

Weekly economic update

26 July – 1 August 2010

The past week has brought the increase in the risk appetite on the global markets, driven by better-than-expected macro data (mostly from the euro zone) and largely positive earnings reports for Q2. Improvement in sentiment on the markets was limited by negative tone of comments from Fed's Bernanke before Congress and uncertainty before publication of the stress-tests for the European banks, which was scheduled for Friday after close of the markets. Better sentiment towards the region and related to that gains of the zloty and Polish bonds was constrained by news about halted talks between Hungary and the IMF/EU. Clearly better than the forecast domestic economic activity indicators (industrial and construction output as well as retail sales) increased optimism regarding the pace of economic growth in Poland. The distribution of likelihood for our forecast on GDP growth in Q2, which assumes stabilisation at 3.0%YoY posted in Q1, becomes asymmetric to the upside. However, we are waiting with a potential revision of our forecast for the data on the foreign trade that are due to be published in August. We also stick to our view regarding further actions of the MPC. The central bankers' positive assessment of current data from the domestic economy accompanied by numerous strong data from the euro zone (last week we saw higher than expected euro zone's PMIs and much stronger than predicted Ifo index that showed the strongest monthly rise since the Germany's unification to the highest level since July 2007) may be neutralized by some negative data from the US and consequently uncertainty regarding the durability of global economic recovery.

This week, the only local macro figures will be the consumer sentiment indicators. That is why events abroad will be even more significant than usual. As to events in the global markets, at least in the early part of the week the focus will be on the stress-test results and then on earning reports and macro figures.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE
				MARKET	BZWBK	
MONDAY (26 July)						
11:00	PL	Auction of 52-week T-bills worth PLN1.3-1.5bn				
16:00	US	New home sales	Jun	m	0.31	0.3
TUESDAY (27 July)						
8:00	DE	GfK index	Aug	pts	3.5	- 3.5
10:00	EZ	Money supply	Jun	%YoY	-0.1	- -0.2
15:00	US	S&P/Case-Shiller home price index	May	%YoY	3.8	- 3.8
16:00	US	Consumer confidence	Jul	pts	51.0	- 52.9
WEDNESDAY (28 July)						
14:00	PL	Consumer confidence	Jul	pts		
14:30	US	Durable goods orders	Jun	%MoM	1.0	- -0.6
20:00	US	Beige book	Jul			
THURSDAY (29 July)						
10:00	DE	Unemployment rate	Jul	%	7.6	- 7.7
11:00	EZ	Economic sentiment	Jul	pts	99.0	- 98.7
14:30	US	Unemployment claims	week	k	460.0	- 464.0
FRIDAY (30 July)						
11:00	EZ	Flash HICP	Jul	%YoY	1.7	- 1.4
14:30	US	Advance GDP	Q2	%QoQ	2.5	- 2.7
15:45	US	Chicago PMI	Jul	pts	55.8	- 59.1
15:55	US	Final Michigan	Jul	pts	67.4	- 66.5

Source: BZ WBK, Reuters;

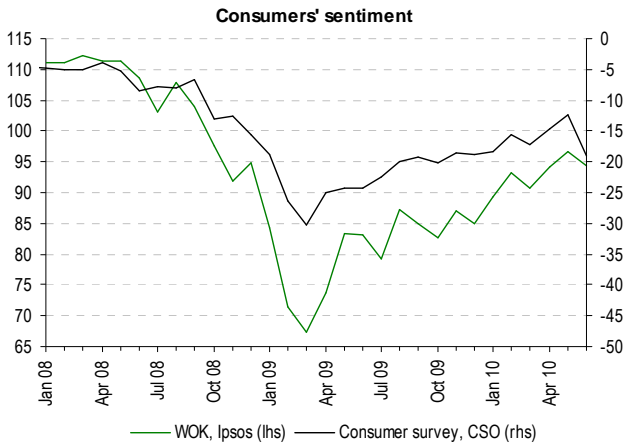
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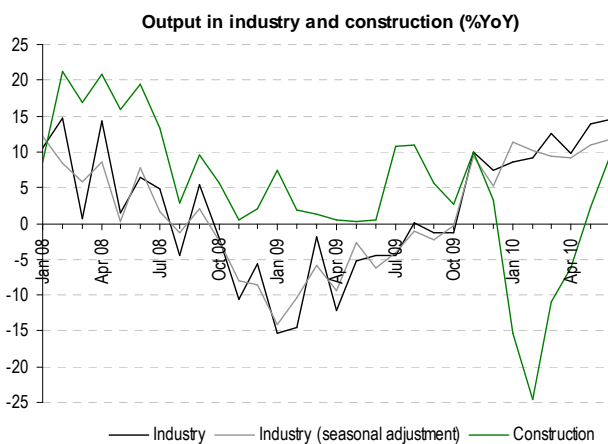
What's hot this week – Fewer macro figures and still many earnings reports



▪ This week will not bring many domestic events, partly due to lack of decision MPC meeting this month. However, as to local macro news, it is worth to pay attention to consumer confidence indicators (the stats office indicators on Wednesday while timing of the Ipsos's WOK release was not exactly indicated). Besides, it will be useful to take a look at the NBP report on the business climate due for release on Friday at 10:00.

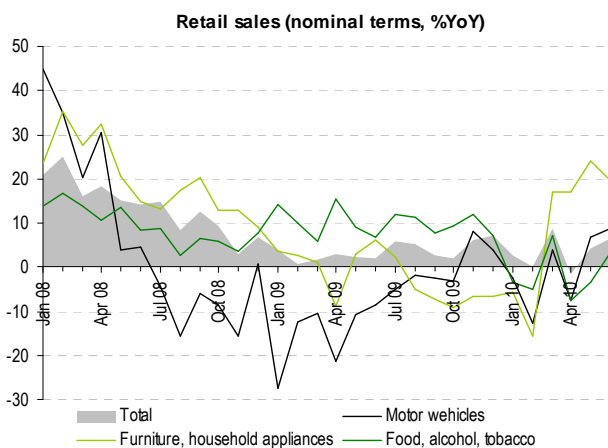
▪ As regards events abroad, at least in the early part of the week the Friday's publication of the results of the EU bank stress tests is likely to dominate the agenda. Later in the week more attention will be paid to next earnings reports (this week is the second out of three consecutive weeks with the largest number of earnings reports) and fresh macro figures (with particular focus on the US preliminary GDP figures for Q2 due for release on Friday).

Economy last week – Strong economic activity indicators



▪ The annual growth rate of industrial output accelerated to 14.5% in June from 13.5% in May, which was above our forecast and market consensus at ca. 12%. Seasonally adjusted data showed the industrial production growth reached accelerated to 11.7%YoY from 10.9% in May, reaching the highest level since January 2008. The annual rise in output was seen in 27 out of 34 sections of industry and that indicates that the growing activity is widespread, and not limited to a few sections of industry. The pace of output growth was again particularly high in the export-oriented sectors, which confirms stronger foreign demand signalled among others by the June's PMI reading.

▪ Construction output growth accelerated to 9.6%YoY from 2.3%YoY in May versus expected rise of ca. 4%YoY. Builders seem to quickly catch up after severe winter and benefit from increasing number of infrastructural projects.



▪ Nominal growth of retail sales accelerated to 6.4%YoY in June from 4.3% in May versus our forecast at 4.5% and market consensus at 4.0%. In real terms the retail sales growth accelerated to 4.5% from 2.0%YoY in May.

▪ Like a month earlier, improvement in retail sales was seen in most of categories. The exception was 'fuels' and 'furniture, electronics and household appliances', but in the former was mainly due to the price effect (significant lowering of annual growth in fuel prices in June), while in the second case we still have very strong growth. Thus, it seems that the improvement in consumer demand is not a one-off phenomenon. Improved situation on the labour market in recent months (confirmed by further drop in the registered unemployment rate in June to 11.6%) positively influences the households income and consumer confidence, increasing propensity to consume.

Quote of the week – The economy will not go crazy

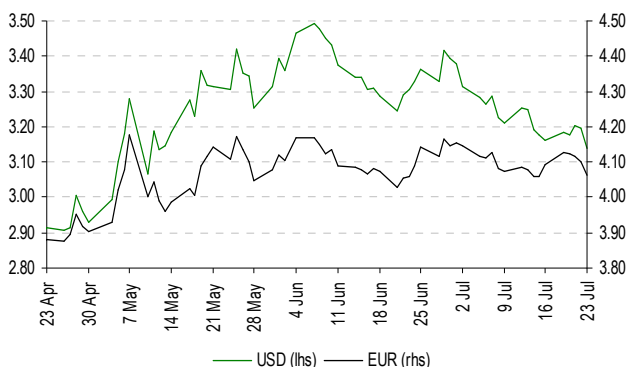
Marek Belka, NBP governor, TVN CNBC, PAP, 20 VII

Output figures for the last two months are very encouraging. (...) It seems that it is driven by external demand, which does not fuel inflation. (...) I personally pay attention to data on employment and wages. (...) Recent data indicate that we are dealing with a very slow pace of wage growth and higher employment growth. This is a good news. We must examine the persistence of this phenomenon, and if it turns out that it is persistent, it will mean that we have a stable recovery. In total, we are dealing with an early phase of recovery. (...) We do not expect, because the international situation is uncertain, so that the Polish economy could go crazy in the near future.

According to the NBP President, the Polish economy is in the early phase of recovery. He stressed that output figures for the last two months are very promising and it is connected mostly with foreign demand, which does not fuel inflation. Head of the NBP stressed that personally he focuses on the data on employment and wages. In his view, the latest labor market data, which showed that "we face very slow wage growth and stronger employment growth", are good. Belka said that if it appears that it is a persistent situation, it will prove that we experience a stable economic rebound. In our opinion, such statements suggest that the head of the central bank thinks about interest rates hikes, but without a haste. This supports our expectations that the first rate hike by 25bps will take place in the final quarter of this year.

Market monitor

Zloty exchange rate

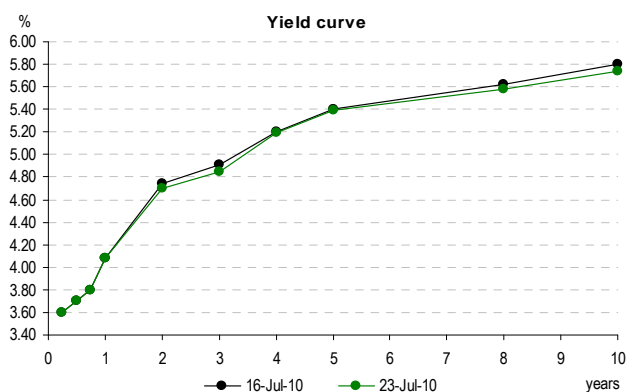


Higher risk appetite strengthens the zloty

EURPLN started the previous week at ca. 4.14 (well above to area of support at 4.11-4.12), what was the result of risk aversion in the CEE region caused after the breakdown of talks between the Hungarian government and the IMF/EU. The market sentiment improved later in the week on optimistic macro data from the euro zone and mostly positive quarterly financial reports from the US. Consequently the EURPLN reached 4.06, the level of lower band of the formation of the triangle, that was emerging on the chart for last 3 months.

In the early part of this week the FX markets will be driven by interpretation of stress-tests' results. The positive assessment would lead to zloty appreciation. Very important level of support is 4.06, and next levels are at 4.04 and 4.00. In negative scenario the zloty's depreciation could reach 4.14 or even 4.20.

Yield curve

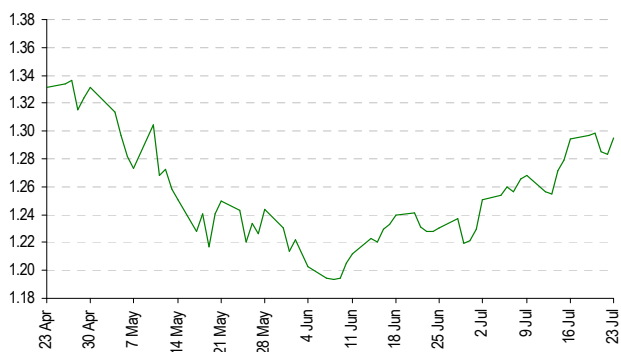


Drop in yields of domestic bonds

Yields of Polish bonds lowered slightly due to data on drop in core inflation in June to 1.5%YoY (that showed that the underlying inflationary pressure is limited) and on the back of the rise in risk appetite later in the week. Higher than expected data on the industrial output and the retail sales did not influence the market. Investors' activity was still low.

There should be rather limited reaction of the domestic fixed income market to the publication of the stress-tests results of European banks. Recent behavior of the market indicates that investors pay bigger attention to the prospects of interest rate's hikes, rather than to the global market sentiment. This week we expect that the yields of Polish bonds will remain stable or slightly rise.

EURUSD rate

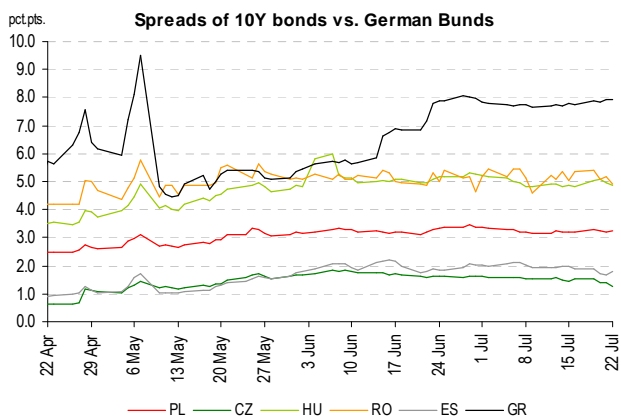


Good data from the euro zone supported single currency

EURUSD ranged between 1.27-1.30 last week. At the beginning of the week the euro stuck to the value from Friday, but the testimony of the Fed chairman in the Congress lowered EURUSD to ca. 1.27. Later on, a bunch of very good data from the euro zone and good results of companies lifted EURUSD to 1.29. In the weekly perspective, EURUSD did not change significantly.

The early part of this week should be dominated by reaction to stress-tests. A positive assessment would probably increase the risk appetite and lifted the euro. Poor or unclear results would strengthen the dollar. Important resistance for EURUSD is 1.32 and 1.34, the support is at the level of 1.27 and then in the range of 1.24-1.25.

Spreads of 10Y bonds vs. German Bunds



Mixed signals from foreign debt markets

At the beginning of the last week, deadlock between Hungary and IMF/UE was the main news. As a result, spreads in yields of 10Y Bunds and Hungarian bonds as well as bonds of other countries in the region widened. Later in the week, concerns about the situation in Hungary eased (attitude towards Romania also improved), and successful bond issues in the euro zone were perceived as positive signals as well - spreads narrowed.

The main factor influencing the yields this week will be the results of stress-tests. Additionally, after Friday's decision of Moody's and S&P to change outlook on Hungary rating from stable to negative, the further development of the situation in Hungary may affect the bond yields of the region.

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