Bank Zachodni WBK

Weekly economic update

10 – 16 May 2010

The last week was marked by significant rise in risk aversion amid growing concerns about the Greek debt problems and its spill-over to other markets. The single currency clearly weakened against the dollar while the global markets saw sharp weakening of credit markets, stocks and emerging market currencies. There was strong increase in CDS rates, mostly for peripheral countries of the euro zone (for Greece to ca. 1000bps). On Wednesday, Moody's added fuel to the flames, putting Portugal's rating on the watch list and warning against a possibility of spill-over effects of the Greek debt crisis. However, the culmination of the rise in risk aversion took place on Thursday, as investors were disappointed by the outcome of the ECB meeting (no actions and only comments that default of Greece is not an option and situation of Portugal and Greece is much better) and scared by protests in Athens. Major stock indices in the US recorded the strongest intra-day fall since 1987, although this could be partly related to erroneous transactions. On Friday, moods in the markets improved thanks to approval of the rescue plan for Greece and the German parliament and due to better than expected labour market data from the US.

This week the markets will remain focused on developments regarding the sovereign debt crisis (important event will be the Eurogroup on Monday). We assume that after approval of the rescue plan for Greece by the German parliament on Monday and by the IMF over the weekend, one should see some improvement in market sentiment this week. Macro figures may become somewhat more important in such circumstances. Recent news from the global economy were mostly positive and this would be supportive for rebuilding of risk appetite. However, it will be important what next data will show with key focus of attention this week on the US retail sales for April. Domestic macro data will recede in the background, especially that we will see only CPI inflation as regards crucial figures. More important will be outcome of the 5Y bonds auction. We expect the zloty and local bonds to strengthen.

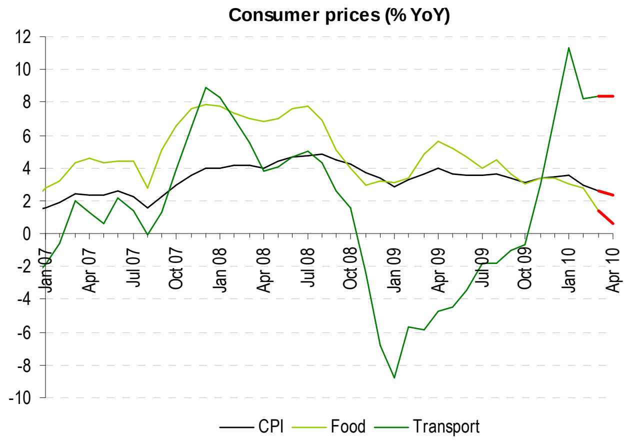
Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		MONDAY (10 May)					
11:00	**PL**	**Tender of T-bills**					
13:00	GB	BoE decision		%	0.5	0.5	0.5
		TUESDAY (11 May)					
16:00	US	Wholesale inventories	Mar	%MoM	0.5	-	0.6
		WEDNESDAY (12 May)					
11:00	**PL**	**Auction of 5Y bonds PS0415**					
11:00	EZ	Preliminary GDP	Mar	%YoY	0.5	-	-2.2
11:00	EZ	Industrial output	Mar	%YoY	6.1	-	4.1
14:30	US	Trade balance	Mar	$bn	-40.0	-	-39.7
		THURSDAY (13 May)					
14:30	US	Import prices	Apr	%MoM	0.8	-	0.7
14:30	US	New jobless claims	w/e	k	440.0	-	444.0
		FRIDAY (14 May)					
14:00	**PL**	**CPI**	**Apr**	**%YoY**	**2.2**	**2.3**	**2.6**
14:00	**PL**	**Money supply**	**Apr**	**%YoY**	**6.7**	**6.2**	**5.6**
14:30	US	Retail sales	Apr	%MoM	0.2	-	1.9
15:15	US	Industrial output	Apr	%MoM	0.6	-	0.1
15:15	US	Capacity utilisation	Apr	%	73.7	-	73.2
15:55	US	Preliminary Michigan index	May	pts	73.3	-	72.2

Source: BZ WBK, Reuters, Parkiet daily

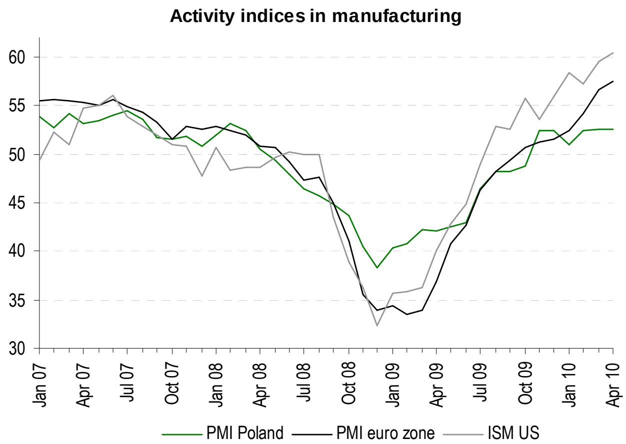
Maciej Reluga Chief economist (+48 22) 586 8363
Piotr Bielski (+48 22) 586 8333
Piotr Bujak (+48 22) 586 8341
Cezary Chrapek (+48 22) 586 8342 e-mail: ekonomia@bzwbk.pl

What's hot this week – Next macro figures against the background of debt crisis

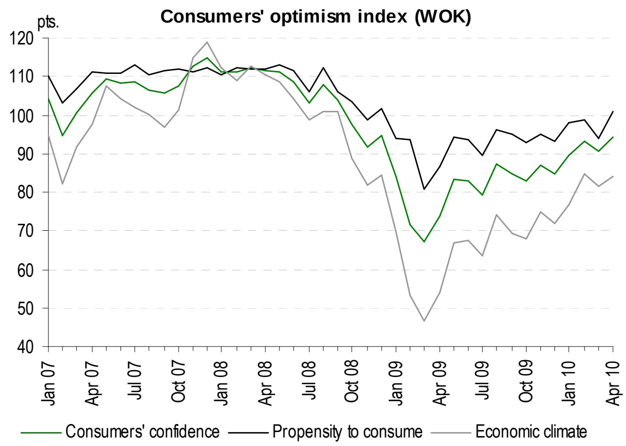


- This week the key factor for the market will be further news regarding possible spill-over effects of the Greek debt crisis. However, assuming gradual weakening of concerns about fiscal condition of the euro zone's peripheral countries (among others thanks to approval of the €110bn rescue plan for Greece by the German parliament and the IMF), macro data may become of somewhat higher importance. The relatively light data calendar will be dominated by the US retail sales figures for April due on Friday.
- Domestic data will recede to the deep background, especially that the only crucial indicator due this week is the CPI inflation for April. We forecast inflation drop to 2.3%YoY from 2.6%YoY in March. Our forecast is consistent the FinMin's estimate while market consensus is at 2.2%YoY. For monetary statistics we predict rebound in annual growth rate among others due to low base in corporate deposits.

Economy last week – Positive macro indicators overshadowed high risk aversion



- Poland's PMI manufacturing in April was unchanged at 52.5pts, remaining at the highest level in more than 2 years. However, the market had expected a rise to 53.2pts and the reading is particularly disappointing in the context of robust rise in the euro zone's PMI manufacturing in April. Nevertheless, one should remember that similar situation was in a few previous months, but industrial output has been rising stronger in Poland, beating market expectations.
- Detailed data showed that April was another month in a row with rise in output and new orders (both domestic and foreign ones), but in each case the pace of increase weakened (indices for output, new orders and new export orders remained above 50.0, but lowered), particularly in case of export orders (index the lowest in 6 months). This suggests that zloty appreciation observed earlier weakened competitiveness of Polish firms.



- Consumer confidence survey carried out by Ipsos showed that April brought continuation of rise in optimism observed since April 2009. April brought improvement in overall indicator of consumer optimism (both as regards the current situation and expectations), in assessment of economic climate and in propensity to consume (above 100pts first time since since December 2008). Ipsos said that the improvement in consumer confidence results mainly from better assessment of households' financial situation, which bodes well for prospects of consumption demand.
- The NBP survey showed that in Q1 the tendency of clear tightening in banks' lending policy was maintained only in case of consumption loans. Terms on corporate loans were slightly eased for the second quarter in a row. Overall change in terms on mortgages was not significant, although changes in particular criteria were large and very diversified.

Quote of the week – Such a pause for breath is not a bad thing

Witold Koziński, deputy NBP governor, Reuters, 6 May

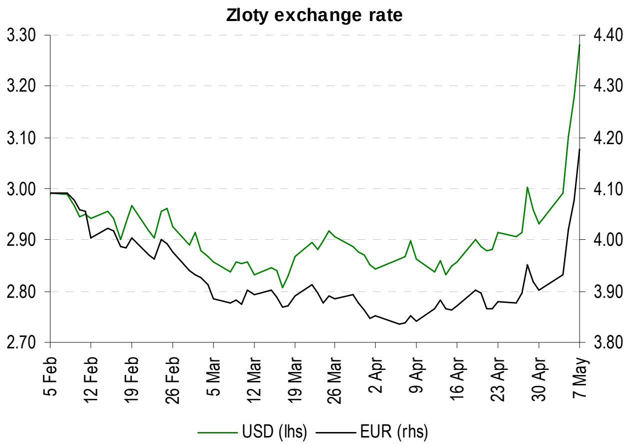
I am not afraid of it [further weakening of the zloty], as not so long ago we were afraid of too rapid appreciation of the zloty. (…) Such a pause for breath is not a bad thing.

Anna Zielińska-Głębocka, MPC member, PAP, 5 May

In circumstances of floating exchange rate and stable economy, such swifts are not dangerous, especially that there are instruments, including the FX interventions – for which there is agreement of the NBP and the FinMin. [Will the NBP intervene to stop the zloty weakening?] No. There is no reason for that yet. These are market fluctuations and if it proves that intervention is necessary, this will be not be heralded in advance.

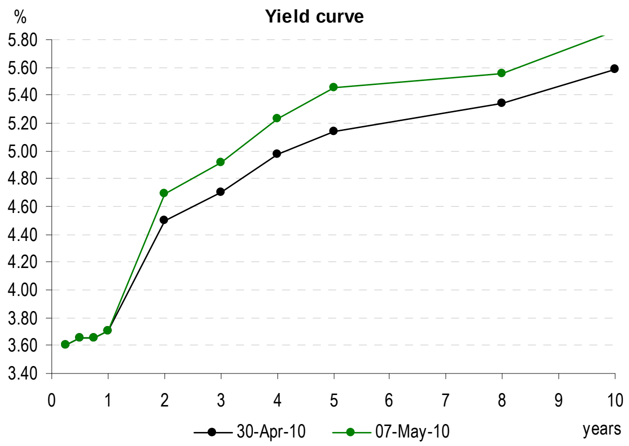
Comments from Polish central bankers to the sharp zloty depreciation last week indicate that one should not expect any nervous moves of the NBP. In our view deputy NBP governor rightly stressed that not so long ago all were afraid of too rapid appreciation of the zloty. From this point of view, the zloty losses amid higher risk aversion globally gives a pause for breath to Polish exporters. However, further uncontrolled depreciation of the zloty would be negative (leading for instance to rise in public debt to GDP ratio). We thinks that counteracting a possible further significant depreciation of the zloty should be take place through sale of foreign currency from EU funds by the state BGK bank and not through FX interventions of the NBP.

Market monitor



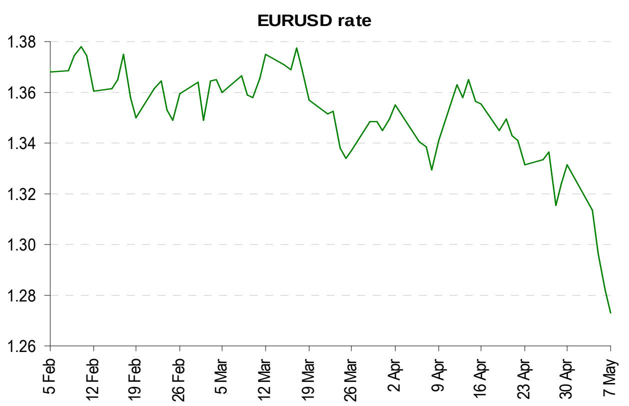
Sharp zloty weakening

- Significant rise in global risk aversion led to sharp sell off of the Polish currency through the week. On limited liquidity in trading Thursday/Friday overnight the EURPLN rose to the weekly maximum of 4.26 (as compared to 3.92 at the end of the previous week). The zloty lost the most out of emerging markets currencies, though other CEE currencies also depreciated driven by the unexpected rate cut of 25 bp by the Czech central bank. On Friday markets moods improved and the zloty recovered finishing the week at 4.14.
- Next week very emotional trading on the market may finally calm don and sentiment may improve after the Greek and German parliaments, as well as the IMF over the weekend, approved the bail-out plan for Greece. While this may lead to zloty strengthening, higher market volatility is likely to stay with us for some time.



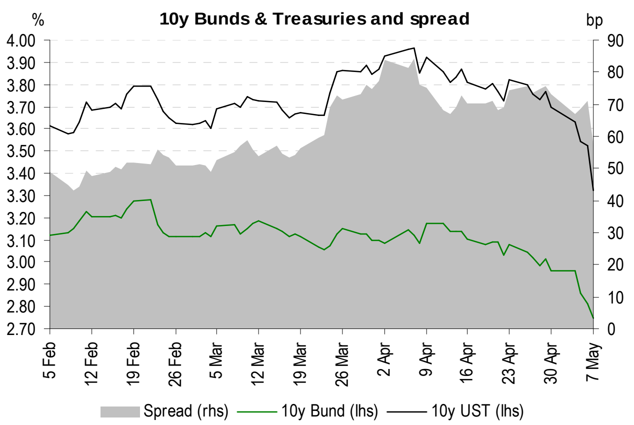
Weakening, but not a panic on the debt market

- The Polish fixed income market, similarly as other bond markets in the region weakened driven by sell off in most of assets across the emerging markets. However, the sentient towards domestic bonds was relatively better as compared to the foreign exchange market (yield curve up by 20-30 bp). Also, demand for Polish papers did not disappear and the Ministry of Finance sold PLN3.7bn with demand of PLN5bn and average yield only slightly higher than observed on the secondary market.
- This week another auction of government bonds will be a test for the market. This time the ministry will offer five-year paper, but in difficult market conditions demand with very high yields may be rejected, given substantial liquidity cushion in the ministry. Assuming better moods in global markets, we expect the Polish bond market to strengthen.



Euro hit by Greece

- The Greek debt problems and concerns over their spread to other south euro zone countries inflated pressure on weakening of the single currency. The EURUSD rate broke a few important support levels and reached the lowest level in 14 months below 1.26. The euro weakened also vs. the Swiss franc, as the SNB stopped interventions against franc appreciation at the levels where is was seen so far.
- Technical analysis points that the EURUSD rate is at clearly oversold levels. If there is an improvement in assessment of the euro zone's fundamentals, i.e. weakening of concerns about fiscal situation of its peripheral countries, one may expect a short-term upward recovery of the EURUSD. The EURUSD rate rebound may decelerate if the inflow of positive US macro data is continued.



Treasuries and Bunds favoured as safe havens

- In the core debt markets there was a significant strengthening, as investors were moving the capital toward the safe haven US and German bonds. In the peak moment of risk aversion yields of 10Y Treasuries and Bunds fell to 3.29% and 2.73% respectively. Amid improvement in moods on Friday a part of the earlier strengthening was erased and at the end of the week yields were at 3.45% and 2.81%. At the same time CDS rates significantly increased, mainly for the peripheral countries of the euro zone (for Greece to ca. 1000 bp).
- In our view this week should bring a correction in the core debt markets. Some rebound in risk appetite will contribute to capital flow toward more risky assets than Treasuries and Bunds.

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