Bank Zachodni WBK

Eyeopener – daily update

Waiting for inflation data

11 July 2005

While crucial data for the perspective of the Polish economy in 2H05 (on industrial output and retail sales) will be released only next week, some information will be published in the following days. Data from the labour market should support hopes for improvement in economic situation, however the most important from the market perspective will be June's inflation figure, to be released on Thursday. While forecast of the Ministry of Finance (1.3%) seemed to influence market expectations (1.4-1.5%), we think that CPI inflation may be slightly higher (though still much lower than May's 2.5%) amid no sharp fall in food prices and higher fuel prices.

According to *Rzeczpospolita* daily finance minister Mirosław Gronicki narrowed the range of planned budget deficit for 2006 to PLN29-33bn from PLN28-34bn. This still shows unfavourable asymmetry against the previous target of PLN30bn. On Friday, the parliament approved the bill, which allows a return of part of VAT for construction materials for individuals. This will cost the budget above PLN4bn within three years, but according to finance minister this was already included in the next year's budgetary assumptions.

Also, *Parkiet* daily presented view on future fiscal policy of Law and Justice's (PiS) economic expert Kazimierz Marcinkiewicz, who said that they would like to freeze the budget deficit at PLN30bn over the next four years. PiS economic programme is to be presented within 10-15 days. Last week, Civic Platform's (PO) official said that their economic programme will be known in August. The two parties are likely to form cabinet after elections.

What's hot this week

Data on balance of payments for May already tomorrow

After one-week break from economic data releases in Poland, in the coming days we will see a couple of statistical indicators that could be important for the financial market. On Tuesday, the NBP will release balance of payments figures for May. They will appear no more than ten days after the data for April have been published, which results from the fact that since this month the central bank returns to the 'old' calendar of BoP data releases, abandoned temporarily due to problems with data collection after EU entry. The data are expected to show slight surplus on the current account, amounting to €80m, after over €500m surplus recorded in April. This would be achieved amid moderate deficits on the trade account and income account (€250m and €300m, correspondingly), and consistently high surplus in the current transfers (over €500m). Growth rates of exports and imports should return to fairly strong levels, both of about 11%YoY, after recovering from negative impact of very high statistical base, confirming strength of domestic demand and persistently high external interest in Polish goods and services. The data should be slightly positive for the zloty, confirming shrinking imbalance on the external account (12-month cumulative C/A deficit should fall to only 0.1% of GDP from 0.4% after April).

… and they should be positive again, showing a surplus on current account, and 12M deficit of only 0.1% of GDP

Sharp fall in CPI inflation expected in June

On Thursday, the market will eye CPI inflation figure for June released by the CSO. A significant drop in inflation rate by ca. 1 pct. point from May's 2.5% is widely anticipated, amid strong effect of high statistical base, caused by surge in food prices just after Poland's entry to the EU. Even significant rise

Maciej Reluga Chief Economist (22) 586 8363

Piotr Bielski (22) 586 8333
Piotr Bujak (22) 586 8341
Tomasz Terelak (22) 586 8342 Email: ekonomia@bzwbk.pl

... though our forecast is above market consensus

in fuel prices would not be able to prevent inflation from falling this time. We predict inflation to reach 1.6%YoY, while most of market analysts are slightly more optimistic, forecasting 1.4-1.5%YoY. The lowest forecast was presented by the Ministry of Finance, which expected CPI growth to fall to 1.3%YoY, which requires very deep fall in food prices (of close to 2%MoM).

Relatively high growth in money supply expected

Also on Thursday, the NBP will release money supply figures. M3 growth is expected to slow down a little in June (after reversal of one-off impact of credit surge for purchase of Lotos shares in May), however still remaining at quite high level of 12%YoY (against 13% in May). It will be important to see developments on the credit market, which showed signs of gradual recovery in recent months. We expect credit growth to keep picking up, confirming forecasts of faster growth in consumption and investment in the second half of the year.

Data from the labour market will be important form the monetary policy point of view

Friday will see data about average wages and employment in enterprises sector. They should confirm gradual, though not extremely speedy improvement on the labour market. Employment is forecasted to rise 1.7%YoY in June, only a notch higher than in May (1.6%), however maintaining in positive trend initiated in early 2004. In turn, wage growth could accelerate to 3.3%YoY from 3.0% in May. Moderate, yet persistent growth in employment, coupled with steadily accelerating pay rise and quickly falling inflation would result in significant improvement in households' real disposable income. In June, total wage bill in enterprises sector is forecasted to rise 5%YoY in nominal terms, and 3.3%YoY in real terms, which would be the highest rate of increase since March 2004 (when the MPC started to be afraid of price-wage spiral). What is more, this effect would probably strengthen in the subsequent months, and we should see over 4.5%YoY real rise in corporate wages in the second half of the year, which would be a factor supporting acceleration in private consumption growth.

While corporate wages still rise moderately, employment growth is accelerating supporting wage bill (especially in real terms amid falling inflation)

Budget surplus in June alone

At the end of the week, on Thursday or Friday, the Ministry of Finance will release preliminary data on state budget realisation in June. According to earlier hints given by the ministry's officials, the data should be quite positive, showing that budget gap after six months of the year reached ca. 50% of the plan for 2005. It would be well below average level in the corresponding period of previous years (except for 2004), and would imply that the budget achieved a surplus in June alone. Such good result was possible thanks to several factors: a delay in compensation payments for pensioners, transfer of 2004 profit from the NBP, and – according to MF official hints – quite good performance of tax revenues.

<u>Bottom line</u>: This week's set of information about Polish economy should support hopes for improvement in economic situation in the second half of the year. However, crucial will be data on industrial output and retail sales, to be released next week.

The zloty trading ranges (08.07.2005)

	Min	Max	Fixing
EUR	4.0670	4.0980	4.0885
USD	3.4000	3.4350	3.4351

F/X rates (today's opening)

EURUSD	1.2000	**CADPLN**	2.7820
USDPLN	3.3910	**DKKPLN**	0.5458
EURPLN	4.0744	**NOKPLN**	0.5166
CHFPLN	2.6134	**SEKPLN**	0.4311
JPYPLN*	3.0305	**CZKPLN**	0.1351
GBPPLN	5.9097	**HUFPLN***	1.6463

*per 100 units

Treasury yield curve (08.07.2005)

T-bills	Yield	Change (bp)
3M	4.55	0
6M	4.52	0
9M	4.38	0
12M	4.35	0
Bonds		
2Y	4.46	1
3Y	4.51	-2
4Y	4.58	0
5Y	4.57	-2
8Y	4.61	1
10Y	4.64	2

WIBOR rates (08.07.2005)

Term	Rates	Change (pb)
O/N	5.11	8
T/N	5.11	4
SW	5.06	2
2W	5.04	0
1M	5.00	0
3M	4.72	-1
6M	4.58	1
9M	4.51	-1
1Y	4.49	0

Market monitor

The zloty strengthened in Friday morning in spite of the EURUSD rate trading near 1.19 mark, as fears of outflow of capital from the Polish market following events in London faded. The EURPLN rate breached 4.07 mark, but stabilised slightly above that level ahead of US labour market data. USDPLN rate hovered around previous close not showing any directional change. An increase in the euro value in core markets to 1.194 caused the zloty to rise against the dollar to 3.405 with stable performance against the euro.

Bonds little changed during initial part of Friday's session ahead of US payrolls release, as Bunds stabilised after unwinding safe haven buying. Weaker than expected US payrolls induced Bunds to recover, but did not have major impact on the Polish interest rate market.

Ministry of Finance will offer at Monday's regular auction 1y bills worth PLN400m and 13-weeks bills – PLN100m.

Friday's movements in financial market were not major ones, as market participants clearly decided to reduce their activity after enormous volatility on Thursday. Even payrolls data, though a bit weaker than expectations, were able to enliven only slightly EURUSD market. Upon that calmness and lower liquidity the zloty benefited. It gained mainly to the dollar, against which it was losing throughout the majority of the week.

***Bottom line:* During Friday's session the zloty strengthened, especially to the dollar following data from US labour market. Treasury papers actually did not change their performance amid lower Bunds' liquidity. The outset of the week is going to be calm, as no important publication is scheduled.**

International update

US employers created 146,000 jobs in June, below analysts' forecasts, but unemployment rate fell to 5% against expectations of 5.1%. Job growth in April and May will be revised up to 292,000 and 104,000, boosting count by 44,000 payroll jobs. The drop in unemployment rate was mostly due to a slight increase in the workforce.

Today there are no important releases scheduled for Monday in international markets.

Additional information is available on request. Please contact Bank Zachodni WBK S.A. Treasury Division, Economic Analysis Unit, ul. Marszałkowska 142, 00-061 Warsaw, Poland, phone (+48 22) 586 83 63, email ekonomia@bzwbk.pl, http://www.bzwbk.pl