Bank Zachodni WBK

Eyeopener – High inflation, low PMI

2 September 2008

- **After Friday's rebound, zloty depreciating again versus main currencies, amid dollar strengthening against euro**
- **Finance Ministry's inflation forecast for August at 5.0%YoY, in line with median market forecast**
- **Today, PPI in the euro zone and ISM in the US**

The Monday session saw low turnover, slight liquidity and investor's activity in the foreign exchange market due to the market holiday in the US. After significant strengthening on Friday after publication of GDP data, yesterday the zloty was loosing again, similarly as other currencies in the region. EURPLN and USDPLN rates gradually went up to 3.341 and 2.29 respectively accompanied by the appreciation move of the dollar against the euro.

The euro was depreciating, while there was lower liquidity in the financial markets due to the Labour Day in the US. EURUSD rate dropped sharply at the opening, and during the session decreased even below 1.46. It was mainly a result of weaker than expected data on retail sales in Germany (drop by 1.5%MoM in July against forecasts at -0.3%MoM). Manufacturing PMI for the euro zone rose to 47.6 pts in August from 47.4 pts in July, slightly above the market forecast at 47.5 pts. Components of the index pointed at increase in the index of stock of finished goods to the highest level since 1997. However, it did not help the common currency. The dollar was supported by decreasing prices of oil due to weakening Gustav hurricane.

Today in the morning the EURUSD continued its falling trend and reached 1.455 at the opening. The zloty followed this move and weakened to over 3.355 against the euro and 2.31 versus the dollar.

As we wrote in the last weekly report the EURPLN rate may test 3.36 level though similarly as in the previous week, this level should not be permanently broken. After substantial strengthening of the dollar against the euro, in the next part of the week one may expect a rebound of the EURUSD rate amid higher liquidity.

The deputy finance minister Katarzyna Zajdel-Kurowska said yesterday that work on the budget assumptions for the next year should be finished this week. She added the ministry considered a downward revision of GDP growth estimate for 2009, which was initially set at 5%. The inflation forecast at 2.9% in 2009 will stay unchanged in her view.

Activity of investors in the domestic debt market was moderate due to situation abroad. The inflation forecast of the Ministry of Finance for August did not significantly affect the market. According to the FinMin inflation in August accelerated to 5.0%YoY, which is line with market expectations. Even though this estimate is below our forecast of 5.1%YoY the expected decline in prices in monthly terms by the Finance Ministry is the same as our estimate of 0.2%. The interest rate market was not influenced also by the PMI data for Poland, which showed a significant drop of the index to 45.8 pts, the lowest level since December 2002. One more time all components of the PMI were below 50 pts. A clear decline was recorded by the industrial output index to 43.9 pts. Drops were also experienced by export orders, employment, and also output prices.

The MPC members' comments, which appeared yesterday and today confirmed the "hawkish" camp will vote in favour of next interest rate hike. As far as Dariusz Filar said in today's *Dziennik* daily that monetary policy tightening should come already in September, Halina Wasliewska-Trenkner and Marian Noga were less determined on the specific moment of such decision, though they also opted for a necessity of a rate hike this year. What is interesting, "dovish" Mirosław Pietrewicz, who did not rule out an interest rate hike in the Friday's interview for the ISB, yesterday softened his stance expressing hope that inflation and the economic growth rate will fall, while rate hikes will not be needed any more. The MPC comments had little impact on the interest rate market.

American Bond market was non-active yesterday. In the euro zone Bunds showed some weakening in the first part of the session, but during the day some recovery was observed. At the end of the day prices of Bunds were at similar level as compared to Monday's close and 10Y yield amounted to 4.12%.

The Ministry of Finance sold PLN502m of 26-week T-bills and PLN500m of 52-week bills with average yields at 6.422% and 6.427%, respectively. The demand was at PLN1.225bn and PLN1.964bn. The ministry also informed that the offer of five-year bonds PS0413 on Wednesday's auction will amount to PLN2.2bn.

As American investors will be back from the long weekend, activity on the market will probably increase. Before noon the data on PPI index for July in the euro zone will be published and market analysts expect it to rise by 9.1%YoY against 8.0% in June. At the end of the domestic session data on economic activity in the US will be published. According to market consensus ISM index in manufacturing fell to 49.9 in August from 50 pct in July.

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F/X rates (today's opening)

EURUSD	1.4526	CADPLN	2.1588
USDPLN	2.3116	DKKPLN	0.4503
EURPLN	3.3557	NOKPLN	0.4212
CHFPLN	2.0879	SEKPLN	0.3550
JPYPLN*	2.1363	CZKPLN	0.1351
GBPPLN	4.1290	HUFPLN	1.4043

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The zloty trading ranges

	min	max	open	close	fixing
EURPLN	3.3326	3.3472	3.3332	3.3472	3.3360
USDPLN	2.2758	2.2947	2.2773	2.2947	2.279
EURUSD	1.4583	1.4666	1.4635	1.4590	-

T-bonds

TERM	BOND	Yield (%)	Change (bp)	Last auction	Average yield
2Y	OK0710	**6.24**	**-7**	6.08	6.471
5Y	PS0413	**6.12**	**-4**	7.05	6.155
10Y	DS1017	**6.03**	**0**	9.07	6.5

IRS rates (Mid)

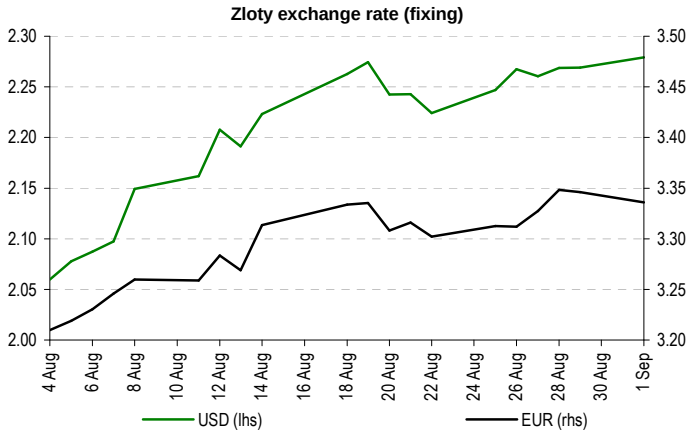
TERM	PL		US		EA	
	%	Change (bp)	%	Change (bp)	%	Change (bp)
1Y	6.50	1	2.95	-4	5.09	-3
2Y	**6.18**	**0**	3.27	-4	4.78	-8
3Y	6.02	-3	3.61	-5	4.65	-12
4Y	5.94	-4	3.83	-3	4.64	-8
5Y	**5.88**	**-4**	3.99	-2	4.60	-9
8Y	5.78	-3	4.37	2	4.59	-6
10Y	**5.73**	**-4**	4.49	0	4.63	-5

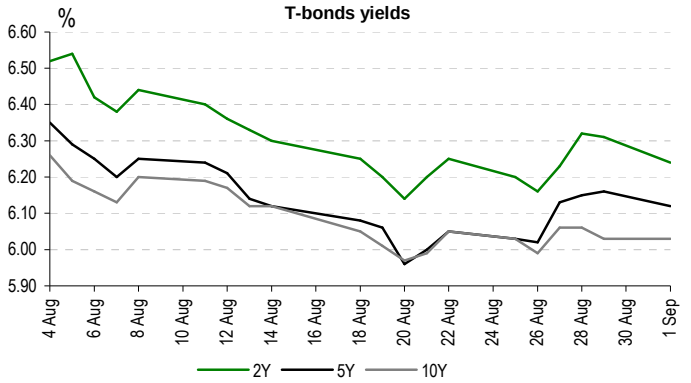
WIBOR rates

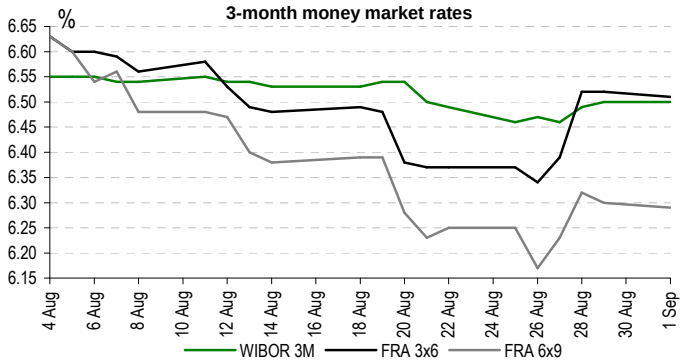
TERM	%	Daily change (bp)
O/N	6.14	-13
T/N	6.14	-8
SW	6.19	-1
2W	6.21	-1
1M	6.25	0
3M	6.50	0
6M	6.59	0
9M	6.61	0
1Y	6.65	0

FRA rates (Mid)

TERM	%	Daily change (bp)
1X2	6.30	-1
3X6	6.51	-1
6X9	6.29	-1
9X12	6.05	-1
3X9	6.42	-5
6X12	6.23	3







* for 100 JPY

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