

# Weekly economic update

4 – 10 March 2013

Last week investors' moods were rather volatile. After Italian elections none party managed to gather enough support to control both houses of the parliament, which visibly strengthened worries about further actions aiming at surmounting the debt crisis. In the following days the global market situation stabilised thanks to better-than-expected data from the USA and Fed governor, who was defending QE3 before the US Congress. Domestic data also proved to be above consensus. In line with our expectations, retail sales in January rose stronger than expected, and at the end of the week GDP growth in 4Q2012 turned out to be better than consensus. These releases have flattened the domestic IRS and bond curve and strengthened the zloty against the euro.

The most important domestic event of the week is the MPC decision on interest rates. Even though some comments of the MPC members suggested that it may not be easy to gather majority to support the cut, we think that such a motion will actually pass. Still, it may be a close call. In terms of forecasting the March decision, another uncertainty lies in the fact that it will be affected by the new projection of GDP and inflation, which will be known for the market only after the meeting. It is quite likely that in the statement and during the press conference the suggestion on pause in rate cuts will emerge again. However, this time this can be signalled more clearly than in past two months. Consequently, despite the interest rate cut, there might be a negative reaction of the interest rate market. Such outcome of the MPC meeting, together with recent slightly better than expected data may have positive impact on the zloty (the EURPLN may test 4.14 again). On the global market, investors' attention will focus at the beginning of the week on the euro zone and challenges it faces. Comments of ministers of finance on the progress on reforms implementation in Greece and the situation in Italy may have some market impact. We do not expect a change in rhetoric of the ECB, though after less optimistic data from manufacturing sector, expectations for a rate cut have strengthened. At the end of the week market attention will switch to US monthly nonfarm payrolls.

## Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
<b>MONDAY (4 March)</b>							
10:30	EZ	Meeting of euro zone ministers of finance Sentix index	Mar	pts	-4.5	-	-3.9
<b>TUESDAY (5 March)</b>							
9:53	DE	Meeting of EU ministers of finance PMI – services	Feb	pts	54.1	-	55.7
9:58	EZ	PMI – services	Feb	pts	47.3	-	48.6
11:00	EZ	Retail sales	Jan	%MoM	0.2	-	-0.8
<b>WEDNESDAY (6 March)</b>							
11:00	<b>PL</b>	<b>MPC decision</b>		%	<b>3.50</b>	<b>3.50</b>	<b>3.75</b>
	EZ	GDP revision	Q4	%QoQ	-0.6	-	-0.1
14:15	US	ADP report	Feb	k	173	-	192
16:00	US	Industrial orders	Jan	%MoM	-1.5	-	1.8
20:00	US	Fed Beige Book					
<b>THURSDAY (7 March)</b>							
<b>11:00</b>	<b>PL</b>	<b>Bond switch auction</b>					
12:00	DE	Industrial orders	Jan	%MoM	0.5	-	0.8
13:00	GB	BoE decision		%	0.50	-	0.50
13:45	EZ	ECB decision		%	0.75	-	0.75
14:30	US	Initial jobless claims	week	k		-	344
14:30	US	Trade balance	Jan	\$bn	-43.0	-	-38.5
<b>FRIDAY (8 March)</b>							
12:00	DE	Industrial output	Jan	%MoM	0.4	-	0.3
14:30	US	Non-farm payrolls	Feb	k	148	-	157
14:30	US	Unemployment rate	Feb	%	7.9	-	7.9

Source: BZ WBK, Bloomberg, Reuters, Parkiet

**Maciej Reluga** Chief economist +48 22 586 8363

**Piotr Bielski** +48 22 586 8333

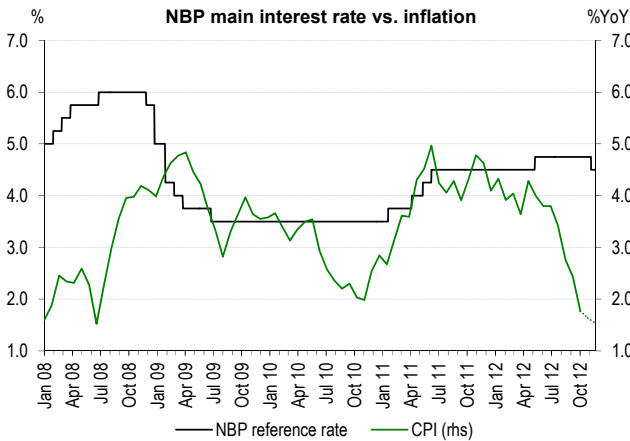
**Agnieszka Decewicz** +48 22 586 8341

e-mail: ekonomia@bzwbk.pl

**Marcin Sulewski** +48 22 586 8342

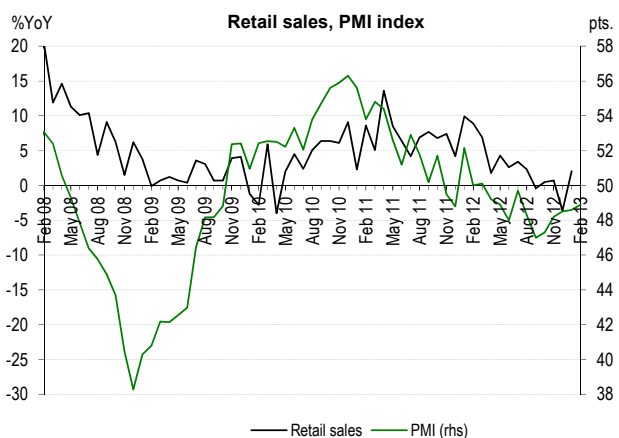
**Marcin Luziński** +48 22 586 8362

## What's hot this week – Next rate cut... and next signal of pause

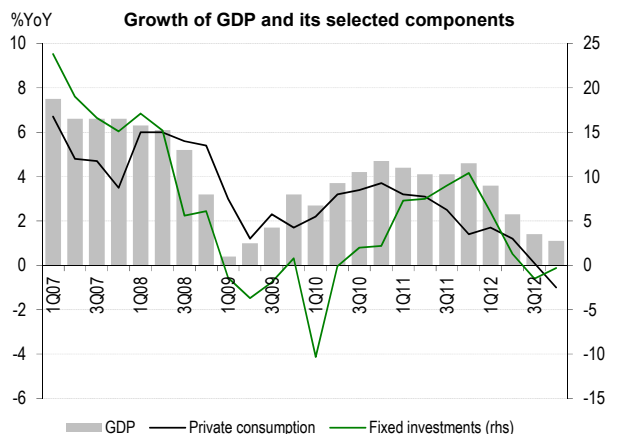


- Meeting of the Monetary Policy Council is surely the most important domestic event this week.
- We are expecting rates to be cut by 25bps, to 3.50%, all-time low set in 2009. However, this time the decision is significantly less certain than in previous months. Still, we predict that a reduction will be supported by a slim majority.
- MPC members were stressing that the decision will be strongly affected by new results of inflation and GDP projection. However, the market will see these numbers only after the MPC meeting. In our view, they should not deliver further arguments against monetary policy easing.
- The MPC has been reiterating its announcement of pause in cycle for so long that this time it will probably clearly announce adoption of "wait-and-see" mode, which will scale back expectations about interest rate cuts in the upcoming cuts.

## Last week in the economy – No major surprises in data



- Retail sales advanced in January by 3.1%YoY, considerably above market expectations, but in line with our forecast. The rebound after a strong decline in December (-2.5%) cannot however be treated as a signal of recovery in consumer demand.
- The registered unemployment rate climbed to 14.2%, the highest level in 6 years. We are expecting that unemployment will continue its upward march in the upcoming months, then it will decline in line with seasonal pattern, but will still be close to 14% at the year-end.
- PMI for Polish manufacturing climbed for the fifth time in a row, to 48.9pts. Increase was slight, but the improvement is systematic, and it suggests that bottoming-out of the cycle is close. Improvement was posted by sub-indices for new export orders and employment.



- GDP growth in the fourth quarter of 2012 was close to our expectations based on flash estimates for the whole year, but better than median market forecast. Economic growth amounted to 1.1%YoY. Consumption fell by 1%, investments contracted by 0.3%.
- The contraction of consumption may prove only temporary as it could have been triggered by postponing the subsidies for farmers. We do not expect the consumption to be main driver of economic growth this year, but we expect it to grow by 1% on average. Regarding fixed investments, we do not interpret smaller decline in Q4 than in Q3 as an omen of fast improvement. We still expect the exports to be main driver of the economic growth. We continue to forecast a bottom of the cycle in Q1 (with GDP growth at ca. 0.5%YoY) and gradual improvement in the following quarters (to 2.0%YoY in 4Q).

## Quote of the week – The worst is already behind us?

**Elżbieta Chojna-Duch, MPC member, TVN CNBC, 1.03**

One can say that this 0.1 pp (of GDP growth above 1%) has surprised us positively and introduced optimistic mood and caused a faith that this trend will persist in Q1, and economic growth will remain above 1%.

**Marek Belka, NBP President, Reuters, 25.02**

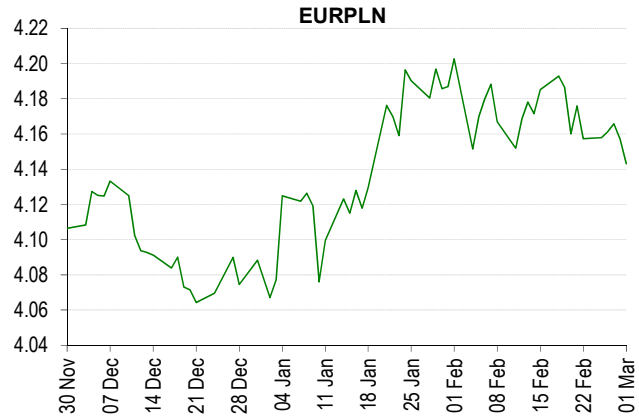
In my opinion the worst is already behind us. According to my forecasts (GDP growth this year) will reach ca. two percent, however it is possible that I will be positively surprised. (...) We are not concerned about inflation at all, obviously the low economic growth is a reason of concern.

**Jerzy Hausner, MPC member, Reuters, PAP, 25.02**

Today's data about retail sales are signalling that we are facing a turnaround of the slowdown trend. (...) One should not perceive the MPC decision in the context of current data. Only information that would be completely surprising could have some influence. A turnaround of downward trend in the economy may be faster.

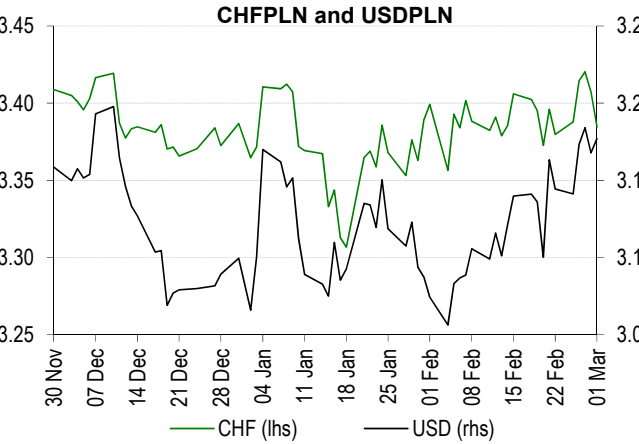
Recent data releases significantly increased optimism of MPC members, as in their opinion they have signalled that economic recovery "has probably started" and we are already in a stage of "gradual rebound". In our view, this was suggested neither by data on retail sales nor on industrial production, as in both cases the results were biased by impact of one-off factors. Economic activity is still low, mainly due to weak domestic demand, which is hardly expected to recover significantly this year. The MPC made a mistake in May 2012, due to their overly optimistic assessment of economic outlook. We hope they will not repeat the same mistake this time. Marek Belka said that the Council is not concerned about inflation at all. Perhaps it should be. The fact is that inflation is in the downward trend and in the nearest months it will remain not only below the NBP's official target but even below the range of tolerable fluctuations around this target.

**Foreign exchange market – Signal from the MPC crucial for the zloty**



**Zloty is appreciating steadily**

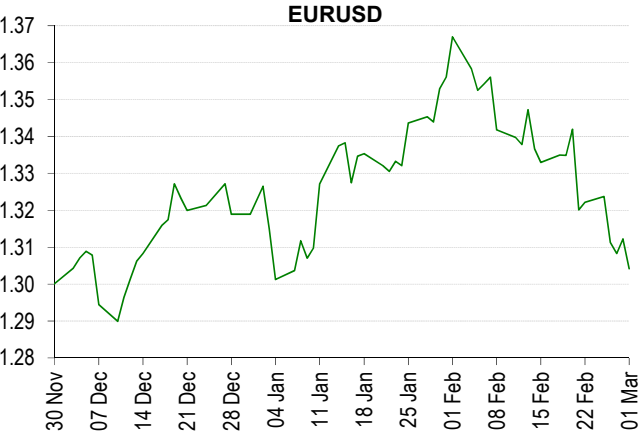
- Last week zloty was vulnerable to macro data and situation on international market. Results of parliamentary elections in Italy, suggesting that a stable coalition is rather unlikely negatively affected zloty's quotations. Consequently, the EURPLN increased to 4.175 in short-run. The second part of the week brought gradual zloty appreciations, with testing 4.14 against the euro after slightly better than expected Q4 2012 GDP reading.
- Higher volatility was observed on the USDPLN chart. We saw significant increase towards 3.20, but this level effectively stopped further increase of the USDPLN. Next days the exchange rate remained in the channel between 3.15-3.20. In weekly terms zloty gained only in relation to GBP (by 0.7%).



- Last week did not bring any significant changes on the EURPLN chart. The exchange rate has remained in relatively wide range between 4.14 and 4.20. This week the MPC meeting will be crucial for the zloty. The Council decision to cut rates might cause zloty depreciation in short run. However, any suggestion about switching to neutral bias (from easing ones) might result in breaking support level at 4.14.

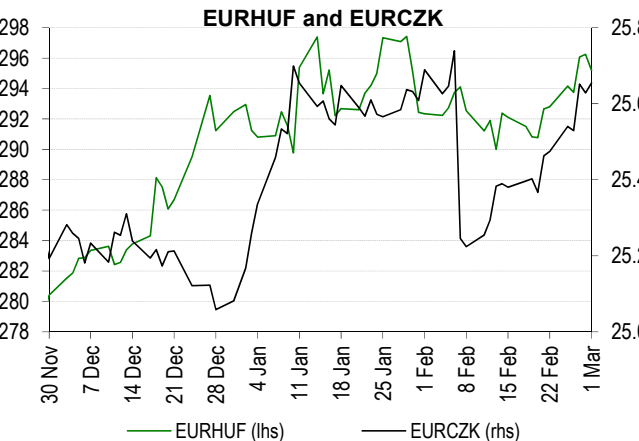
**Uncertainty in Italy to continue**

- The EURUSD has continued downward trend. The euro was under pressure situation in Italy due to investors' worries if the new coalition government will be formed to continue reforms. As a consequence the EURUSD declined towards 1.30, down from above 1.32 at the end of the previous week. On the other hand, both FED and ECB governors statements together with macroeconomic data caused the EURUSD stabilisation around 1.30 at the end of week.
- Until meeting of the Italian parliament (15 March), the uncertainty if a stable government will be formed in this country will remain in place. This will be the main risk factor for the single currency in the upcoming two weeks. Additionally, EURUSD will be affected by macroeconomic data, especially figures from the US labour market. A persistent break of support at 1.30 may generate a move of EURUSD towards 1.28-1.29. In middle term we still expect a rise of EURUSD towards 1.34.

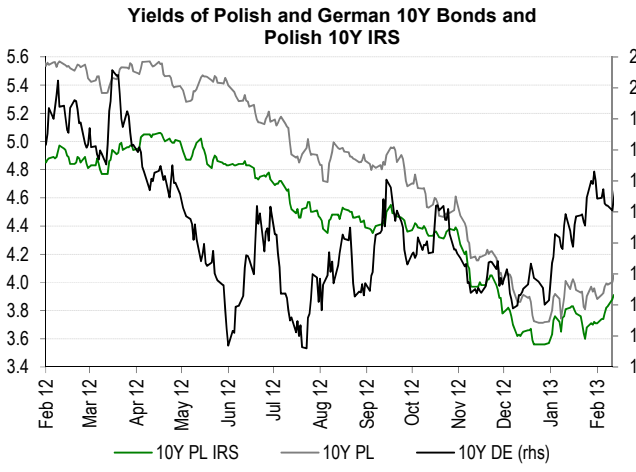
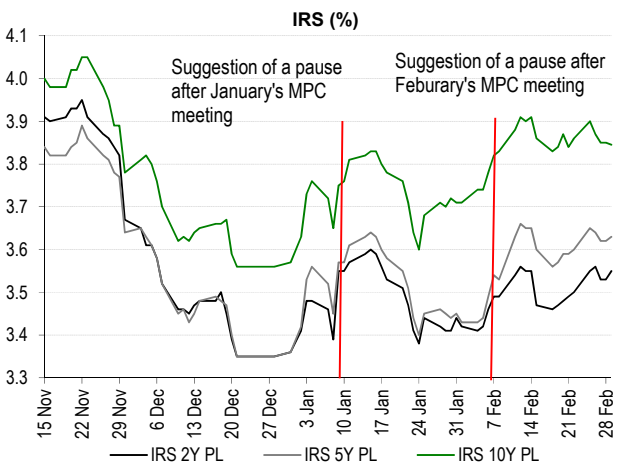
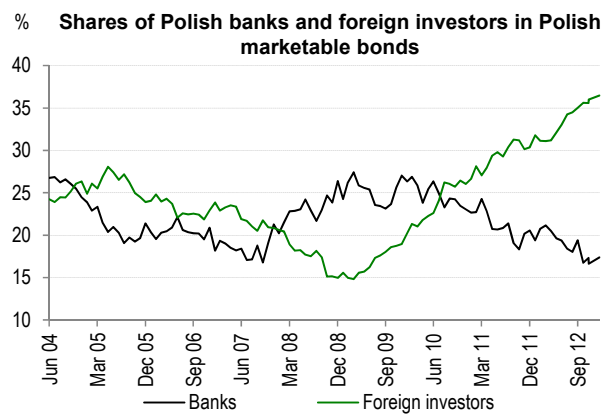
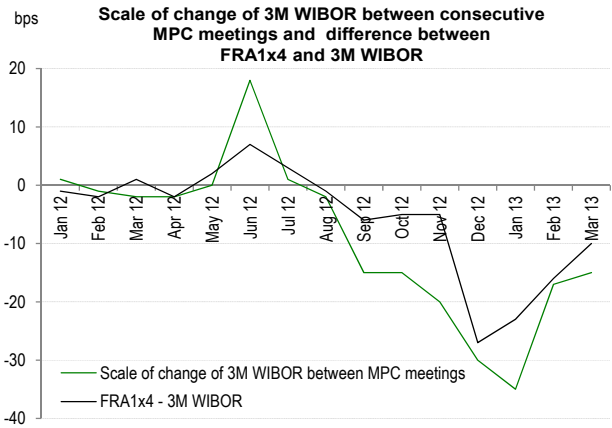


**Forint under pressure of central bank's actions**

- February's decision of the Hungarian central bank to cut rates by 25bps contributed to a weakening of the forint to 300 per euro. However, a rebound took place soon and the rate returned to 290. Friday's appointment of minister of economy G. Matolcsy to post of the central bank's governor undermined the forint. The EURHUF exchange rate climbed above 296 and stabilized close to 295 in the middle of Friday's session.
- Prospects of further cuts will hold the EURHUF at elevated level in the upcoming weeks. Crucial support is at 290.
- Behavior of EURCZK was mirroring moves of EURUSD. We have seen a gradual weakening of the Czech koruna against the single currency. EURCZK stabilized close to 25.7 at the end of the week.



**Interest rate market – The outcome of MPC meeting may weaken short end of the curve**



**Slower decline of WIBOR, faster increase of FRA**

- During the past week the money market rates declined by 1-4bps, most in case of 6M WIBOR, at smallest scale for 1M rate. FRA surged due to the releases of Polish data, mainly after the GDP publication. FRA9x12 increased by 10bps while 6x9 and 3x6 by 8bps on weekly basis.
- In our opinion the MPC will cut interest rates by 25bps. The first chart shows that the pace of decline of 3M WIBOR between consecutive meetings of the Council has declined quite visibly. This was due to two remarks on possible pause in easing cycle. We expect that in the statement from the March meeting there will be also a suggestion of break but will be presented more clearly than in January and February. Thus, the pace of decline of WIBOR may decelerate further while FRA may continue to increase.

**Flattening of IRS and bond curve**

- During the past week the IRS and bond curve flattened in response to domestic data. 2-10 spreads declined by 12bps (to lowest level since first decade of January) and by 6 bps (lowest since early February), respectively. All week long the trade volume on the debt market was very low.
- The Ministry of Finance informed that switching auction will take place on 7 March, and it is going to offer long-term bonds in return for buyback of PS0413, OK0713 and DS1013. Standard auction is scheduled for 20 March and offer comprises of OK0715 / WZ0117 / PS0418 worth PLN2.0-6.0bn. The Ministry will also offer 25-week T-bills on 4 March, worth PLN2.0-3.0bn. The March's offer of treasury securities is flexible, dependent not only on market situation but also on investors' demand. Head of Public Debt Department in the Ministry, informed that already 51% of 2013 borrowing needs were covered at the end of February.
- At the end of January foreign investors held Polish zloty denominated marketable bonds worth PLN195.6bn. After biggest monthly nominal increase since June 2012, the 9th consecutive record was established.

**MPC statement may push IRS up**

- We expect the MPC to trim NBP rates by 25bps. This may prove surprising for the market as recent data (on industrial output, retail sales and finally on GDP) has been interpreted by investors as rather limiting chances for a rate cut. Consequently, if the MPC meets our expectations this may generate the short-term impulse for IRS, FRA and bond' yields decrease.
- However, we assume that in the statement from the meeting the MPC will signal a pause more clearly than in the last two months. In our opinion, this suggestion on break may have similar impact on the interest rate market as previous ones. If swap rates approach local peaks established in first half of February, then after next macro data (low CPI and output) some downward correction may occur again.
- Though the results of Italian elections indicate that we will face some period of unstable situation in this country, the global market stabilised quite fast. Bernanke defended the QE3 when talking at US Congress and suggested at the same time that labour market has improved recently. At the end of the week monthly data from US labour market will be released and shall attract investors' attention. This publication will be most important, next to MPC statement, event for the long end of the IRS and bond curve.

---

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