

# Weekly economic update

10 – 16 September 2007

Last week showed that the Polish financial market has become quite resistant to uncertainty dominating in the international financial markets. The zloty exchange rate, despite increase in risk aversion after publication of very week data from the US, strengthened as compared to the previous week. Of course, the much weaker than expected US non-farm payrolls report, which was published on Friday, weakened the domestic currency and decreased scale of its appreciation over the whole week, but the influence of the US data was weaker than one could have expected. The local debt market was quite stable, although one should note increase in yields of 2-year bonds and widening of spread between long-term yields in Poland and on the core markets due to significant fall in yields of Treasuries and Bunds. The Sejm's vote over the parliament's dissolution that was scheduled on Friday took place only after close of the Polish session, so its possible impact on the markets may only be visible this week. However, we do not think that events on the political scene, including an outcome the early elections could have significant influence on the domestic financial markets.

This week the main event on the domestic financial market will be Thursday's publication of CPI data for August. We predict that inflation fell to 1.8%YoY last month from 2.3%YoY in July. The market consensus and FinMin's estimate point to 1.9%YoY. Anyway, confirmation of expected fall of CPI inflation to below 2% should be positive factor for the short end of the Polish yield curve. Longer dated bonds will remain under influence of moods in the global markets. In this context, an important day will be Friday, when a large set of major macro data from the US will be published.

## Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
<b>TUESDAY (11 September)</b>							
12:30	US	Trade balance	Jul	\$ bn	-59,5	-	-58,74
<b>WEDNESDAY (12 September)</b>							
9:00	PL	Auction of PLN1.0-2.5bn 20Y WS0922 bonds					
12:00	PL	Trade balance	Jul	€ m	-724	-668	-557
12:00	PL	Current account	Jul	€ m	-1016	-1038	-1182
<b>THURSDAY (13 September)</b>							
12:00	PL	CPI	Aug	%YoY	1.9	1.8	2.3
12:00	CH	Bank of Switzerland meeting – decision		%		-	2.5
12:30	US	New jobless claims		'000		-	318
18:00	US	Federal budget	Aug	\$ bn	-61.3	-	-64.72
<b>FRIDAY (14 September)</b>							
12:00	PL	Money supply	Aug	%YoY	15.1	15.1	15.6
9:00	EMU	Final HICP	Aug	%YoY	1.8	-	1.8
12:30	US	Import prices in foreign trade	Aug	%	0.6	-	1.5
12:30	US	Retail sales	Aug	%MoM	0.3	-	0.3
13:15	US	Capacity utilization	Aug	%	82.0	-	81.9
13:15	US	Industrial output	Aug	%MoM	0.3	-	0.3
14:00	US	Preliminary Michigan index	Sep	pkt	83.5	-	83.4

Source: Reuters

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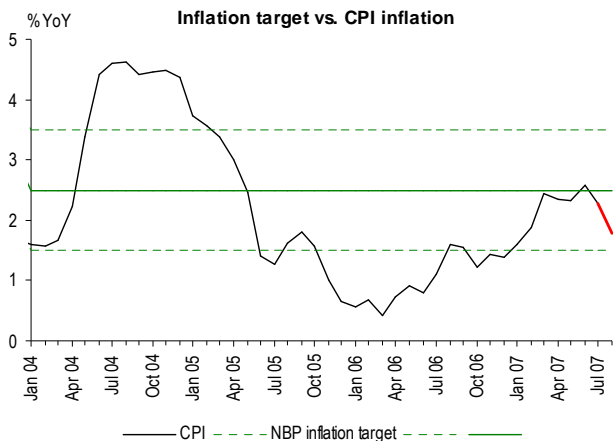
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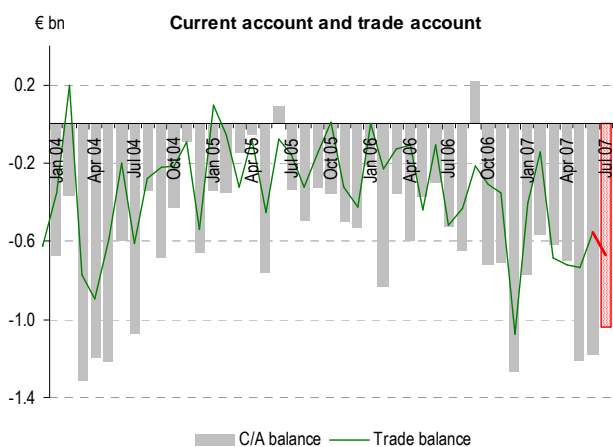
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## What's hot this week – How deep will CPI inflation fall?

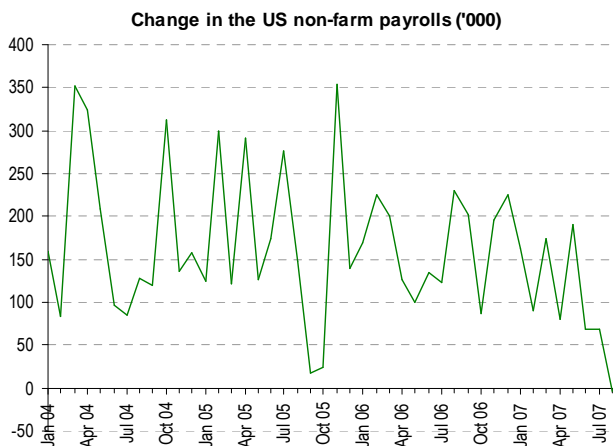


- This week will bring publication of the first set of monthly macroeconomic data for August (CPI and monetary statistics) and balance of payments for July.
- The key focus of attention will be of course on inflation figures. Our forecast point to a fall in the headline inflation rate to 1.8%YoY and again it is different from the market consensus and FinMin's estimate which stood at 1.9%YoY. In the previous months our predictions were more accurate.
- Anyway, expected fall in inflation to below 2% will make it more difficult for the MPC to deliver another rate hike, especially after three rate hikes already made this year.
- In our view, the MPC will wait with further tightening of monetary policy until November when the CPI data will again show inflation above 2% and the Council will know quarterly data on the labour market for Q3.



- The publication of balance of payments for July, that is due on Wednesday, will show on what pace external imbalance of the Polish economy increases due to strengthening of domestic demand. According to our estimates, 12-months cumulative C/A gap in relation to GDP increase to above 3%, but with large inflow of FDIs this is still not a dangerous level. What is important, we forecast that July saw continuation of robust export expansion, which would support our prediction of GDP growth in Q3 at slightly above 6%.
- Monetary statistics for August should show continuation of fast increase in money supply, including total deposits (mostly due to rapid increase in corporate deposits). At the same time we expect slight deceleration in total loans growth, although it should remain at around 30%YoY until the end of this year.

## Economy last week – No domestic data, focus on events abroad



- Last week, the domestic financial market waited for important events abroad (mainly the ECB meeting and the US non-farm payrolls report) and on the Sejm's vote over the parliament's dissolution, that was scheduled on Friday. The vote was delayed and took place only after close of the markets.
- In line with expectations, the ECB did not increase interest rates, but it said that monetary policy in the euro zone remain accommodative, which suggests that lack of hike this month does not mean an end in monetary tightening cycle, yet only a pause until the situation on the markets calm down.
- The US non-farm payrolls report proved dramatically weak. Instead of the expected job creation of 110k, it showed a decline by 4k. Additionally, there were downward revision to data for previous months.

## Quote of the week – Faster information on MPC meetings

### Stawomi Skrzypek, MPC, PAP, 6 September

*Personally, I can say that I will insist on such a changes in law, so that on the day of MPC decision the markets could receive full information about all aspects of the decision, including voting results.*

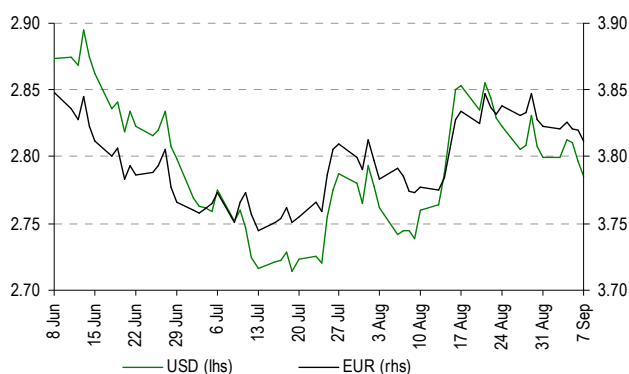
*I was one of these MPC members who were against rate hikes, I had different view on frequency of hikes and their exact timing. Especially the hike in June was surprising for the markets. It can be seen by looking at FRA changes. It confused the markets and strengthened expectations for next hikes.*

Declaration of the NBP governor as regards faster publication of information on MPC meetings, including voting results, are very ambitious. In our opinion the faster publication of *minutes* in their current form will not significantly improve transparency of domestic monetary policy, but faster publication of voting results is surely desirable.

NBP governor admitted explicitly that he voted against rate hikes this year, but he suggested that possibly he would have supported them with slightly different timing. If there was actually a chance for wide consensus in the Council for a rate hike in July, it is a pity the Council hurried and raised rate already in July.

## Market monitor

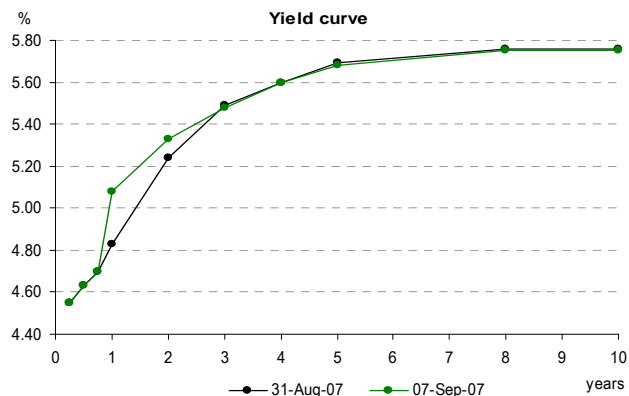
Zloty exchange rate



## Zloty to resistant to changing moods in global markets

- Last week was a good one for the zloty. Domestic currency strengthened both against the euro and versus the dollar. On Monday, which was a market holiday in the US, the zloty was appreciating with scant activity in the markets. Tuesday's opening was weaker, with the EURPLN slightly above 3.83, but later on the zloty gained, showing that to a large extent it is resistant to turmoil in the global financial markets. Much weaker than expected US non-farm payrolls report weakened the zloty, but not very significantly and at the end of the week the zloty was stronger than a week earlier.
- For this week we maintain the expected range of the zloty fluctuations at 3.75-3.85 for the EURPLN and lower to 2.72-2.82 for the USDPLN due to weakening of the dollar against the single currency.

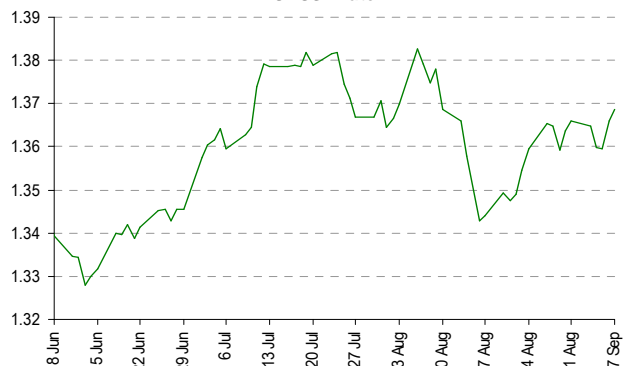
Yield curve



## Local debt market stable

- Yields of longer dated domestic bonds were fluctuating in very narrow ranges last week. The segment of 2-year bonds weakened following MPC decision the previous week, but long end of the curve slightly strengthened over the whole week. Increase in risk aversion in the global markets, and simultaneous fall in yields on the core markets, does not lead to increase in yields of domestic bonds. However, it leads to widening of spread between bond yields Poland and on the core markets.
- This week the key focus of attention on the domestic debt market will be publication of CPI figures. If the data confirms forecasted fall in the headline inflation rate to below 2%, the short end of the yields curve may strengthen.

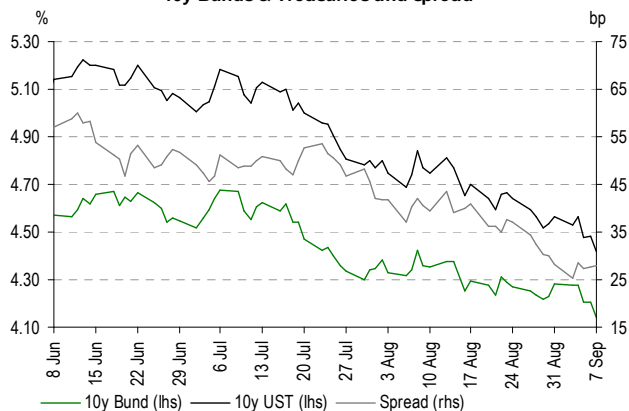
EURUSD rate



## Weaker data from the US weaken the dollar

- Last week was not good for the dollar. Macro data published in the US proved much weaker than expected. The dollar was hurt not only by dramatically weak US non-farm payrolls report, but also by other labour market statistics and the housing data released earlier during the week. This was reflected in lowering of investors' confidence in the US currency. The EURUSD rate increase to almost 1.38 following the release of the US non-farm payrolls report from slightly above 1.36 at the end of the previous week.
- This week the key day for the dollar will be Friday when a large set of important data from the US will be published.

10y Bunds &amp; Treasuries and spread



## Clear strengthening in the core debt markets

- Weak data from the US and no rate hike in the ECB translated into significant strengthening on the core markets. At the end of the Polish session on Friday, yields of 10-year Treasuries and Bunds was at 4.42% and 4.14%, respectively, against 4.56% and 4.26% a week earlier. The strengthening in the US market is likely to be more persistent as recent data from the US increase probability of rate cut in the world's largest economy at the FOMC meeting on September 18. The economic situation in the euro zone remain good and investors are likely to recall soon that the ECB probably has not ended the monetary tightening cycle.
- This week, the same as in case of the EURUSD rate, the key day for the core debt markets will be Friday with a large number of major data releases on the agenda. Earlier during the week we should see stabilisation in the markets.

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