

Weekly economic update

18 – 24 December 2006

While the holiday mood favours calming down the financial market, the last week before Christmas will be thick with new information. The president will probably designate the new candidate for the NBP governor's post. It cannot be ruled out that the choice will be equally surprising as the former one. The financial market should welcome this decision with peace, unless a search for the candidate stretches in time threatening that after Leszek Balcerowicz's tenure expires the central bank will have no governor at all for some time. In the meantime, the current NBP chief will head the last meeting of the Monetary Policy Council in his career. We do not expect to see changes in policy and main interest rates should remain on hold once again, as the majority of MPC members still does not see a significant threat to the inflation target in the medium run. Especially, that the latest data on inflation and wages proved to be lower than expected. The set of macroeconomic data to be released this week should confirm the strength of economic growth in the final quarter of the year, yet without decisively negative signals for the inflation prospects. Large portion of events is also planned abroad, with US data releases about inflation and GDP growth on the top of agenda, as well as German Ifo activity index.

Economic calendar

Time GMT	COUNTRY	INDICATOR (importance level*)	PERIOD	UNIT	FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (18 December)							
11:00	PL	Auction of PLN2.2bn of 5-week and PLN1bn 52-week T-bills (M)					
10:00	EMU	Foreign trade (M)	Oct	€ bn	1.9	-	2.0
TUESDAY (19 December)							
13:00	PL	PPI (H)	Nov	%YoY	3.1	3.4	3.4
13:00	PL	Industrial production (H)	Nov	%YoY	14.8	13.9	14.6
6:00	JP	BOJ meeting – report (H)					
8:00	DE	Index Ifo (H)	Dec		106.8	-	106.8
13:30	US	Houses starts (H)	Nov	m	1.5	-	1.486
13:30	US	PPI (H)	Nov	%MoM	0.4	-	-1.6
WEDNESDAY (20 December)							
	PL	MPC meeting (H)		%	4.0	4.0	4.0
THURSDAY (21 December)							
9:00	PL	Retail sales (H)	Nov	%YoY	14.0	12.7	13.3
9:00	PL	Unemployment (H)	Nov	%	14.8	14.8	14.9
13:30	US	Core PCE (H)	Q3.	%	2.2	-	2.2
13:30	US	Final GDP (H)	Q3	%	2.2	-	2.2
19:00	US	Philadelphia Fed index (H)	Dec		5.5	-	5.1
FRIDAY (22 December)							
13:00	PL	Business climate (H)	Dec				
13:00	PL	Core inflation (H)	Nov	%YoY	1.4	1.6	1.3
13:30	US	Core PCE (H)	Nov	%	0.2	-	0.2
13:30	US	Durable goods orders (H)	Nov	%	1.1	-	-8.2
15:00	US	Final Michigan (H)	Dec		90.0	-	92.1

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

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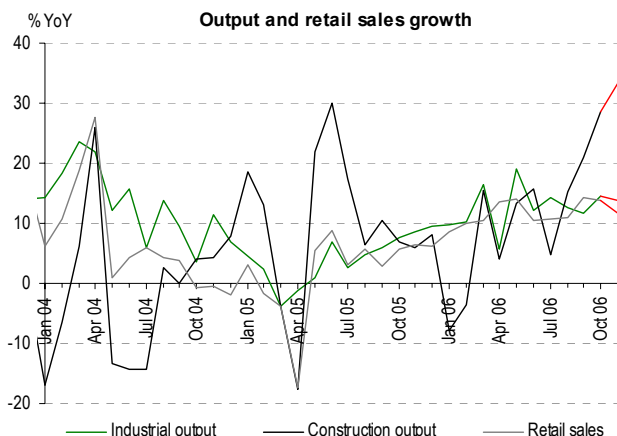
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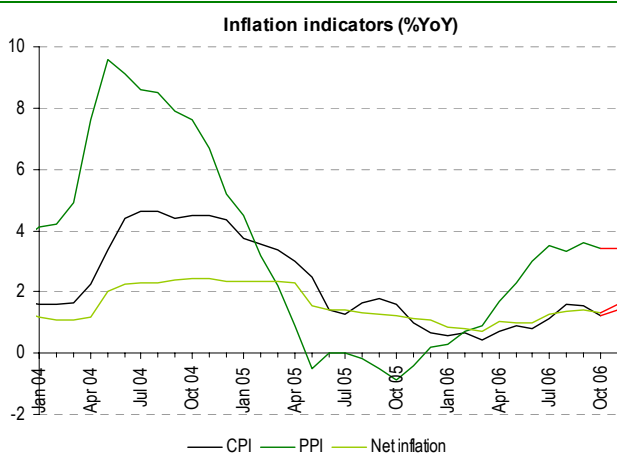
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What's hot this week – Many information before Christmas

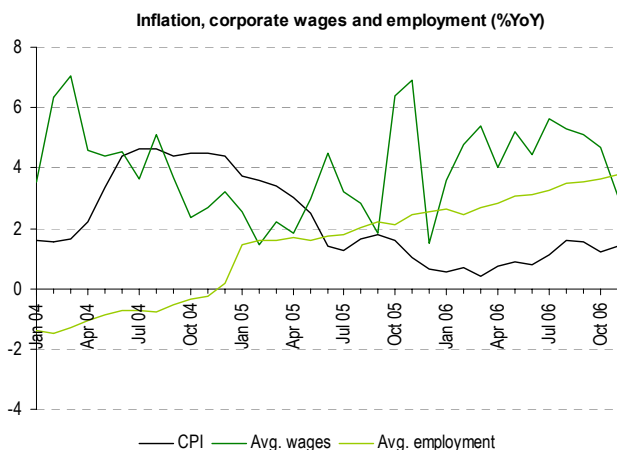


- The last week before Christmas is usually a period of diminishing activity in the financial markets. This year it will be probably the same, however before holiday moods prevail, there will be a number of important information.
- The President will probably designate a new candidate for the NBP governor. New nomination should welcome neutral market reaction, like the previous one. The Sejm will not manage to consider this candidature before Christmas and the vote will take place at the meeting starting on 10 January.
- Monetary Policy Council's meeting will conclude before all this month's economic data will be released so the Council will not have a complete picture of situation. The more so, we expect interest rates to remain unchanged again, and the MPC will maintain its wait and see approach, looking to more information about inflation prospects.



- Financial market expects very high industrial production growth in November, by almost 15%YoY. In our view the result could be somewhat smaller, around 14%, as the number of working days will not play a role this time. Still, this would be a very good outcome.
- Retail sales data should be equally optimistic – 14%YoY according to market consensus, ca. 13% in our view. In sum, the data are likely to confirm solid pace of GDP growth in Q4, exceeding 5.5%.
- Labour market should deliver optimistic news as well – drop in unemployment rate to 14.8% and confirmation of extremely upbeat LFS data for Q3.
- Inflation data should have little impact on the market. PPI will show lack of pressure on producer prices, while rise in core inflation will be released late on Friday so it will not have time to affect moods before holiday break.

Economy last week – Moderate inflation and wages



- Inflation rise in November to 1.4% was lower than expected. On the other hand, it was possible mainly thanks to food and fuel prices, while according to our estimates net inflation increased stronger, to 1.6%YoY. But in our view, it does not change monetary policy prospects as this level is still well below the MPC's inflation target.
- Wages rose only 3.1%YoY in November (market expected ca. 4%), while jobs number soared 3.8%YoY (new record). In sum, data strengthened debt market, however lower wage growth could have resulted from high statistical base (last year, bonus payment for mining sector took place), so it is likely to rebound up in December.
- Current account deficit was higher than predicted, but the data was positive for the economy, as it confirmed strong rise in foreign trade turnover and large inflow of foreign direct investment.

Quote of the week – Who will be the next NBP chief?

Lech Kaczyński, Poland's President, Reuters, 15 Dec

[Q: How many candidates for NBP head do you have?] *Maximum two at present. Not much time has left, but I cannot give you names yet.*

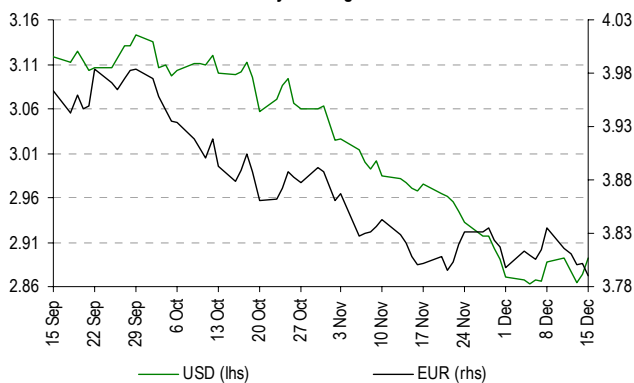
Zyta Gilowska, finance minister, PAP, Reuters, 15 Dec

[Q: Will you become NBP governor?] *No, I feel good where I am right now. [...] I haven't received the proposal. I do not care much about this. I know nothing about such proposal.*

As yet, the financial market is waiting patiently until a search for the new NBP governor concludes. The new candidate nomination could be equally surprising as the first one, however it should welcome neutral market reaction if the applicant will have similar skills and experience. However, market anxiety could go higher if the hunt for a candidate stretches in time so much that causes a risk that the central bank will have no governor at all until the next MPC meeting when interest rate decision is made.

Market monitor

Zloty exchange rate

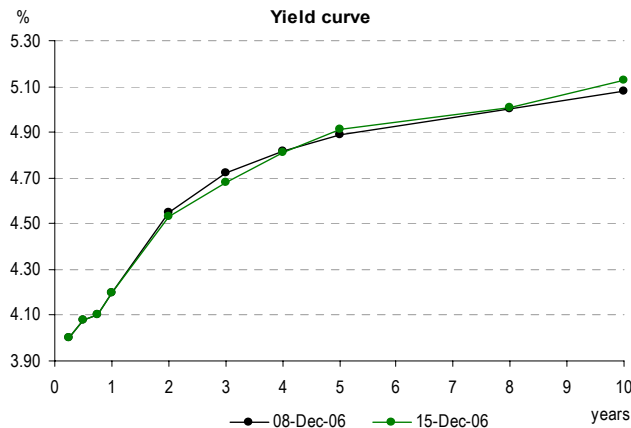


Zloty strongest since March

▪ Zloty strengthened throughout most part of the week thanks to positive interest of foreign investors toward the region. On Friday there was a slight correction, which was connected with moves currency moves in the region (comments of Slovak central bank chairman on overestimated crown). EURPLN rate broke 3.8, and USDPLN rate dipped only slightly due to dollar regaining strength in international markets.

▪ We assume that positive moods in the region may hold before the year's end without any major zloty's depreciation. Polish currency may strengthen further vs. euro with next resistance level at 3.78 and 3.75. The USDPLN rate will depend to high extent on EURUSD rate moves and data from US. We expect the EURPLN rate will fluctuate in range of 3.75-3.85, and USDPLN of 2.83-2.93.

Yield curve

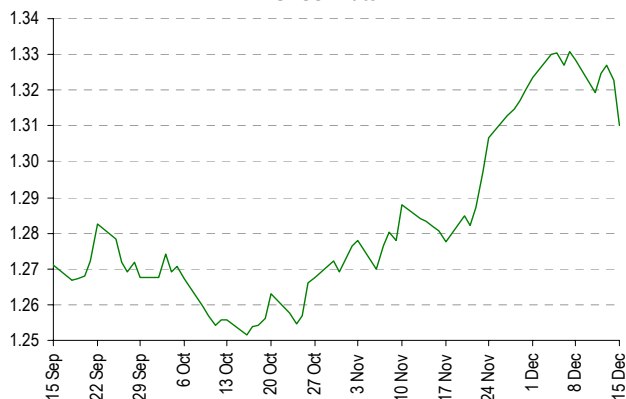


Debt weakened by abroad

▪ Polish bonds weakened in the last days by ca. 10 bp, mainly at the longer end of the yield curve with regards to significant drop in prices in the core markets. Switch auction also did not improve the moods. The short end of the curve was supported by CPI below forecasts. At the end of the week the market strengthened on lower than expected US CPI and wages.

▪ In our view in December the Monetary Policy Council will leave rate unchanged, and the communiqué might not include any significant changes as compared to previous month taking into consideration new data. Polish government bonds will be under influence of retail sales, core inflation (possible debt weakening) and situation in the core markets.

EURUSD rate

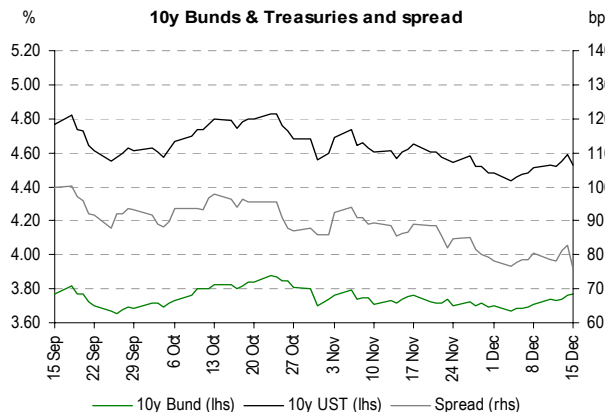


Dollar slightly recovers

▪ In the last days there was a significant appreciation of the dollar in the foreign markets by 1,6% vs. euro. The drop of EURUSD rate followed better than expected previous week's labour market data, retail sales and US trade balance, which appeared positive for GDP. At the end of the week there was a slight correction after the release of CPI inflation.

▪ We expect this is not the end of the depreciation trend of US currency, and recent move was just a correction on substantial weakening. The EURUSD rate may stabilise around the range of 1.31-1.33 with the upside risk of a rise to 1.35. Ifo index and US housing market data, PPI, final GDP as well as Philadelphia index will be the most essential this week.

10y Bunds & Treasuries and spread



Slight yields rise in the core markets

▪ The US and German bonds weakened since the previous Friday in further reaction to US non-farm payrolls. This move was boosted by higher than expected retail sales data. Yields of 10Y Treasuries and Bunds rose even to 4.6% and 3.79%, though after the lower than expected inflation in US there was a correction to 4.54% and 3.75%.

▪ Data from the US labour market may support the US debt in the context of Fed's communiqué. Ifo index and Wednesday's speech of ECB's president will be the most important for the euro zone markets. The final GDP data for the Q3 in United States, including important for Fed inflation PCE index will be the most essential. Markets will also eye durable goods orders.

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