

Weekly economic update

15 – 21 July 2013

Global market sentiment improved during the past week, among others due to release of minutes of the last FOMC meeting and speech of Fed's governor who said the US economy will need highly accommodative monetary policy. Consequently, prices of commodities, stocks and bonds increased. Lower worries over fast QE3 tapering triggered also sudden depreciation of the dollar. The zloty did not gain much on the improvement of market moods, it stayed above 4.30 per euro. Negative inflow from Southern Europe (mainly from Portugal) cooled optimism slightly.

This week investors' attention will focus on Polish macro data releases. We expect the CPI reached trough at 0.3%YoY in June, reaching record-low level established in April 2003. June's data from the real economy (despite some acceleration in industrial output) will still not show any visible improvement in domestic economy. In our view data should be supportive for the debt market, especially for the shorter end of curve. The domestic market will be still waiting for government's information on budget amendment (PM Tusk announced it for this week again). Investment moods may be affected stronger by comments of Fed members, including the governor Ben Bernanke. If moderate stance about the asset purchases is maintained, this may reinforce expectations that starting data of QE3 tapering may be more distant than September, currently priced-in by the markets. Apart from these comments, market moods may also be affected by release by Beige Book, weekly US jobless claims, ZEW index for the German economy and numbers about Chinese GDP for Q2. High uncertainty about these readings may generate elevated market volatility. That is why we are expecting that EURPLN and USDPLN will remain at heightened levels. Important levels for EURPLN are 4.26 and 4.35.

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD	FORECAST			LAST VALUE
				MARKET	BZWBK		
MONDAY (15 July)							
4:00	CN	GDP	2Q	%YoY	7.5	-	7.7
14:00	PL	CPI	Jun	%YoY	0.3	0.3	0.5
14:30	US	Retail sales ex autos	Jun	%MoM	0.4	-	0.3
TUESDAY (16 July)							
11:00	EZ	HICP	Jun	%YoY	1.6	-	1.6
11:00	DE	ZEW index	Jul	pts	39.0	-	38.5
14:00	PL	Core inflation	Jun	%YoY	0.9	0.9	1.0
14:00	PL	Wages in corporate sector	Jun	%YoY	2.3	2.0	2.3
14:00	PL	Employment in corporate sector	Jun	%YoY	-0.9	-0.9	-0.9
14:30	US	Core CPI	Jun	%MoM	0.2	-	0.2
15:15	US	Industrial output	Jun	%MoM	0.3	-	0.0
WEDNESDAY (17 July)							
14:00	PL	Industrial output	Jun	%YoY	1.5	1.2	-1.8
14:00	PL	Construction and assembly output	Jun	%YoY	-21.1	-20.1	-27.5
14:00	PL	PPI	Jun	%YoY	-1.8	-1.6	-2.5
14:30	US	House starts	Jun	k	950	-	914
14:30	US	Building permits	Jun	k	1000	-	974
16:00	US	Speech of Ben Bernanke					
20:00	US	Fed Beige Book					
THURSDAY (18 July)							
14:30	US	Initial jobless claims	week	k		-	360
16:00	US	Philly Fed index	Jul	pts	6.8	-	12.5
FRIDAY (19 July)							
No important data releases							

Source: BZ WBK, Bloomberg, Reuters, Parkiet

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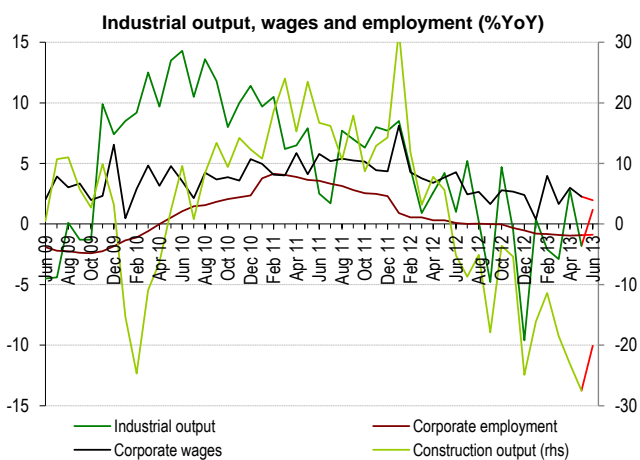
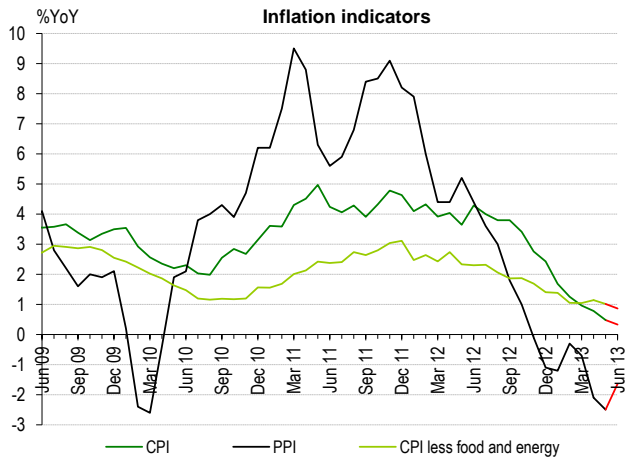
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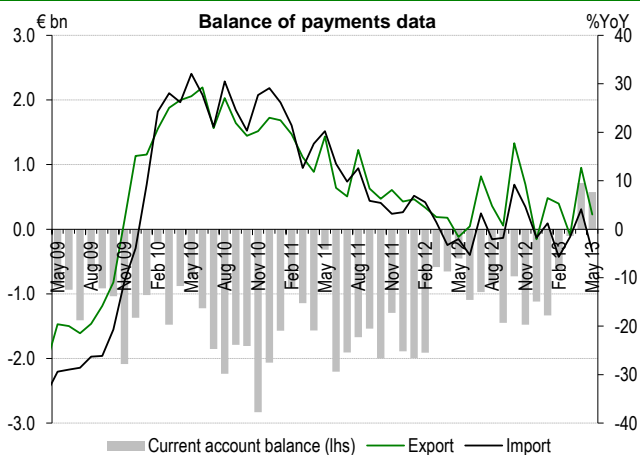
What's hot this week – Bunch of important domestic data

▪ This week is rich in releases of important macro data, which will show still weak conditions of the economy and lack of inflationary pressure and may affect the market's assessment of monetary policy outlook in Poland.

▪ We are expecting that CPI inflation fell in June to 0.3%YoY, reaching the all-time low from April 2003. Decline of annual inflation rate was supported by continuation of price war in telecommunication and base effect in food prices. Our forecasts are in line with median of market predictions. We think that the June's reading will be the lowest level this year and from July on the CPI inflation will start climbing slowly, to ca. 1.4%YoY at the year-end. Core inflation will probably also reach its year's minimum in June at 0.9%YoY (it is still quite far away from all-time low at -0.3%YoY in May 2006) and can stay close to this level for a couple of months, before climbing to ca. 1.6%YoY at the year-end. On the other hand, PPI will rebound to -1.6%YoY, among others due to the weaker zloty.

▪ June's data from the labour market will show if May's rise in employment was due to improving demand for labour or was only a one-off rebound after weak April. We are expecting a slight increase in employment (in line with seasonal pattern) so that annual growth rate will remain at -0.9%YoY. We are expecting some slowdown of wage growth.

▪ In our view growth rate of industrial output will return into positive territory (1.2%YoY), mainly due to waning negative working days effect. An important sign about future situation in industry will be delivered by situation in export-oriented branches. We expect that construction output will also rebound somewhat, but will stay deep in negative territory (-20%YoY).

Last week in the economy – Weaker exports but current account still in surplus

▪ In May we saw again a surplus on the current account (€574m) but this time this was not due to further improvement of trade balance, but surprising (one-off?) change on the income account. Pace of export growth decelerated to 3%YoY in May but we expect resuming the growth at higher pace in coming months amid revival of foreign demand. This will lead to surplus on trade account in 2013 – for the first time since early 90. – and a clear positive contribution of net exports to GDP growth.

▪ Pace of growth of money supply, deposits and loans accelerated in June but it is too early to announce already a reversal of earlier trends. Deposits of households increased as compared to May after two months of their decline, which suggests that in line with what we suspected, the outflow from deposits to mutual funds halted due to higher volatility on the financial market in June.

Quote of the week – Polish economy may perform better**Elżbieta Chojna-Duch, MPC member, 08.07, Reuters**

We should see a gradual [economic] improvement, so interest rates should remain flat. At the end of the year we will see how is the economic situation developing. But as for the time being, I see no possibility to gather a majority to support further cuts.

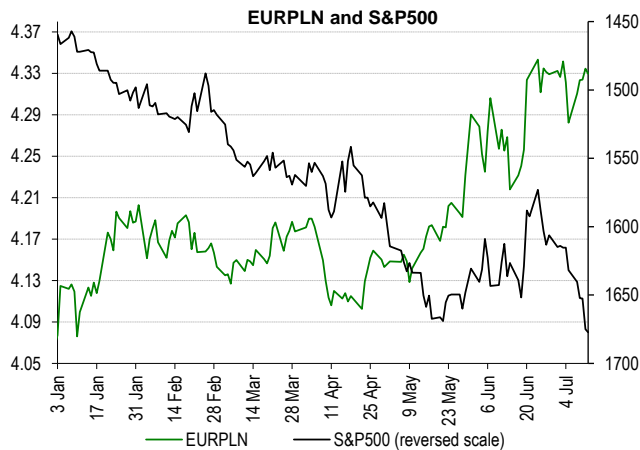
Anna Zielińska-Giębocka, MPC member, 08.07, Reuters

We cannot speak about new cycle, as we have just ended the last one. We are switching into neutral bias. I do not think that rates will need to be cut further. Our level is historically low and adequate to our conditions.

Marek Belka, NBP governor, 12.07, Reuters

July GDP projection is rather pessimistic in my view. I think that Polish economy may perform better.

Comments of those MPC members, who were most dovish and used to push for rate cuts, are clearly showing that monetary policy easing has come to an end and rates will probably stay flat until the year-end. But what happens then? Forecasts of analysts are really divergent: some are expecting more cuts, other are betting for hikes already in early 2013. Decision to end the cycle shows that the MPC is more optimistic about the economic growth than the NBP projection (see Belka's comment). In this context quite interesting is recent comment of CSO governor who was worried that GDP growth in Q2 may be lower than in Q1. In our view the GDP path presented by the NBP is realistic, but the inflation path is too low. Realization of a higher CPI may encourage the MPC to hike rates in 2H2014 even despite still not very high GDP growth.

Foreign exchange market – Zloty under pressure despite improving moods**EURPLN at elevated level**

▪ No breaking changes occurred on the EURPLN market during the past week. The zloty – just like stock indexes and the EURUSD – faced a correction after an appreciation vs. the euro and other main currencies recorded after the MPC and ECB meetings. Despite clear improvement on the global market after dovish signals from the Fed, the zloty remained under pressure. The EURPLN broke temporarily 4.34 vs. 4.26 at the beginning of the week. At the end of the week, after data on Polish current account, it declined below 4.30. The zloty gained to 3.26 per dollar from 3.39, but retreated back to ca. 3.30 at the end of the week.

▪ The past week showed that a really strong positive impulse would have to emerge on the market to generate bigger and long-lasting appreciation of the zloty. S&P500 recovered very fast after a 7.5% decline recorded at the turn of June and July and closed at all-time high last week. While indexes from Western Europe have not pared recent losses, the zloty clearly lags behind other gaining risky assets.

▪ This week four voting members of the FOMC will give speeches, including Ben Bernanke who will speak twice. Next dovish comments may thus emerge and they may temporarily support the zloty. Important levels for the EURPLN are 4.26 and 4.35. Currently, we do not see room for more visible and long-lasting appreciation of the zloty, EURPLN may reach 4.20 only around the year-end.

Sharp euro's appreciation vs. the dollar

▪ Minutes of the last FOMC meeting and speech of Ben Bernanke had biggest impact on the EURUSD during the past week. Fed's governor reassured that the central bank will keep highly accommodative monetary policy amid low inflation. This tamed market worries over fast tapering/termination of QE3. Consequently, the EURUSD surged to 1.32 (highest since late June) after a decline to the lowest level since April (ca. 1.275).

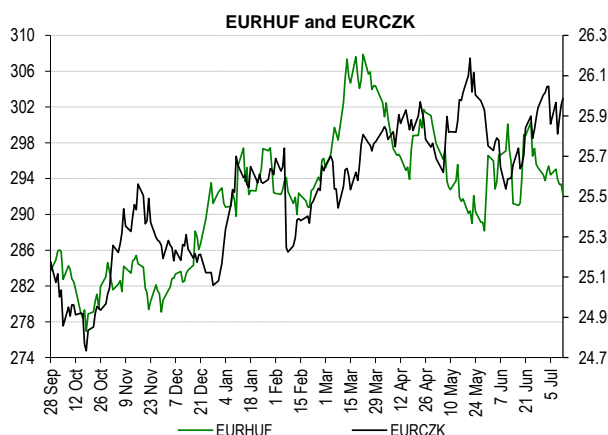
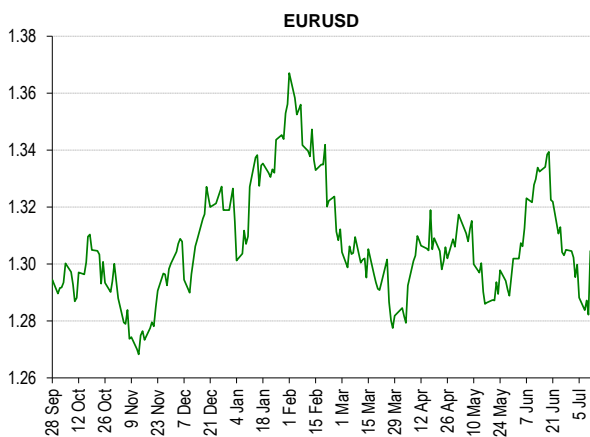
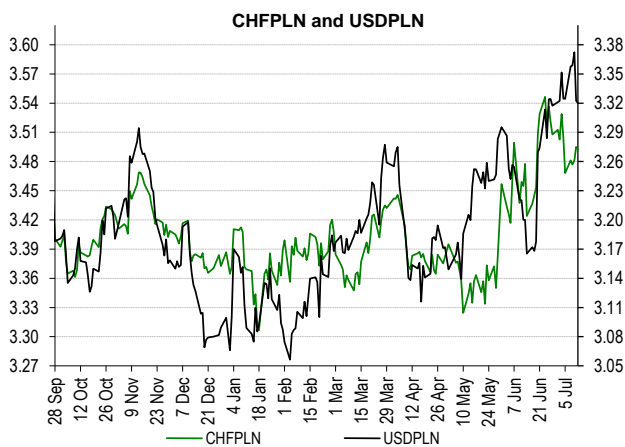
▪ Despite correction to 1.30 at the end of the week, it seems that after last speech of the Fed governor the potential for deeper falls of the EURUSD is significantly lower. This week will be rich in comments of FOMC members, we will also see a row of important US data. If these FOMC members will try to calm the market, then further test of 1.32 are likely.

Forint is gaining, koruna losing

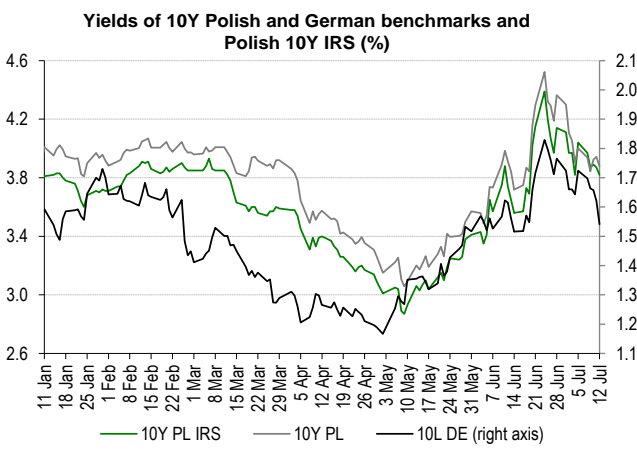
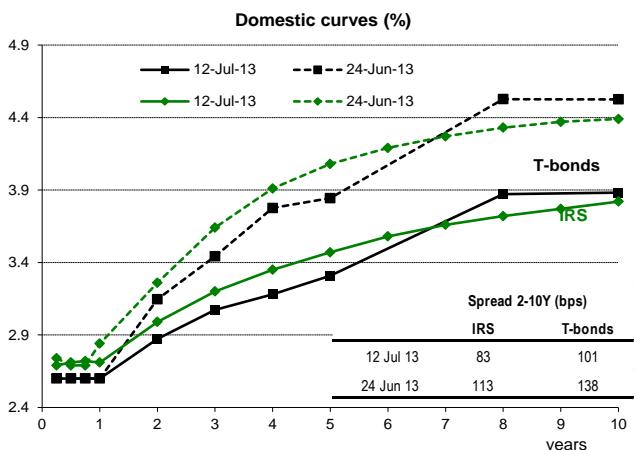
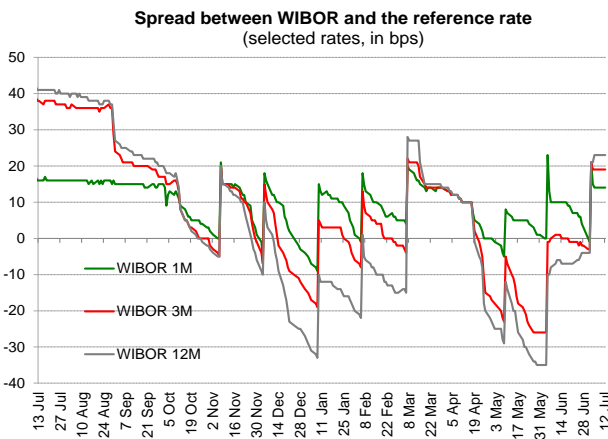
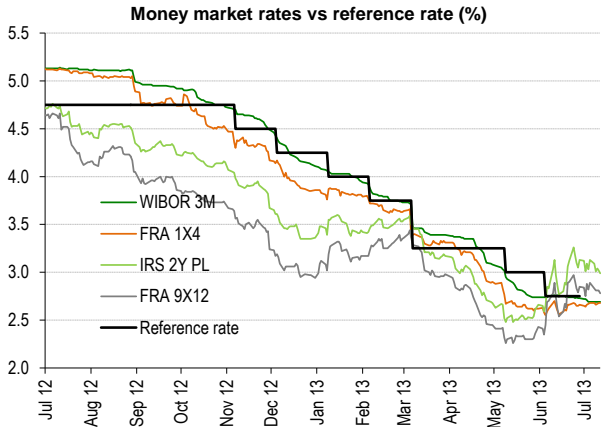
▪ The forint was losing since the beginning of the week, similarly as the zloty. The EURHUF exchange rate climbed temporarily from ca. 292 to slightly above 294. Considerable improvement of global market moods supported the forint, which gained against the euro so the rate declined temporarily to almost 291. The forint was not undermined by minutes for the last meeting of Hungarian central bank, which showed that further easing of monetary policy is possible.

▪ After short-lived strengthening at the beginning of the week, the Czech koruna was losing against the single currency. In June Czech CPI was visibly above expectations (1.6%YoY as compared to 1.3%YoY), but easing worries about further monetary easing by the Czech central bank supported the koruna only temporarily. The EURCZK exchange rate climbed to 25.7 from 26.0 in the followings days, so it was only slightly below important resistance at 26.18, which has limited potential for rise in exchange rate since 2010

▪ No important macro releases are planned for this week in the Czech Republic and in Hungary. Thus, global moods are crucial for these currencies.



Interest rate market – Some rebound due to risk-on mode



Stable money market

- Last week the money market was calm and stable. Both WIBOR and OIS rates (after some decline at the beginning of the week) were more or less unchanged. Low investors' activity was also observed on FRA market. After slight decline at the beginning of week, FRA rates stayed unchanged. What is more FRA still suggests gradual increase in WIBOR in 9 months perspectives.
- As we mentioned in the [weekly report](#) in mid-June, adjustment on WIBOR curve due to end of easing cycle by the MPC in July brought only limited decline in case of 1M and 3M rates. Since July's MPC decision up to now those rates declined by 10bps (to 2.64%) for WIBOR 1M and by only 3bps (to 2.69%) for WIBOR 3M. In case of longer rates, we noted gradual increase (by 1bp for 9M and by 2bps for 12M). What is more WIBOR curve has shifted from relatively flat to normal one.
- This week investors will focus on domestic macro data (calendar for this week is heavy). From the market side the most important will be release of CPI inflation for June (15.07) and industrial output (17.07). We think that continuation of disinflation trend will be supportive for the front end of curve (up to 3M), bringing some moderate decline in rates.

Risk-on mood supports domestic debt market

- Last week interest rate market slightly rebounded, however IRS market strengthened more than T-bond ones. It came from global mood improvement due to unexpected dovish statement of Fed's governor. In weekly terms IRS curve shifted down by 11-17bps (with the deepest decline in case of 5Y and 10Y rates), while T-bond curve went down by 9-13bps (with the highest decline in case of 5Y benchmark). What is more both, IRS and yield in 10Y sector fell below 4%.
- One should notice that asset swap spread (ASW) widened in 10Y sector. It was negative (-3bps) at the beginning of the week, while at the end it moved to positive territory, reaching +8bps. In our opinion, upcoming macro data from domestic economy (together with positive global mood) might cause further widening of ASW in 10Y sector towards 20bps.

Macroeconomic data in the centre of attention

- On the fixed income market investors' activity declines due to summer holiday period. Notwithstanding, we foresee macro data, which will be released this week might (even in short-run) influence the mood on the domestic debt market. We think that further decline of CPI inflation rate (our forecasts: 0.3%YoY, which is in line with market consensus) should support the front end of the curve. Additional supportive factor might be data from industry sector (our forecast of industrial output is slightly below market consensus).
- The mid and long end of curves will stay under strong influence of mood on core market. Still high appetite for risky assets should support gradual strengthening, or even stabilization of yields and IRS rates for 5Y and 10Y sectors. It might result in slight narrowing in 2-10Y spread.

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