage the regional EU programmes, only the Mazowieckie voivodship currently uses the advance funding mechanism. Some provinces do not even envisage such a possibility. Other regions do not exclude this option, but they do not provide any advance payments at the moment. Still, it should be noted that even in those EU programmes where the use of advance payments is possible problems do occur. The problems include for example the use of collaterals for the advance payments which value exceeds PLN4m, which may hamper realisation of large projects, including infrastructural ones. The more so as the economic slowdown adversely affects the possibility of co-financing the EU projects by the state budget and by the local government, on the top of the difficulties with obtaining bank financing.

Let alone the potential difficulties with the fast use of the EU funds, another factor that might discourage to increase investment activity is the growth of the relative prices of capital goods. Since the zloty started to depreciate in the middle of 2008, the prices of capital goods have been on a the rise and towards the end of 2008 their growth started to outpace the overall growth of PPI (see the chart below).

Chart 2. Indices of annual changes in total PPI and prices of investment goods



Source: Central Statistical Office

The increase in the relative prices of capital goods may add to the negative effect on investments connected with deterioration of the current and expected growth of enterprises revenues and the strong decline in the use of production capacity.

Investments to fall inevitably, but moderately

Summing up, our econometric analysis shows that changes in the growth of gross fixed investments may be explained by the slower growth of enterprises revenues (which reflects the expectations of enterprises as to their sales potential in the future and shows their financial stance) as well as by the use of production capacity (which indicates the need for development of the production potential).

In terms of the structure of investments, given the high share of other construction in total investments, their pace of growth is key to the growth rate of total gross fixed investment. In the second half of 2008 and probably in the first quarter of 2009, investment in other construction decelerated, but to a relatively low extent and still their growth was positive. With their significant share in the total investment activity, they prevented the growth of total investments from falling below the line for the first time since Q2 2003. However, one may expect that the slowdown in the construction sector will become increasingly evident, which combined with the lowering growth rate of other types of investments (e.g. into machinery and equipment, and transport equipment), will make it unable to sustain the positive growth of total gross fixed investments in the following quarters. Hence, a fall in gross fixed investments in next quarters of this year and in 2009 as a whole seems inevitable. In the light of the projections based on our estimated equation of the aggregated gross fixed investments, one may expect these investments to fall already in the Q2 2009. Yet, even taking account of any other negative factors that are not included in the estimated equation, the decline in investments in Q2 should be rather moderate. Later on during the year, realisation of EU projects should limit the fall in investments, which should not exceed one-digit figure in the whole of 2009. This combined with the still positive consumption demand growth rate and the clearly positive contribution of next exports to GDP growth should allow Poland to avoid recession this year, which will be an outstanding achievement against other European economies.

Technical Appendix

An aim of our analysis was estimation of the aggregate investment equation, describing dependence of gross fixed investments on its potential determinants and serving as effective tool for short-term forecasts of gross fixed investment.

Definition of variable taken into account in our analysis and sources of data are presented in the table below:

variable	description	source
INV	Real annual growth rate of gross fixed investment	GUS
IR	Annual change in the real interest rate defined as WIBOR3M deflated by the current CPI inflation	Reuters, GUS
KRED	Annual growth rate in the sum of total corporate loans and mortgage loans for households	NBP
CPI	Annual growth rate in consumer prices	GUS
REER	Annual growth rate in the real effective exchange rate of the zloty calculated for 36 main trading partners and deflated with use of unit labour costs	Eurostat
REV	Annual growth rate of total enterprises revenues	GUS
BC	Annual change in the average of the stats office's overall business climate indices for industry, construction and trade	GUS
PMI	Annual change in domestic PMI manufacturing	Reuters
WIG	Annual change in WIG	Reuters
GP	Annual change in relation of oil prices to domestic CPI	Reuters, GUS
CU	Annual change in capacity utilisation in industry	GUS
D2004	Dummy variable reflecting an institutional change related to reduction in CIT rate since January 2004 and Poland's entry to the EU on May 1, 2004; the variable has a value of 0 until Q4 2003 and a value of 1 from Q1 2004 onwards	BZ WBK

Estimation of the aggregate investment equation is difficult for many reasons. Difficulties connected with quality of data on gross fixed investment or problems related to the level of data aggregation were discussed in the main part of the text. Besides, an important problem with estimating equation of aggregate investment is strong seasonality seen in the time series of many of the analysed variables.

As the elimination of the seasonality with use of popular tools such as the Census X-12, ARIMA X-11 or Tramo/Seats is always connected with some dose of discretionary decisions – the issue was widely debated by the occasion of the release of GDP data for Q1 – we decided to use variables in the form of annual growth rates / changes. Such a form of the time series enables to avoid a problematic transformation of forecasted values in seasonally adjusted terms into annual growth rates for non-seasonally adjusted data.

All variables that cannot have negative values were log-transformed. As a first step, we have checked the order of integration of the analysed variables. Results of the ADF tests (Augmented Dickey-Fuller test) indicated that all time series are non-stationary, integrated at an order of I(1). Given the order of the variables integration, potentially there may be co-integrating relations between different combinations of all variables taken into account in the analysis.

The co-integration tests we have carried out for different combinations of variables pointed to existence of more than one co-integrating vector. In such situation one should use multi-equation methods of estimation of the long-run relationship between variables, e.g. VECM. However, an important problem in such case would be the low number of observations. For the small sample it would be crucial to choose a proper order of lag in the model. On the one hand, adoption of too low lag order could lead to autocorrelation of the residuals of the model and produce biased coefficients. On the other hand, too high lag order could significantly lower precision of the coefficients estimation.

As a result, we abandoned estimation of the co-integrating relation and decided to estimate a simple regression, possibly well-fitted to the existing data set and enabling to produce reasonable short-term forecasts of fixed investments. At this stage, we again took into account different combinations of potential determinants of investment activity. Finally, we chose an aggregate investment equation of the following form:

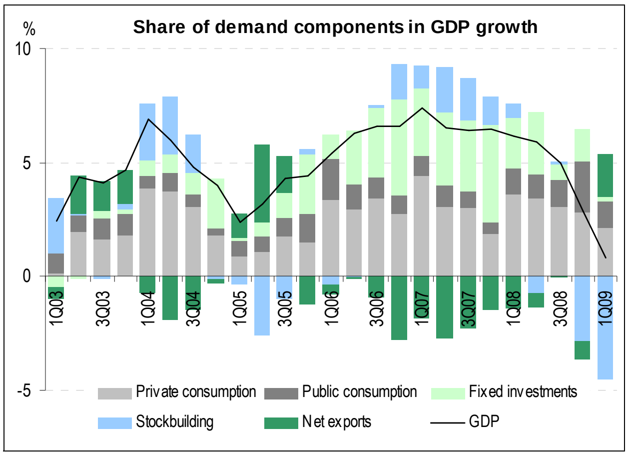
$$dINV_t = \alpha_1\, dREV_t + \alpha_2\, dCU_t + \varepsilon_t$$

Taking into account the availability of the time series, the above equation was estimated for the period of Q1 2004 to Q3 2008 using the method of ordinary leas squares. Results of coefficient estimates of the above equation are presented in the table below:

dREV	0.863618 (0.0126)
dCU	0.231436 (0.0351)

Note: p-values are given in brackets, i.e. the probabilities of making mistake when rejecting null-hypothesis about statistical non-significance of a given coefficient.

Economic update

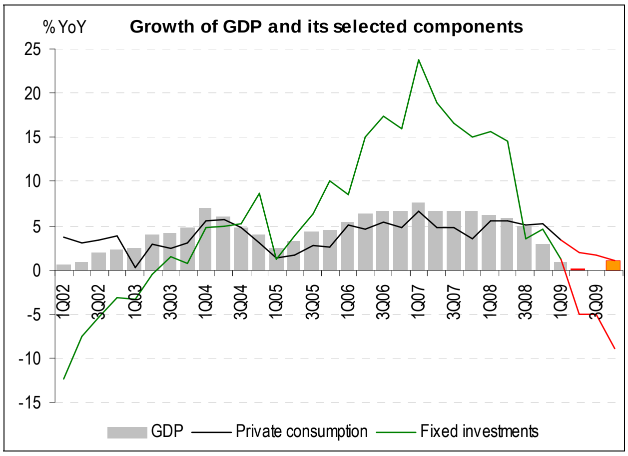


Consumption and investments positively surprised

- GDP growth in Q1 2009 was at 0.8%YoY, i.e. was exactly in line with our recent estimates, which took into account the full set of monthly data from the first three months of this year. This means a clear deceleration of economic growth as compared to previous quarters, though the result strongly distinguishes Poland among other countries in Europe and globally. It is worth to notice that seasonally adjusted quarterly growth was also above zero and reached 0.4%QoQ.
- GDP breakdown was different from our assumptions with a strong positive surprise in fixed investments, which recorded a slight increase by 1.2%YoY. Private consumption decelerated less than expected (to 3.3%YoY). This shows that so far the most pessimistic forecasts on corporate and consumer behaviour during crisis in the global economy did not fulfil.

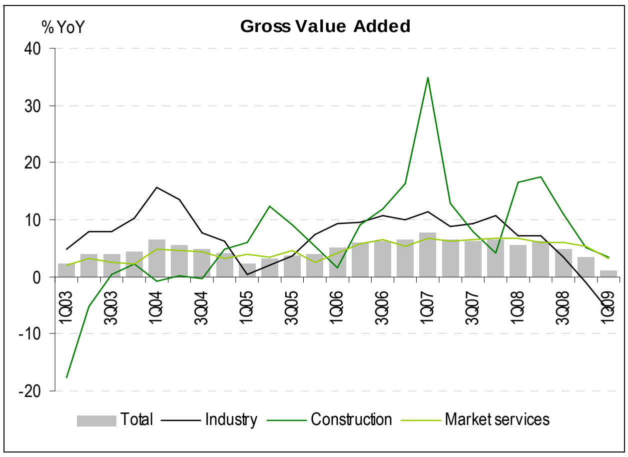
Positive contribution of net exports will be continued

- Despite the two above-mentioned components of the demand were positive and better than expected, the total domestic demand recorded a drop in Q1 by ca 1%YoY, mainly due to substantial reduction in inventories (defensive reaction of companies expecting weakening of demand). Such significant adjustment in stockbuilding (negative contribution to GDP of 4.5 pp) at the start of the year suggests that in the following quarters the influence of this factor on GDP may be not so negative.
- It was confirmed that with a significant adjustment of domestic demand, we see strong positive contribution of net exports (almost 2pp) amid more significant drop in import than in export.
- This was consistent with balance of payments data and our forecast shows another C/A surplus in April. We expect that influence of net exports will remain positive in following quarters.



Next quarters weaker, but may be still in positive territory

- Nevertheless, we maintain forecasts of further slowdown in economic growth in the next quarters, which will be influenced by fall in fixed investments and slowdown in private consumption. In our opinion, one should expect fixed investment to decrease in deferred reaction to slump in economic climate and lower credit availability, while consumption will decelerate under influence of deteriorating labour market situation.
- The better-than-expected starting point in 2009 decreases the risk of realisation of scenario assuming a significant recession in the Polish economy this year. We expect GDP growth of 0.5% and a moderate downward adjustment of our forecast as compared to previous month is a result of lower GDP growth forecast for the euro zone this year (-5%).

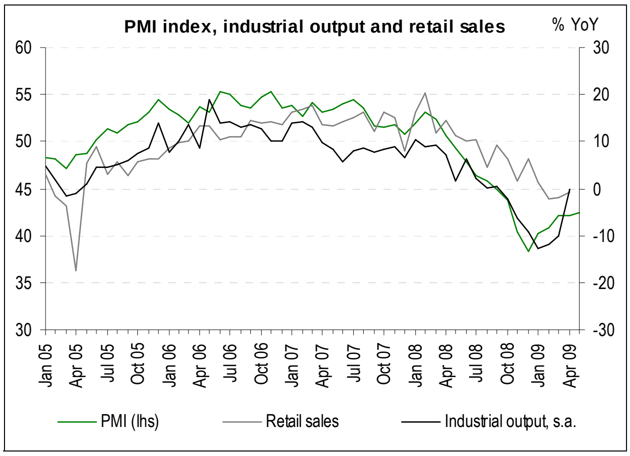


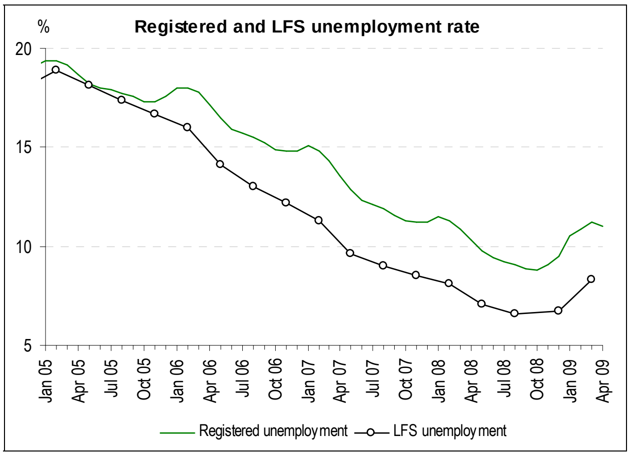
Source: CSO, own calculations

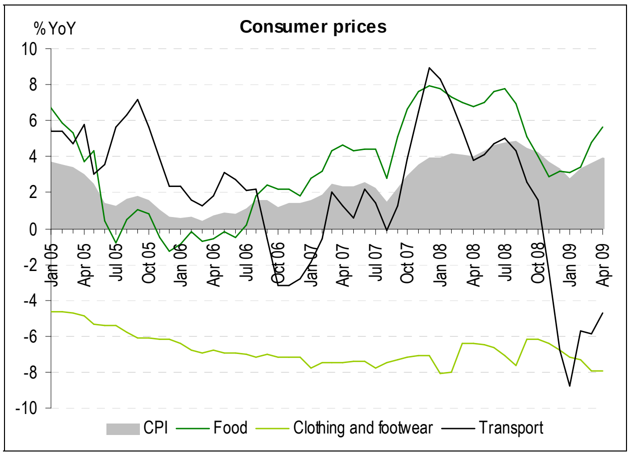
In Q1 fall in industry, significant rise in services

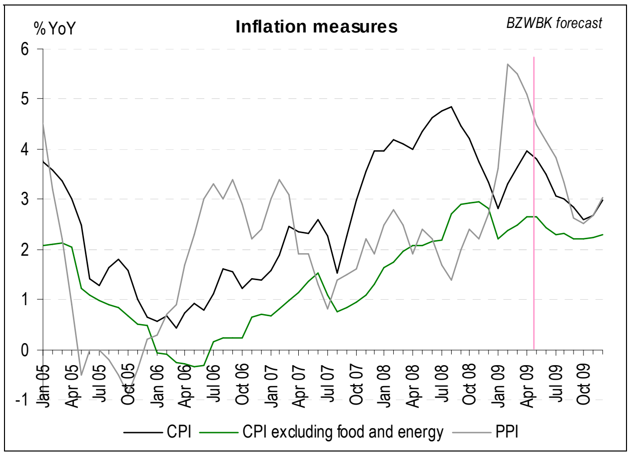
- Looking at supply side of the national account, the clear drop in value added was seen in industry (-5.9%YoY), although its scale was smaller than one could have estimated on the basis of monthly data on industrial output growth.
- In construction and market services there was a moderate slowdown in value added growth, in line with our forecast. On the other hand, non-market services saw an unexpected significant acceleration to almost 5%YoY.
- First data for the second quarter confirmed trends observed in the Polish economy. Industrial production fell again quite significantly (by 12.4%), while retails sales increased by 1% at the same time showing lower propensity to spend money for durable goods.

Economic update









Source: CSO, NBP, own calculations

Mixed signals in first data for Q2

▪ Though the figures of production and sales brought mixed signals, overall the data seems to confirm keeping economic growth rate close to zero.

▪ Business climate indicators stabilised. The Polish manufacturing PMI index inched up to 42.5 from 42.1, while market was expecting a more rapid growth to 42.8. This implies only a slight deceleration in fall of economic activity (13th straight month of the index below 50).

▪ Also, CSO survey on consumer confidence showed another month of a moderate rebound (current consumer confidence increase by ca. 0.6 pts. to -24.3 pts., the leading consumer confidence rose by 0.7 pts. to -34.8). However, the indices are still at the very low levels, much below those recorded a year ago.

Further deterioration in the labour market

▪ Unemployment rate reached 11% in April. The seasonal fall in unemployment was low. The number of unemployed was higher than a year ago by 114 thousands (increase by 7%YoY!) and one should expect this trend to continue.

▪ Situation is the worst in manufacturing, as in this sector drop in employment accelerated in April to -7%YoY and the wage growth decelerated to 2.8%YoY from 4.8% in March. So far the situation in the labour market is stabilised by slightly smaller changes in services and construction sectors, though some signs of weakening are noticeable there as well.

▪ LFS data showed increase in rate of unemployment in Q1 to 8.3% from 6.7% in 4Q08. Thus, in only one quarter it increased by the same amount it fell in the previous four quarters. Number of unemployed rose in Q1 (by 3.9%YoY) for the first time since 2002.

Rising food prices keep CPI inflation at high level

▪ CPI inflation rose in April by 0.7%MoM and 4.0%YoY, which was above expectations again. Food and non-alcoholic beverages prices had important influence, as they rose by 1.6%MoM and 5.6%YoY (4.8%YoY in March). Fuel prices increased by 1%MoM.

▪ Inflation growth in April resulted not only from these two factors, as core inflation measured by CPI excluding food and energy prices also rose, though it maintains at ca. 2.5%.

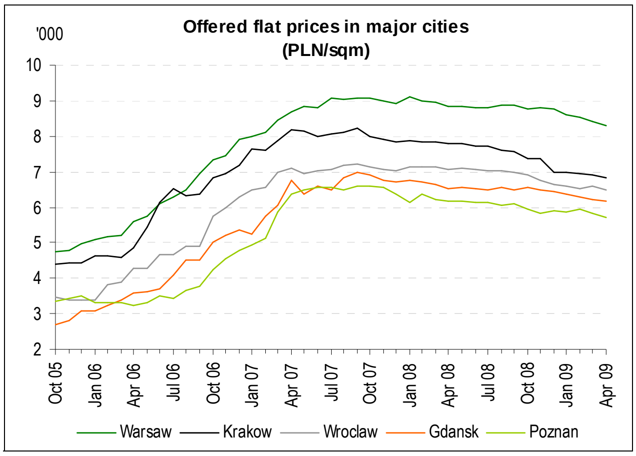
▪ Inflation increase was also the result of earlier observed zloty depreciation. However, one should remember that in the medium-term this factor would be more than offset by low domestic demand. Additionally, prices will be negatively affected by strong adjustment in unit labour costs and the expected zloty appreciation.

▪ The Ministry of Finance expects inflation to decrease in May to 3.8% amid monthly price growth of 0.6%. This estimate was again above market expectations, which was connected with a significant increase in food prices (contribution of this factor to monthly price increase is estimated by the FinMin at 0.35pp, while in the case of fuels at 0.1pp).

▪ At the same time, according to ministry's officials, in August inflation will approach 2.5% and in subsequent months it will stabilise close to this level. Assuming that this scenario is fulfilled, CPI would have to drop substantially in monthly terms in three straight months, most likely due to reversal of upward trend in food prices.

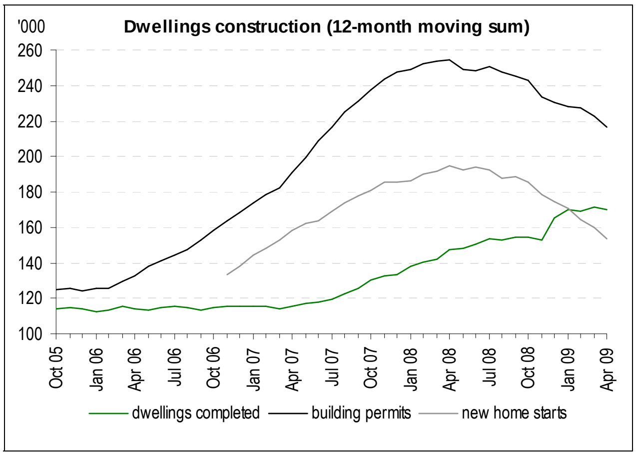
▪ Our forecasts show both CPI inflation and core inflation to decrease gradually and reach respectively ca. 3% and ca. 2% at the end of the year.

Housing market update



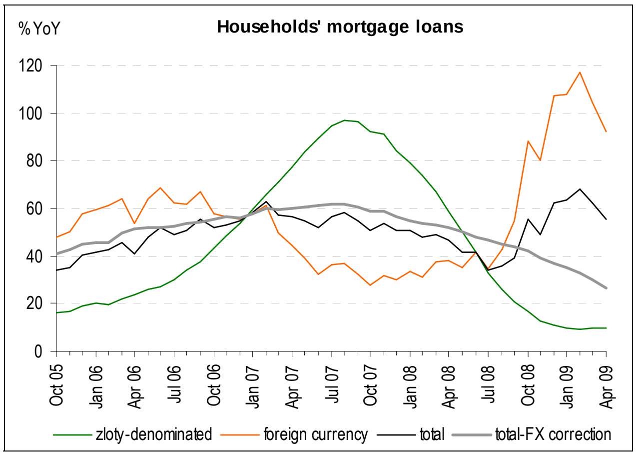
House prices going down

- Most of available reports show a continuation of downward trend in house prices. Pace of annual price drop has increased slightly, particularly in biggest cities, however in most cases it remains below 10%YoY (according to Szybko.pl, the only two exceptions are Kraków and Sopot).
- However, data from Oferty.net showed even a slight increase in offered house prices in some cities. At the same time, the report emphasised growing spread between offered prices and transaction prices. The latter can be lower by over 10%.
- Troubles with selling property resulted in a surge in the supply of flats for rent, especially in big cities. According to Oferty.net, in the first quarter the number of rental offers increased by ca. 400%YoY.



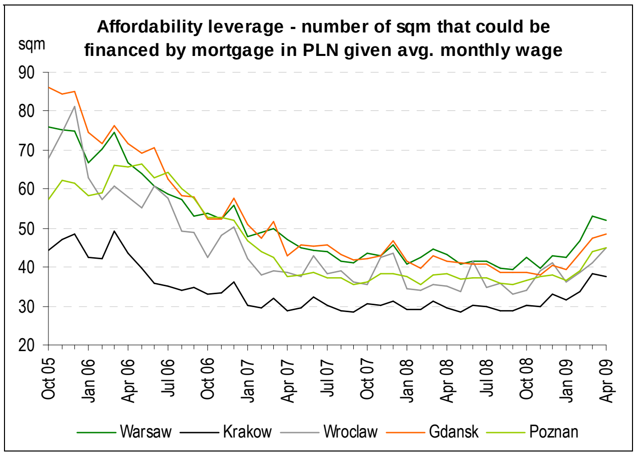
Supply of new flats still high

- Possibly, a large part of flats for rent are those apartments that had been purchased as investment in the time of bullish market and recently had been completed.
- The number of new house completions in April was lower than last year (by 14.3%YoY), however the cumulated supply in the last twelve months remains close to all-time record high.
- The number of new house starts and new building permits have been falling (in both cases drop was ca. –30%YoY). Developers are suspending or even abandoning some of already started investments, which heralds fall in supply in future.



Mortgage loans still hard to get, yet cheaper

- In the credit market, a slight increase in demand for zloty-denominated mortgage loans was observed, while a rise in foreign currency loans has been diminishing (which was probably influenced also by restrictive credit policy of banks).
- Overall, a growth in mortgage credit has been gradually weakening – according to our estimates, and after adjustment related with exchange rate fluctuations, in April loan growth decelerated to 26.7%YoY versus 30.1% in March and over 52%YoY a year ago.
- Banks' interest margins for new loans have been stabilising at high levels. However, average interest rate on mortgage loans has decreased slightly in April, following a drop in WIBOR rates. In May, interbank interest rates went up in Poland, which will lift costs of zloty-denominated mortgage loans again.



Source: CSO, NBP, Szybko.pl, Oferty.net, own calculations

More square meters for average salary

- Index of average citizen's purchasing power in the housing market calculated by us (assuming purchase of flat financed entirely by zloty-denominated loan), despite slight corrections in Warsaw and Krakow, is generally in upward trend and in most of big cities is at highest level since late 2006. The number of square meters than can be afforded wit a help of zloty-denominated loan for person earning average salary in the region has increased during a year by ca. 20% in Warsaw and ca. 27% in Krakow and Wroclaw.
- One should remember about limitations of this methodology – the index does not show effects of tightening credit procedures, including lowering maximum LTV ratio, shortening maximum length of loans, tightening requirements concerning mortgage collateral.

Central bank watch

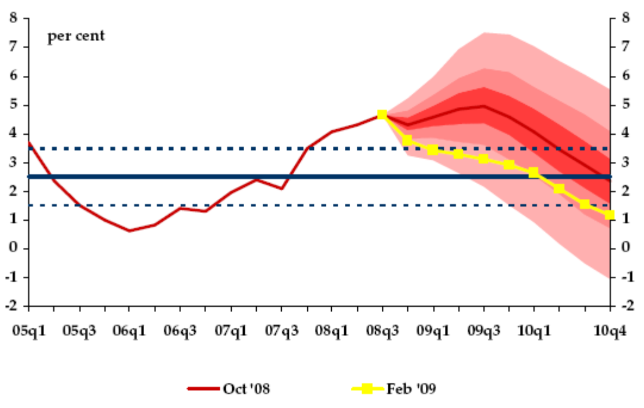
Fragments of the MPC statement after its meeting in May (changed font indicates changes as compared to April's statement)

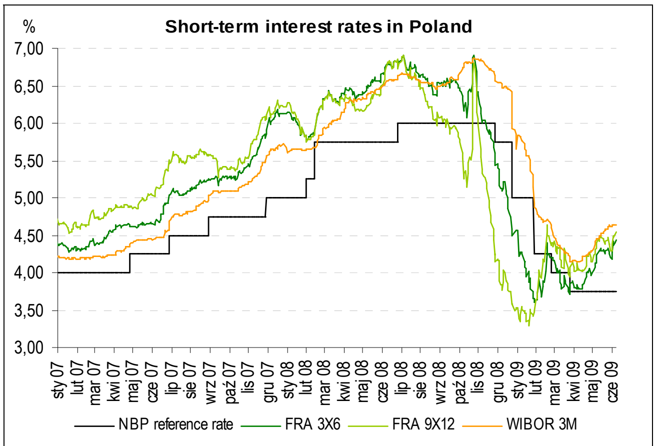
Data released since the last meeting of the Council point to a continuation of the recession in the United States and its deepening in the euro area. At the same time, some information on the United States may be signalling a certain revival of activity in this economy in the time to come, while – despite improvement in some economic climate indicators – the forecasts of economic growth in the euro area, which is Poland's main trading partner, were lowered again. Further deterioration of the economic climate is also observed in Central and Eastern European countries. ~~Data released recently confirm low economic activity in Poland.~~ **The latest information on the Polish economy confirms that economic activity has been continuing at a low level.** ~~Decline in manufacturing, exports and retail sales in the first months of 2009 points to a slightly lower GDP growth in 2009 Q1 than previously forecast. At the same time, the data on economic situation abroad confirm that recession in Poland's major trading partners has deepened. Similarly to other countries, lower~~ **Slowing growth is driven by the decline in** demand connected with ~~deteriorated sentiment of economic agents and their worsened financial condition, driven by limited credit availability stemming from increased risk aversion in the financial sector and considerable tightening of banks' lending conditions, contribute to slowing economic growth in Poland~~ **recession abroad, lowering of growth in households' real wages and worse financial standing of enterprises as well as limited credit availability**. ~~Amidst~~ **Despite** persisting excess liquidity of the banking sector, ~~as a result of increased risk premium,~~ the cost of credit~~, despite certain reduction,~~ remains at a relatively high level **due to increased risk premium**. **Deterioration in the sentiment of economic agents is another factor limiting demand.** At the same time, information on labour market developments ~~points to~~ **confirms** further decline in employment and ~~increase in unemployment~~ **gradual lowering of wage growth**, which is conducive to curbing inflationary pressure.

~~Gradual~~ **Further** deterioration of the situation in the labour market and **the ensuing decline in the growth of real wages and worse than in the previous period** ~~of~~ financial standing of enterprises ~~as well as tightening of banks' lending conditions~~ will also be conducive to curbing demand and, consequently, the inflationary pressure.

Moreover, the Council decided that a more comprehensive assessment of inflation outlook will be possible after considering the results of the June projection based on the NECMOD model.

CPI projection in February against October projection





Source: NBP

MPC dovish with no rate changes

- As expected, the MPC did not lower interest rates at the May meeting keeping the reference rate at 3.75%.
- Contents of the MPC's official statement were not surprising and it had again a dovish overtone, which is justified given the overall macroeconomic situation. Most of all, the MPC maintained informal easing bias in monetary policy, saying that probability of inflation staying in the medium run below the inflation target is higher than probability of inflation running above target. Moreover, NBP governor Sławomir Skrzypek stressed during the press conference that no rate cut two months in a row is not a signal of a swift change to neutral bias.
- The Council wrote in the statement that the new data show persistence of recession in the US and its deepening in the euro zone (despite improvement in some business climate indicators), as well as further deterioration of business climate in CEE countries. The MPC maintained assessment that recession in world economy will be limiting inflationary pressure in Poland through impact on economic growth slowdown. Among factors working towards limiting demand and inflationary pressure, the MPC mentioned again further deterioration in situation in the labour market (a new element is that fall in real wages growth rate was pointed out), deterioration in companies' financial situation and moods of enterprises, and tightening of credit policy by banks.
- In the nearest months the Monetary Policy Council expects a fall in inflation, although it expects that it will remain at elevated level due to relatively high food prices and controlled prices (mainly energy).

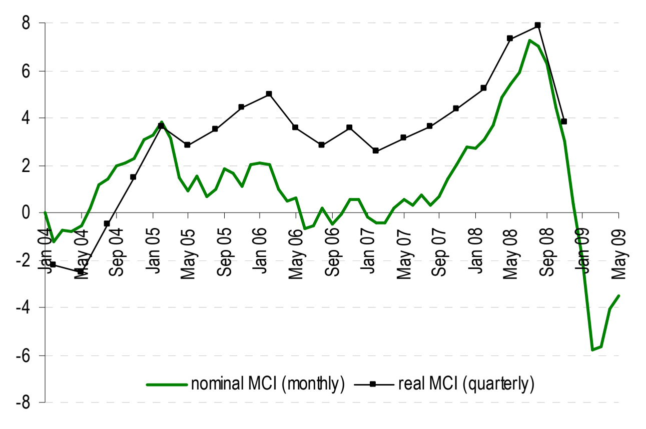
What changes in NBP's projection?

- Key factor for the next MPC decisions is not the scale of inflation fall in the next months, but its path in the quarters (or even years) to come. Expectations of the central bank in this regard will be presented in the new inflation projection. Unfortunately it will be known publicly after June's meeting.
- It is worth to remind that the previous projection showed GDP growth on average at slightly above 1% in 2009, slightly above 2% in 2010 and almost 4% in 2011. At the same time, CPI inflation was expected to fall below 2% next year and below 1% in 2011.
- MPC's Dariusz Filar said that "in 2010 it may turn out that inflation won't be below target, but at the target". It will be very interesting to see what factors will drive it given that the pace of economic growth will be probably lowered in the projection.

Obligatory reserve requirement down by 0.5pp

- In May the Council took decision to lower the reserve requirement rate by 50bp to 3%. According to the Council, this is going to give banks additional possibilities of increasing credit activity, although the move may not be sufficient given capital constrains of banks and high credit risk. We do not assume that the lowering of reserve requirement rate is a substitute for reduction of the main interest rates of the NBP.
- Apparently, events in the interbank market over the past weeks (e.g. rise in WIBOR) convinced the MPC about a need to increase liquidity (in scale estimated at PLN3-3.5bn). Comments by central bank's representatives (see next page) suggested that potential further reductions of obligatory reserve will depend on the effects of May's decision.

Restrictiveness of the Monetary Policy (Council)



Another rise in MCI

- In line with the tendency seen at the beginning of May, and signalled in the previous MACROscope, the last month brought rise in nominal MCI. The rise in effective monetary policy restrictiveness in May was caused both by increase in WIBOR rates (narrower deviation of WIBOR downwards from the trend) and appreciation of the zloty (narrower deviation of EURPLN upwards from the trend).
- Real MCI for Q4 2008 confirmed changes in monetary policy stance indicated by monthly nominal MCI for that period. This was an effect significant depreciation of the real effective exchange rate (during one quarter the REER changed from large deviation from the trend in direction of appreciation to direction of depreciation, despite real interest rates rose and their deviation upwards from the trend widened.

4.00%

Filar 1.63 (1.61)

Wasilewska-Trenkner 1.59 (1.48)

Noga 1.52 (1.52)

Wojtyna 1.48 (0.91)

Sławiński 1.19 (0.91)

3.00%

Czekaj 1.00 (0.86)

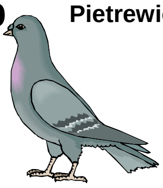
Skrzypek 0.85 (N/A)

Owsiak 0.89 (0.91)

Nieckarz 0.89 (0.83)

2.50%

Pietrewicz 0.81 (0.74)



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 restrictiveness axis 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.

Rate cut in March amid casting vote of the NBP President, no motion in April

According to the results of the MPC votes at the MPC meeting in March, decision to lower rates by 25bp was determined by casting-vote of the NBP governor Sławomir Skrzypek. Among opponents of the rate cut were Dariusz Filar, Marian Noga, Andrzej Sławiński, Halina Wasilewska-Trenkner and Andrzej Wojtyna. These five members moved relatively higher on our scale of restrictiveness.

Next voting in June

Based on minutes of the MPC meeting in April, one can conclude that in April central bankers were unanimous that there was no need to change rates (there was no motion submitted in April to reduce rates). The upcoming *Inflation Report* will not include the result of voting in May regarding obligatory reserve requirement. The only new information on voting in the report will concern the motion to cut interest rates by 50 bp in March. Then, three members (Filar, Noga, Wojtyna) were even against cutting rates by 25 bp. Of course, the most interesting will be the result of voting in June, as we believe the rate cut will be proposed and it has chances to find support of majority within the MPC. We do not think the Council should concentrate on elevated current level of CPI inflation, while its medium-term prospects are improving. Such view should be confirmed by the NBP's new projection.

Most members waiting for projection, some voices about neutral bias

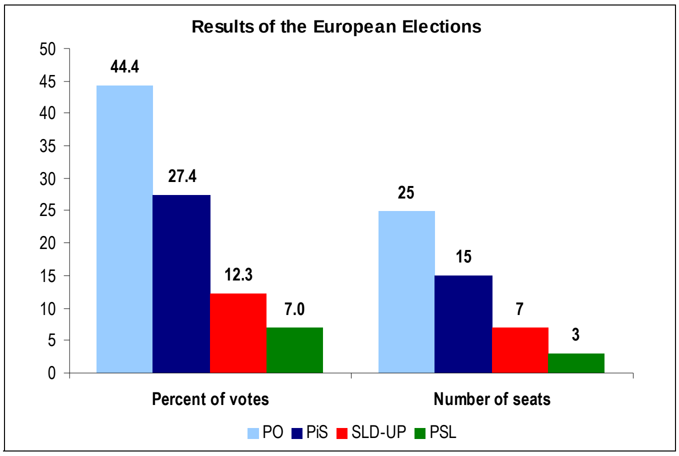
In most recent comments MPC members pointed only the importance of inflation and GDP projection, which has been prepared by analysts of the National Bank of Poland. Some of the members will probably find justification of further rate cuts (though even Mirosław Pietrewicz changed the view regarding the scale – now he sees additionally "only" 75 bp). Other members may propose a change in monetary bias into neutral from easing, trying to find signals of economic recovery in the medium-term which could affect inflation prospects. This was not very surprising when this possibility was mentioned by members from the hawkish faction (Filar and Wojtyna). However, recently, a mainstream member, Jan Czekaj, also did not exclude such a possibility already in June. On the other hand he still sees some ammunition to be used by the MPC and he added that the next steps will depend on the shape of the economy. We think that the new projection will rather not justify swift change in bias from easing, but taking into account the above statements one cannot exclude this. In such a case, further cuts would be still possible though risk for our scenario of reference rate at 3% in this cycle would increase.

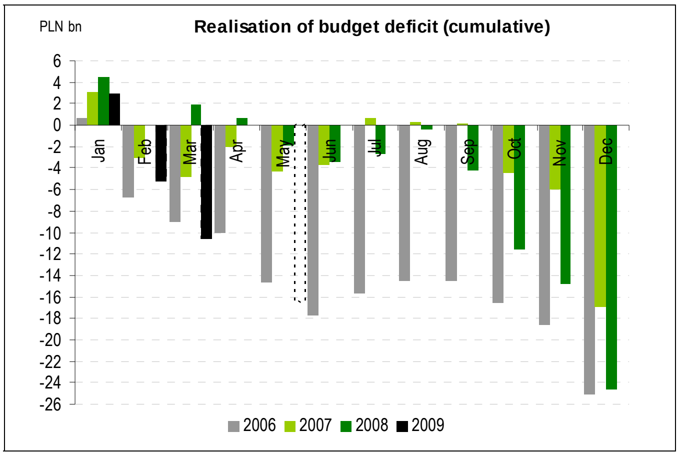
Further cut in obligatory reserve possible after WIBOR decrease

The decision to cut obligatory reserve requirement was accompanied by comments by NBP's representatives as regards elevated levels of three-month and six-month WIBOR. Deputy President of the central bank Witold Koziński advanced a hypothesis, which may be partly justified, that "probably there is a group of banks, which is interested in elevating WIBOR rates, as they are used in calculating credit rates". Dariusz Filar from the MPC said directly that "the Council would like to see what will be the effects of increased liquidity"" and "if banks start to quote three-month WIBOR in a way that would show a better transmission mechanism (…) this may convince us that further steps make sense".

Source: CSO, Eurostat, NBP, own calculations

Government and politics





Fragments of agenda of work on 2009 budget amendment

Event	Deadline / Responsible	Comment
Preliminary information from settlement of PIT for 2008	until 22.06. / FinMin	Information allowing for more precise estimation of scale of impact of annual PIT settlement on budget revenues in 2009
"Information about macroeconomic situation and state of state budget in 2009"	until 22.06. / FinMin	In information about the most up to date macroeconomic and budgetary data the assessment of economic situation and stance of state budget will be made, together with projection until the end of 2009. The document will allow designing directional measures and conditions and constraints necessary for preparing budget bill amendment for 2009.
Discussion of the "Information" by the government and passing it to the social partners	until 23.06. / government	Sending information to social partners (Three-Party Committee), administration organs, MPC and NBP
Work on budget bill amendment	23.06 - 06.07. / FinMin	
Approval of the budget bill amendment by the government and sending it to the parliament	until 07.07. / government	

List of countries with ongoing EDP procedures

Country	Date of the European Commission report	Council Decision on existence of excessive deficit	Deadline for correction
Poland	13.05.2009		
Romania	13.05.2009		
Lithuania	13.05.2009		
Malta	13.05.2009		
France	18.02.2009	27.04.2009	2012
Latvia	18.02.2009		
Ireland	18.02.2009	27.04.2009	2013
Greece	18.02.2009	27.04.2009	2010
Spain	18.02.2009	27.04.2009	2012
UK	11.06.2008	8.07.2008	2013/14
Hungary	12.05.2004	5.07.2004	2009

Source: European Commission, Ministry of Finance, own calculations

PO wins European Elections in Poland

- The ruling Civic Platform has won the European Elections in Poland, gaining support of 44.43% of votes (which gives as much as 25 out of 50 seats in the European Parliament). The Law and Justice was at the second place, with 27.04% of votes (15 seats), SLD-UP was third with 12.34% (7 seats) and PSL won 7.01% of votes (3 seats). The turnout in Poland was 24.53%.
- In majority of European Union member states, right wing parties won the elections, ahead of social-democratic parties.
- Despite good result of the PO in European Elections, the public support for the government has been decreasing (in June, government had 38% supporters and 27% opponents according to CBOS) as well as for government's economic policy (34% positive and 52% negative opinions).

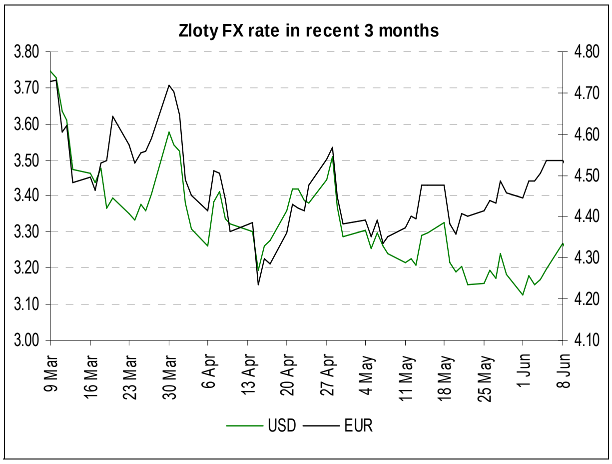
Budget amendment getting closer

- According to the Ministry of Finance's data, budget deficit after four months of the year increased to PLN15.3bn (84.3% of the annual plan) versus PLN11.3bn after March. Budget expenditure reached 32.6% of the plan and revenues 29.5%.
- In April, there was a significant deterioration in growth rate of direct taxes, both from companies (-29.6%YoY) as well as from individuals (-11.7%YoY). Total budget revenues fell in April by 11.4%YoY and after four months of the year decreased 1.4%YoY, versus 12.5%YoY growth planned in budget bill for the entire year.
- It is becoming more and more evident that realisation of this year's budget deficit will not be possible. The Ministry of Finance presented an agenda, saying that work on the budget amendment should be completed until 7 July.
- According to prime minister, the government will try to avoid significant rise in budget deficit at all costs. FinMin officials said that solutions should be searched on both sides – spending side and revenue side.
- We estimate that shortfall in budget revenue in the central budget due to economic slowdown will reach ca. PLN40bn, and additionally in local governments and social security funds there will be additional PLN15 underperformance. Most likely, despite holding some spending, shifting some of them outside central budget, and possibly a rise in some taxes (although government says it wants to avoid it), the central budget deficit will have to be increased. We assume moderate hike to PLN25bn.
- A true scale of fiscal problems will be revealed in general government balance, which we estimate to grow this year to 5.5% of GDP (ca. PLN73bn) versus 3.9% of GDP in 2008.

Excessive deficit procedure initiated

- In May, the European Commission released reports about Poland, Lithuania, Malta and Romania, initiating Excessive Deficit Procedure for those countries because of exceeding fiscal deficit limit of 3% of GDP.
- The Commission stated that a rise in deficit in Poland above 3% of GDP cannot be attributed to economic crisis, as in 2008 Poland was expanding faster than potential. Expansionary state of Poland's fiscal policy is reflected in growth of structural fiscal deficit from 3.2% of GDP in 2007 to 5.3% in 2008.
- Although launching EDP against Poland seems to be a deal done, it seems that in a situation when level of allowed fiscal deficit will be exceeded by majority of EU states, one should hardly expect any sanctions from EU because of this reason.

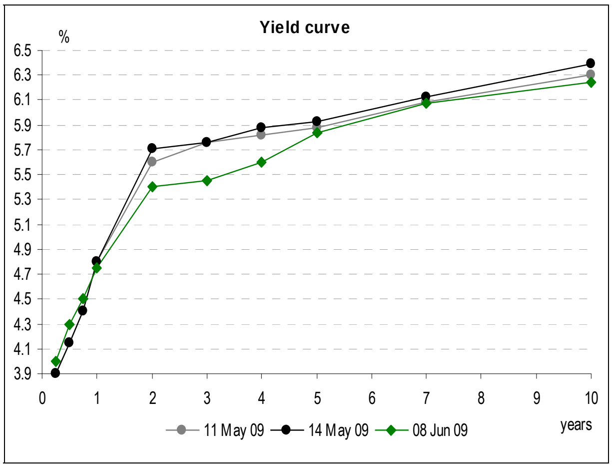
Market monitor



Zloty temporarily weaker

▪ The domestic currency weakened a few days after our previous report to the support level pointed by us at. 4.50. Later the zloty recovered to an essential resistance level of 4.33. At the end of May and the start of June the Polish currency depreciated again under negative influence of concerns over the budget amendment and most of all concerns over the Latvian lat. On these factors the zloty temporarily weakened to ca. 4.58.

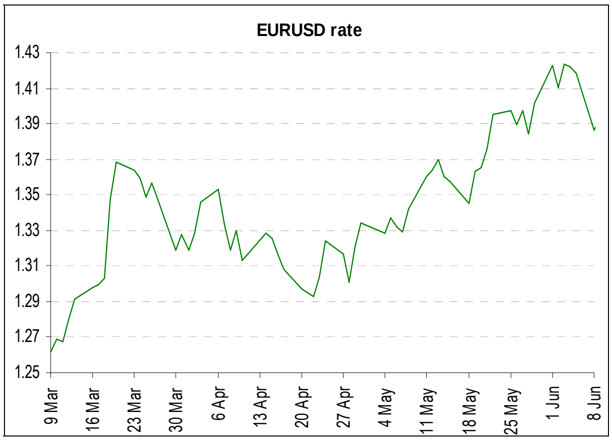
▪ We maintain our view that the zloty should strengthen in medium term toward 4.20. However, in the short-term negative sentiment towards the region connected with fears over lat devaluation and changes in the budget scheduled at the start of July may be a burden for the domestic currency. We see no fundamental reason for the zloty to be traded above 4.60 against the euro and in our view such level should be used to sell euro.



Yields down, FRA and IRS rates up

▪ After a stabilisation and a slight decline in FRA rates at the end of May, in June there was a significant rebound, which could have been connected with lower expectations regarding the total scale of interest rate cuts after less dovish comments from the MPC. In the last weeks there was a significant increase of the IRS curve. Meanwhile, in the debt market after yields stabilisation in May, at the start of June the debt strengthened, which was accompanied by successful auction of short-term bonds and cancelled tender of long terms securities.

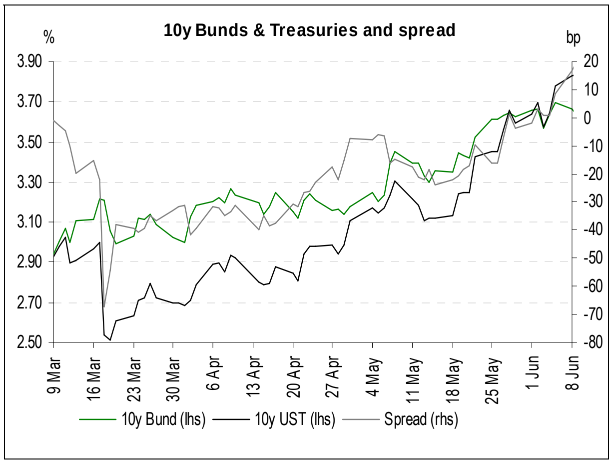
▪ Along with the approaching date of the budget amendment the bond market may be under pressure from concerns over an increase in debt supply. In the short-term bond market may be negatively affected by potential zloty weakening and May inflation figure. Debt prices should rise before MPC meeting on expected reduction of rates.



Dollar recovers from the weakest levels in 6 months

▪ The depreciation of the dollar against the euro was continued since May report. An increase in risk appetite and better than expected data positively affected the euro. Concerns over the US rating after a downgrade of rating outlook of Great Britain hurt the dollar. Nuclear tests in North Korea only temporarily stopped the dollar weakening. It significantly recovered in the last few days on much better than expected data from the US labour market and decline of Ireland's rating by the S&P.

▪ We expect the EURUSD rate near 1.40 at the end of the Q2. We also see gradual appreciation of the dollar in the following months, as the US economy will probably experience recovery before other developed economies, which together with narrowing trade deficit would help the dollar. US currency would be also supported by any speculation of Fed rate hikes.



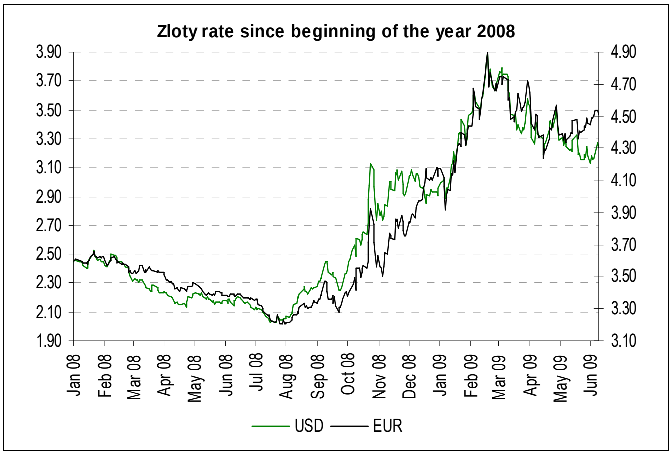
Rise in long term yields in the core debt markets

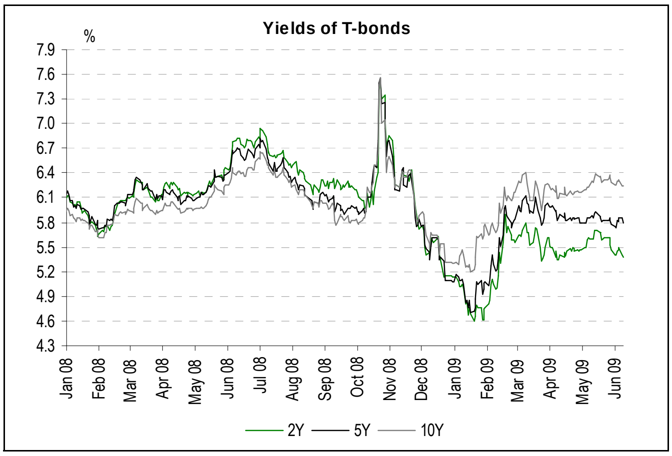
▪ In the last weeks there was a significant increase in long term yields in the core debt markets. Apart from lower appetite for safe haven assets, other factors contributing to the weakening of the long-term debt included concerns over the debt supply and rising expectations of sooner end of recession. Additionally the US market was under negative influence of speculation and concerns over possible deterioration of prospects for the US rating. During the last month yields of 10Y Treasuries rose by 61 bp (to 3.82%) and of 10Y Bund rose to 27 bp to 3.66%.

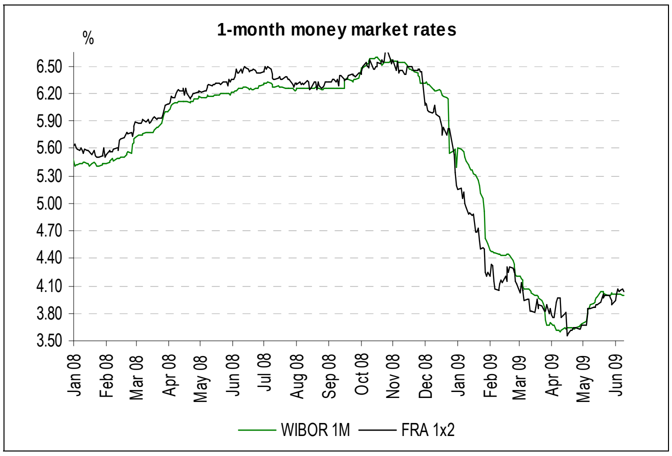
▪ Rates in the US are going to stay at low levels in the coming quarters and Fed actions will focus on operations supplying the market in money. If the euro zone remains in deep recession another rate cut may not be ruled out, though the last ECB official statement disappointed the markets in this matter.

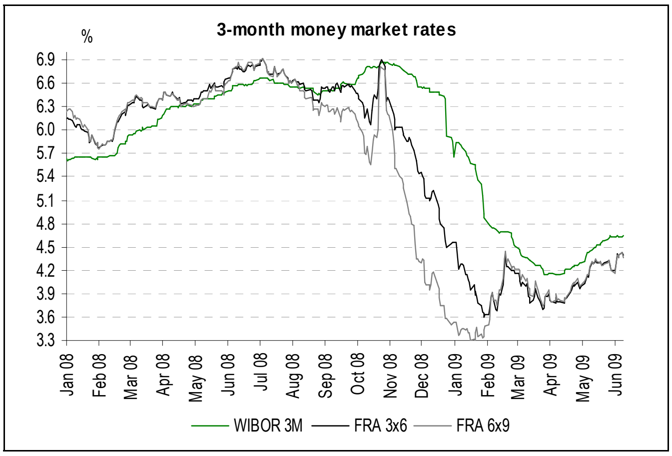
Source: Reuters, BZ WBK

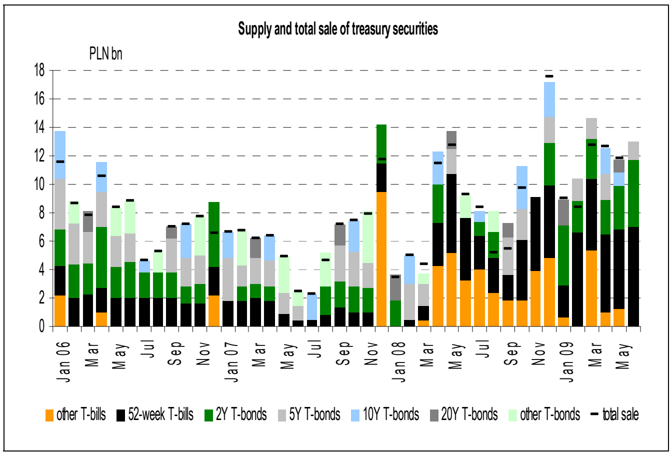
Market monitor











Treasury bills auctions (PLN m)

	(OFFER)*/SALE			
Auction date	52W	28W	26W	25W
4.05.2009	<2700/1328	-	-	<2700/1294
11.05.2009	600-800/758	-	-	-
18.05.2009	600-800/633	-	-	-
25.05.2009	2000-2500/2515	-	-	-
1.06.2009	1500-2000/2125	-	-	-
8.06.2009	1200-1600/1600	-	-	-
15.06.2009	1100-1400	-	-	-
22.06.2009	800-1000	-	-	-
29.06.2009	800-1000	-	-	-
6.07.2009	-	-	-	-
13.07.2009	-	-	-	-
20.07.2009	-	-	-	-
27.07.2009	-	-	-	-

* *based on data of the Ministry of Finance*

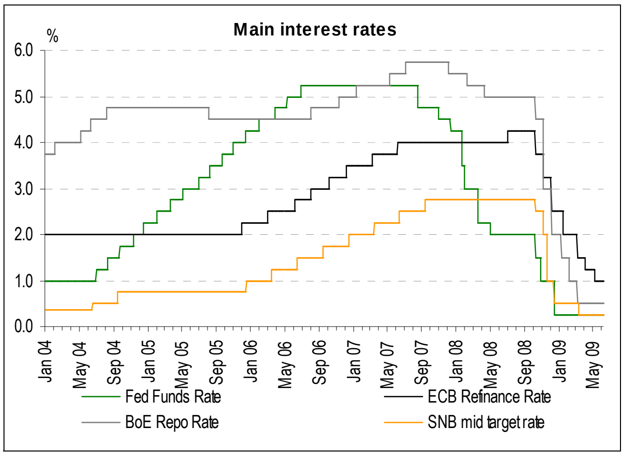
Treasury bond auctions in 2008/2009 (PLNm)

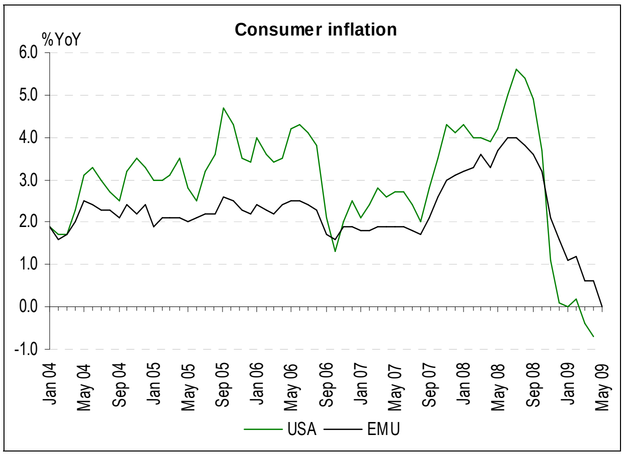
month	First auction				Second auction				Switch auction		
	date	T-bonds	offer	sale	date	T-bonds	Offer	sale	date	T-bonds	sale
January	7.01*	OK0711	4200	4296	14.01	WS0429	1500	1500	21.01	PS0414/DS1019	2800/1300
February	4.02	OK0711/PS0414	2200/1600	722/1186	-	-	-	-	18.02	-	-
March	4.03	OK0711/PS0414	2760/1500	2550/640	-	-	-	-	11.03	OK0711/PS0414	2759/1809
April	1.04	OK0711/PS0414	2400/1800	2544/1814	8.04	DS1019	1000-1800	2120	15.04	PS0414/DS1019/WS0922	1437/3129/1158
May	13.05*	OK0711	3150	3286	20.05	DS1019|WS0429	1000-1800	1835	6.05	DS1013/DS1015	765/2505
June	3.06*	OK0112|PS0414	4000-6000	4359/1122	10.06	DS i/lub WS	0-2000	-	17.06	-	-
July	1.07	OK0711	4200	4296	8.07	DS1019|WS0429	0-2000	cancelled	-	-	-
August	5.08	OK/PS	-	-	12.08	DS/WS	-	-	-	-	-
September	2.09	OK/PS	-	-	9.09	DS/WS	-	-	-	-	-
October	7.10	OK/PS	-	-	14.10	DS/WS	-	-	-	-	-
November	4.11	OK/PS	-	-	18.11	DS/WS	-	-	-	-	-
December	2.12	OK/PS	-	-	-	-	-	-	-	-	-

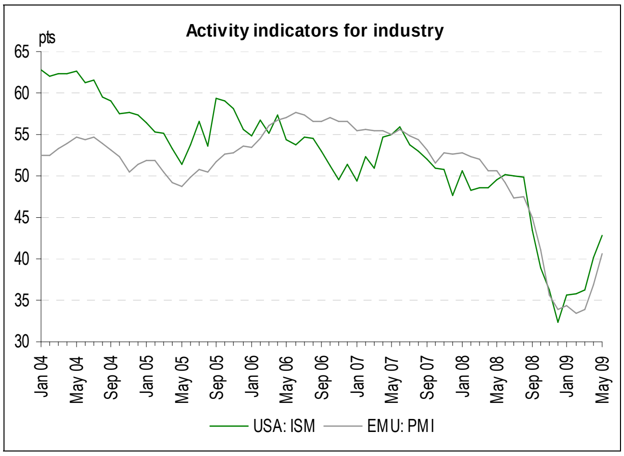
* with supplementary auction

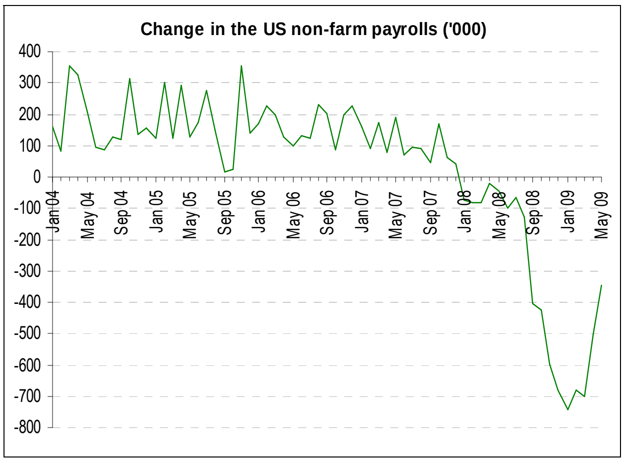
Source: Ministry of Finance, Reuters, BZ WBK

International review









Source: Reuters, ECB, Federal Reserve

Lower GDP forecasts

▪ In the April minutes Fed said that recession in the US in 2009 will be deeper than previously forecasted (currently Fed forecasts GDP drop in range of 1.3-2% vs. drop of 0.5-1.3% previously), and the economic recovery in 2010 will be slower (current Fed's forecast is GDP growth of 2-3% vs. 2.5-3.3% expected earlier). At the same time, the Fed underlined that perhaps it will have to increase its assets purchases in order to support stronger recovery. Fed board members stated that they will wait and see how the economy and the financial markets react to previous actions before making any new decisions.

▪ In June the ECB kept interest rates on hold (main reference rate at record low of 1%). Despite signs of ending recession noticed by the ECB chief, the bank reduced its economic forecasts for the euro zone – currently it predicts GDP fall this year by 4.1-5.1% versus previously forecasted fall by 2.2-3.2%. In 2010 the GDP change is predicted to range between –1% and +0.4%. Trichet said also that the bank would start purchasing covered bonds worth €60bn in primary and secondary markets starting in July. He also suggested the ECB may focus on papers with maturity 3-10 years, and there are no plans of purchase of any other securities.

▪ Euro zone inflation was at 0.6%YoY in April and according to flash estimates of the Eurostat inflation fell in May to 0%YoY against expected 0.2%. Producer prices in the euro zone declined in April by 4.6%YoY, the largest decline in the history against an expected drop by 4.5%.

▪ Consumer prices in the US remained unchanged in April in monthly terms as expected (-0.7%YoY) and the core CPI index rose by 0.3%MoM (1.9%YoY) against forecasted 0.1%MoM. PPI increased in April by 0.3%MoM (-3.7%YoY).

New data less pessimistic

▪ In China there was a slight decline in PMI index to 53.1, though the index remained above 50 for the third consecutive month. There was also the first in a few months increase in exports orders.

▪ The PMI index for manufacturing in the euro zone recorded a significant increase to 40.7 from 36.8 against preliminary estimates and market expectations at 40.5. The PMI index in the services sector rose in May to 44.8 from 43.8 in April.

▪ The euro zone GDP fell in Q1 2009, after excluding seasonal factors, by 2.5%QoQ (-4.8%YoY), mainly due to significant fall in investments (-0.9 p.p.) and drop in inventories (-1 p.p.). The GDP growth decline was much larger in case of German economy (-6.9%YoY). Our current estimates point to GDP decline in the euro zone by 5%YoY this year.

▪ The ISM index in the US rose to 42.8 from 40.1 against expected 42. ISM for services rose to 44pts from 43.7pts slightly below forecasted 45pts. Meanwhile Michigan consumer sentiment index rose in May to 68.7pts (the highest level in 8 months) from 65.1pts in April against expected 67.9pts.

▪ The GDP growth in Q1 was revised to –5.7% from –6.3% vs. expected –5.5%. The upward revision resulted from smaller drop in inventories and smaller deficit in net exports. On the other hand the improvement was smaller than expected due to downward revision of the private consumption. We estimate the US GDP to decline this year by 3.6% r/r.

▪ The US non-farm payrolls fell in May by 345k, the least for 8 months, against a forecasted decline by 520k. Additionally the data for April were revised upwardly from –539k to –504k. The rate of registered unemployment was slightly higher than expected and increased to 9.4% from 8.9% in April, against a forecast of 9.2%.

Economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
8 June ***PL: Auction of Treasury Bills***	**9** US: Wholesale inventories (Apr)	**10** ***PL: Auction of Treasury bonds*** US: Trade balance (Apr)	**11** ***PL: Market holiday*** US: Retail sales (May)	**12** ***PL: Money supply (May)*** EZ: Industrial production (Apr) US: Import prices (Jun) US: Preliminary Michigan (Jun)
15 ***PL: Auction of Treasury Bills*** ***PL: CPI (May)*** US: Empire State index (Jun) US: Capital flows (Apr) JP: BOJ decision	**16** DE: ZEW index (Jun) EZ: Final HICP (May) US: House starts (May) US: Building permits (May) US: Industrial production (May) US: PPI (May)	**17** ***PL: Switch auction*** ***PL: Balance of payments (Apr)*** EZ: Trade balance (Apr) US: CPI (May)	**18** ***PL: Wage and employment (May)*** ***PL: MPC minutes (Apr)*** CH: SNB decision US: Philly Fed index (Jun) US: Leading indicators (May)	**19** ***PL: Industrial production (May)*** ***PL: PPI (May)***
22 ***PL: Auction of Treasury Bills*** ***PL: Core inflation (May)*** ***PL: Business climate (Jun)*** DE: Ifo index (Jun) DE: Gfk index (Jul)	**23** ***PL: MPC meeting*** US: Home sales (May) US: Home prices (Apr) EZ: Flash manufacturing PMI (Jun) EZ: Flash services PMI (Jun)	**24** ***PL: MPC meeting – decision*** US: Durable goods orders (May) US: New home sales (May) US: Fed decision	**25** ***PL: Retail sales (May)*** ***PL: Unemployment rate (May)*** US: Final GDP (Q1) US: Core PCE (Q1)	**26** US: Core PCE (May) US: Final Michigan (Jun)
29 ***PL: Auction of Treasury Bills*** EZ: Economic sentiment index (Jun) EZ: M3 money supply (May) EZ: Flash HICP (Jun)	**30** ***PL: Balance of payments (Q1)*** US: Case/Shiller report (Apr) US: Chicago PMI (Jun) US: Consumer confidence (Jun)	**1 July** ***PL: Auction of Treasury bonds*** ***PL: PMI (Jun)*** EZ: Manufacturing PMI (Jun) US: ADP report (Jun) US: Pending home sales (May) US: Manufacturing ISM (Jun)	**2** EZ: PPI (May) EZ: ECB decision US: Non-farm payrolls (Jun) US: Rate of unemployment (Jun) US: Factory orders (May)	**3** US: Market holiday EZ: PMI services (Jun) EZ: Retail sales (May)
6 ***PL: Auction of Treasury Bills*** US: Non-manufacturing ISM (Jun)	**7**	**8** ***PL: Auction of Treasury bonds*** EZ: Revised GDP (Q1)	**9** US: Wholesale inventories (May)	**10** US: Import prices (Jun)

Source: CSO, NBP, Finance Ministry, Reuters

MPC meetings and data release calendar for 2009

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
MPC meeting	27	24-25	24-25	28-29	26-27	23-24	28-29	25-26	29-30	27-28	24-25	22-23
MPC minutes	22	19	19	23	21	18	23	20	24	22	19	17
GDP*	-	-	2	-	29	-	-	28	-	-	30	-
CPI	14	13[a]	13[b]	15	14	15	14	13	15	14	13	15
Core inflation	21	20	22	21	22	22	20					
PPI	20	19	18	20	20	19	17	19	17	19	19	17
Industrial output	20	19	18	20	20	19	17	19	17	19	19	17
Retail sales	29	24	24	27	26	25	-	-	-	-	-	-
Gross wages, employment	19	17	17	17	19	18	16	18	16	16	18	16
Unemployment	29	24	24	27	26	25	-	-	-	-	-	-
Foreign trade	about 50 working days after reported period											
Balance of payments*	-	-	31	-	-	30	-	-	-	-	-	-
Balance of payments	15	12	13	14	15	17	14	11	-	-	-	-
Money supply	14	13	13	14	14	12	14	13	-	-	-	-
NBP balance sheet	7	6	6	7	7	5	7	7	-	-	-	-
Business climate indices	22	20	20	22	22	22	22	21	22	22	20	22

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

Source: CSO, NBP

Economic data and forecasts

Monthly economic indicators

		May 08	Jun 07	Jul 08	Aug 08	Sep 08	Oct 08	Nov 08	Dec 08	Jan 09	Feb 09	Mar 09	Apr 09	May 09	Jun 09
Industrial production	%YoY	1.4	6.5	4.8	-4.4	5.5	-2.0	-10.6	-5.6	-15.3	-14.6	-1.9	-12.4	-8.3	-8.8
Retail sales [c]	%YoY	15.2	14.3	14.7	8.3	12.4	9.2	3.0	6.9	1.3	-1.6	-0.8	1.0	1.4	-1.8
Unemployment rate	%	9.8	9.4	9.2	9.1	8.9	8.8	9.1	9.5	10.5	10.9	11.2	11.0	10.8	10.8
Gross wages [b c]	%YoY	10.8	12.3	11.8	9.9	11.2	10.1	7.6	5.6	8.1	5.1	5.7	4.8	4.8	3.0
Employment [b]	%YoY	5.3	4.7	4.6	4.1	4.0	3.5	3.0	2.2	0.7	-0.2	-0.9	-1.4	-1.6	-1.8
Export (€) [d]	%YoY	13.5	20.2	24.3	10.8	23.0	3.0	-9.8	-15.1	-25.8	-26.6	-16.3	-28.6	-27.3	-27.6
Import (€) [d]	%YoY	16.4	23.2	23.5	20.1	23.7	6.7	-6.9	-12.2	-27.4	-33.0	-26.2	-34.4	-32.9	-33.6
Trade balance [d]	EURm	-1413	-1678	-1606	-1420	-1334	-1473	-1526	-1710	-454	29	-77	-159	-389	-485
Current account balance [d]	EURm	-1781	-2173	-972	-1278	-2088	-1733	-1689	-1703	-1069	915	75	141	-319	-235
Current account balance [d]	% GDP	-5.2	-5.2	-5.0	-5.1	-5.3	-5.4	-5.6	-5.5	-5.5	-4.8	-4.3	-3.9	-3.5	-3.0
Budget deficit (cumulative)	PLNbn	-1.9	-3.5	-2.7	-0.3	-4.2	-11.6	-14.8	-24.6	2.9	-5.3	-10.6	-15.3	-16.4	-16.9
Budget deficit (cumulative) [e]	% of FY plan	7.5	14.1	10.9	1.3	17.0	47.1	60.3	100.0	-16.0	29.0	58.3	84.3	90.3	92.9
CPI	%YoY	4.4	4.6	4.8	4.8	4.5	4.2	3.7	3.3	2.8	3.3	3.6	4.0	3.8	3.5
PPI	%YoY	2.4	2.2	1.7	1.4	2.0	2.4	2.2	2.7	3.6	5.7	5.5	5.1	4.5	4.2
Broad money (M3)	%YoY	15.1	16.3	16.8	16.8	17.3	17.3	18.1	18.6	17.6	17.8	17.5	14.4	13.3	12.7
Deposits	%YoY	17.4	18.5	19.4	18.9	20.0	18.7	19.4	20.6	19.5	19.2	19.4	16.1	14.7	13.8
Loans	%YoY	27.6	27.7	25.3	26.7	28.0	32.8	31.7	36.0	35.8	37.2	34.5	30.3	28.8	25.4
USD/PLN	PLN	2.19	2.17	2.07	2.19	2.34	2.69	2.93	2.98	3.18	3.63	3.55	3.36	3.23	3.19
EUR/PLN	PLN	3.40	3.37	3.26	3.29	3.37	3.57	3.73	4.01	4.22	4.65	4.62	4.43	4.41	4.40
Reference rate [a]	%	5.75	6.00	6.00	6.00	6.00	6.00	5.75	5.00	4.25	4.00	3.75	3.75	3.75	3.50
Lombard rate [a]	%	7.25	7.50	7.50	7.50	7.50	7.50	7.25	6.50	5.75	5.50	5.25	5.25	5.25	5.00
WIBOR 3M	%	6.41	6.58	6.62	6.52	6.56	6.80	6.74	6.40	5.51	4.69	4.30	4.20	4.52	4.31
Yield on 52-week T-bills	%	6.10	6.63	6.70	6.60	6.46	6.45	6.52	6.10	4.85	4.62	4.78	4.80	4.91	4.70
Yield on 2-year T-bonds	%	6.27	6.73	6.66	6.32	6.25	6.46	6.26	5.43	4.81	5.37	5.60	5.44	5.60	5.40
Yield on 5-year T-bonds	%	6.25	6.62	6.53	6.15	6.01	6.48	6.21	5.42	4.96	5.57	5.97	5.88	5.85	5.80
Yield on 10-year T-bonds	%	6.10	6.41	6.43	6.10	5.89	6.39	6.25	5.57	5.43	5.94	6.21	6.17	6.30	6.20

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] 2008 - % of Dec, 2009 - % of plan

Quarterly and annual economic indicators

		2006	2007	2008	2009	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09
GDP	PLNbn	1 060.0	1 175.3	1 271.7	1 331.3	298.0	310.5	314.2	349.0	314.5	327.7	326.4	362.7
GDP	%YoY	6.2	6.7	4.9	0.5	6.1	5.9	5.0	2.9	0.8	0.1	-0.1	1.0
Domestic demand	%YoY	7.3	8.6	5.5	-1.4	7.3	6.4	4.9	3.7	-1.0	-1.6	-1.7	-1.3
Private consumption	%YoY	5.0	5.0	5.4	2.0	5.6	5.6	5.1	5.3	3.3	2.0	1.6	1.0
Fixed investments	%YoY	14.9	17.6	8.1	-5.5	15.7	14.6	3.5	4.6	1.2	-5.0	-5.0	-9.0
Industrial production	%YoY	12.5	9.7	3.5	-7.0	8.2	7.0	2.2	-6.3	-10.0	-9.9	-6.1	-1.9
Retail sales (real terms)	%YoY	11.9	14.0	9.6	-1.9	16.1	11.8	8.4	4.8	-1.4	-1.2	-2.5	-2.7
Unemployment rate [a]	%	14.8	11.2	9.5	13.5	10.9	9.4	8.9	9.5	11.2	10.8	11.9	13.5
Gross wages (real terms) [c]	%YoY	4.2	6.7	5.9	1.1	7.5	7.9	5.6	3.6	3.2	0.4	0.6	0.4
Employment [c]	%YoY	3.2	4.6	4.8	-1.9	5.9	4.9	4.5	3.9	0.1	-1.6	-2.6	-3.3
Export (€) [b]	%YoY	20.4	13.4	12.7	-23.8	21.2	19.8	19.5	-7.5	-22.9	-26.1	-29.0	-16.0
Import (€) [b]	%YoY	24.0	19.5	14.9	-29.2	22.5	21.7	22.6	-4.4	-28.9	-32.1	-33.0	-22.0
Trade balance [b]	EURm	-5 539	-12 369	-16 538	-5 278	-3 241	-4 218	-4 356	-4 723	-502	-1 032	-1 651	-2 094
Current account balance [b]	EURm	-7 445	-14 586	-19 613	-4 155	-4 727	-5 401	-4 361	-5 124	-79	-412	-1 271	-2 394
Current account balance [b]	% GDP	-2.7	-4.7	-5.4	-1.3	-5.0	-5.2	-5.3	-5.4	-4.3	-3.0	-2.2	-1.3
General government balance	% GDP	-3.8	-2.0	-3.9	-5.5	-	-	-	-	-	-	-	-
CPI	%YoY	1.0	2.5	4.2	3.2	4.1	4.3	4.7	3.8	3.3	3.8	3.0	2.7
CPI [a]	%YoY	1.4	4.0	3.3	3.0	4.1	4.6	4.5	3.3	3.6	3.5	2.8	3.0
PPI	%YoY	2.4	2.0	2.2	3.9	2.6	2.2	1.7	2.4	4.9	4.6	3.3	2.7
Broad money (M3) [a]	%YoY	16.0	13.4	18.6	5.2	13.6	16.3	17.3	18.6	17.5	12.7	8.7	5.2
Deposits [a]	%YoY	15.2	14.5	20.6	5.1	15.3	18.5	20.0	20.6	19.4	13.8	9.1	5.1
Loans [a]	%YoY	23.4	29.9	36.0	3.9	29.7	27.7	28.0	36.0	34.5	25.4	15.5	3.9
USD/PLN	PLN	3.10	2.77	2.41	3.21	2.39	2.18	2.20	2.87	3.45	3.26	3.11	3.04
EUR/PLN	PLN	3.90	3.78	3.52	4.33	3.58	3.41	3.31	3.77	4.50	4.41	4.30	4.10
Reference rate [a]	%	4.00	5.00	5.00	3.00	5.75	6.00	6.00	5.00	3.75	3.50	3.00	3.00
Lombard rate [a]	%	5.50	6.50	6.50	4.50	7.25	7.50	7.50	6.50	5.25	5.00	4.50	4.50
WIBOR 3M	%	4.21	4.73	6.36	4.12	5.80	6.43	6.57	6.65	4.83	4.34	3.79	3.52
Yield on 52-week T-bills	%	4.18	4.69	6.26	4.51	5.84	6.28	6.59	6.36	4.75	4.80	4.50	4.00
Yield on 2-year T-bonds	%	4.57	5.23	6.22	5.16	5.99	6.40	6.41	6.05	5.26	5.48	5.10	4.80
Yield on 5-year T-bonds	%	5.03	5.52	6.15	5.55	6.02	6.33	6.23	6.04	5.50	5.84	5.55	5.30
Yield on 10-year T-bonds	%	5.22	5.56	6.06	5.95	5.87	6.16	6.14	6.07	5.86	6.22	5.90	5.80

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 08.06.2009 has been prepared by:

ECONOMIC ANALYSIS UNIT

TREASURY DIVISION

ul. Marszałkowska 142, 00-061 Warszawa, fax +48 022 586 83 40

Email: ekonomia@bzwbk.pl Web site (including Economic Service page): http://www.bzwbk.pl

Maciej Reluga – Chief Economist

tel. +48 022 586 83 63, Email: maciej.reluga@bzwbk.pl

Piotr Bielski	+48 022 586 83 33
Piotr Bujak	+48 022 586 83 41
Cezary Chrapek	+48 022 586 83 42

TREASURY SERVICES DEPARTMENT

Gdańsk

Długie Ogrody 10
80-765 Gdańsk
tel. +48 058 326 26 40
fax +48 058 326 26 42

Kraków

Rynek Główny 30/8
31-010 Kraków
tel. +48 012 424 95 01
fax +48 012 424 21 41

Poznań

pl. Gen. W. Andersa 5
61-894 Poznań
tel. +48 061 856 58 14
fax +48 061 856 55 65

Warszawa

ul. Marszałkowska 142
00-061 Warszawa
tel. +48 022 586 83 20
fax +48 022 586 83 40

Wrocław

ul. Rynek 9/11
50-950 Wrocław
tel. +48 071 370 25 87
fax +48 071 370 26 22