

Eyeopener – daily update

GDP data due today

30 January 2006

After construction catastrophe and national mourning binding until Wednesday, political scene should calm down for a while. Therefore, market participants will focus on important economic events due for this week. Today, the CSO will release preliminary GDP data for 2005, while tomorrow the MPC will announce decision on interest rates and the new Inflation Report will be published. We predict GDP grew 3.4% in the whole previous year, which implied ca. 4.5% rise in the final quarter. Market consensus is consistent with our predictions. If the actual figures are not much better than the forecasts, they should not be an obstacle for widely expected 25bps rate cut.

Deputy finance minister Cezary Mech said on Friday that Poland proposed during discussion with the European Commission so that countries with public debt lower than 60% of GDP could include such institutions as Polish open pension funds into the public finance sector. It is hard to expect that the EU side could accept such proposition in a foreseeable future.

What's hot this week

Focus on GDP figures and news from the central bank

At the beginning of this week Polish financial market will focus on GDP data for 2005, MPC decision, and publication of new Inflation Report. The second part of the week will be dominated by data releases abroad, while politics should recede into the background amid persisting uncertainty regarding future political scenario.

GDP growth in 4Q05 is estimated at around 4.5%

GDP figures will be released today at 12:00 local time during Central Statistical Office's press conference summarising economic situation in December. Although the CSO will show data for entire year, it will be possible to extract numbers for Q4 as well, which will be crucial for the market, giving an idea of strength of economic revival at the turn of the year. Market consensus (and also our forecast) shows GDP growth in 2005 at 3.4%, which implies ca. 4.5% rise in the last quarter. Such figure would confirm very good performance of the economy, but should not be an obstacle for slight monetary easing, given continuously low pressure on prices reflected in virtually all inflation measures. According to our predictions, pickup in economic growth should be achieved amid increasingly strong domestic demand (over 3.5%YoY in Q4 in our view), although net exports contribution should be still strongly positive (responsible for almost 1 pp GDP rise). We forecast investment growth acceleration in the fourth quarter to over 6%YoY and private consumption growth by more than 3%YoY, which means that whole year figures should be at 4.9%YoY and 2.3%YoY, correspondingly. Such results should be supportive for the zloty, at the same time being neutral for interest rate market, as they will not rule out a cautious interest rate reduction this week.

...amid strengthening domestic demand

...but this should not be an obstacle for a rate cut

The Monetary Policy Council's decision will be announced the next day after GDP publication. We believe that good inflation prospects will allow for 25

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Eyes on official statement and the new Inflation Report

bps rate cut, as despite acceleration in economic growth, it seems that risk of CPI going above 2.5% inflation target in the medium term is rather limited. Market players are deeply convinced that such monetary easing will take place on Tuesday, thus its materialisation should be neutral for the market. However, investors will carefully eye an official statement of the MPC released after the meeting, as it would probably refer to the newly updated Inflation Report to be released shortly after, and could include important hints regarding Council's assessment of inflation prospects. The contents of Inflation Report would be also a key information influencing market's interest rate expectations; but timing of its publication is still unknown.

Political scene should calm down for a while amid national mourning

As regards political scene, uncertainty regarding conclusion of recent havoc in the parliament will persist. No final decisions regarding either premature election or some pact with opposition should be expected in the nearest days, especially in the period of national mourning lasting until Wednesday, which could give investors some relief for a while. However, it seems apparent now that Poland's president Lech Kaczyński will not receive 2006 budget bill for signature before end of January, and thus door to fresh election will be open until 14 February. It is really hard to predict whether he will execute this option and what will happen on the political scene in this period, but it is more and more clear that it will be not a PiS-PO coalition. A new worrying signal is that in the weekend's interview with Gazeta Wyborcza daily PO leader Donald Tusk strongly declared that his party will not allow to dissolve the parliament against the constitution (as the opposition believes that president's interpretation of deadline for completing budget work is wrong, and it should be 18 February rather than 31 January), and that in case of such move there will be great political destabilisation and one should consider acts of citizen's disobedience. Such strong declarations could spoil investors' sentiment in case of no compromise solution between ruling PiS and the opposition.

Bottom line: *The week will be dominated by GDP data and MPC decision on interest rate, while politics should recede to the background but only for a while. Good economic data could be supportive for the zloty, although a scope for appreciation will be limited by looming risk of political destabilisation.*

What's hot today

Good start of the 2006 budget

2006 budget performed very well in January

An anonymous source at the Ministry of Finance said on Friday that state budget deficit after January reached 5-6% of the full-year plan while earlier projections pointed to 8-10%. This would mean that January of this year was almost as good for the state budget as the first month of the previous when the gap reached 4.3% of the PLN35bn initial deficit target (and 5.6% of the PLN28.6bn actual outcome) and much better than multiyear average of above 10%. According to the source, budget revenues performed very well. This suggests economic activity remained high at the beginning of 2006, but one should also remember that a part of budget revenues were transferred from December. The information is not important for the market at the

moment, amid many other more relevant events, but it is worth to be aware that performance of state budget throughout this year should not come across any major problems.

Bottom line: Performance of this year's budget should not be important issue for the market.

Market monitor

On Friday session zloty appreciated against the euro and lost versus the dollar. Polish currency stabilised after Thursday depreciation as political risk and downgrading of Hungarian credit rating outlook weighed on the FX markets in the region. Finally zloty gained versus the single currency from 3.8265 at the opening to 3.8145, while the USDPLN rate initially fell from 3.134 to 3.1177 though later on jumped to 3.1461, and was mainly influenced by the EURUSD rate moves. After release of advance Q4 U.S. GDP data the dollar lost against the single currency from 1.2196 at the opening to 1.2230. However, inflation component of GDP data was quite strong and supported expectations on rate rise in January, which was positive for the dollar. New home sales figure appeared to be stronger than forecasted and in the result the greenback recovered losses and appreciated to 1.2122 and 1.2098 late on Friday.

Fixed income market slightly strengthened after a few days of yields' rise, mainly in reaction to core bond markets behaviour. Investors await MPC's decision that is due on Tuesday and overwhelming majority of analysts think that the reference rate will drop by 25 bps. Market will focus on the tone of the official communiqué and it will look for signals suggesting further monetary policy easing. Political situation will still affect Polish markets though amid national mourning and fewer political disputes in the nearest time the market should focus mainly on economic news. U.S. Treasuries strengthened after much lower than expected U.S. GDP data, but as much unexpected higher home sales figure trimmed losses and supported American government bonds, and 10Y yields rose from 4.48 after GDP data to 4.51% after housing market news and from 4.52% on Thursday closing.

Today the market will focus on GDP data for 2005, which if stronger may support the Polish currency, though it should hardly affect MPC decision of rate cut on Tuesday.

Bottom line: Zloty appreciated against the euro and erased Thursday's losses. Bonds slightly strengthened on yields drop on core bond markets and amid expected Tuesday's rate cut. The market will focus on GDP data, which may be zloty supportive.

International update

In this December money supply rose in the euro zone by 7.3%YoY as compared to market forecast at 7.5% and 7.6% a month before. The 3-month figure soared by 7.6%YoY.

The zloty trading ranges (27.01.2006)

	Min	Max	Fixing
EUR	3.8130	3.8370	3.8310
USD	3.1200	3.1500	3.1379

F/X rates (today's opening)

EURUSD	1.2104	CADPLN	2.7418
USDPLN	3.1590	DKKPLN	0.5186
EURPLN	3.8241	NOKPLN	0.4803
CHFPLN	2.4985	SEKPLN	0.4172
JPYPLN*	2.7311	CZKPLN	0.1364
GBPPLN	5.6413	HUFPLN*	1.5541

*per 100 units

Treasury yield curve (27.01.2006)

T-bills	Yield	Change (bp)
3M	4.15	-3
6M	4.15	-3
9M	4.15	-3
12M	4.14	0
Bonds	Yield	Change (bp)
2Y	4.4	-1
3Y	4.6	3
4Y	4.75	0
5Y	4.82	-1
8Y	4.87	1
10Y	4.95	-1

3Y - DS0509, 4Y - PS0310, 5Y - DS1110

WIBOR rates (27.01.2006)

Term	Rates	Change (bp)
O/N	4.65	6
T/N	4.65	6
SW	4.50	0
2W	4.47	-3
1M	4.43	-1
3M	4.39	-1
6M	4.38	0
9M	4.38	0
1Y	4.38	0

New home sales in U.S. rose in December from revised 1.233m units in November to 1.269m units annually, while market consensus pointed to 1.225m.

According to the Department of Commerce, Q4 U.S. GDP amounted to 1.1% and was surprisingly low as analysts expected 2.8% from 4.1% in Q2.

Today Personal Consumption Expenditures index will be released at 13:30 GMT. This week host of data are going to be published, and important events such as Fed and ECB decisions will take place.

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