

# Weekly economic update

9 May – 15 May 2005

After a couple of weeks of hot political debate in Poland, which had influenced financial markets, it seems this week will be quite calm on the Polish market as no major data releases are scheduled and political scene seems to have stabilised for some time. The Sejm did not pass the motion on shortening parliament's term of office, and the president Aleksander Kwaśniewski refused to accept PM Marek Belka's resignation, as promised before. Therefore, despite the fact that an idea of constructive non-confidence vote appeared among SLD politicians, current government will most likely stay in the office until election, to be held in the autumn. Until then, PM Marek Belka plans to continue privatisation and prepare the 2006 budget, while the president vowed to prevent a pre-elections spending spree. Such political prospects should improve sentiment on the Polish market, at least until political uncertainty mounts again as election approaches. From the monetary policy perspective, political uncertainty as regards economic programs of the next government has not decreased, while it was one of the most important factors for the MPC when neutral bias was introduced.

In other countries in the region (Czech Republic, Hungary, Slovakia) inflation figures will be published already this week, and followed by bond auctions, which could impact moods on Polish fixed income market as well.

For global financial markets, US foreign trade data and retail sales figures (released on Wednesday and Thursday, respectively) will have crucial importance. Additionally, speculation regarding revaluation of the yuan looks set to continue influencing foreign exchange markets, at least in the early part of the week, with the Chinese central bank due to meet US Treasury officials and bankers on Monday.

## Economic calendar

Time GMT	COUNTRY	INDICATOR (importance level*)	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
<b>MONDAY (9 May)</b>							
11:00	GB	BoE meeting – decision (H)	May	%	4.75	-	4.75
14:00	USA	Wholesale inventories (H)	Mar	%	0.7	-	0.6
<b>WEDNESDAY (11 May)</b>							
<b>09:00</b>	<b>POL</b>	<b>Auction for 12y CPI bonds (IZ0816) – PLN1bn (M)</b>					
12:30	USA	International trade (H)	Mar	\$bn	-61.5	-	-61.04
18:00	USA	Monthly budget statement (M)	Apr	\$bn	35.45	-	71.23
<b>THURSDAY (12 May)</b>							
12:30	USA	Retail sales (H)	Apr	%	0.4	-	0.3
<b>FRIDAY (13 May)</b>							
12:30	USA	Business inventories (H)	Mar	%	0.6	-	0.5
12:30	USA	Import prices (H)	Apr	%	0.4	-	1.8
13:45	USA	Preliminary Michigan index (H)	May	-	88.8	-	87.7
<b>14:00</b>	<b>POL</b>	<b>Money supply (M)</b>	<b>Apr</b>	<b>%YoY</b>	<b>9.7</b>	<b>10.0</b>	<b>10.8</b>

\* Importance level: (H)igh, (M)oderate; Source: Reuters, BZ WBK, Parkiet

**Maciej Reluga** Chief economist (+48 22) 586 8363

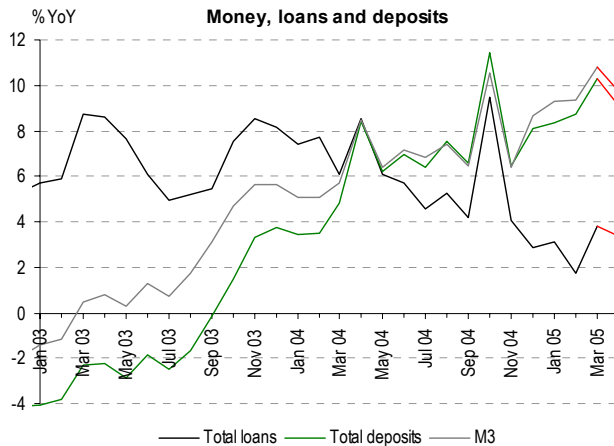
**Piotr Bielski** (+48 22) 586 8333

**Piotr Bujak** (+48 22) 586 8341

**Tomasz Terelak** (+48 22) 586 8342

e-mail: ekonomia@bzwbk.pl

## What's hot this week – Time for little stabilisation



- After key events of last week, political scene in Poland should settle down for some time.
- Lack of important data releases and events should allow for stabilisation in Polish financial market this week.
- On Friday afternoon, the NBP will release money supply figures for April. We forecast ca. 10%YoY M3 rise, however the data should be neutral for investors, awaiting for more important economic figures next week (CPI, PPI, output, wages and employment).
- In other countries of the region, inflation figures will be published already this week. Those figures, followed by results of bond auctions, could have influence on sentiment on Polish fixed income market as well.

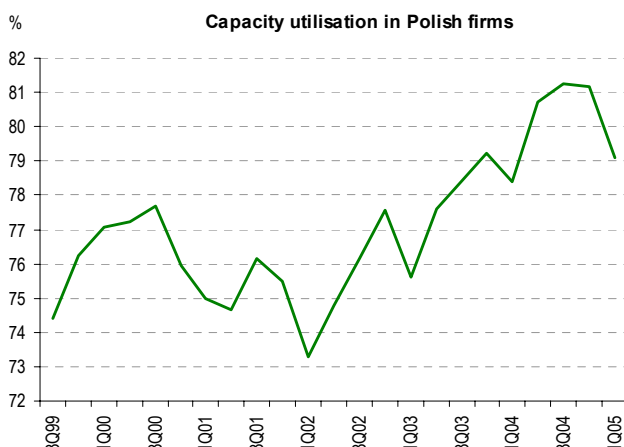
## Economy last week – The parliament and the government stay until autumn

### Results of voting over parliament's self-dissolution

	for	against	abstained	not present
SLD	2	140	-	8
PO	56	-	-	-
PiS	46	-	-	-
PSL	38	-	-	2
Samoobrona	31	-	-	-
SdPI	27	1	1	2
UP	-	11	1	-
LPR	25	-	-	-
others	30	20	9	10
<b>TOTAL</b>	<b>255</b>	<b>172</b>	<b>11</b>	<b>22</b>

Source: Gazeta Wyborcza; Note: required 2/3 majority i.e. 307 votes

- The Sejm did not shorten its term of office – more than 50 votes were missing. PM Marek Belka submitted his resignation after the voting, but the president Kwaśniewski refused to accept it, in line with his earlier declarations.
- It implies that parliamentary election will be held in the autumn, between 25 September and 16 October (the president will set the date until 21 July).
- The deputies are not going to wait doing nothing – new motions aimed at pleasing electorate and increasing public spending have been already submitted.
- Fortunately, the president declared to veto such legislation initiatives, so the risk of serious damage to public finances before the election is limited.
- Financial market should have some relief from politics now. Gronicki's budget draft for 2006 is likely to receive good reception in the financial market.



- According to NBP report on business climate in 2Q05, economic improvement in Poland has been losing momentum, although general economic conditions are still good. Forecasts of demand and output are optimistic.
- Surprisingly, capacity utilisation fell strongly in March. But what is interesting, NBP report shows that lack of spare capacity is not the most important factor deciding about investment activity. Current business climate and firms' financial results are more important.
- Index of forecasted investment was the highest since 1998. Employment forecasts improved as well.
- Maintaining strong wage discipline and diminishing scale of planned price hikes suggest favourable inflation perspectives.

## Quote of the week – Rate cut in the summer, if any

### Mirosław Pietrewicz, MPC member

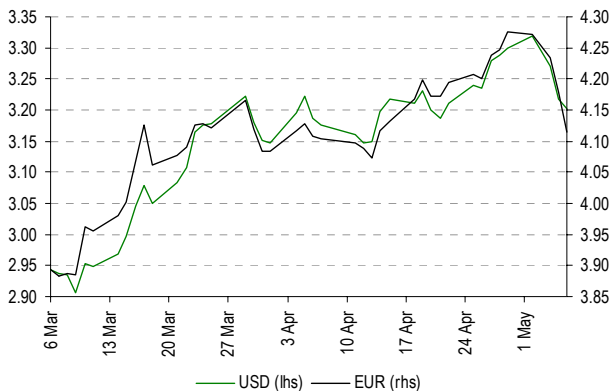
PAP, 6 May

*Neutral bias informs well that there is a balance between possible MPC moves and it does not rule out changes in interest rates. It signals that one should not expect maintaining a pace of rate reductions.*

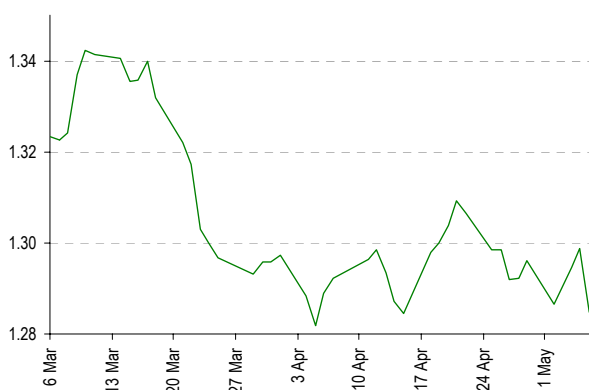
Pietrewicz still sees a room for rate cuts, but it seems that his appetite for monetary easing has diminished. Given that other MPC members are probably in favour of more cautious policy, we maintain our view that only slight fine-tuning moves in rates are likely later during this year. We believe rate cut in May is not likely (uncertainty regarding politics has not changed much), more likely is decision in the summer.

## Market monitor

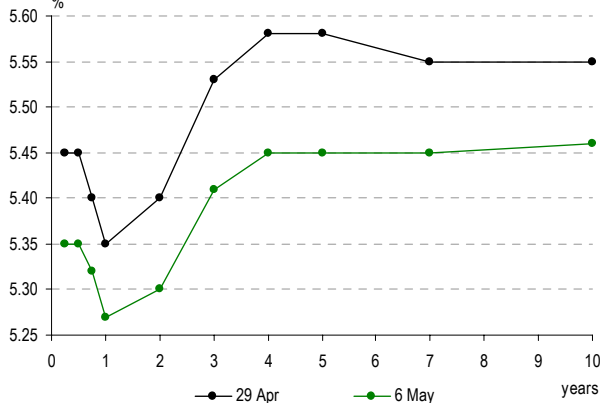
Zloty exchange rate



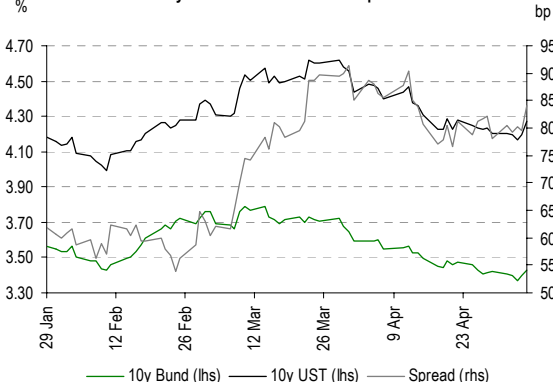
EURUSD rate



Yield curve



10y Bunds &amp; Treasuries and spread



## Political risk disappeared

▪ Last week FX market was encompassed by massive unwinding of long positions in foreign currencies by investors due to a series of conducive factors. Above all PM's declaration was involved, but also Fed statement had huge importance. The zloty gained against both main currencies by ca. 3%.

▪ Due to the lack of important events in domestic market the zloty as usual will be dependant on the cross moves and technical analysis indications. It enables the zloty to reach the level of 4.08, which is 50% retracement of last high and lower band of a range from a turn of March and April. Moreover the zloty gets closer to overbought zone. Thus we expect the zloty to fluctuate between 4.08-18 to the euro and 3.14-24 against the dollar.

## "Neglected" deficit returns

▪ Fed statement, perceived by the markets as dovish one weakened the dollar. The pressure was boosted by ECB chief who cooled down market expectation for interest rate cut in euro zone. Since, as ISM indicators showed decline in employment components, the markets retained strong euro. Surprisingly strong US labour market data triggered a surge of the dollar on Friday which during last week advanced by 0.4%.

▪ Owing to the fact that US inflation figures will be released only next week, the international market will probably revert to the issue of US trade deficit. Those data will surely show again a substantial imbalance that may support the euro in the short term. The market will turn its attention also to US retail sales.

## In the wake of the zloty

▪ During last week Polish papers followed the zloty supported by core markets. However their moves were not so meaningful, as the zloty's, because political risk was discounted mainly by the currency. It constituted to the success of the new 2y bond auction. Ultimately the curve moved downwards by 7-13 bp backing up slightly on Friday after US employment data release.

▪ Amid the lack of significant releases for bond market, Polish curve will follow the zloty and core markets. Impact of the auction of 12y inflation-linked bond will be probably negligible. Yield increase abroad may be compensated by expectations for inflation and industrial production figures next week, which should support Polish papers.

## Yield back-up at the end of the week

▪ Spread 5/5y between Polish and euro curve remained still within a range of 90-95 bp. Renewed calmness in politics may cause it to tighten.

▪ The Fed and ECB statements caused a rise in volatility in foreign bond markets. Considering of US authorities renewed issuance of 30y bonds and strong employment data triggered yield increase in US to 4.27% and in Germany to 3.42% in 10y sector. Spread between them widened to 85 bp.

▪ This week core curves may continue to move even upwards as consequence of US labour data. Magnitude of that increase will be surely larger for the American market than the German one, thus further widening of the spread between them is also possible.

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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](mailto:ekonomia@bzwbk.pl), <http://www.bzwbk.pl>



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