

# Weekly economic update

25 February – 2 March 2008

The next days will bring an answer to the question bothering the market since the surprising data from the economy on the CPI, production and from the labour market, whether the MPC will decide to change its strategy of gradual steps, one hike every 2-3 month, in running the monetary policy. In our view the rates will rather not be raised this months, and the Council will hold with such decision till March, though one may not rule out that the MPC may bend under the burden of the current data and market expectations. The comments of the MPC members also do not suggest there will be a majority to raise rates already this month, especially taking into consideration that after the recent data there were no comments of Jan Czekaj, who is one of the most crucial Council members for the decisions in this cycle. The retail sales data should show acceleration of growth as compared to December and signal maintaining sound consumption demand. At the end of the week the CSO is going to release the Q4 GDP data, though after the figure for the whole year they may be slightly less important. The calendar of the data releases abroad is very busy, which may contribute to higher volatility in the domestic market.

## Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
<b>MONDAY (25 February)</b>							
9:00	PL	Retail sales	Jan	%YoY	16.4	14.3	12.4
9:00	PL	Unemployment	Jan	%	11.7	11.7	11.4
15:00	US	Home sales	Jan	m	4.82	-	4.89
<b>TUESDAY (26 February)</b>							
-	PL	MPC meeting	-	-	-	-	-
9:00	DE	Ifo Index	Feb	pts	102.8	-	103.4
13:30	US	PPI	Jan	%MoM	0.3	-	-0.1
14:00	US	House price index Case/Shiller	Dec	%MoM			-2.1
15:00	US	Consumer confidence	Feb	Pts	85.0	-	87.9
<b>WEDNESDAY (27 February)</b>							
-	PL	MPC meeting – decision		%	5.50	5.25	5.25
9:00	EZ	M3 money demand	Jan	%YoY	11.4	-	11.5
13:30	US	Durable goods	Jan	%MoM	-1.2	-	5.0
15:00	US	New homes sales	Jan	m	0.6	-	0.604
<b>THURSDAY (28 February)</b>							
13:30	US	GDP preliminary	Q4	%	0.6	-	0.6
13:30	US	GDP deflator	Q4	%	2.6	-	2.5
13:30	US	Core PCE	Q4	%	2.7	-	2.7
13:30	US	Jobless claims	w/e	'000	350	-	349.0
<b>FRIDAY (29 February)</b>							
9:00	PL	GDP	Q4	%YoY	-	5.9	6.4
10:00	EZ	Economic sentiment index	Feb	pts	0.0	-	1.0
10:00	EZ	Final HICP	Jan	%YoY	3.2	-	3.2
13:30	US	Core PCE	Feb	%MoM	0.2	-	0.2
14:45	US	Chicago PMI	Feb	pts	51.0	-	51.5
15:00	US	Michigan final	Feb	pts	69.6	-	78.4

Source: BZ WBK, Parkiet, Reuters

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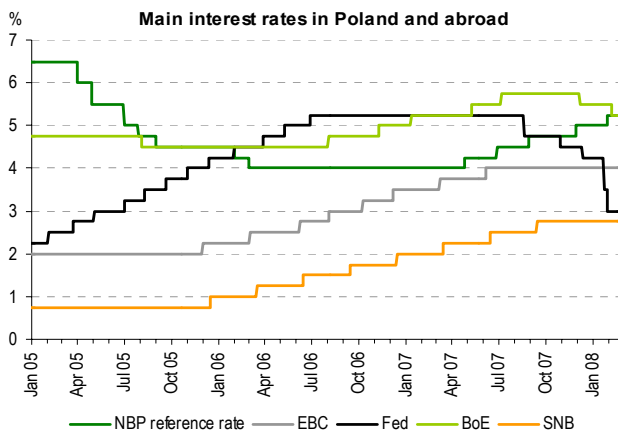
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## What's hot this week – Will the MPC change its strategy?



▪ This week's key event is the MPC meeting. After recent publications of 'hawkish' data on inflation and production it came to strengthening of fears concerning the aggregate scale of the monetary policy tightening as well as an interest rate hike already at the February meeting. In our view this will rather not happen, as the new set of domestic data in the context of worsening of perspectives for the global economy should not dissuade the MPC from their step-by-step strategy of a move every 2-3 months, which was applied so far. Nevertheless it is hard to say if the MPC will not accommodate the market pressure. The 50 bp motion will be applied similar as in January, though the risk of it being passed is marginal.

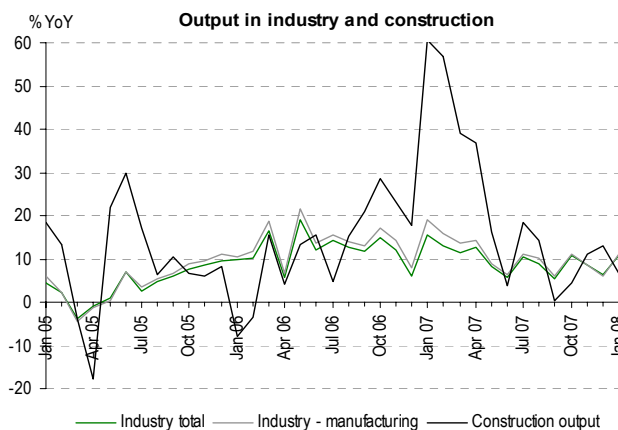
▪ In our view the MPC communiqué will be hawkish, similar as the new inflation projection, which basic elements will be presented at the conference after the meeting



▪ At the start of the week, before the Council meeting the Central Statistical Office is going to release the retail sales for January. In our view the sales growth accelerated up to 14.3%YoY amid a high statistical base effect in the previous year against surprisingly weak information about December sales when the retail sales growth slowed down to 12.4%YoY. We also expect the registered unemployment to increase to 11.7% in January from 11.4%.

▪ CSO publishes also GDP growth for the fourth quarter. According to estimations made after the publication of the preliminary data for 2007 we expect a Q4 GDP growth of 5.9%YoY against 6.4% in the third quarter. The slowdown is mainly a result of the falling growth in the private consumption as well as of a minor degree a slight slowdown in the investment growth.

## Economy last week – Surprising data on production and PPI



▪ Industrial production grew in January by 10.8%YoY (consensus: 6.8%), mostly because of an accelerating manufacturing, however the growth of the construction-assembly production was 6.8% amid high base effect (consensus: 12.1%). The mixed information about the production do not change our forecasts of the GDP growth for the first quarter 2008.

▪ PPI grew in January by 1.2%MoM and 2.8%YoY (consensus 2.1%YoY) because of a high growth in mining prices (10.7%MoM). Manufacturing prices grew by 0.5%MoM (2.1%YoY). It seems that the zloty and the strong competition still limit the scale of growing prices in the industry.

▪ The published *minutes* from the January's MPC meeting follows, that the decision to raise rates was not unanimous as in November.

## Quote of the week – Rate hike in the nearest future?

**Andrzej Wojtyna, MPC member, Bloomberg, 19 February**

*I think there are no reasons to wait for more data and if a hike were to happen, it should be in the near future, when the risk of second-round effects is rising. The impact of shocks on inflation has a different character today than it did in previous years, and it would be a tactical error to bring inflation back to the target too quickly.*

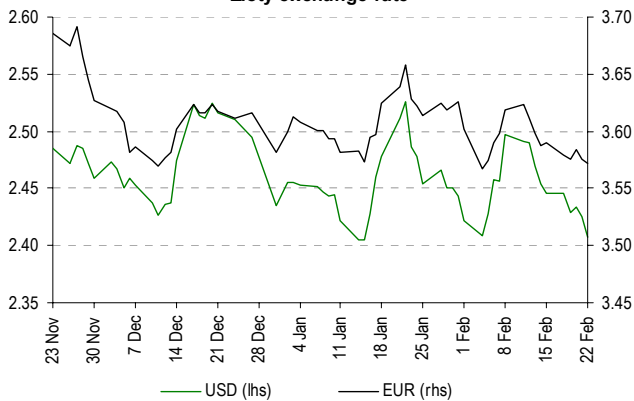
**Andrzej Sławiński, MPC member, Thomson, 19 February**

*The rise in inflation in recent months was the result of factors which monetary policy does not affect. Wciąż jesteśmy w cyklu zacieśniania polityki pieniężnej. We still remain in a cycle of monetary policy tightening. But its final scale is difficult to determine, because uncertainty remains about how the slowdown in euro zone growth, which is already quite visible, will impact our economic growth.*

According to Andrzej Wojtyna an interest rates should be raised in the nearest time, which suggests that he will vote in favour of a rate hike motion already in February. On the other hand the tone of his comments does not suggest he prefers a larger total scale of the tightening, as he said that the price shocks should be allowed to dissipate, which should be accompanied by an appropriate communication that inflation will return to the central banks target. Andrzej Sławiński signalled again that inflation is rising due to factors, which are out of MPC's control. The GDP growth prospects in the euro zone seem to be important for Sławiński, as it may slow down even regardless of the situation in the US. This may lead to higher interest rate disparity and unwanted excessive zloty appreciation.

## Market monitor

Zloty exchange rate

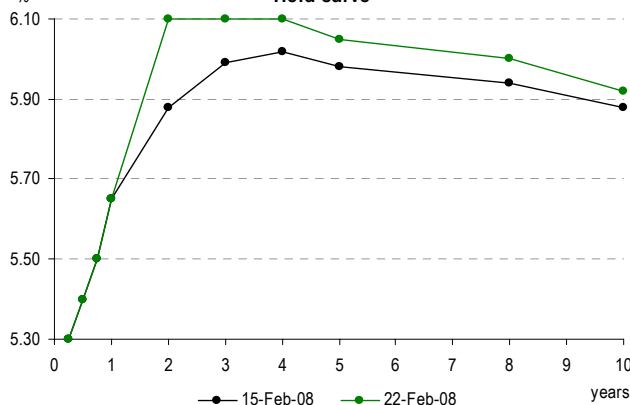


## Zloty at a strong levels

During the past week the zloty consolidated against the major currencies. The appreciation against the euro was insignificant, because the strong strengthening took place already after past week's CPI and labour market figures. The EURPLN fluctuated in a narrow range between 3.75 and 3.59 and after the upgraded outlook of Poland rating for debt in foreign currencies by S&P the zloty appreciated to below 3.57. At the end of the week there was a slight correction. The zloty strengthened more against the dollar because of the EURUSD rate increase.

We expect the zloty to remain relatively stable during the next week with a tendency for slight depreciation if the interest rates remain unchanged at the MPC meeting. We expect the EURPLN trading range of 3.53-3.63 and 2.36-2.46 for the USDPLN rate.

Yield curve

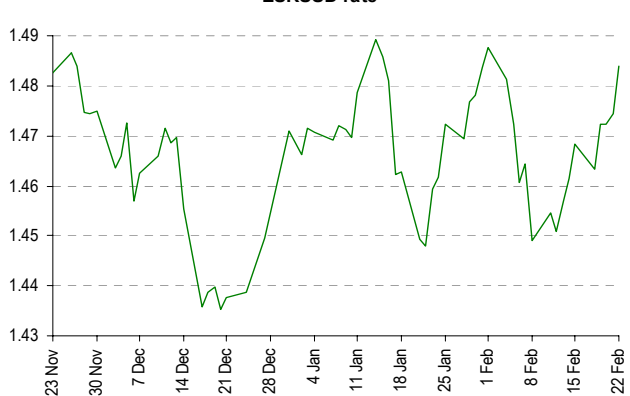


## Local bonds again weaker after production

The beginning of the week was dominated by further fall of prices of local bonds after higher than expected CPI and wages data in the previous week. Information about the production and the PPI caused a further weakening. After the information of an upgraded rating outlook by S&P a light rebound followed. During the week local bonds yields were about 3 bp higher at the long end and over a dozen bp higher at the shorter end. The money market prices in an interest rate hike in February.

After the retail sales release the rates moves may be insignificant because the market players will be waiting for the results of the MPC meeting. If the MPC decides to wait with the hike till March the interest rate market may take breath slightly. The communiqué and the inflation projection will work in the opposite direction.

EURUSD rate

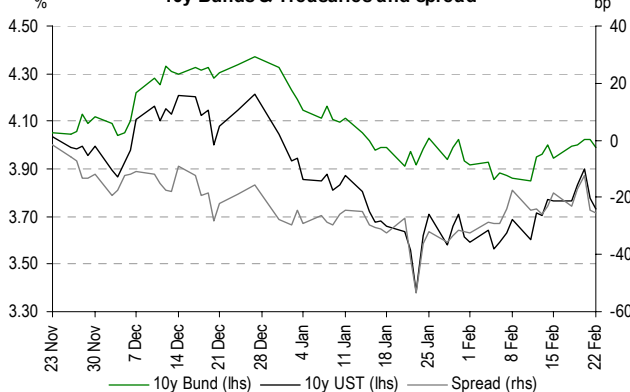


## The dollar near the weakest level vs. euro

After a slight strengthening of the dollar against the euro at the start of the week to 1.462, the EURUSD rate was rising for the rest of the week. The comments from the ECB distancing from a possibility of rate cuts in the euro zone as well as poor data in the US resulted in euro recovery. High US inflation increased concerns that the overall monetary easing may be smaller which will not support the economy, and much weaker than forecasted Philly Fed index significantly deteriorated moods and resulted in EURUSD spike to 1.48.

This week the data from the US from the housing market, the PPI and the activity Chicago PMI index will be important for the dollar. Weak figures may contribute to go dollar weakening. Ifo index will be the most important for the euro zone.

10y Bunds &amp; Treasuries and spread



## Fears over growth and inflation

In the core debt markets the start of the week was dominated by weakening trend among others amid higher than expected US CPI. Moreover, information on the ECB representatives comments limited market expectations of rate cuts in the EMU. However, after the release of Philadelphia Fed index, market fears over economic slowdown in the US increased which resulted in a strong rebound. At the end of the day yields of 10Y yields of Treasuries and Bunds reached 3.73% and 3.99% against 3.77% and 3.95% a week earlier.

Apart from the data from the US and euro zone data, also the Ben Bernanke appearance will be very important for the core debt markets. Amid slowing economy also inflation data in the US (PPI, PCE) and the euro zone (HICP), which recently aroused higher concern, will be essential.

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