

Weekly economic update

8 – 14 December 2008

Last week the government approved amendment to budget bill, lowering GDP forecast for 2009 from 4.8% to 3.7%. Government also presented anti-crisis package worth PLN91.3bn, however thus far there are little information about practical aspects of its implementation. Recently, zloty saw slight weakening. There was also further significant fall in market interest rates under influence of dovish comments of MPC members and situation in core debt markets. EBC cut main interest rates by 75 bp and signaled further policy easing is in the pipeline due to lower forecasts of GDP and inflation. Bank of England trimmed interest rates by 100 bp and Riksbank but rates by 175 bp. Weaker than expected foreign data and Fed's announcement about purchase of US Treasuries triggered further strengthening in core debt markets. Domestic perspectives of inflation and interest rates are positively influenced by signals from Energy Regulatory Office about little size of energy price hikes next year and possible return to full price regulation in energy market. Ministry of Finance's inflation forecast for November remained without impact on the market, as it showed a decline in CPI to 3.8%, in line with market consensus. PMI manufacturing index was a negative surprise again, although it had little impact on the market. FRA market is already pricing in a reduction in reference rate below 4%. Our forecast assumes 4.5%, however after ECB meeting we see a downward risk for this assumption. Moreover, expectations for December cut with sizeable risk of 50 bp move may keep market interest rates at low levels. This week, the local financial market will be still affected by changing global risk aversion. In Poland, there will be release of balance of payments data (we expect a rise in cumulated 12M deficit to 5.2% of GDP, amid decrease in trade deficit), and monetary statistics.

Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
MONDAY (8 December)							
10:00	PL	Auction of Treasury Bills					
TUESDAY (9 December)							
10:00	DE	ZEW index	Dec	pts	-5.5	-	-53.5
15:00	US	Pending home sales	Oct	%	-3.5	-	-4.6
WEDNESDAY (10 December)							
10:00	PL	Auction of PLN1-2.5 bn 2Y bonds					
15:00	US	Wholesale inventories	Oct	%	-0.1	-	-0.1
THURSDAY (11 December)							
8:30	CH	SNB meeting – decision			1.0	-	1.0
13:30	US	Trade balance	Oct	mld \$	-55.0	-	-56.47
13:30	US	Import prices	Nov	%	-4.0	-	-4.7
13:30	US	New jobless claims	w/e	'000	-	-	509
FRIDAY (12 December)							
13:00	PL	Trade deficit	Oct	mIn €	-	980	1124
13:00	PL	Current account deficit	Oct	mIn €	2015	1980	1967
13:00	PL	Money supply	Nov	% r/r	16.8	17.6	17.6
10:00	EZ	Industrial output	Oct	% r/r	-3.8	-	-2.4
13:30	US	PPI	Nov	% m/m	-1.7	-	-2.8
13:30	US	Retail sales	Nov	% m/m	-1.4	-	-2.8
14:55	US	Preliminary Michigan	Nov	pkt	5.5	-	55.3

Source: BZ WBK, Reuters

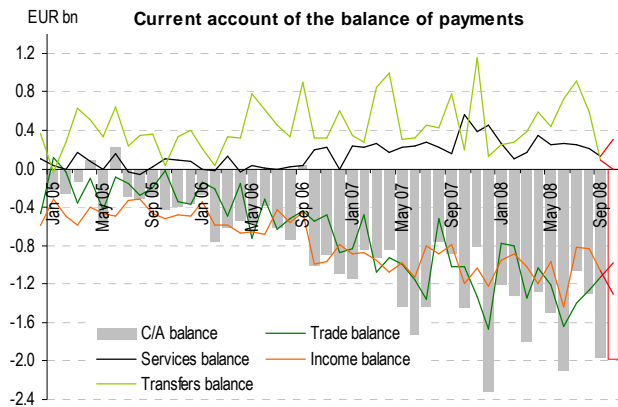
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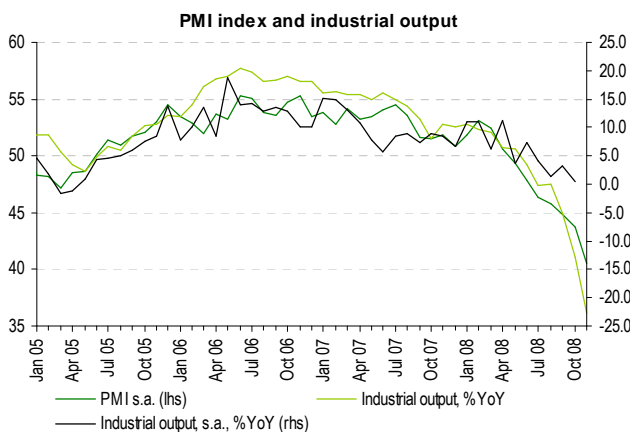
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What's hot this week – Next data locally and abroad, SNB decision

▪ Locally, this week we will get balance of payments for October. We expect that the C/A gap was €1.98bn in October, similar as in September. Trade gap probably narrowed to €980m with growth rates for exports and imports down to around 9%. We also predict smaller surplus in transfers account due to negative transfers from the EU.

▪ We forecast that money supply growth remained at 17.6%YoY in November with slight slowdown in growth of total deposits to 18.3%YoY. We also expect that weakening of total loans growth in November was not large as negative effect of tighter credit conditions was offset by effect of weaker zloty.

▪ Apart from domestic data, this week there will be again many data releases abroad, which may affect moods in the global markets and thus also performance of the Polish financial market. The SNB decision could also be important.

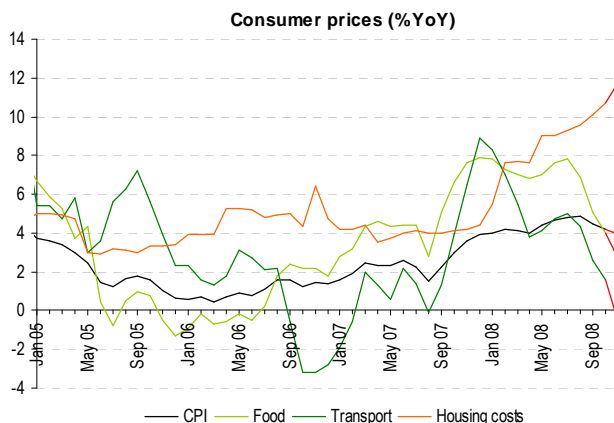
Economy last week – PMI reached new low, FinMin's inflation forecast as expected

▪ Poland's PMI for manufacturing lowered stronger than we had expected in November, reaching 40.5, i.e. the lowest level since the beginning of the survey in 1998, against 43.7 in October. The data indicate further deterioration in the manufacturing sector and herald weak output data.

▪ The government prepared an anti-crisis plan (for the amount of PLN91.3bn), which is aimed at keeping financial stabilisation and the country's economic development.

▪ The government lowered GDP growth forecast for next year from 4.8% to 3.7% with revenue and spending down by PLN1.7bn and unchanged target for deficit at PLN18.2bn.

▪ Results of Reuters survey showed average GDP growth forecast for next year was lowered from 3.5% to 2.8%. Our estimate down from 3.3% to 2.6%. Contrary to the market we expect that GDP growth will bottom out in 2Q09 and then economic growth should gradually rise.



▪ The FinMin's inflation forecast for November is 3.8%YoY (0.3%MoM), in line with our forecast and market consensus. According to FinMin, food prices rose 0.5%MoM, transport prices fell 2.5%MoM (fuel prices drop of 5.6%MoM) and housing and energy costs rose 1.5%MoM. Our forecast for the CPI inflation is consistent with the FinMin estimate.

▪ The Energy Regulatory Office decided to limit growth in energy prices will affect inflation path and may cause that inflation will return to target already next year, which would be conducive to rate cuts by the MPC.

▪ The ECB reduced rates by 75bps, the Bank of England by 100bps and the Riksbank by 175bps. ECB's Trichet said that the pace of inflation fall since the previous meeting had increased. The ECB lowered GDP and inflation forecasts for 2009 to -0.5% and 1.4%, respectively.

Quote of the week – Possible deeper interest rate cut**Marian Noga, RPP, PAP, 4 December**

A few rate cuts are ahead. Current macroeconomic parameters do not rule out interest rate cut in December. I would not also rule out a pause in January. I am not in favour Nie opowiadam się za ruchami 50 pb.

Mirosław Pietrewicz, RPP, PAP, Gazeta Prawna, 1,4 December

There is no sense in postponing necessary decisions only to keep tradition. In my opinion the [MPC] should continue this process [rate cuts], though at faster pace. I would not be surprised if reference rate was at 4% at the end of 2009.

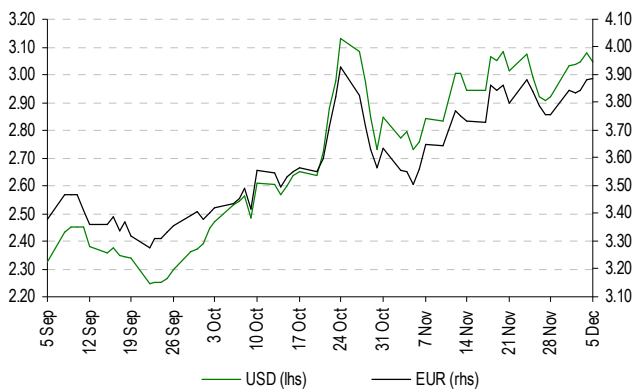
Jan Czekaj, RPP, TVN CNBC, 5 December

(...) this was a good policy [of small steps] in the past period. At present situation in extraordinary and it may require extraordinary actions. I do not rule out decision of deeper interest rate cut.

Although Dariusz Filar is still not convinced about the necessity to cut rates again in December, other hawk from the MPC, Marian Noga did not exclude it. However, he is not opting for larger moves than 25bp, while one of radical doves, Mirosław Pietrewicz, is in favour of more decisive steps. He also suggested a need for delay in EMR2 entry until the situation in global markets stabilises. NBP governor Sławomir Skrzypek again spoke in dovish tone while moderate Jan Czekaj did not exclude a rate cut in December and even suggested that rates could be reduced by 50bps. Dovish Stanisław Nieckarz said that the Council is obliged by law to support the economy and cut rates at the next meeting.

Market monitor

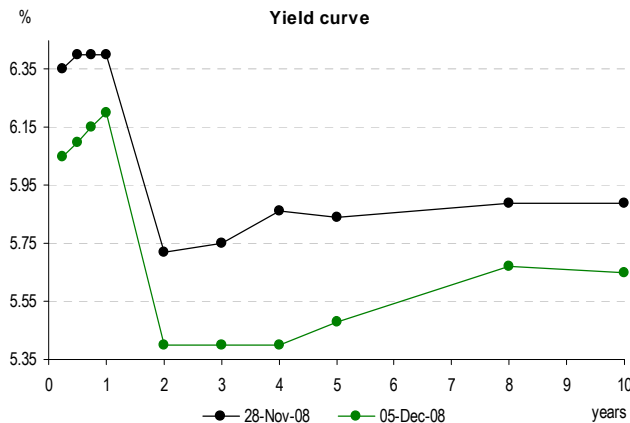
Zloty exchange rate



Zloty weaker again

- After significant strengthening of the zloty at the start of the previous week in the last few days the domestic currency returned to the weakening trend. The currencies in the region were depreciating amid poor data in the major economies. The EURPLN rate temporarily rose above 3.90 again, though the end of the week brought slight recovery on dollar's weakening against the euro. Since previous Friday the zloty depreciated 2% against euro and 2.5% vs. dollar.
- This week the domestic currency is going to stay under influence of global sentiment amid low number of domestic data. Current account figure should have lower influence on the zloty this time. In our view this week the zloty will fluctuate in range of 3.80-3.95 against the euro and 2.95-3.10 versus the dollar.

Yield curve



Further rates falls in the interest rate market

- After the interest rate cut of the MPC several Council members took the floor, and their comments were quite dovish, which contributed to strengthening of expectations for interest rate cuts and contributed to FRA rates decline (9x12 already below 4.0%) and IRS rates (5Y rates below 4.5%). Declining curve in the euro zone also supported the latter. IRS rates decline fuelled also the debt prices, which were rising also due to strengthening in the core debt markets.
- This week the behaviour of core debt markets and further comments of the MPC members will be more important than domestic data. In our opinion the potential for IRS and FRA rates fall may gradually diminish. The 2-year bonds auction will be market sentiment indicator.

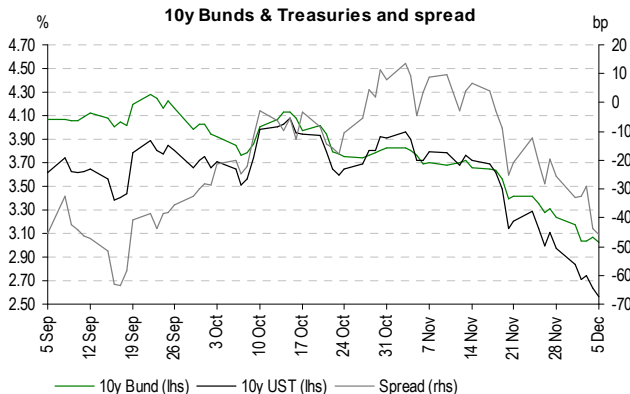
EURUSD rate



Euro supported by the ECB move

- The EURUSD rate was trading in a quite narrow range in the past week. After a slight strengthening of the dollar at the start of the week in the following days the euro was recovering, and clear strengthening of the single currency followed in the second part of the week after the ECB decision to cut rates. The markets positively interpreted the ECB's move as a supportive action for euro zone economy. The EURUSD rate rose during the week by 0.5%.
- The economic releases from the US will dominate this week. They include figures from housing market, trade balance and most important retail sales and consumer sentiment released at the end of the week. In the euro zone ZEW index and industrial output figures will be crucial. We expect dollar strengthening at the year-end toward ca. 1.24.

10y Bunds & Treasuries and spread



Continued strengthening in the core debt markets

- The rising trend of government bond prices in the euro zone and the US was continued also in the last few days under influence of very poor data from the euro zone and the US. Yields of 10Y US Treasuries fell to the lowest level in 50Y (bottom at 2.55%), which was supported by comments of Ben Bernanke that Fed may start purchasing government bonds. Yields of 10Y Bunds temporarily broke 3% and were supported by expectations of interest rate cuts by the ECB.
- After the decision and comments from the ECB we expect deeper rate cuts in the euro zone (reference rate down to 1.5% in Spring 2009). Low ZEW index and poor data on industrial production from the euro zone as well as retail sales figure in the US may support bond prices at high levels.

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