Bank Zachodni WBK

Weekly economic update

14 – 20 June 2010

The following days will bring a number of important macroeconomic publications for May. We expect a moderate fall in CPI inflation and rise in PPI index, confirmation of improvement in the labour market and some moderate slowdown in industrial production (growth of close to 9%YoY driven mainly by foreign demand). The data will be first signs on possible impact of flood on the Polish economy. Also, a number of data releases will be a kind of test for the new NBP President as regards his self-restraint on commenting current economic situation. A lot of important information will also be released abroad giving hints on the pace of economic recovery in global economy. Publications in core markets will be the key drivers for investors' risk appetite and market moods.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
		MONDAY (14 June)					
11:00	**PL**	**Tender of 52-week T-bills worth PLN0.8-1.2bn**					
11:00	EZ	Industrial production	Apr	%MoM	0.5	-	1.3
14:00	**PL**	**Money supply**	**May**	**%YoY**	**6.0**	**6.1**	**6.0**
14:00	**PL**	**Current account balance**	**Apr**	**€m**	**-625**	**-670**	**-559**
		TUESDAY (15 June)					
	JP	BoJ decision		%	0.1	-	0.1
11:00	DE	ZEW index	Jun	pts.	42.0	-	45.8
14:00	**PL**	**CPI**	**May**	**%YoY**	**2.4**	**2.3**	**2.4**
14:30	US	Import prices	May	%MoM	-1.3	-	0.9
14:30	US	NY Fed index	Jun	pts	20.5	-	19.11
15:00	US	Capital flows	Apr	$bn	-	-	-
		WEDNESDAY (16 June)					
11:00	**PL**	**Auction of 10Y bonds DS1020**					
11:00	EZ	HICP final	Apr	%YoY	1.6	-	1.6
14:30	US	Building permits	May	m	0.63	-	0.61
14:30	US	House starts	May	m	0.65	-	0.672
14:30	US	PPI	May	%MoM	-0.6	-	-0.1
15:15	US	Industrial orders	May	%MoM	0.8	-	0.8
15:15	US	Capacity use	May	%	74.5	-	73.7
		THURSDAY (17 June)					
9:30	CH	SNB decision		%	0.25	-	0.25
14:00	**PL**	**Wages in corporate sector**	**May**	**%YoY**	**4.0**	**4.4**	**3.2**
14:00	**PL**	**Employment in corporate sector**	**May**	**%YoY**	**0.5**	**0.5**	**0.0**
14:30	US	New jobless claims	w/e	k	450.0	-	456.0
14:30	US	CPI	May	%MoM	-0.2	-	-0.1
16:00	US	Leading indicators	May	%MoM	0.3	-	-0.1
16:00	US	Philadelphia Fed index	Jun	pts	20.4	-	21.4
		FRIDAY (18 June)					
14:00	**PL**	**Industrial production**	**May**	**%YoY**	**8.4**	**8.9**	**9.9**
14:00	**PL**	**Construction production**	**May**	**%YoY**	**-3.9**	**-4.6**	**-6.1**
14:00	**PL**	**PPI**	**May**	**%YoY**	**0.4**	**1.5**	**-0.5**

Source: BZ WBK, Reuters, Dow Jones

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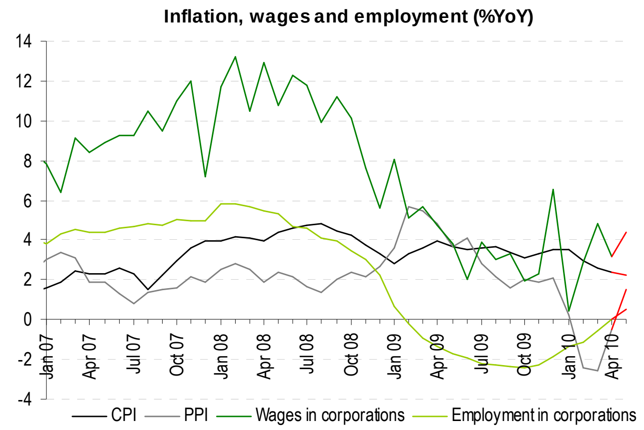
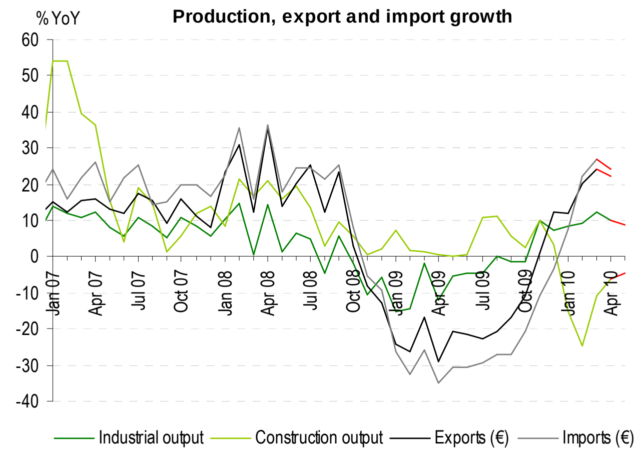
What's hot this week – Heavy economic calendar, not to mention World Cup

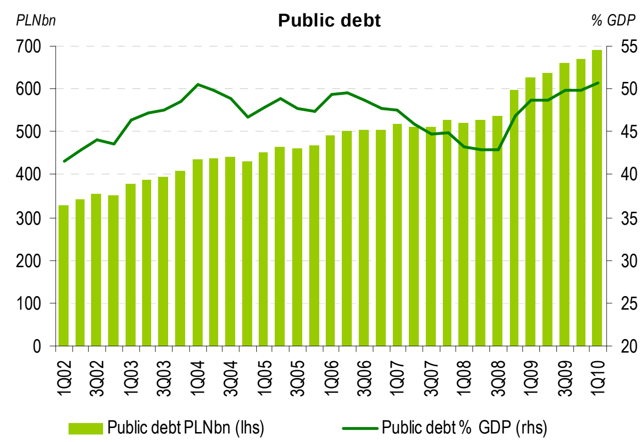


- The week ahead will be full of important economic data releases in both Polish and global economies. Additionally, emotions of market players will be elevated by the final stage of presidential campaign (in Poland, first round of election 20/06) and FIFA World Cup (mainly abroad, as Poland has not qualified to the finals).
- We expect that inflation in May fell slightly to 2.3%YoY (according to MinFin even to 2.1%). Market assumes stabilisation at 2.4%. The main risk is connected with food prices (possible negative effect of flood) and fuel prices (weaker zloty).
- Depreciation of the zloty in May and higher fuel prices were also the main factor influencing PPI inflation in May.
- We expect moderate acceleration in money supply and credits, which was mostly related to FX effect.



- Industrial production growth slightly decelerated in May, though in our opinion to a lower extent as compared to market consensus. This was suggested by PMI reading earlier this month. Still the key factor for production are export orders.
- The flood in May is well another one-off temporary factor this year, which may significantly affect production in construction sector. However, we assume the annual rate of growth improved moderately to -4.6% from -6.1% in April (the market is slightly more optimistic).
- The improvement in the labour market observed in recent months was in our opinion continued in May and as a result the employment rose in annual terms for the first time in 1.5 years. We also expect acceleration in wages after a temporary slowdown in April.

Economy last week – Spending rule is not enough



- Polish public debt rose in the first quarter of 2010 to PLN688.5bn i.e. by 18.5bn from end-2009. According to our estimate, the relation of public debt to GDP increased to 51%, the highest levels for many years. In the remainder of the year the trend will be probably continued, but the safety level of 55% should not be broken (unless zloty depreciates significantly).
- According to the Minfin, spending rule assuming limit of 1% growth above inflation will bring savings of PLN3bn next year and PLN8.5bn in 2011-12. In our opinion, it is hard to say there will be any savings, as limiting spending growth as compared to previous years is a necessity anyway (and was taken into account in Convergence Programme). We positively perceive formal commitment to limit spending, but please note that the rule concerns only one fourth of central budget expenditures.

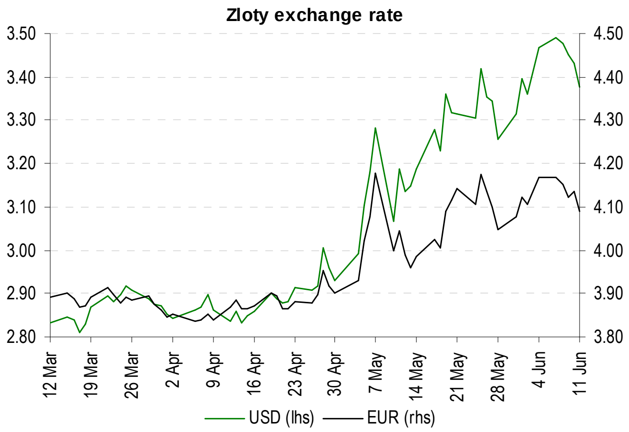
Quote of the week – No revolution in monetary policy

Marek Belka, NBP governor, 10-11 June

Monetary policy does not need a revolution. We have to give a strong signal to markets that the zloty is stable, the economy is stable, and there is will of cooperation between the independent NBP, and the government. First, there is no reason to change the strategy of direct inflation targeting. I think that this strategy has served us well. Secondly, I think that today there is no reason to make significant moves in interest rates. NBP must carefully monitor the situation on the interbank market - how the interbank transactions and the level of liquidity in the banking system is evolving. (...) There is no such interval (for the zloty.) I would like to deny that there was any interval. (...) As for the Polish economy, I do not see the big risks. Fortunately, from the viewpoint of the NBP, also on the inflation side. But of course this is an assessment of today, not for ever.

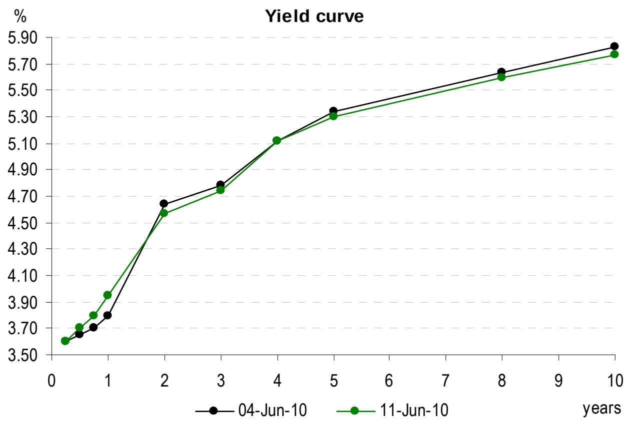
The Sejm accepted Marek Belka as new NBP governor. PO and left-wing SLD were in favour, while opposition PiS and minor coalition partner PSL were unanimously against. View of PiS and PSL was mostly based on procedural arguments (they preferred to wait until presidential elections), though deputy PM Pawlak mentioned a few aspects he did not like in Belka's candidature. We locate Belka's views on monetary policy as somewhere between hawks and doves within the Council, with a possible bias towards doves. His first comments indicated a continuation of current monetary policy. It was also suggested that the new Governor will be more restrained in terms of commenting rates and the zloty. Let's hope he will convince to such attitude also some other members of the Council.

Market monitor



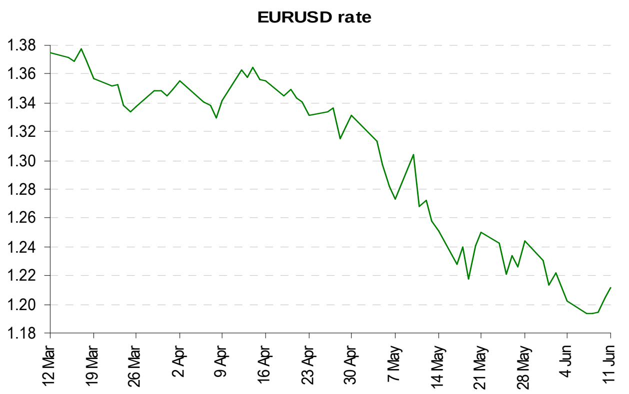
Weakening risk aversion strengthens the zloty

- Over the past week the zloty pared losses seen during the previous week related to negative news from Hungary. EURPLN lowered during the week from nearly 4.20 to slightly above 4.08. This was thanks to lower risk aversion after positive macro data from Asia, Germany and the US, outcome of the ECB meeting and weakening in concerns about situation in Hungary. Over the past week the zloty gained 1.8% to the euro, less than the forint (2.7%), but more than the Czech crown (1.0%). At the end of the week the gain was trimmed by disappointing retail sales figures from the US with EURPLN up to 4.10.
- We expect that this week sentiment in the global markets may improve somewhat, which could drive the zloty stronger. EURPLN should break the support level at 4.08 and the next support is 4.04. Important resistance is 4.12.



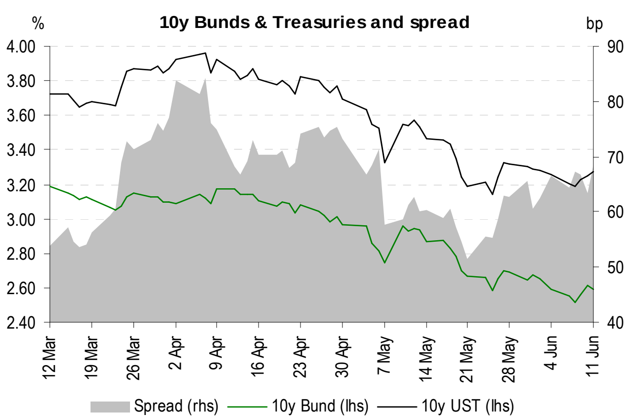
...and local bonds

- Rise in risk appetite on the global markets positively affected Polish debt market. Yield curve went down by a few basis points. IRS curved moved down on a similar scale. At the Wednesday's auction of road bonds BGK sold IPS1014 papers worth PLN2.54bn against offered PLN1-2.5bn while demand was PLN4.97bn and average yield 5.53%, i.e. 20bps above yield of 5Y treasury bond. At the top-up tender papers worth PLN489m were sold. Gain of local bonds was constrained by unsuccessful tenders of T-bills in the Czech Republic and Hungary as well as disappointing US retail sales figures released on Friday in the afternoon.
- This week we expect further slight strengthening of the local bonds along with improved moods in the global markets and neutral impact of domestic macro figures.



Euro recovered to above 1.20

- Last week the worries of market players regards fiscal problems in the peripheral countries of the euro zone and their possible effects on GDP growth prospects in the euro zone receded into the background. This led to recovery of European single currency against the dollar. While at the beginning of the week EURUSD was even below 1.19, it then rose to 1.215 on Friday. The week ended below 1.21, as higher risk appetite was limited by disappointing on US retail sales data.
- As we do not expect market moods in global markets to deteriorate this week, the EURUSD should remain above 1.20. The intra-day movements will depend on data releases in both the euro zone and the US.



The weakening of the core debt markets

- A fall in interest in safe assets during the past week associated with higher risk appetite has stopped strengthening trend in the core debt markets. Deterioration of sentiment towards Treasuries and Bunds was connected with a reduction of concerns about the situation in Hungary and successful bond auctions in Belgium, Spain and Portugal. Also, expectation for large supply of Treasuries adversely affected the core debt markets. At the end of the week yields of 10Y Treasuries and Bunds reached 3.27% and 2.59%, versus 3.26% and 2.59% respectively a week earlier.
- This week we expect a slight weakening in the core debt markets in the face of recently observed decrease in risk aversion.

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