

Weekly economic update

1 – 7 June 2009

In line with expectations the Monetary Policy Council kept official rates on hold, though they decided to lower obligatory reserve requirement by 50 bp to 3%. The content of the Council's statement, including maintaining easing bias in monetary policy, confirms our expectations the MPC will resume interest rate cuts at the next meeting after the publication of new NBP's inflation projection. The timing of next steps regarding reduction in obligatory reserve will depend on results of last move. The GDP data for the first quarter should not be an obstacle in easing cycle by the MPC. They showed growth by 0.8%YoY with private consumption increase by 3.3%, investment growth by 1.2% and strong positive contribution of net exports.

At the beginning of the week investors' attention will be focused on inflation forecast for May, which will be announced by the Ministry of Finance, as well PMI data. Just after the publication of CPI for April the ministry said they expected a decrease of 12M CPI in May to 3.4%, however, we think this estimate could have been revised upward amid higher prices of food and fuel. Our CPI forecast is at 3.6%, while market consensus at 3.7%. As regards manufacturing PMI, we foresee increase stronger than the market given better moods in recent flash data for euro zone. The second part of the week will be packed with foreign data, with US labour market data as the key. Also, the European Central Bank and the Bank of England will meet this week.

Economic calendar

Time GMT	COUNTRY	INDICATOR	PERIOD	FORECAST			LAST VALUE
				MARKET	BZWBK		
MONDAY (1 June)							
7:00	PL	PMI manufacturing	May	pts		44.0	42.1
7:58	EZ	PMI manufacturing	May	pts	40.5	-	36.8
9:00	PL	Auction PLN2-2.5bn of 52-week Treasury Bills					
12:30	US	Core PCE	Apr	%MoM	0.2	-	0.2
14:00	US	ISM manufacturing	May	pts	42.5	-	40.1
TUESDAY (2 June)							
14:00	US	Pending home sales	Apr	%MoM	0.5	-	3.2
WEDNESDAY (3 June)							
7:58	EZ	PMI services	May	pts	44.7	-	43.8
9:00	PL	Auction of OK and PS bods worth PLN 3-5 bn					
9:00	EZ	PPI	Apr	%YoY	-4.4	-	-3.1
12:15	US	ADP report	May	k	-520.0	-	-491.0
14:00	US	Factory orders	Apr	%MoM	0.8	-	-0.9
14:00	US	ISM non-manufacturing	May	pts	45.0	-	43.7
THURSDAY (4 June)							
9:00	EZ	Retail sales	Apr	%YoY	-3.2	-	-4.2
11:00	GB	BoE decision		%	0.5	-	0.5
11:45	EZ	ECB decision		%	1.0	-	1.0
12:30	US	Jobless claims	w/e	k	620.0	-	623.0
12:30	US	Unit labour costs	Q1	%	2.9	-	3.3
FRIDAY (5 June)							
12:30	US	Non-farm payrolls	May	k	-517.0	-	-539.0
12:30	US	Unemployment rate	May	%	9.2	-	8.9

Source: BZ WBK, Parkiet daily, Reuters;

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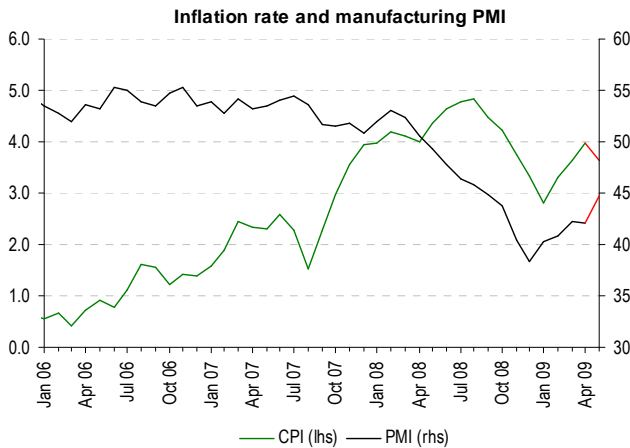
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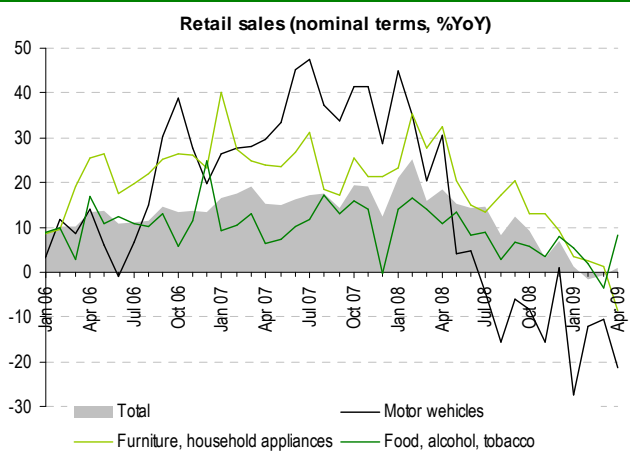
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What's hot this week – PMI, inflation forecast, data abroad

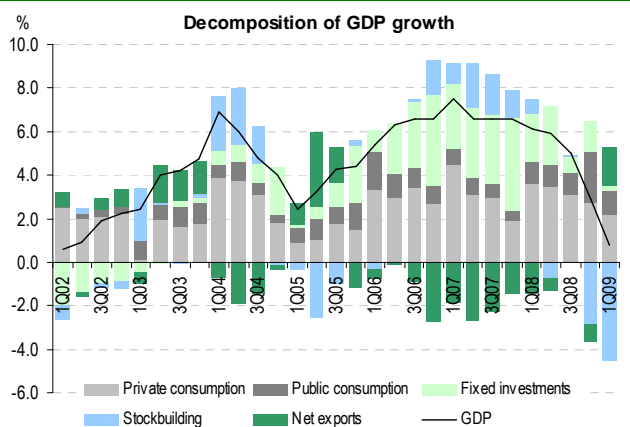


- As usual at the beginning of a month, we will get the FinMin's inflation estimate and domestic PMI.
- The market consensus points to fall in inflation in May to 3.7%YoY and our forecast is 3.6%YoY. The main risks to the CPI forecast is again the scale of rise in food and fuel prices.
- After another strong rise in flash PMI in the euro zone, we predict that also the domestic index rose in May, to 44pts, the highest level in three quarters.
- Following Monday's data releases locally, this week will be dominated by important information in the euro zone and the US, out of which the key focus of attention will be economic activity indicators and the US labour market data.
- Decision meetings of the ECB and the BoE are expected to bring no change in rates and markets' attention will be on details regarding quantitative easing of monetary policy.

Economy last week – Rates on hold, GDP data not so bad



- The MPC kept interest rates on hold, but lowered reserve requirements rate by 50bps to 3%. The contents of the official statement, including maintaining the informal easing bias in monetary policy, confirm our expectations the MPC will resume rate cuts at the next meeting following expected inflation fall in May and given results of the new central bank's projection of inflation and GDP.
- Increase in retail sales in April was slightly higher than expected and reached 1%YoY, to a large extent thanks to rise in food sales. Demand for durable goods weakened.
- The registered unemployment rate slightly fell to 11% thanks to seasonality, but more important is accelerating unemployment rise in annual terms. LFS unemployment rate in Q1 rose to 8.3%. Negative tendencies in the labour market will weaken consumption demand during this year.



- Poland's GDP growth in Q1 was in line with our forecast and reached 0.8%YoY. Seasonally adjusted quarterly growth rate also was positive (0.4%YoY), which means Poland is positive outlier in Europe.
- The breakdown of GDP growth was a positive surprise, showing relatively strong private consumption (3.3%YoY rise) and fixed investment (1.2%YoY). However, annual growth rate of domestic demand was negative (-1.1%) due to considerable fall in change in inventories.
- In line with our estimates, contribution of net exports to GDP growth in Q1 was strongly positive (1.8pp).
- In next quarters one should expect lower GDP growth rate due to fall in fixed investments and slower consumption rise. However, still positive contribution of net exports should maintain overall GDP growth rate in the positive territory.

Quote of the week – MPC members do not exclude further cuts

Andrzej Sławiński, MPC member, Polsat News, 28 May

If demand is not a reason for inflation increase, which is quite obvious, this is probable that the MPC will cut interest rates if concludes that there is higher risk of further deterioration in economic climate, on a larger scale than previously expected.

Jan Czekaj, MPC member, PAP, 28 May

I do not exclude further interest rate cuts as we are still in easing bias.

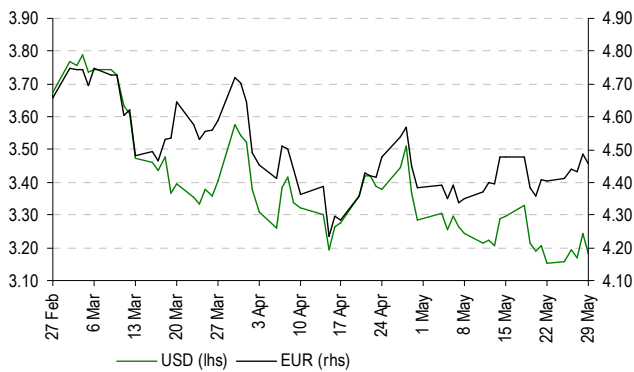
Andrzej Wojtyna, MPC member, PAP, 29 May

We still maintain informal easing bias in monetary policy, but depending on new data and the new inflation projection of inflation and GDP, we will take adequate decisions. These will be the factors causing maintaining or changing the bias to neutral, depending on the balance of risks. I do not exclude that such a change may take place in following months.

Most of the comments of MPC members after the meeting in May were rather dovish, showing a possibility of interest rate cut in June (depending on results of CPI and GDP projection of the NBP and new data releases). Rate cut next month was not excluded even by a hawkish member, Marian Noga. Given that, the comment by Andrzej Wojtyna on possibility of changing monetary policy bias to neutral form easing, was very hawkish. However, it should be remembered that rate cuts are possible without support from this member, as it happened in the past. Members, whose votes may be crucial to find majority for further easing (Jan Czekaj and Andrzej Sławiński) repeated opinions on possible continuation of relaxation in monetary policy, also after GDP data release.

Market monitor

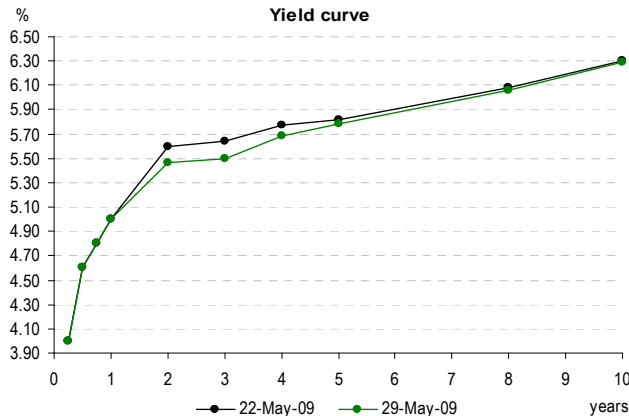
Zloty exchange rate



Weaker zloty at the end of the month

- The past week brought zloty weakening, which resulted from deterioration of moods in the region (concerns over devaluation in Latvia, negative opinion of Moody's on CEE banks) and perhaps also the maturation of FX option contracts at the end of the month. The important resistance level at 4.52 for the EURPLN, which we indicated last week was only temporarily exceeded.
- 4.52 will still be an important resistance and the next level would be 4.60. However in our view the zloty strengthening is more likely than weakening. The issue of maturing FX options at the end of month will be over, GDP figure was quite positive than one could expect and we see rebound in PMI, which should support the domestic currency. The zloty will be also affected by changes in global moods.

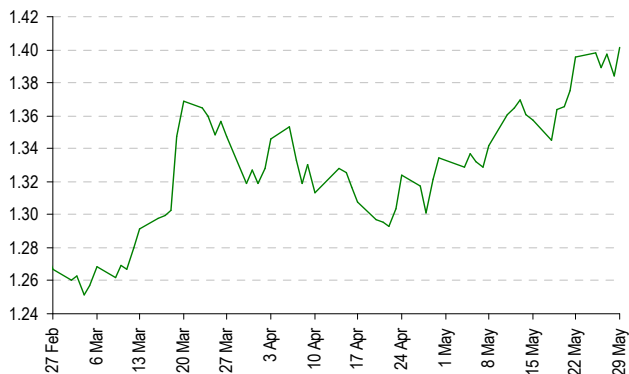
Yield curve



Relative stability in the debt market

- The debt market initially was weakening in line with the depreciation of the zloty, though at the end of the week this pattern was broken. Consequently, as compared to the previous Friday the yield curve did not change significantly (there was a slight steepening, due to larger lowering of the short end of the curve).
- The forecast of the FinMin and (to smaller extent) the value of the PMI index may influence the market expectations regarding the next decision of the MPC. We expect lower inflation from the consensus, though we do not know what will be the FinMin's forecast. The Wednesday bond auction with large supply (PLN3-5bn) will be a test for the market. Later this week the trend will be rather determined by the data releases abroad.

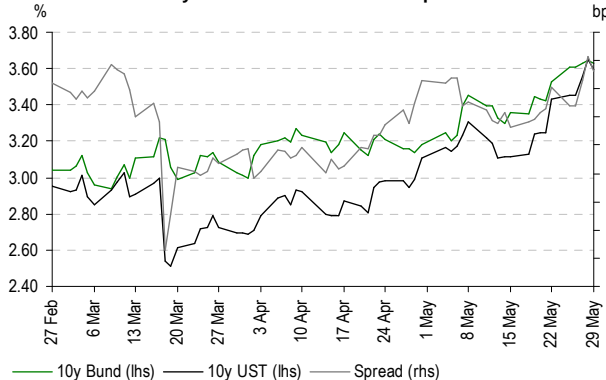
EURUSD rate



The dollar without a clear trend

- After a clear rise of the EURUSD rate to almost 1.40 in the previous week this trend weakened and the dollar tried to recover, which was supported by the temporary increases in the risk aversion (inter alia nuclear tests of North Korea, equity market declines). However, the end of the week brought weakening of the US currency, among others due to higher risk appetite. At the end of the Friday session the EURUSD rate clearly rose above 1.41, the highest level since the end of the past year.
- The changes in risk appetite and news on quantitative monetary easing by European central banks will be the crucial factors affecting the trend in the coming days. The most important release will be figure on non-farm payrolls in the US, which were scheduled for Friday and which will show another deep decline.

10y Bunds & Treasuries and spread



Further increases of yields in the core debt markets

- In the core debt markets a significant increase in bond yields was continued, especially at the long end of the yield curve (2-10Y spread in the US rose near to record high level). Yields of 10Y Treasuries rose faster as compared to the euro zone bonds. This resulted from the concerns over the prospects of US economy and fears over the US rating outlook.
- The key factors for the debt in the euro zone will be information from the ECB about the details of the covered bonds purchase, as well potential comments from the ECB regarding the possibility of further interest rate cuts.

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