

Weekly economic update

31 August – 6 September 2009

The past week initially brought zloty appreciation, though an increase in risk aversion in the global markets later in the week resulted in fall in EURUSD and yields in the core debt markets as well as correction of the domestic currency exchange rate. However, towards the end of the week investors's believe in recovery of the global economy strengthened again and demand for risky assets increased, thus the zloty more than offset earlier losses and at the end of the week was stronger than a week earlier. During the week the domestic currency was positively influenced by better than expected data from real economy (surprising clear acceleration in retail sales growth in July and slight rebound in GDP growth rate in Q2). At the same time the data led to increase in market interest rates, as they lowered probability that the MPC may reduce interest rates again. In our view, economic revival is still burdened with high uncertainty and one cannot rule out that there will be one more rate cut, but under condition that data to be released in the next months will show clearly that a rebound signalled by recent indicators is not persistent. This week important information from this point of view will be manufacturing PMI for Poland. Besides, we will receive the Ministry of Finance's inflation estimate for August and many important data from the US and the euro zone that may have significant impact on risk appetite on global markets. ECB meeting may also be important market driver.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
MONDAY (31 August)							
11:00	PL	Auction PLN 0.8-1.0bn of 52-week Treasury Bills					
11:00	EZ	Flash HICP	Aug	%YoY	-0.3	-	-0.7
15:45	US	Chicago PMI	Aug	pts	47.0	-	43.4
TUESDAY (1 September)							
9:00	PL	PMI manufacturing	Aug	pts	47.9	47.9	46.5
9:58	EZ	Manufacturing PMI	Aug	pts	47.9	-	46.3
16:00	US	Manufacturing ISM	Aug	pts	50.5	-	48.9
16:00	US	Pending home sales	Jul	%	1.8	-	3.6
WEDNESDAY (2 September)							
	PL	Auction of 2Y and/or 5Y bonds					
11:00	EZ	Revised GDP	Q2	%YoY	-4.6	-	-4.9
14:15	US	ADP report	Aug	k	-250.0	-	-371.0
14:30	US	Unit labour costs	Q2	%	-5.8	-	-5.8
14:30	US	Labour productivity	Q2	%	6.4	-	6.4
16:00	US	Factory orders	Jul	%	2.2	-	0.4
20:15	US	FOMC minutes	-	-	-	-	-
THURSDAY (3 September)							
9:58	EZ	PMI services	Aug	pts	49.5	-	45.7
11:00	EZ	Retail sales	Jul	%YoY	-2.2	-	-2.4
13:45	EZ	ECB decision	-	%	1.0	1.0	1.0
14:30	US	New jobless claims	w/e	k	560.0	-	570.0
16:00	US	ISM non-manufacturing	Aug	pts	48.0	-	46.4
FRIDAY (4 September)							
14:30	US	Non-farm payrolls	Aug	k	-230.0	-	-247.0
14:30	US	Unemployment rate	Aug	%	9.5	-	9.4

Source: BZ WBK, Dow Jones, Reuters

Maciej Reluga Chief economist (+48 22) 586 8363

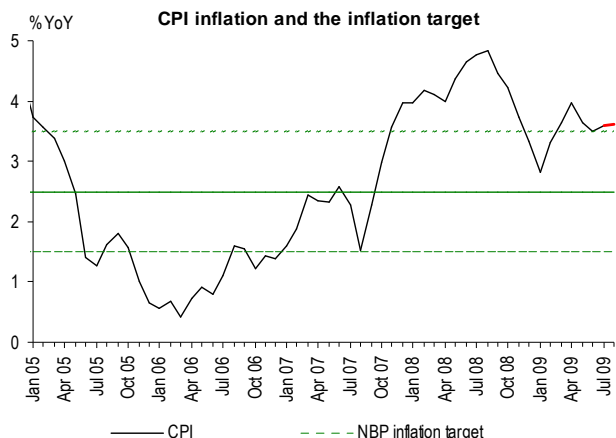
Piotr Bielski (+48 22) 586 8333

Piotr Bujak (+48 22) 586 8341

Cezary Chrapek (+48 22) 586 8342

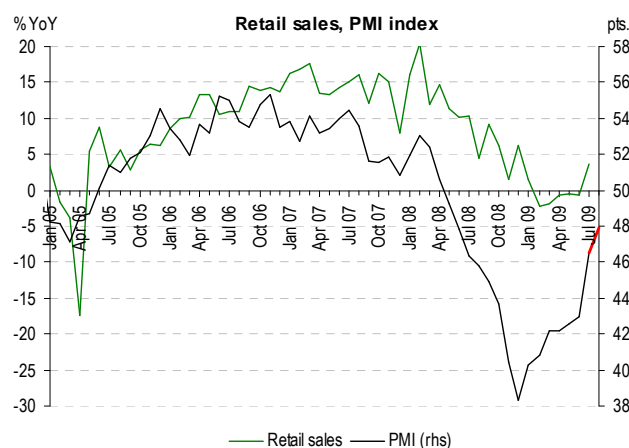
e-mail: ekonomia@bzwbk.pl

What's hot this week – Domestic PMI, FinMin inflation forecast and important data abroad

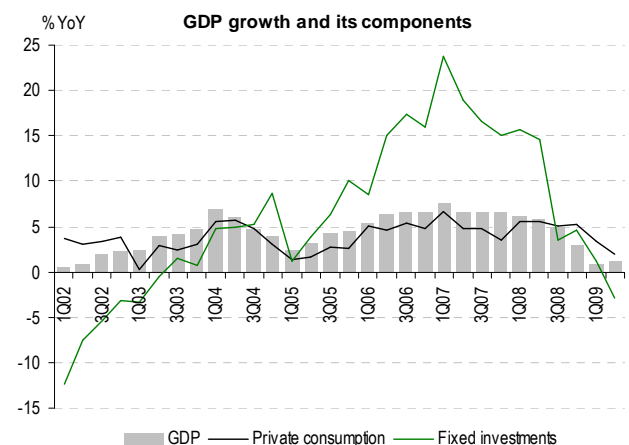


- In our view the PMI index for domestic manufacturing sector to be released this week will rise to level reached by the preliminary value for the euro zone manufacturing PMI. This will confirm that the activity in Polish manufacturing still diminishes though on smaller scale than earlier.
- It is hard to say what the August inflation forecast of the Ministry of Finance scheduled for Tuesday will show. Our estimate points to stabilisation of inflation at 3.6%YoY posted in July.
- Apart from this, the domestic market may be under influence of possible news on fiscal policy. Perhaps, at the start of September more details will be presented about the next year's budget, after in the past week the PM said that the central budget deficit in 2010 will be higher than PLN27.2bn scheduled in the amendment of this year's budget.

Economy last week – MPC did not surprise, data clearly better than expected



- At its meeting last week the MPC kept interest rate unchanged, but at the same time maintained the informal easing bias in monetary policy.
- The tone of the of the post-meeting statement was similar as a month earlier, suggesting that although the inflation prospects in the medium term speaks in favour of continuation of interest rate cuts, the elevated current inflation and improving data from the real economy pose significant risk for such scenario.
- An improvement in the real economy was signaled by retail sales data for July, which showed rise of 5.7%YoY (stronger than expected 0.7%YoY and 0.9%YoY in June). This allows for more optimism as regards consumption demand in Q3, especially amid improvement in consumer moods in August visible in data released last week by the CSO and results of Ipsos survey.



- GDP data for Q2 were another positive surprise showing increase of 1.1%YoY. In contrast to most of the EU countries, Poland is not only avoiding recession, but the economic growth even accelerated, which increases optimism on economic growth forecast for the whole year.
- Quite positive breakdown of GDP growth pointed to moderate slowdown of consumer demand. Although in case of domestic demand there was a deepening of decline to -2.0%YoY from 1.0% in Q1, this was mainly the result of stronger than we expected drop in inventories (according to our estimate its negative contribution to GDP in Q2 was at almost 3pp). This is likely to be followed by restocking process along with strengthening demand.
- Seasonally adjusted GDP rose by 0.5%QoQ in Q2 against 0.3% rise in Q1.

Quote of the week – Doubtful need for a change in interest rates?

Stanisław Nieckarz, MPC member, Reuters, 28 August

Currently it is difficult to state whether the economy is in the recovery stage and thus it is appropriate to adopt a wait and see approach in monetary policy, which means keeping rate on hold, if there are no new risks to inflation and GDP.

Stanisław Owsiak, MPC member, Reuters, 28 August

These data show that a change in the interest rates' level is doubtful over the next two quarters. With such inflation, it would be difficult to expect a change to interest rates.

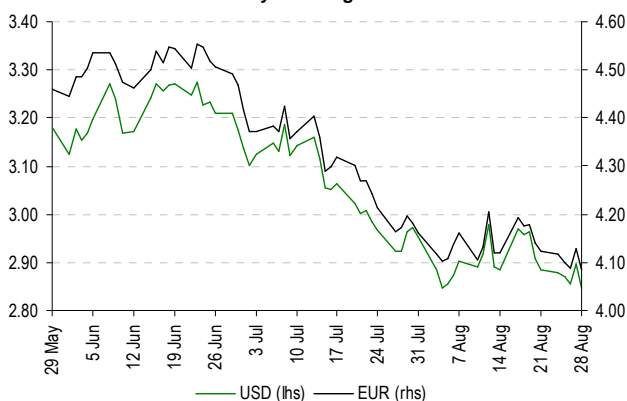
Mirosław Pietrewicz, MPC member, Reuters, 28 August

It is good news because it means there is no need for action on our part, meaning changes in monetary policy. The timeframe we're talking about here would be till the end of this Council's term, though in October we will have new projection, which may change something.

Improving data from the real economy, including retail sales for July and GDP figures for Q2 released last week seem to weaken the willingness of dovish MPC members to reduce interest rates. Comments from Stanisław Owsiak and Mirosław Pietrewicz point out that positive surprise in GDP data and earlier retail sales data are next factors lowering probability that the Monetary Policy Council could deliver another interest rate cut this year. Taking into account the most recent news from the economy it seems to us that the interest rate cut in October may happen, but under condition that the new data, which will be published till then will show that the economic recovery signaled by recent indicators is not permanent.

Market monitor

Zloty exchange rate

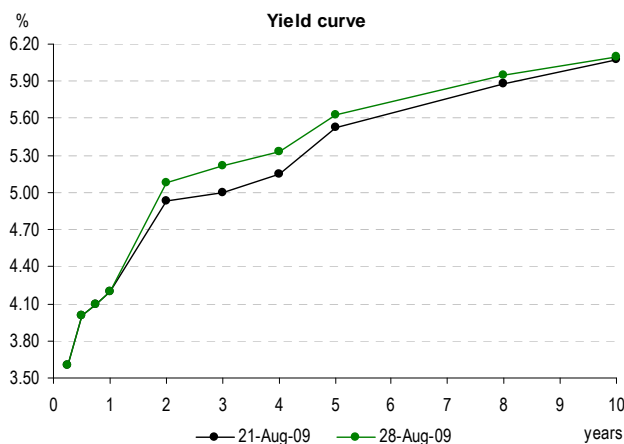


Zloty gradually stronger

■ In the first part of last week the zloty was strengthening amid stabilisation of world stock markets. The EURPLN broke through 4.08 and 4.07. Later on there was a correction after deterioration of moods in stock markets. However, on Friday the risk appetite rose again, which was supportive for the zloty. Also, better than expected GDP data for Q2 were a support for the local currency. During the entire week the zloty performed better than the forint and Czech crown.

■ This week the zloty performance will depend on important data to be released abroad and domestic PMI. We think that the zloty is still more vulnerable to bad news (and thus a correction to 4.20 is possible), but if good news will be dominating again, the EURPLN may go back below 4.08 and march towards 4.00.

Yield curve

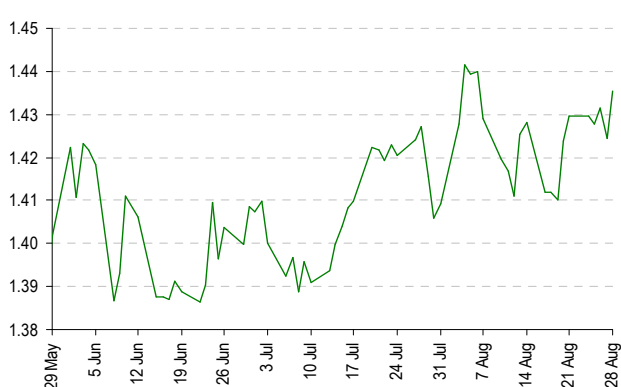


Weakening in the local debt market

■ Domestic interest rate market was weakening last week, under influence of better than expected macroeconomic data, which reinforced market expectations that the next move of the MPC may not be a cut but a rate hike. Bond yield curve moved up, but at the same time became flatter (2-10 spread down to 102 bp), amid stronger rise in yields in the short end of the curve. At the same time there was a fall in asset swap spread (to 0 bp for 2-5Y) thanks to a fall in credit risk for Poland.

■ This week the crucial factor for local interest rate market will be FinMin's inflation forecast for August and PMI data for manufacturing sector. Stabilisation of CPI inflation above the tolerance range around the central bank's target and simultaneous rise in PMI expected by us would be negative for the market, even amid the zloty strengthening.

EURUSD rate

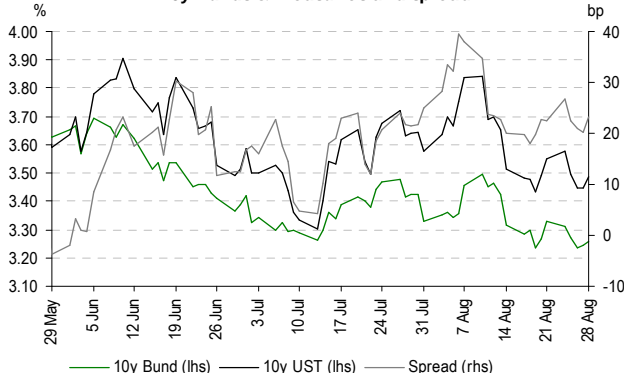


EURUSD higher amid returning risk appetite

■ After stabilisation of EURUSD at the start of the week, a drop in risk appetite later on strengthened dollar versus the euro. However, the end of the week saw a rebound in euro thanks to restoration of investors' belief in persistence of economic recovery. At the end of the week the EURUSD was close to 1.44 against ca. 1.43 a week earlier, although during the week it reached minimum at 1.42. Market participants are still pondering whether a main driving force for the EURUSD is risk aversion or relative strength of economies in the US and the euro zone.

■ This week the level of risk aversion and assessment of situation in main economies will be changing under influence of important macroeconomic indicators that will be released every day.

10y Bunds & Treasuries and spread



Correction after gains in the core debt markets

■ In the first part of the week yields in the core debt markets were gradually falling amid stabilisation and later on also decline of the major world stock indices. The core debt markets also found support in positive results of bond auction in the US. At the end of the week there was a correction due to increase in risky assets. At the end of the Friday's session yields of 10Y Treasuries and Bunds were lower than a week before and were at 3.49% and 3.26%, respectively, against 3.55% and 3.33% on the previous Friday.

■ This week the direction of changes in yields in the core debt markets will depend on the data from the euro zone and the US. If positive moods will dominate yields may rise further.

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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>



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