Bank Zachodni WBK

Weekly economic update

15 – 21 April 2013

During the first days of the week the global market was still under the impact of decision of the Bank of Japan and monthly US nonfarm payrolls. Hopes for a higher inflow of fresh cheap cash had positive impact on both more and less risky assets. Those expectations had – next to European debt markets – also very visible impact on domestic interest rate market. Yields of bonds and IRS reached fresh record lows (2Y rates declined below 3%) while the EURPLN plunged temporarily below 4.09. In the following days correction occurred on the interest rate market, which was triggered by results of bonds auction, at which demand was not that high. The MPC decided to keep interest rates unchanged and the message of the statement and the press conference was similar to the one from March. After Aprils' meeting we do not think that next rate cut became more possible.

This week a set of Polish data is due, among which inflation and industrial output seem to be crucial. The NBP Governor claimed that data from real economy will be more important that level of current inflation. This week we will see whether market believed him – inflation will be very low and our forecast of industrial output is above the consensus. Numerous releases are also due abroad. We expect that given latest decisions (or announcement of possible actions) by central banks, these data might be interpreted in the context of any possible response by monetary authorities. Thus, any disappointments do not have to lead to weakening of risky assets while may strengthen bond markets further (this may again be visible on the middle and long end of the Polish curve). This week the zloty will remain under the impact of Polish and foreign macro data. We expect the EURPLN to stay in the range of 4.09-4.15, so we see rather an increase from 4.10 seen at the end of the week.

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		MONDAY (15 April)					
14:00	**PL**	**CPI**	**Mar**	**%YoY**	**1.1**	**1.0**	**1.3**
14:00	**PL**	**Exports**	**Mar**	**€m**	**11 901**	**12 067**	**12 178**
14:00	**PL**	**Imports**	**Mar**	**€m**	**12 105**	**12 024**	**12 173**
14:00	**PL**	**Current account**	**Feb**	**€m**	**-1 507**	**-1 488**	**-1 546**
		TUESDAY (16 April)					
11:00	EZ	HICP	Mar	%YoY	1.7	-	1.7
11:00	DE	ZEW index	Apr	pts	42.0	-	48.5
14:00	**PL**	**Core inflation**	**Mar**	**%YoY**	**1.0**	**1.0**	**1.1**
14:30	US	Core CPI	Mar	%MoM	0.2	-	0.2
14:30	US	House starts	Mar	k	930	-	917
14:30	US	Building permits	Mar	k	945	-	946
15:15	US	Industrial output	Mar	%MoM	0.2	-	0.7
		WEDNESDAY (17 April)					
14:00	**PL**	**Wages in corporate sector**	**Mar**	**%YoY**	**2.8**	**2.1**	**4.0**
14:00	**PL**	**Employment in corporate sector**	**Mar**	**%YoY**	**-0.9**	**-0.9**	**-0.8**
20:00	US	Fed Beige Book					
		THURSDAY (18 April)					
14:00	**PL**	**Industrial output**	**Mar**	**%YoY**	**-2.5**	**-1.4**	**-2.1**
14:00	**PL**	**Construction and assembly output**	**Mar**	**%YoY**	**-14.5**	**-17.8**	**-11.4**
14:00	**PL**	**PPI**	**Mar**	**%YoY**	**-0.5**	**-0.7**	**-0.4**
14:30	US	Initial jobless claims	week	k		-	346
16:00	US	Philly Fed index	Aar	pts	3.0	-	2.0
		FRIDAY (19 April)					
		No important data releases					

Source: BZ WBK, Bloomberg, Reuters, Parkiet

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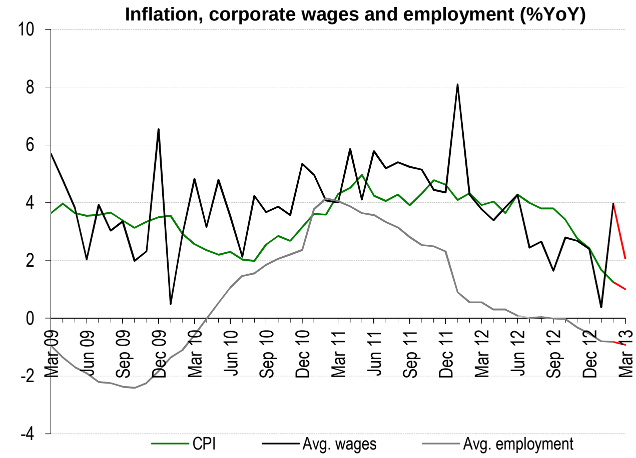
What's hot this week – A bunch of data

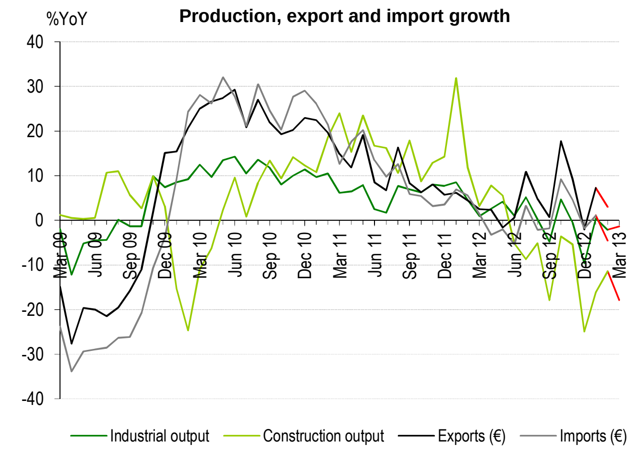


▪ This week we will see a number of important economic data releases. Already on Monday CPI inflation will be published and this will be probably the most important figure. We expect another fall of 12M CPI to 1.0%, which would be below market consensus forecast (1.1%). The low inflation (also in April) would be the result of relatively high statistical base effect of last year, as monthly change of consumer prices won't be that low (of 0.2-0.3%).

▪ The core inflation excluding food and energy prices is also expected to fall to 1%.

▪ 12M PPI index will remain in deflation territory (fall in prices also in monthly terms), even in a larger scale than in the previous month

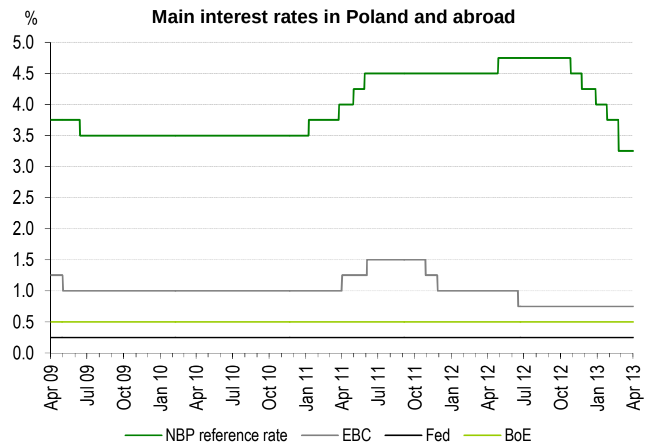
▪ Labour market statistics will confirm the continuation of employment reduction and low wage pressure.



▪ Besides inflation, the key figure for the market will be also industrial output. The data for the last month of the first quarter should not bring any breakthrough, especially as there was one working day less as compared to March last year. Our forecast indicates the scale of annual decrease in production a bit lower as compared to market expectations. On the other hand, we assume lower growth rate (deeper fall) in construction output.

▪ We forecast that foreign trade turnover for February will show moderate annual growth rate in exports, which together with small imports reduction should produce roughly balanced trade account. Nevertheless, high deficit in income balance and the negative net transfers (second month in a row) will lead to another month of current account deficit of €1.5bn.

Last week in the economy – No major changes from the MPC



▪ The Monetary Policy Council decided to keep main interest rates on hold, which was in line with expectations.

▪ Making a remark on economic information available since the previous meeting, the NBP Governor pointed particularly to lower-than-expected data on CPI, stronger zloty (after temporary depreciation), data from real economy (industrial output and retail sales) being not very surprising and GDP for 4Q2012 better than the forecast. Regarding the path of economic growth presented in the last NBP projection, central bank governor said "**there are no significant changes**", though he noticed there was an inflow of some negative news form the euro zone.

▪ As one could have expected, the MPC has left open a possibility of interest rate cut, making it conditional on the new data to be released.

Quote of the week – Medium-term CPI outlook is the key

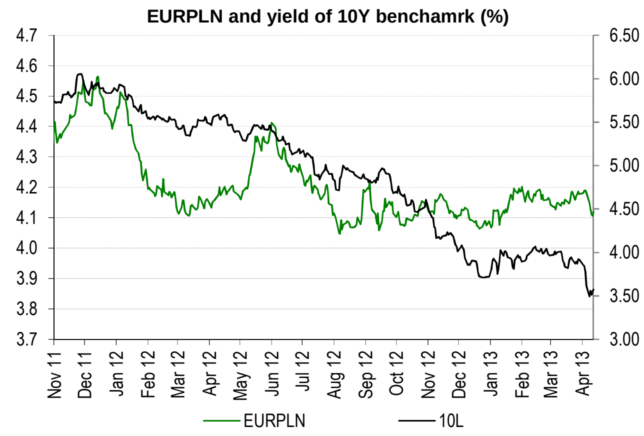
Fragments of MPC communiqué after April's meeting

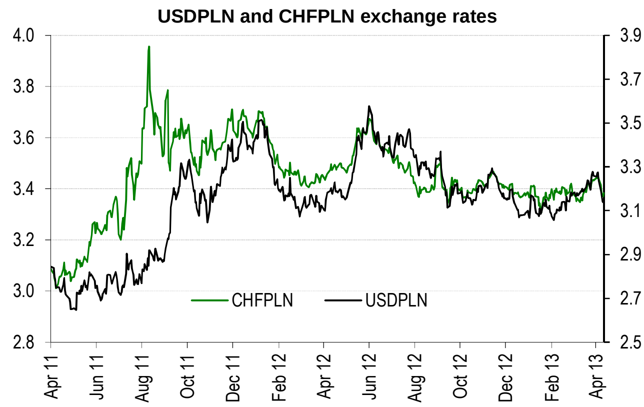
Incoming data confirm low economic growth in Poland as well as no wage and inflationary pressures. Economic activity may gradually improve in the coming quarters. However, GDP growth will probably remain moderate, which will continue to contain inflationary pressure..

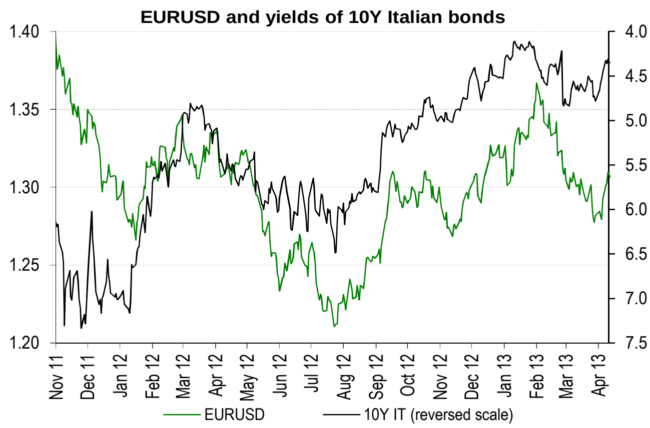
The Council's decisions in the following months will depend on the assessment of the incoming data with regard to the probability of inflation remaining markedly below the NBP inflation target in the medium term and regarding economic activity.

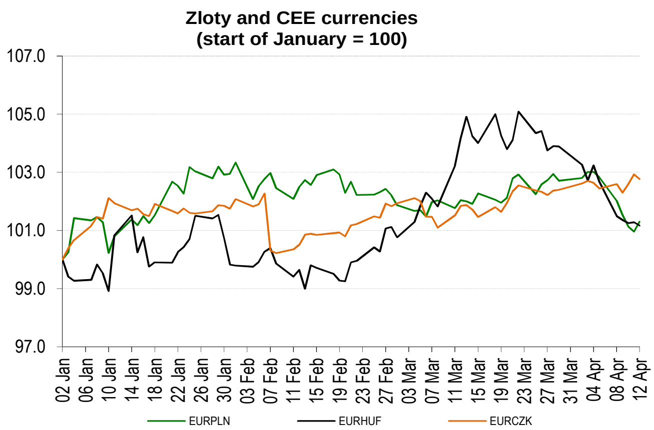
MPC's decisions in the following months will depend on the incoming data from the point of view of probability of inflation remaining markedly below the target. In March it was announced that the medium-term economic outlook would have to change to encourage the MPC's majority to cut rates further. April's statement and the press conference showed that (so far) this is not happening. So, if the MPC keeps its word and does not bow to the pressure of data showing very low inflation in the short run, and the scenario of gradual revival of the economy materialises, then there may be no more rate cuts. Of course, there is still a risk of another rate cut in June-July. However, if the MPC does not bow to the pressure of very low inflation in the short run, and the scenario of gradual revival of the economy materialises, then there may be no more rate cuts.

Foreign exchange market – Rather upward move of EURPLN









Zloty rallied after the MPC. Pressure from macro data?

▪ Last week the crucial event for the zloty was the MPC meeting. The Council's decision was in line with expectations, while rhetoric of statement did not suggest further rate cuts, which positively affected the zloty. Consequently, zloty has continued its rally. Domestic currency was also supported by still strong inflows of foreign capital on bond market. As a result, the EURPLN declined slightly below 4.09 in short run. The end of the week brought some profit taking, however the upward move of the EURPLN was limited and the exchange rate ended the week near 4.10.

▪ The domestic currency also rallied against other main currencies. However, some profit taking at the end of the week trimmed earlier gains. In weekly terms zloty was stronger by 2.5% in relations to the US dollar, by 1.7% in relation to GBP and by 1.6% against the CHF.

▪ Situation on the EURPLN chart did not change significantly last week despite higher volatility. This week we see trading range of 4.09-4.15. Macroeconomic data, which will be published this week might decide whether the EURPLN increases towards the upper limit of the fluctuation channel. The most important data for the market will be CPI inflation and industrial output. We expect the downward trend of inflation to continue and weak data from industry sector.

The EURUSD again above 1.30

▪ Last week euro rallied against the US dollar despite some negative information from the euro zone. EUR strengthened thanks to hopes that central banks will maintain scale of economic stimulus. Moreover, additional factor supporting the common currency was auction results of Italian debt. Consequently, the EURUSD increased above 1.31. Fed minutes release slightly limited upward move, but the exchange rate ended the week only slightly below 1.31.

▪ This week investors focus on macroeconomic data, mainly from the US economy. From the European side the most important will be released of ZEW index for Germany. Market assumes significant decline in index (to 42 points in April, down from 48.5 points in March). These data might affect the EURUSD in short run.

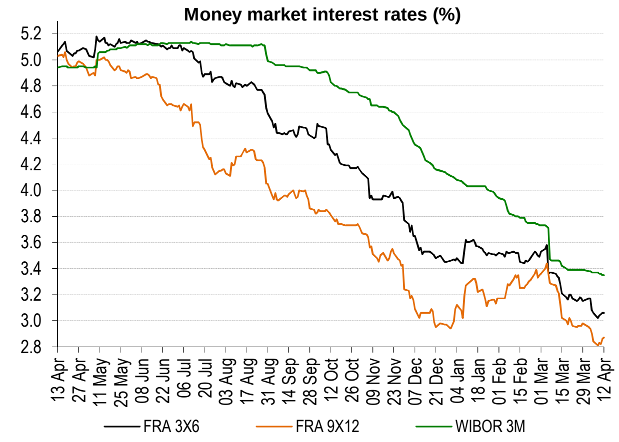
▪ Recent appreciation of euro was relatively strong. Therefore, we foresee the EURUSD to stay between 1.30-1.318 in coming days, with possibility of testing both the lower and upper limit of fluctuation band.

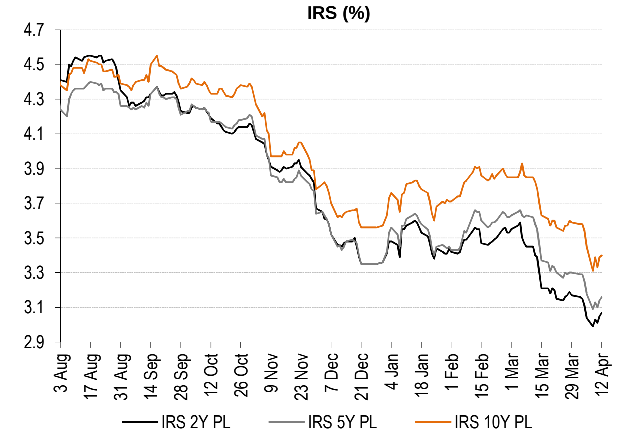
Diversified moves in CEE FX markets

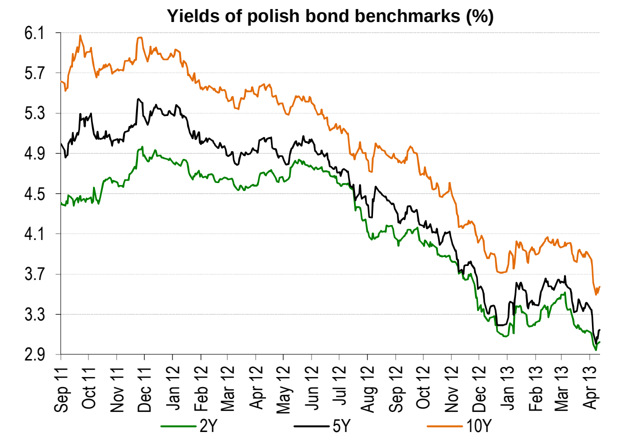
▪ Global investors' mood improvement also supported the Hungarian currency. In weekly terms HUF gained ca. 2% against the euro (more than the zloty). April's CPI inflation reading surprised with lower than expected reading, strengthening expectations that NBH will continue easing cycle in coming months. Some profit taking after this data was only short-lived. The exchange rate ended the week near 296 (important support level).

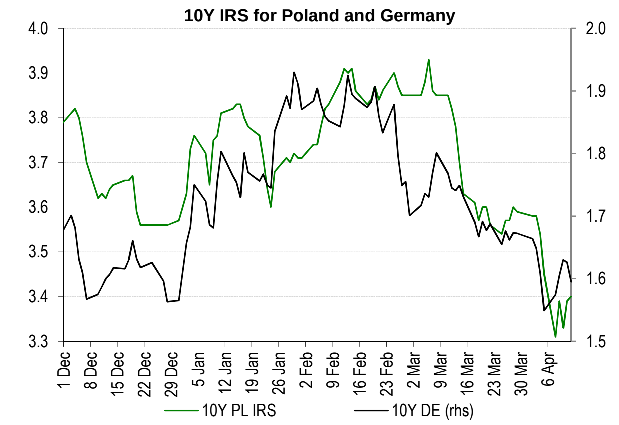
▪ Situation on the Czech koruna has been slightly different. CZK gained only in short-term due to better global mood. Uncertain political situation and still weak data from real economy caused that depreciation trend was dominated. The EURCZK gradually declined, ending the week slightly below 25.9.

Interest rate market – Data vital for short end of the curve









Marginal decline of WIBOR

▪ During the past week 1-12M WIBOR rates declined by only 2bps. Since late August 2012 rates for 3-12 months plunged by slightly more than 175bps while the main NBP rate was trimmed by 150bps. As the MPC did not "promise" more rate cuts and pointed it wants to avoid ultra-low interest rates, this should encourage the market to verify its expectations of rate cuts deeper than 25bps.

▪ In our opinion this will be visible both on WIBOR and FRA market. The latter have already increased slightly during the week, but still price in decline of 3M WIBOR by 50bps in next 9 months. We perceive this as too aggressive expectations, though inflow of next data may continue to support them for the time being. All in all, we see little room for further decline of interbank cost of cash. Our base scenario assumes stable NBP rates until the end of the year – in our view the MPC's rhetoric does not suggest that during the past months next rate cut became more possible.

High volatility of IRS and bonds

▪ At the beginning of the past week IRS curve again reached fresh all-time lows. As the rates followed the strengthening of the bond market – where the decline of yields was fuelled not only by expectations for inflow of fresh cash, but also by stop-loss orders – the 2Y IRS declined below 3%. 5Y rate established new record at 3.09% and 10Y one at 3.31%. The yield of 2Y benchmark also plunged below 3% (it reached 2.94%). The market reaction to the outcome of the MPC meeting was only temporary and marginal – lack of a rate cut pushed yields of bonds and IRS slightly up while after the press conference the recovery was recorded. Visible impact on the interest rate market was provided by results of bond auction.

▪ Poland's Ministry of Finance sold T-bonds DS1023 worth PLN3.05bn (demand at PLN3.9bn) and WZ0124 worth nearly PLN2bn (demand at PLN3.2bn). Auction yield of 10Y benchmark DS1023 (3.515%) was slightly lower than on the secondary market. However, from investors' point of view it was more important that the demand for Polish assets was relatively low. Taking into account the latest circumstances on global markets, starting with Bank of Japan action (rally on the European debt markets and also on Polish), recorded demand seemed to be – as market showed – disappointing. That was an impulse for upward move of IRS and bond yields in the following days.

▪ After the auction the government's gross borrowing needs are covered in ca. 63%. Deputy finance minister Wojciech Kowalczyk said that this number may climb to 70% at the end of April and to 80% at the end of Q2.

Data from Poland and abroad in the spotlight

▪ This week a set of Polish data is due, among which inflation and industrial output seem to crucial. The NBP Governor claimed that data from real economy will be more important that level of current inflation. This week we will see whether market believed him – inflation will be very low and our forecast of industrial output is above the consensus.

▪ After recent series of publication of indexes of economic activity in the euro zone, the market adjusted its expectations for fast recovery. This week German ZEW data will be released and the publication may influence market expectations regarding changes of rate cuts by the ECB (and the MPC as well) in coming months.

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, http://www.bzwbk.pl