

Weekly economic update

10 – 16 April 2006

In line with expectations, the Sejm rejected a motion on self-dissolution, so there will be no snap election in May. Thus, ruling PiS is likely to start talks on government coalition with Samoobrona and minor caucuses and one could be aware that such negotiations could carry on for at least a week or two. More details regarding plans of the ruling party should be known after a meeting of PiS Political Committee during the weekend. Soon we will find out whether some key ministers, including finance minister Zyta Gilowska, will agree to stay in the cabinet after Samoobrona head Andrzej Lepper takes over a chair of deputy Prime Minister. Perhaps, earlier than planned presentation of draft public finance reform prepared by the Ministry of Finance was not accidental. On the other hand, dismissal of deputy finance minister Cezary Mech seems to suggest strengthening of Gilowska's position in the cabinet.

Having an eye on political developments, the market will not forget about pending data releases. CPI data will be the most important this week. A fall to 0.6%YoY is broadly expected, and such result should not change expectations regarding future monetary policy decisions, being neutral for the market. However, lower number could help in strengthening the short end of the yield curve, reviving hopes for interest rate cut in coming months. Balance of payments data should show another strong rise in exports and imports and current account deficit lower than last year (we predict ca. €300m, although median market forecast is higher). As usually, money supply data will be less important for the market, and they will show fast rise in M3 (ca. 11.5%YoY) and continuation of upward trend in loans and deposits.

Economic calendar

TIME GMT	REGION	INDICATOR (importance level*)	PERIOD	FORECAST		LAST VALUE	
				MAREKT	BZWBK		
TUESDAY (11 April)							
9:00	GER	ZEW index	Apr	pts	65.0	-	63.4
	JPN	BOJ meeting – decision					
WEDNESDAY (12 April)							
9:00	POL	Auction of PLN1.5-2.5bn 10Y bonds					
14:00	POL	Balance of payments / current account balance	Feb	€ m	-420	-303	-163
9:00	EMU	Final GDP	Q4	%	1.7	-	1.6
12:30	USA	Trade balance	Feb	\$ bn	-67.5	-	-68.51
18:00	USA	Budget deficit	Mar	\$ bn	-70.0	-	-71.21
THURSDAY (13 April)							
12:30	USA	Foreign trade prices	Mar	%	0.2	-	-0.5
12:30	USA	Retail sales	Mar	%MoM	0.5	-	-1.4
13:45	USA	Preliminary Michigan	Apr	pts	89.5	-	88.9
FRIDAY (14 April)							
	GB	Market holiday					
14:00	POL	CPI	Mar	%YoY	0.6	0.6	0.7
14:00	POL	Money supply	Mar	%YoY	10.7	11.5	11.7
13:15	USA	Capacity use	Mar	%	81.4	-	81.2
13:15	USA	Industrial production	Mar	%MoM	0.5	-	0.7

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

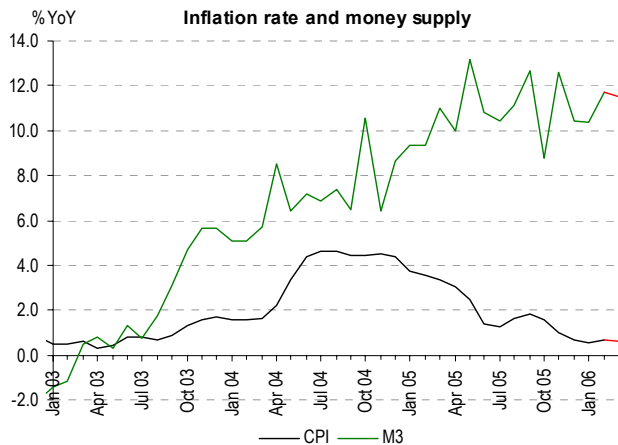
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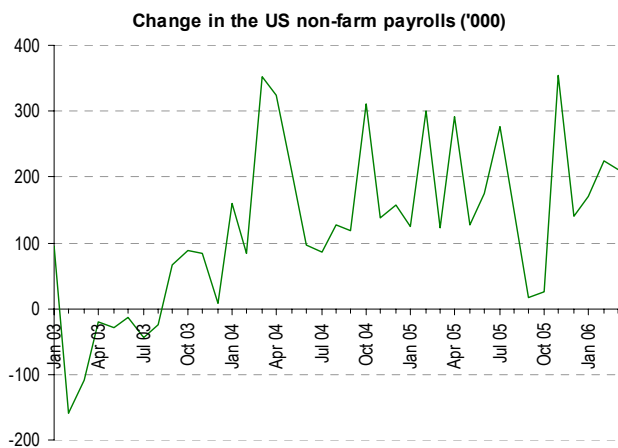
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What's hot this week – Awaiting new data and new coalition

- While watching events on the political arena, market will be already awaiting new economic data releases this week.
- On Wednesday the NBP will show balance of payments figures for February. We predict current account deficit of around €300m, well below last year's level, and a rapid rise in export and import, being mildly positive for Polish currency.
- The most important for the market will be Friday's data on CPI. Inflation is likely to fall once again, and the scale of a decline could impact market sentiment. If our forecast at 0.6%YoY confirms, it should have little effect on expectations re further monetary policy decisions and should be neutral for the market. Lower number could help in strengthening short end of the yield curve.
- Money supply data will be less important, showing fast rise in M3 (11.5%YoY) and continuation of upward trends in loans and deposits.



- Sejm rejected a motion on self-dissolution, and so there will be no snap election in May. In such situation, PiS will probably start talks about government coalition with Samoobrona and minor caucuses. More details regarding plans of ruling party should be known after a meeting of PiS Political Council during the weekend.
- Still, a valid question is whether in the cabinet with Andrzej Lepper as a deputy PM some key ministers will stay, including head of finance ministry Zyta Gilowska. It could be important factor for investors' trust in government's economic policy, although one way or another this trust will be heavily tested after setting up a coalition with populists.
- Market players' moods in the region could be also affected by the results of first turn of election in Hungary. In turn, core markets will eye data releases in US and euro zone, important for future actions of central banks.

Economy last week – Next proposals from Ministry of Finance

- Zyta Gilowska presented a draft of reform of public finances – the motion aims at consolidation of funds, increasing transparency and control over public spending, and should produce savings of ca. 1% of GDP in two years.
- Non-farm payrolls in the US were better than expected in March, rising 211,000, while unemployment rate decreased to 4.7%, the lowest level since July 2001. The data supported hopes for more rate hikes by Fed.
- According to information in government's monitor, the MPC voted 7:3 on cutting interest rates by 25 bp in January, with only Leszek Balcerowicz, Dariusz Filar and Marian Noga against. It means that Halina Wasilewska-Trenkner who used to oppose rate cuts in July and August 2005, has changed her mind in January. However, it does not seem to be a permanent change in mood, judging by her recent comments warning against inflation rise.

Quote of the week – Inflation rate will be very low in the near term

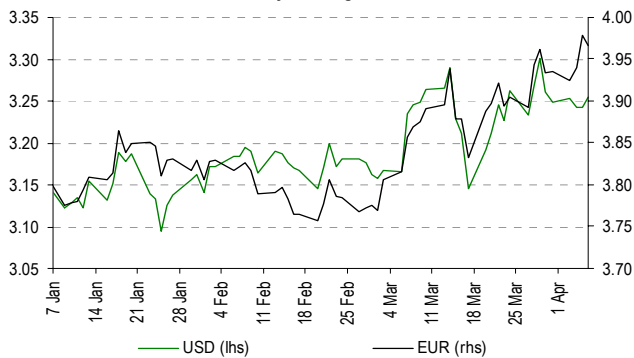
Jacek Krzyślak, head of FinMin's research department
Reuters, 3 April

Our most recent estimate assumes that inflation in March reached 0.4-0.5%YoY, while month-to-month it was 0.0% or declined by 0.1%. In the next few months inflation rate should not exceed 0.5% thanks to lack of inflationary pressure from food prices, wages, and due to strong zloty. We do not expect shocks from fuel market.

Inflation will remain very low in the nearest months. Although the Monetary Policy Council has anticipated such scenario to some extent already in March – which was signalled by its official statement after the meeting – it is not clear whether a scale of inflation decline will not surprise, at least some of MPC members. While in case of members with more hawkish attitude, views on monetary prospects are unlikely to change, one should carefully watch comments of those rate-setters with balanced and more dovish nature.

Market monitor

Zloty exchange rate

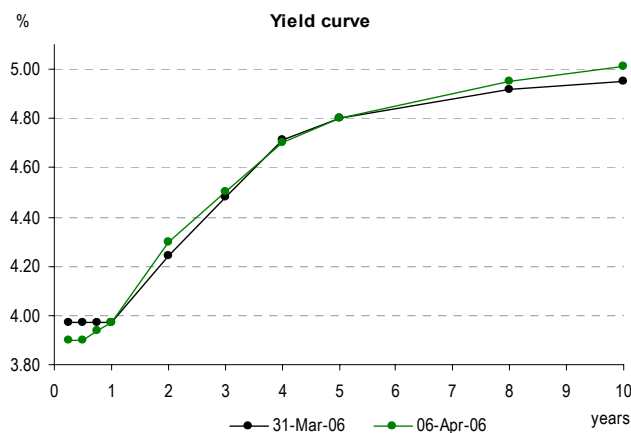


Zloty still weakens further

▪ Last week zloty gradually weakened together with other currencies in the region in line with last weeks trend. Additionally awaiting for the voting on parliaments self-dissolution negatively affected Polish currency. It was near 4.0 against the single currency, and at the end of the week there was a correction. Since previous Friday Polish currency lost ca. 1.2% against the euro and ca. 1.4% versus the dollar.

▪ We think the depreciation cycle of the zloty may continue also in the recent periods, while the negative influence of the political risk in perspective of Samoobrona entering the government may be limited next week. We think the EURPLN rate will trade in range of 3.90-4.00, and for USDPLN between 3.21-3.31.

Yield curve

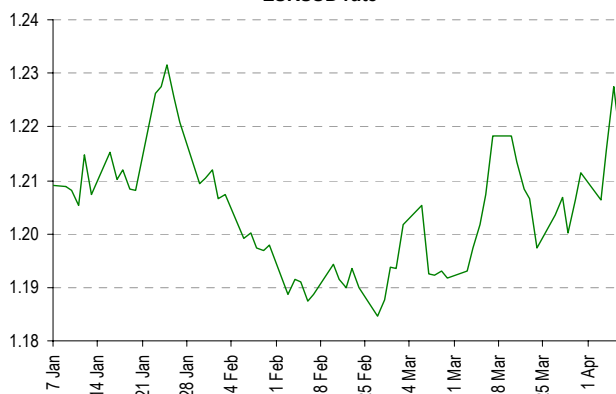


Yields slightly higher

▪ At the start of the week the bond market strengthened in reaction to lowering by the Ministry of Finance its inflation forecasts. However later on Polish debt weakened following the yields rise on the core bond market. Statement of MPC member Andrzej Sławiński that the rates are near neutral level also negatively affected Polish debt, although the stabilisation in politics limited losses. During the week yields rose by ca. 0-6 bp.

▪ In the coming week consumer debt prices may increase as investors will await lower CPI. If it turns out to be in line with MF's forecasts (0,4-0,5%) the market expectations of further rate cuts may appear, and the Polish debt (especially short end of the curve) may substantially strengthen. We think though, that the CPI is going to be at 0.6% and NBP rates will stay flat till the year-end.

EURUSD rate

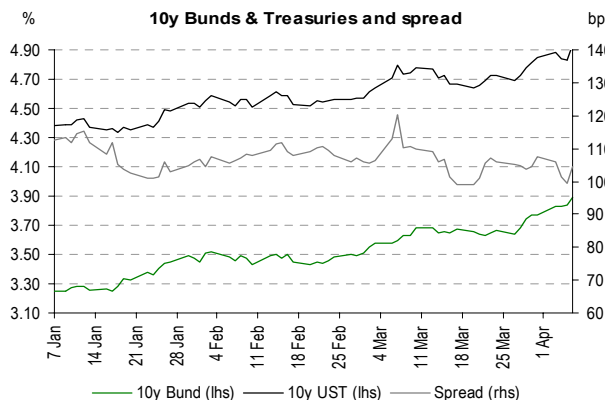


Euro gains thanks to good macroeconomic data

▪ Euro strengthened against the dollar for the most part of the week after strong PMI indices, lower manufacturing ISM and amid ECB's rate meeting with regards to expectations of the ECB's communiqué, which would suggest the pace of further rate hikes. The tone of the ECB's president statement was less hawkish than expected and the dollar recovered some losses supported by strong non-farm payrolls. Throughout the week EURUSD rose by ca. 0.6%.

▪ In the coming week the relation of the euro to the dollar may be influenced by the German ZEW index, which would show the consumer sentiment among enterprises of the most important economy in the EMU, and which is main index before Ifo (the highest for 15Y). U.S. trade deficit and industrial production data may be important as well.

10y Bunds & Treasuries and spread



Macro data weaken bonds despite ECB communiqué

▪ Core markets weakened due to high economic activity indices, as well as amid ECB meeting. Although the tone of the communiqué was less hawkish than expected, and market expectations of next rate raise were postponed from may to June, yields of Treasuries and Bunds remained at high levels supported by strong non-farm payrolls. Yields of 10Y Treasuries increased from 4.83% to 4.92% and Bunds from 3.75% do 3.89%.

▪ In the nearest time the most important for the core bond markets will be data influencing expectations as regards interest rates in United States, i.e. mainly data capacity utilisation (which may indicate some increased inflation pressure), industrial production as well as retail sales. In the EMU investors will focus on the ZEW index.

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