

Weekly economic update

19 – 25 May 2008

CPI inflation data for April were in line with our forecast and did not have significant impact on the interest rate market. Debt market was weakening throughout the week amid increased supply of papers from foreign investors and small demand with unfavourable bond auction. In turn, the zloty was fluctuating during the week in narrow ranges, close to record highs versus euro. In contrast to CPI, the data released by the NBP delivered some surprises. Balance of payments figures showed higher than predicted current account deficit in March, resulting mainly from higher rise in trade deficit (high import growth). In turn, money supply growth in April was much above forecasts due to faster rise in deposits.

The nearest week will be shorter on the domestic market due to holiday on Thursday. However, before it starts the market activity may be high because of publication of important macroeconomic data. Labour market figures should show acceleration in wage growth in April with an upward risk for our projection. In our view, production data will show a substantial rebound. Furthermore, we expect a similar scale of acceleration in net inflation as the market. The MPC minutes to be released at the end of the week, may show a propensity of MPC members to delay an interest rate hike. An agenda of data releases abroad is rather short. One should pay attention to data about economic activity in the euro zone that may impact perspectives of the economy and interest rate movements in the euro zone as well as to minutes from the last FOMC meeting.

Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (19 May)							
12:00	PL	Wages	Apr	%YoY	11.5	11.2	10.2
12:00	PL	Employment	Apr	%YoY	5.8	5.8	5.9
TUESDAY (20 May)							
9:00	DE	ZEW index	Apr	%	-37.5	-	-40.7
12:30	US	PPI	Apr	%MoM	0.5	-	1.1
WEDNESDAY (21 May)							
9:00	PL	Switch auction					
12:00	PL	Industrial production	Apr	%YoY	14.5	18.0	0.9
12:00	PL	PPI	Apr	%YoY	2.7	2.6	2.9
12:00	PL	Net inflation	Apr	%YoY	2.9	2.9	2.8
8:00	DE	Ifo index	May	pts	102.0	-	102.4
18:00	US	FOMC minutes					
THURSDAY (22 May)							
	PL	Market holiday					
12:30	US	New jobless claims		'000		-	371
FRIDAY (23 May)							
12:00	PL	MPC minutes	Apr				
12:00	PL	Business climate	May				
8:00	EZ	Preliminary PMI – manufacturing sector	Apr	pts	50.5	-	50.7
8:00	EZ	Preliminary PMI – services sector	Apr	pts	51.7	-	52.0
14:00	US	Home sales	May	m	4.85	-	4.93

Source: BZ WBK, Parkiet, Reuters

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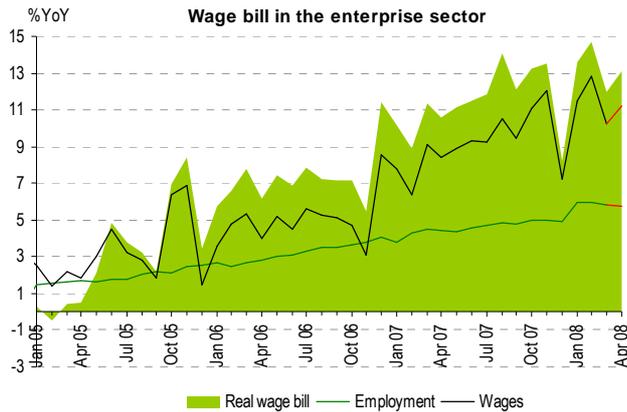
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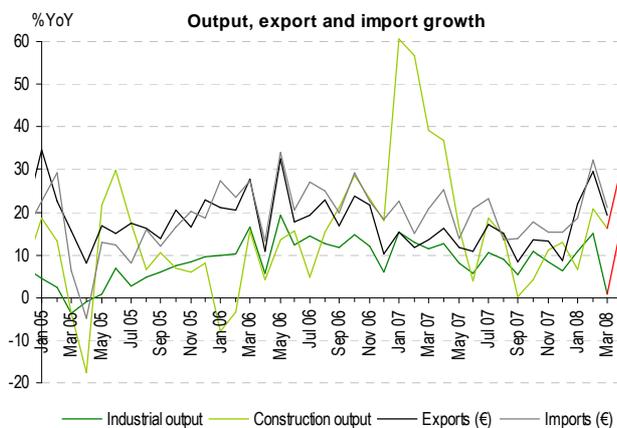
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What's hot this week – Another set of data

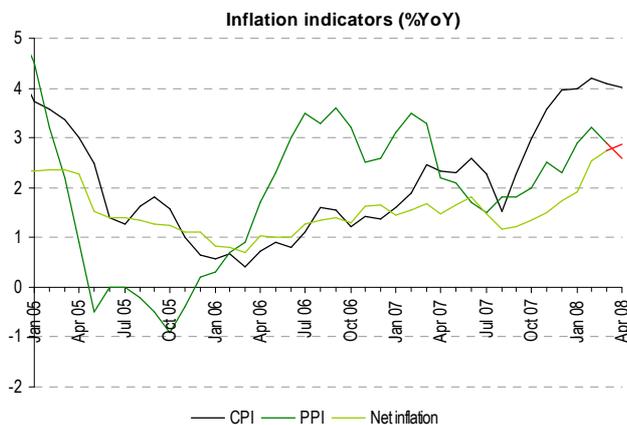


- Despite the fact this is going to be a shorter week taking into account the Corpus Christi holiday, it will be full of domestic data releases.
- We forecast an acceleration in wage growth to 11.2%YoY from 10.2% in March. We see an upside risk to our estimate after the money supply data, which showed significant rise in households' deposits. Meanwhile, in our view the employment growth stayed at 5.8% level recorded in March.
- In our view the industrial output growth rate is going to accelerate in April to 18%YoY (6.8%MoM) after surprising slowdown in March. A significant jump in the production growth rate results from the set of Easter holiday periods this and last year (there were two more working days in April 2008 than in 2007). The seasonally adjusted output rose in our view by 7.2%YoY (-2.9%MoM).



- Along with the output data the CSO is going to release the producer prices figure. According to our forecasts the PPI index rose by 0.2%MoM, which means a 2.6% growth rate in annual terms. The market forecast is slightly higher at 2.7%YoY.
- After the publication of the CPI data we did not decide to change our net inflation estimates on net inflation. We presume acceleration to 2.9%YoY, which is line with rising trend forecasted for the next months.
- *Minutes* of the last meeting of the MPC, when the Council decided to pause with the interest rate hike may show the willingness of the MPC members to wait with the next move changing interest rates for the next month. On the other hand the release of the document (as well as the CSO's business climate indices) will fall in the middle of the long weekend, which may limit its impact.

Economy last week – CPI in line with expectations



- In April the CPI inflation was at 0.4%MoM and 4%YoY against 4.1% in March. The food prices increased by 0.7%MoM and 6.8%YoY, which means the annual growth rate fell for the fourth month in a row. The price growth in transport also slowed fourth consecutive month. The annual growth of other prices increased in line with expectations.
- The growth of money supply in April was at 14.9% against expectations of 13.6%YoY and our forecast of 13.3%YoY. This was a consequence of significant acceleration of annual deposits growth (overall to 16.7% from 15.3%), which was seen in all categories.
- The current account deficit rose in March to €1.6bn from €1.16bn in February and €0.8bn in March 2007. The cumulated deficit for the last 12 months rose to 4.2% GDP. The trade deficit rose to €1.5bn amid significantly faster imports growth as compared to our assumptions.

Quote of the week – Risk of excessive zloty appreciation starts materialising

Andrzej Sławiński, MPC member, TVN CNBC, 14 May

So far the level of real interest rates is such there is room for manoeuvre [as this] is not a factor, which could influence the decisions of companies. Zloty appreciation trend is the thing firms have to take into account. The zloty appreciation rate is moderate, though if it is above the zloty equilibrium level appreciation rate we will have a problem. [This] risk (...) starts materialising. It is more important for the monetary policy what is happening outside Poland (...) and forecasts [for the euro zone] are revised to the downside.

Dariusz Filar, MPC member, Thomson Financial, 14 May

Trend on wages, industrial output likely to prove decisive in May. The CPI data for April have minimal influence on policy.

According to prof. Filar the CPI inflation fall in April is little important information, while the real economy and labour market data will be the key. They may show risks for the core inflation prospects. Andrzej Sławiński still sees some room for interest rate hikes, which in situation of low level of real interest rates, would have moderate impact on activity of the enterprises. In his view the risk of excessive zloty appreciation may be significant barrier for the companies. Apart from this he mentions the deteriorating forecasts for the euro zone economy. In our view these comments suggest that we are still in the monetary policy tightening cycle.

Market monitor

Zloty exchange rate

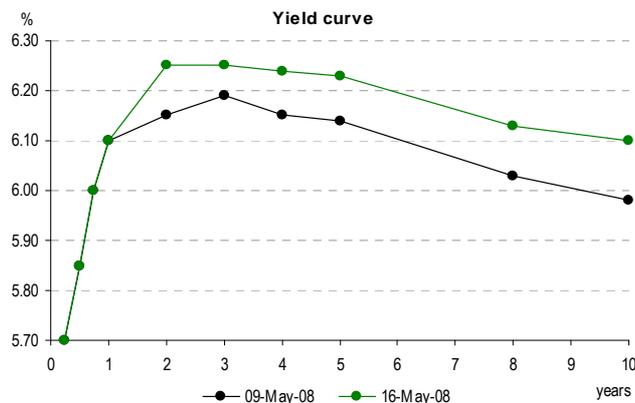


Zloty stable, close to historical maximum

Zloty exchange rate fluctuated during the week in narrow ranges against both dollar and euro and did not change much since previous Friday. Initially, the zloty remained strong and was testing 3.38 against euro. After a correction in EURPLN above 3.40, it started recovering losses quite soon.

We maintain opinion that there is a risk that investors will try to bring the EURPLN rate close to historical low, which will be supported by production data. On the other hand, technical indices show that the zloty is close to overbought, which suggests that a correction should take place quite soon. However, one should take into account that all corrections this year were very short-lived. We maintain a band of currency fluctuations for this week at 3.35-3.45 for EURPLN and 2.12-2.22 for USDPLN.

Yield curve

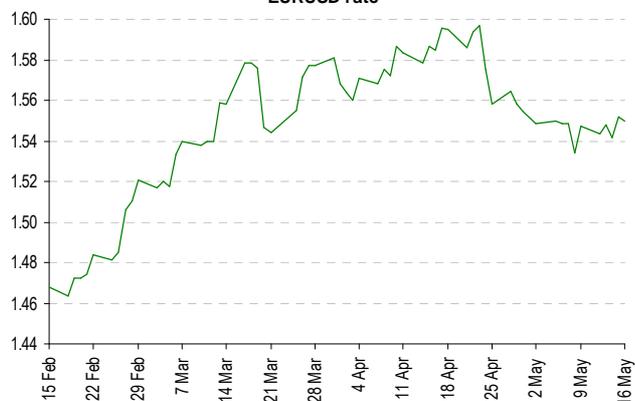


Yields keep on rising

In recent days, upward trend in money market rates was maintained. A sale-off on the debt market lasted throughout the week, and its consequence was also in FRA rates. The data about inflation did not help the market. Failure of 20Y bond auction could also have negative impact on the moods. At the end of the week, there was a slight rebound. One should notice analogous rise in German yields and slight increase in spread vs. German Bunds.

In our view, yields on the debt market are already high. However, the market may find little support in wages data. Moreover, the industrial output figure may put additional pressure on bond prices.

EURUSD rate

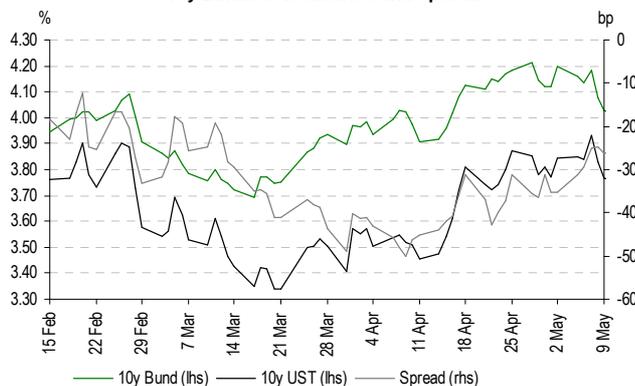


Quite stable EURUSD rate

Despite large fluctuations in recent days, the EURUSD did not change much since previous Friday. At the end of the week it reached 1.556. On Monday, the dollar lost ground, however after better than expected retail sales data, US currency was slowly regaining. Another rise in EURUSD was caused by lower than forecast data about CPI and core inflation in the US, and higher than predicted GDP growth in the euro zone. Later on the dollar recovered despite weak US data (industrial output, NY Fed), however, it fell again on poorer consumer Michigan index.

Because of delay in interest rate cuts predicted by us in the euro zone until the next year, we assume that the euro should be gaining against dollar until the end of the year, however 1.60 will be an important resistance level.

10y Bunds & Treasuries and spread



Significant jump in yields in the core debt markets

In the last week a weakening was recorded in the core debt markets. US bond yields rise resulted after the US retail sales. However, after the US CPI and output data the markets recovered. The rates increase in the euro zone resulted from higher than expected Q1 GDP in the EMU. At the end of the week the market slightly recovered. During the week the yields of 10Y Treasuries and Bunds rose by 5 bp and 16 bp to 3.88% and 4.21% respectively.

This week the calendar of data releases is not very busy. In Europe the data from Germany (ZEW, Ifo) will be important from the point of the view of interest rate prospects in the euro zone, especially in the context of higher GDP growth in Germany. In the US investors will focus on PPI inflation, home sales figures and FOMC minutes.

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