

Weekly economic update

24 – 30 June 2013

As expected, the FOMC meeting was the key event of the past week. Ben Bernanke's speech at the post-meeting press conference, in which he suggested that the Fed may start moderating the monthly pace of asset purchases later this year, and end the purchases by the middle of 2014, sparked a massive sell-off in the world financial markets. The correction hit also the zloty and Polish fixed income market – EURPLN approached 4.35 and yield of 10Y bond rose above 4.3%). Among domestic data releases the biggest surprise was the balance of payments data, showing a sharp export rise (and raising chances of realisation of our expected scenario of export-led gradual economic revival). Other indicators were much less optimistic, showing generally low economic activity in the middle of second quarter. In our view those data, as well as the results of new NBP's projections, will convince the MPC to cut main interest rates again in July, by 25bps. However, recent comments of Council members are clearly suggesting that this may be the last rate cut in the easing cycle. This would be consistent with the scenario expected by us.

Data about retail sales, due for release this week, will probably join the set of information showing muted economic activity and supporting decision about interest rate cut in July. Much more numerous and more important for the financial market will be data releases abroad, in particular in the USA. Investors, concerned about possible tapering of Fed's quantitative easing, will be looking for more signals of growth revival in the American economy. Also, important from this point of view will be speeches of several regional Fed members, scheduled during the week.

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (24 June)							
10:00	DE	Ifo index	Jun	pts	106.0	-	105.7
TUESDAY (25 June)							
10:00	PL	Retail sales	May	%YoY	0.0	-0.2	-0.2
10:00	PL	Unemployment rate	May	%	13.7	13.6	14.0
14:00	HU	Central bank decision		%	4.25	-	4.50
14:30	US	Durable goods orders	May	%MoM	3.0	-	3.5
15:00	US	S&P/Case-Shiller home price index	Apr	%MoM	1.2	-	1.1
16:00	US	Consumer confidence index	Jun	pts	75.2	-	76.2
16:00	US	New home sales	May	k	460	-	454
WEDNESDAY (26 June)							
14:30	US	Final GDP	Q1	%QoQ	2.4	-	0.4
THURSDAY (27 June)							
10:30	GB	Final GDP	Q1	%QoQ	0.3	-	-0.3
13:00	CZ	Central bank decision		%	0.05	-	0.05
14:30	US	Personal income	May	%MoM	0.2	-	0.0
14:30	US	Consumer spending	May	%MoM	0.3	-	-0.2
14:30	US	Core PCE	May	%MoM	0.1	-	0.0
14:30	US	Initial jobless claims	week	k	350	-	354
16:00	US	Pending home sales	May	%MoM	1.0	-	0.3
FRIDAY (28 June)							
14:00	PL	Inflation expectations	Jun	%YoY	-	-	0.9
15:55	US	Michigan index	Jun	pts	83.0	-	82.7

Source: BZ WBK, Bloomberg, Reuters, Parkiet

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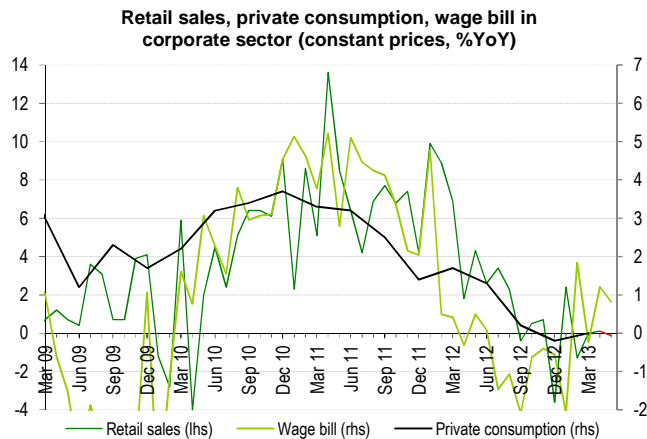
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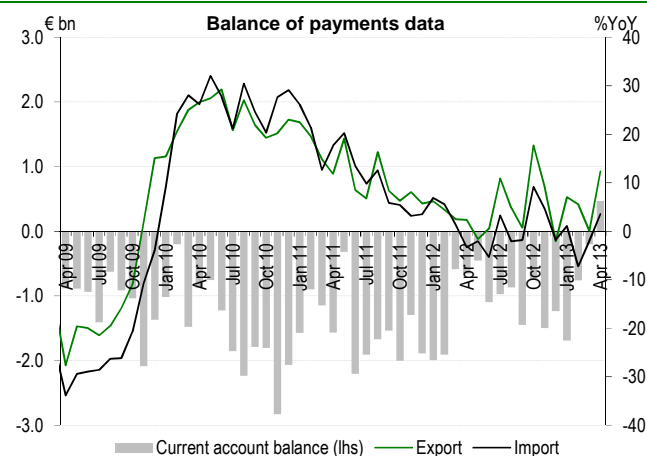
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What's hot this week – Seasonal decline of unemployment, contracting retail sales

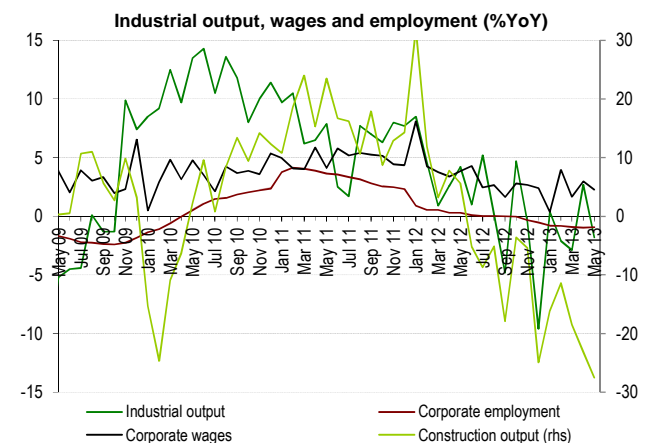


- This week we will see the last bunch of data due for release in June. We are estimating that registered unemployment rate decreased in May to 13.6% from 14.0% in April. However, in our view this was mostly due to higher employment in seasonal jobs and intervention of Ministry for Labour and Social Policy, not due to persistent revival of demand for labour. We are estimating that nominal pace of growth of retail sales remained at April's level, i.e. -0.2%YoY. Headline figure was possibly dragged down by weak results of car sales. Such a result – below market expectations – can bolster expectations that the MPC will cut rates at the upcoming meeting.
- In general, Tuesday's data will confirm weak outlook of individual consumption growth in the second quarter of the year.

Last week in the economy – Better exports, slump in construction, weak labour market



- April saw a strong acceleration of Polish export growth (by 12.3%YoY), while imports advanced more or less in line with our expectations, by 3.6%YoY. As a result, trade and current account balances posted significant surpluses.
- Still, even if April's data were under influence of one-off factors (including working days effect), it seems that revival in exports, which in our view will be the main engine of Polish economic growth in the upcoming quarters, slowly starts materializing.
- This conclusion is supported by data on May's industrial output, as some export-oriented branches posted growth in output – like furniture manufacturing (+6.7%YoY) or car manufacturing (+4.3%YoY) – despite general weakness in the manufacturing sector.



- Industrial output contracted in May by 1.8%YoY. Clear deceleration as compared to April was due to working days effect. The sector still remains in stagnation and so far data do not show any significant signs of recovery. Construction and assembly output continued deteriorating sharply (plunging by 27.5%YoY, more than expected), despite improvement of weather conditions in May. There are no signs of upcoming improvement in this sector.
- PPI inflation decreased in May to -2.5%YoY, indicating a lack of cost pressure on producers.
- Employment in corporate sector in May (-0.9%YoY) was slightly above, while wages (2.3%YoY) were slightly below expectations. We still cannot see any marked improvement on the Polish labour market, with moderate growth in labour incomes, which will be capping dynamics of consumer demand in the upcoming months.

Quote of the week – July's rate cut should end the cycle

Anna Zielińska-Głębocka, MPC member, 17.06, Reuters

There is some room to cut rates, by 25 or 50bps. I think that easing cycle should be ended in July and then we will observe what is happening in the economy.

Jerzy Hausner, MPC member, 18.06, Reuters

We are approaching a moment, where rates are adequate. July will be important, as we will see the new projection.

Marek Belka, NBP president, 19.06, PAP

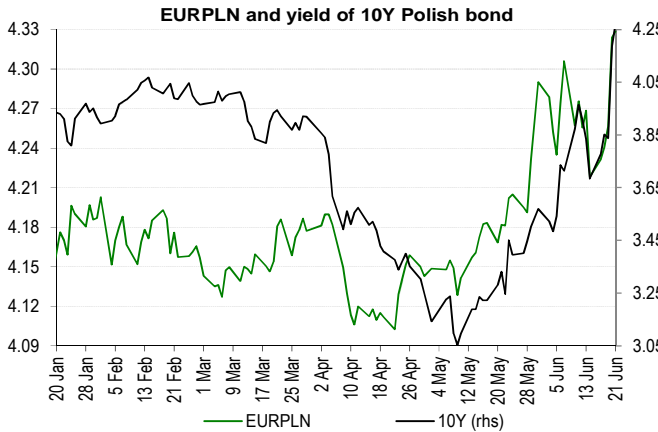
As I said already, we are close to end of the cycle. I think that the July's projection will shape our decision and then we will enter another mode, maybe "wait and see", but I do not know if it will be called like that.

Andrzej Bratkowski, MPC member, 20.06, PAP

I am supporting cut by 50bps and the July's cut should end the cycle.

Minutes of the June MPC meeting showed that majority of Council members see approaching end of the monetary easing cycle. Recent comments of several MPC representatives confirmed that they still very much agree with this opinion. They also suggested that the next decision will be strongly dependent on the new projection of CPI and GDP. A. Zielińska-Głębocka (who has probably already seen flash results of projection) revealed that CPI may return to target in 2015. Thus, we think that both the projection and recent weak data from the economy should convince the MPC to cut rates one more time in July. This will be the last reduction in the cycle; later the Council may switch to some kind of neutral bias in monetary policy.

Foreign exchange market – New wave of zloty depreciation



Strong weakening of PLN, but with no breakthrough

▪ Bernanke's press conference after the Fed meeting was the main driver of the zloty last week. Even though we saw another wave of weakening of the zloty against the euro, dollar, pound and Swiss franc, the EURPLN and GBPPLN exchange rates climbed only slightly above peaks set at the turn on May and June only temporarily, while USDPLN did not even reach them. Thus, despite rapid correction on the global market, initiated after the Fed meeting, changes on the PLN market were not dramatic.

▪ EURPLN dynamically retreated from 4.20 and reached 4.35 (an important resistance). In due course, the formation of "head and shoulders", which could have been realized last week, is no more valid.

▪ Rebound of the EURPLN at the end of the week were not considerable. Despite light gains on the Western stock markets, EURPLN remained close to 4.32, which can suggest that the zloty needs a stronger impulse to record a more significant appreciation. Domestic data may encourage to purchase cheaper Polish bonds, which can positively affect the currency. However, global market sentiment after the US data will be more important.

Plunge of EURUSD

▪ While awaiting the outcome of Fed meeting, EURUSD was hovering close to 1.34. Ben Bernanke's suggestion that the QE3 can be ended in mid-2014, expressed during the press conference, initiated a rapid appreciation of the dollar against the euro. The rate plummeted to 1.316.

▪ Stabilization at the end of the week was only temporary, the rate tested 1.316 again. Thus, it seems that investors will keep the message of Fed meetings in their minds for some time. This week we will see important data from the USA, including Conference Board consumer confidence index. Release of this indicator in May was one of the most important factors, which triggered the first wave of correction on the global market. Last month the index climbed considerably, so on Tuesday investors will be able to assess if this move was only a temporary rebound or a more persistent move. 1.316 is a major support on the daily chart, another is at 1.308. Resistance is at 1.33.

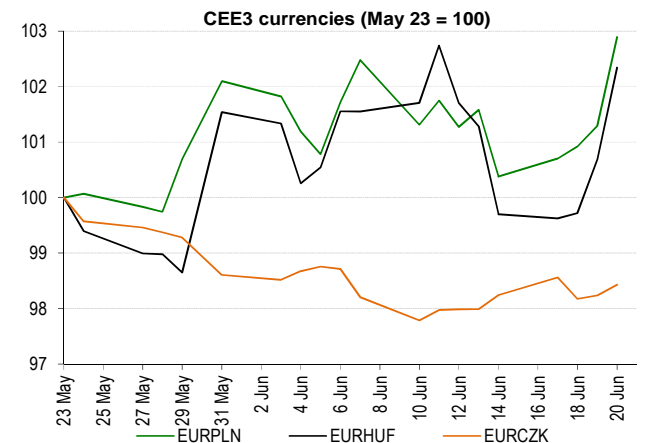
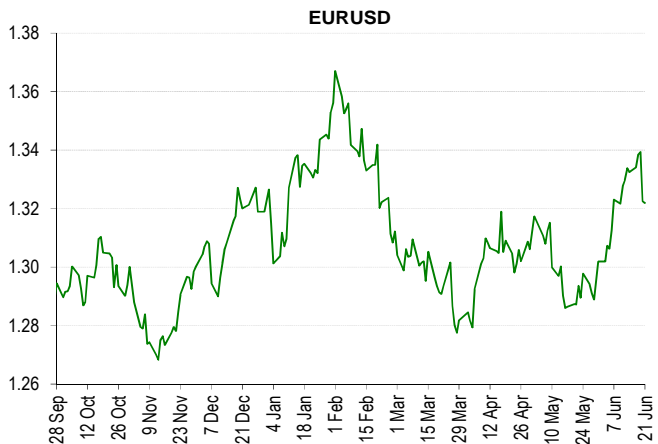
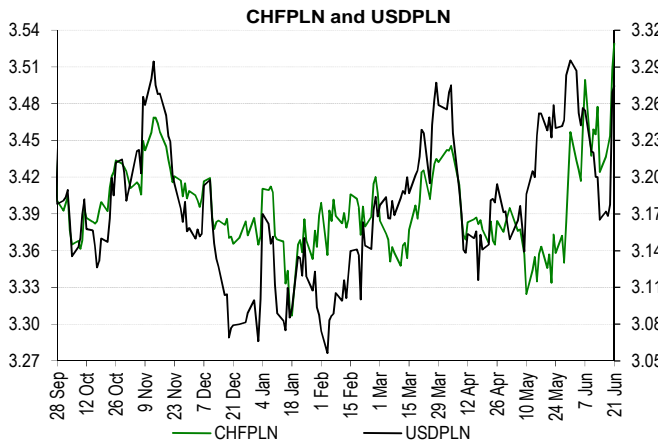
Central bank decisions important for forint and koruna

▪ Forint and koruna also suffered due to dynamic changes on the global market. The EURHUF exchange rate rebounded from support at 290 and temporarily surpassed 300. The Czech koruna – despite political instability – was outperforming other CEE3 currencies. EURCZK climbed from 25.54 temporarily to 25.9.

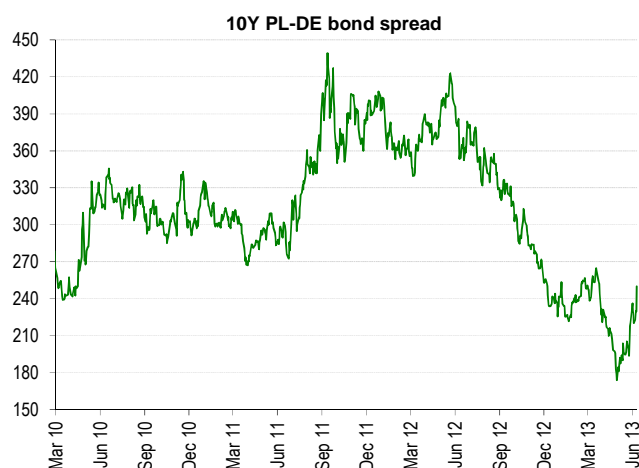
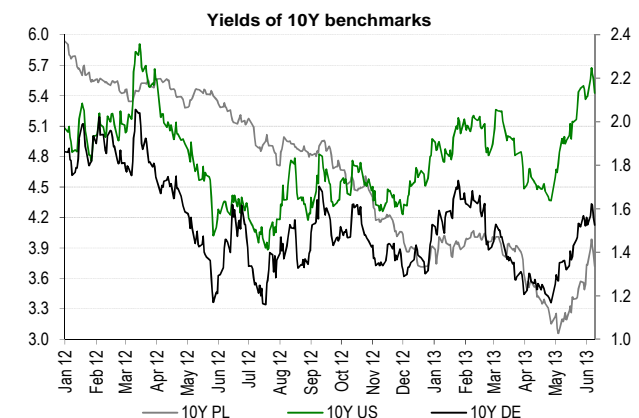
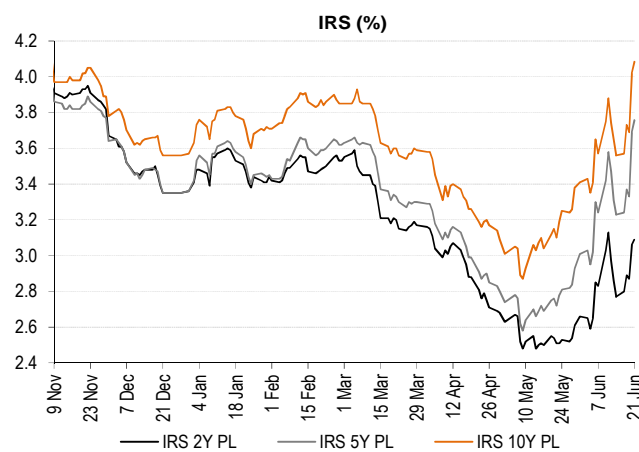
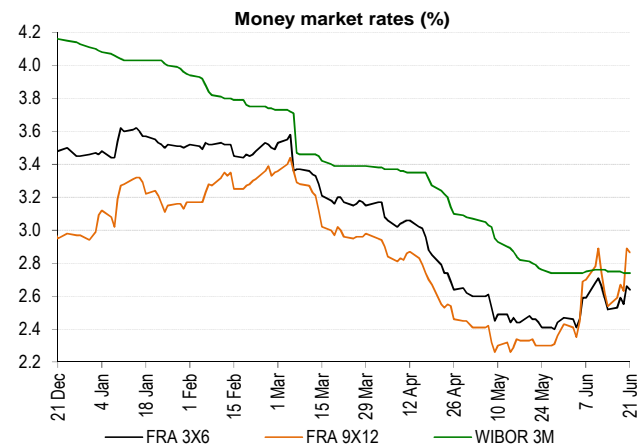
▪ Chart beside is showing behaviour of CEE3 currencies after the first suggestion of Ben Bernanke that the Fed may limit the quantitative easing purchases at some point of time. It is visible that the Czech koruna even gained slightly, while the zloty and forint lost markedly.

▪ This week the central banks of Hungary and the Czech Republic are holding meetings. Market is expecting that the latter will cut rates by 25bps.

▪ As regards the Czech Republic, after last meeting of the central bank a set of weaker-than-expected data was released (flash GDP for Q1, industrial and construction output, retail sales). This can encourage the Czech monetary authority to stress (again) the importance of EURCZK exchange rate in economic recovery. Suggestion of possible CNB's intervention may push EURCZK upwards.



Interest rate market – US and Polish data will be the key

**FRA above 3M WIBOR again**

▪ WIBOR rates remained relatively stable the whole week and moderate changes were observed only in the case of one- and three-month rate, which decreased by 3 and 2 bp, respectively. While awaiting the Fed meeting, the market did not react to the publication of local data, which were also close to consensus forecasts. On the other hand, volatility in FRA market substantially increased in reaction to Ben Bernanke's comments. Longer tenors (6X9 and 9X12) mirrored sharp moves in IRS and bond market (see below) and rose by 18 and 26 bps.

▪ Though FRA 6x9 and 9X12 are already above 3-month WIBOR, we do not perceive it as an indicator that market participants suddenly have changed expectations as regards monetary policy into tightening.

▪ This week, another piece of Polish macro data will be released. We forecast retail sales figure for May to be below market consensus, which may reinforce expectations regarding a possibility of rate cut in July, which might be reflected in short-term FRA rates.

Another wave of selling after FOMC meeting

▪ Uncertainty regarding FOMC policy led to deterioration in global moods, which was reflected in sharp increase in Polish IRS and bond yields. The sell-off intensified after Fed meeting. As a consequence, two-year IRS rose in just one day by 19 bp, while five-year by 36 bps (the most significant increase since October 2008). Swaps in 2-8 segment are above 3%, while the ten-year closed the day after Fed with the rate above 4% (for the first time since November 2012). Bond yields for five and ten year tenor increased by 30 bp, which was the strongest daily move since October 2008. However, then yields were at the levels of 6.8% and 6.64%, respectively (for 5Y twice as high as on Wednesday's close). The weakening was less significant in the front-end of the curve and therefore the curve steepened - spread 2-10 up from 107 bps to 131 bps.

▪ Wednesday's switch auction organised by the Ministry of Finance was quite successful. They sold new 2Y bond OK0116 for PLN7.8bn with yield at 2.812-2.897%, which was below secondary market level. The Ministry bought back OK0713 for PLN6.2bn and DS1013 for PLN1.1bn. We estimate that at the end of the June this year's borrowing needs may be already covered in 88%.

Macro data and supply plan in the spotlight

▪ At the end of last week we saw some stabilisation and a moderate decrease in short-term yields, while the long end suffered again. This week a number of US data will be released, which might affect market moods, especially given reaction to the last Fed meeting. Domestically, the stat office will publish data on retail sales, which we expect to surprise market negatively. However, a possible impact on yields, will depend to a large extent on global factors.

▪ The Ministry of Finance will publish the issuance plan for the third quarter. In terms of liquidity, the next three months will be quite favourable as coupon payments and redemptions will cause inflow of above PLN9bn, out of which above PLN7bn in July only due to maturity of OK0713 bond. That is why, the Ministry of Finance may take advantage of this situation (deputy finance minister Kowalczyk said last week that auction's in July and August's would be conditional).

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