

Weekly economic update

12 – 18 November 2007

The past week brought most of all a yield curve inversion, which resulted firstly from the surprisingly high inflation forecast of the Ministry of Finance which was followed by slightly more hawkish comments of the MPC members, and secondly from the strengthening in the core debt market, which supported the longer end of the curve. The European Central Bank left interest rates unchanged similarly as the Bank of England, while comments of Jean Claude Trichet indicated waiting for more data and development of the situation on the financial markets. Ben Bernanke in his appearance before the Joint Economic Committee noticed increasing concerns about the US economic growth.

With regards to mounting fears over the acceleration of inflation on globally rising food prices, the CPI data are going to be especially important. We presume that inflation rise will be slightly smaller as compared to market expectations. It is worth to follow the MPC members' comments analysing their view on possible supply shock and potential second round effects as well as the effectiveness of available instruments of the Council in preventing these phenomenon. Data from the labour market may appear slightly less important, as their growth may soon decelerate. After designation of Donald Tusk for the Prime Minister there may appear some proposals of economic programme of the new government, which may affect the investors' sentiment. The domestic market will be also influenced by a high number of important data releases abroad. In our view the zloty may experience a slight correction soon.

Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
MONDAY (12 November)							
	US	Market holiday					
TUESDAY (13 November)							
13:00	PL	Current account balance	Sep	EUR m	-875	-859	-637
13:00	PL	Trade balance	Sep	EUR m	-625	-959	-289
10:00	GER	ZEW index	Nov	pts	-20.0	-	-18.1
10:00	EMU	Preliminary GDP	Q3	%YoY	2.5	-	2.5
20:00	US	Pending home sales	Sep		-1.5	-	-6.5
WEDNESDAY (14 November)							
10:00	PL	Auction of PLN1.5-3.0bn 10Y floating rate WZ0118 bonds and PLN0-1bn CPI linked bonds					
13:00	PL	CPI	Oct	%YoY	3.0	2.8	2.3
13:00	PL	M3 money supply	Oct	%YoY	14.3	14.8	14.3
13:30	US	PPI	Oct	%MoM	0.3	-	1.1
13:30	US	Retail sales	Oct	%MoM	0.2	-	0.6
THURSDAY (15 November)							
10:00	EMU	Final HICP index	Oct	%YoY	0.8	-	0.8
13:30	US	CPI	Oct	%MoM	0.3	-	0.3
13:30	US	New York Fed index	Nov	pts	21.1	-	28.75
17:00	US	Philadelphia index	Nov	ots	5.5	-	6.8
FRIDAY (16 November)							
13:00	PL	Wages in enterprises sector	Oct	%YoY	9.6	9.5	9.5
13:00	PL	Employment in enterprises sector	Oct	%YoY	4.7	4.7	4.7
14:00	US	Net capital flow	Sep	\$ bn			-69.3
14:15	US	Industrial output	Oct	%MoM	0.1	-	0.1

Source: BZ WBK, Parkiet, Reuters

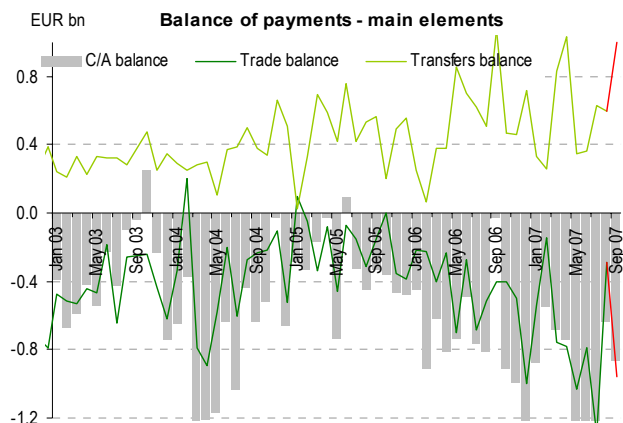
Maciej Reluga Chief economist (+48 22) 586 8363

Piotr Bielski (+48 22) 586 8333

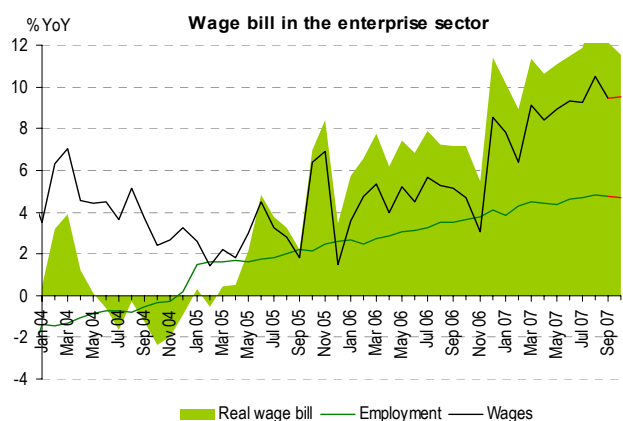
Piotr Bujak (+48 22) 586 8341

Cezary Chrapek (+48 22) 586 8342

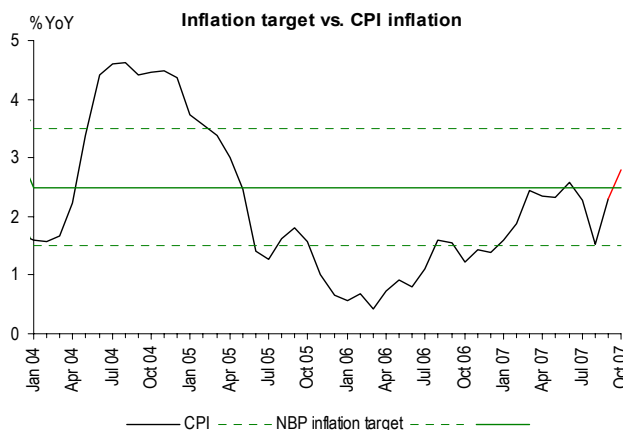
e-mail: ekonomia@bzwbk.pl

What's hot this week – Crucial inflation and labour market data

- The start of the week should be quite calm due to the market holiday in the United States.
- Investors will await the main release of the week, i.e. inflation data. It is especially important taking into consideration the high forecast of the Ministry of Finance, which strongly affected the market. After its release we decided to upwardly revise our inflation forecast for October to 2.8%YoY vs. 2.6% forecasted earlier.
- We expect a significant deterioration of trade balance due to the weakening of the exports growth (to slightly above 10%) with imports growth staying at quite high level (ca. 16%). An increase in the current account deficit will be constrained by expected substantial inflow of current transfers and thus the C/A gap should be smaller than the trade balance.



- We expect a slight acceleration of the money supply growth in October to 14.8%YoY amid minimum slowdown of the overall credit growth (30%) and stabilisation of households' loans growth (at ca. 40%).
- At the end of the week the labour market data are going to be released, which will probably recede to the background with regards to inflation acceleration. We presume, that the wages growth remained at 9.5% recorded in September. This (after one more rise of growth rate in November) may be nearly the end of wages acceleration trend, though employees' reaction to further inflation acceleration may a risk factor. We also presume that the employment rose by 4.7% similar as in September.
- Abroad ample essential data are going to be released, among others CPI and retail sales in the United States.

Economy last week – High inflation forecast of the MinFin

- According to the Ministry of Finance, inflation amounted to 0.7%MoM in October, which may mean a rise of CPI index by 3.0%YoY. Although the MinFin did not present the details of the forecast, the inflation acceleration might result from food prices growth.
- The ECB left interest rates unchanged (similar as the Bank of England) with the main rate at 4.00%. Jean Claude Trichet said that ECB is ready to fight against inflation and added that it remains in "wait and see" mode awaiting next data and the development of situation in the financial markets. It seems that the tightening bias has been maintained.
- Ben Bernanke in his appearance before the Economic Committee of the US Congress pointed to growing expectations of investors' concerns over the situation in the credit market and over the influence of the slowdown in the housing market on the economy.

Quote of the week – Views in the MPC divided, though a rate hike in November

Marian Noga, MPC member, Reuters, 8 Nov

(...) at least four more rate hikes are required. Strong zloty does only half of the MPC work (...) actually almost all factors are proinflationary. This year (...) [a rate hike] is necessary and probable in November. (...) two more in H1 2008. February (...) a good month (...) I do not believe too much in a rate hike in January. (...) We have no influence on shocks, though we have to anchor inflation expectations.

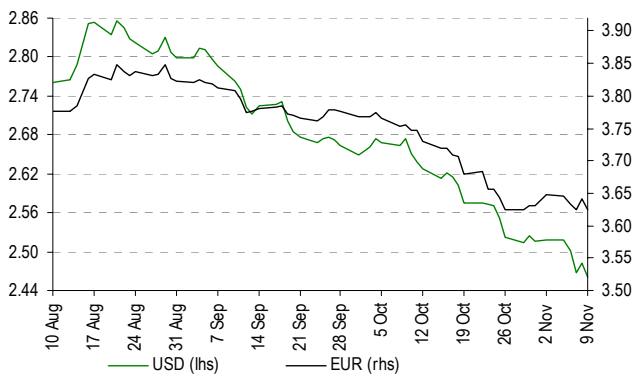
Miroslaw Pietrewicz, MPC member, PAP, 6 Nov

The [inflation] projection is quite optimistic. We are not driven by current figures (...). I allow a possibility of a rate hike this year (...) So far there have been no problems with second round effects.

Opinions of the MPC members belonging to opposite groups of the MPC still point there are differences among the Council members regarding the scale of further monetary tightening. However it seems that there is a majority, which believes that continuation of interest rate hikes is necessary. Marian Noga sharpened its hawkish comments and increased expected target level on interest rates. Even one of the biggest "doves" Miroslaw Pietrewicz, who does not see reasons for sudden moves and for reacting on current data taking into consideration a shock on the supply side, he would allow a monetary policy tightening. Jan Czekaj's comments will still be crucial regarding further moves of interest rates, and he said some time ago that the probability of a rate hike in November is 55%.

Market monitor

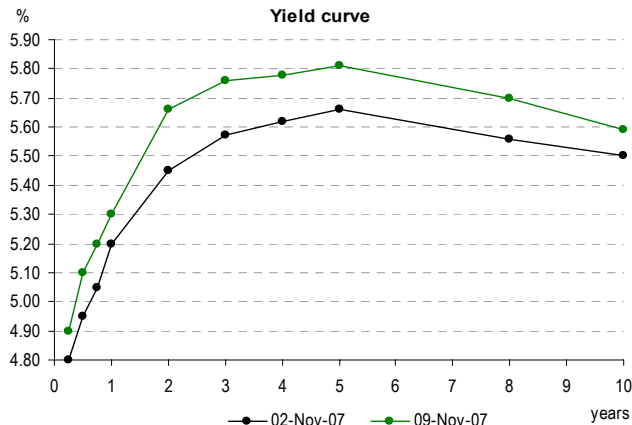
Zloty exchange rate



“Safe haven” zloty strengthens

- Despite risk aversion maintained at elevated levels, among others due to next negative releases on the performance of foreign institutions, the zloty slightly appreciated against the euro as compared to the previous Friday and strongly gained versus the dollar on its weakening in the global markets.
- After designation of new PM there may be some new more official comments on the economic programme of PO-PSL coalition. The current strength of the zloty besides the weak dollar results from expectations for economic reforms and interest rate hikes. In the latter context the CPI data may be important. We keep our trading range for the EURPLN at 3.60-3.70 (a possible zloty correction vs. the euro), and we lower the range for the USDPLN rate to 2.44-2.54 on risk of further rise of the EURUSD rate.

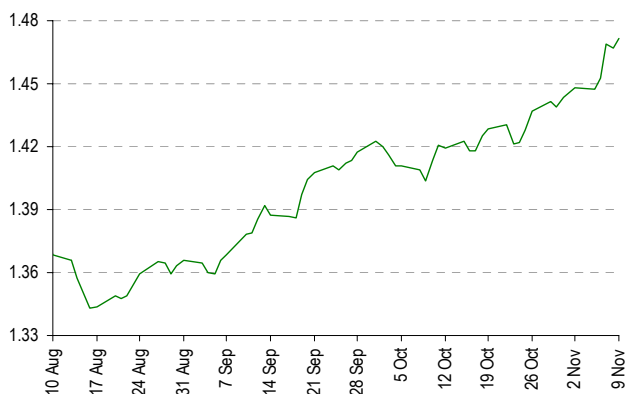
Yield curve



The curve inverted

- After the release of the inflation forecast of the Ministry of Finance the 2Y bonds significantly weakened and FRA rates rose on expectations of higher number of interest rate hikes than it was previously expected. Yields rise was continued in reaction to comments of the MPC members. At the longer end of the yield curve after an initial weakening there was some recovery driven by yields decline in the core debt markets, which resulted in yield curve inversion.
- We presume that the bond market may slightly recover after the inflation data release. The labour market figures may be slightly less important this month. Comments of the MPC members will be crucial for further moves of the yields.

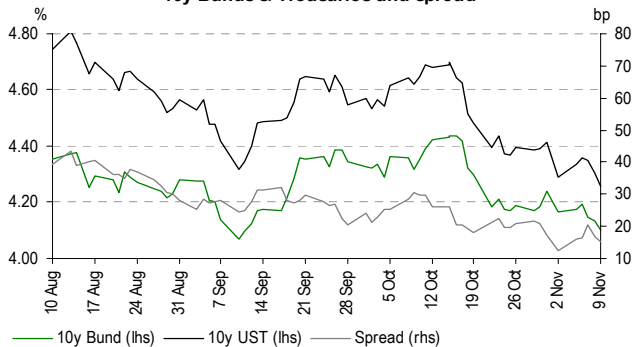
EURUSD rate



EURUSD rockets further

- After more negative news from the US financial institutions, the news that China plans to diversify its currency reserves, and Ben Bernanke's comments, the dollar weakened once again, reaching a record weak level against the single currency (1.473). This was also fuelled by expectations of further interest rate cuts and falling interest rate disparity vs. the rates in the euro zone.
- After such significant moves of the EURUSD rate, we still see potential for further dollar depreciation vs. the euro for some time. This week the ZEW index (fall among others on strong euro) and GDP data will be important for the euro. In the US key will be data from the housing market and inflation figures (if it stays under control this may give some place for manoeuvre for next rate cuts). Retail sales, which will show the consumers moods will be also essential for the dollar.

10y Bunds & Treasuries and spread



Yields falls were recorded

- A higher risk aversion on negative news about some US financial enterprises contributed to a sell-off in the stock markets and flight to safe haven assets such as US and German Treasury bonds. Not very hawkish comments of ECB and Fed's presidents fuelled the rise of core debt prices. During the week the yield of 10Y Treasuries and Bunds fell by ca. 8 bp to 4.28% and 4.11% against the previous Friday levels.
- The expectations of further moves in the US will be crucial for the core debt markets. The level of economic activity will be important, particularly retail sales data, as well as housing markets data and activity indices. CPI and PPI figures will be essential for inflation prospects.

This publication has been prepared by Bank Zachodni WBK S.A. (a member of AIB Group) for information purposes only. It is not an offer or solicitation for the purchase or sale of any financial instrument. All reasonable care has been taken to ensure that the information contained herein is not untrue or misleading. But no representation is made as to its accuracy or completeness. No reliance should be placed on it and no liability is accepted for any loss arising from reliance on it. Bank Zachodni WBK S.A., its affiliates and any of its or their officers may be interested in any transactions, securities or commodities referred to herein. Bank Zachodni WBK S.A. or its affiliates may perform services for or solicit business from any company referred to herein. This publication is not intended for the use of private investors. Clients should contact analysts at and execute transactions through a Bank Zachodni WBK S.A. entity or an AIB Group entity in their home jurisdiction unless governing law permits otherwise. Copyright and database rights protection exists in this publication.

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, <http://www.bzwbk.pl>



Bank Zachodni WBK is a member of Allied Irish Banks Group