Bank Zachodni WBK

Weekly economic update

6 – 12 September 2010

Last week brought many positive surprises in macro figures released locally and abroad. Domestic GDP data for Q2 confirmed that the economic growth in Poland gains momentum and we expect that the subsequent quarters will see a sustained economic growth of ca. 3.5-4.0% (our forecast for the 2010 as a whole was revised up to 3.5% from 3.2%). The surprisingly strong rise in the Polish PMI manufacturing for August confirmed our optimistic prediction of a clear rebound in the manufacturing sector. We remain cautious as regards economic prospects for the next year and we keep our GDP growth forecast of 3.5% for 2011, mostly due to the global risks. However, fresh macro data from China (rebound of PMI manufacturing) and from the US (surprising rise in ISM manufacturing, better-than-expected data on pending home sales and above all weaker than expected drop in the non-farm payrolls) weakened concerns about double-dip scenario in the global economy. Strong macro figures locally and abroad were coupled with hawkish comments from MPC members. Andrzej Bratkowski said that it is unlikely that the Council will not hike rate this year. Hawkish signals from the MPC, together with information about a vote on a rate hike already in August, confirm the scenario of the upcoming monetary policy tightening (with the first rate hike probably in October). On the back of rising risk appetite in the global markets, the zloty gained clearly in the past week. At the same time, yields of Polish bonds rose considerably. Short end of the curve was under pressure of strengthening expectations for rate hikes while long end of the curve followed rise in yields on the core debt markets related to lower probability of the double-dip scenario in the global economy.

This week is much less crucial in terms of new data than the previous week, and additionally there is market holiday in the US on Monday. We expect that in the markets there will be continuation of tendencies seen in the previous week, i.e. the zloty will appreciate and yields of bonds will go up.

Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
		MONDAY (6 September)					
	US	Market holiday					
		TUESDAY (7 September)					
12:00	DE	Industrial orders	Jul	%MoM	0.5	-	3.2
		WEDNESDAY (8 September)					
11:00	**PL**	**Auction of 5Y bonds worth PLN1.5-3.5bn**					
12:00	DE	Industrial output	Jul	%MoM	1.0	-	-0.6
	US	Fed' Beige book					
		THURSDAY (9 September)					
8:00	DE	CPI	Aug	%MoM	0.0	-	0.3
14:30	US	Initial jobless claims	week	k	470.0	-	472.0
16:00	US	Trade balance	Jul	$ bn	-47.0	-	-49.9
		FRIDAY (10 September)					
14:00	**PL**	**Current account balance**	**Jul**	**€m**	**-783**	**-630**	**-1 004**
14:00	**PL**	**Exports**	**Jul**	**€m**	**10 250**	**10 720**	**10 656**
14:00	**PL**	**Imports**	**Jul**	**€m**	**10 800**	**11 000**	**10 943**
16:00	US	Wholesale inventories	Jul	%MoM	0.4	-	0.1

Source: BZ WBK. Dow Jones. Parkiet. Reuters

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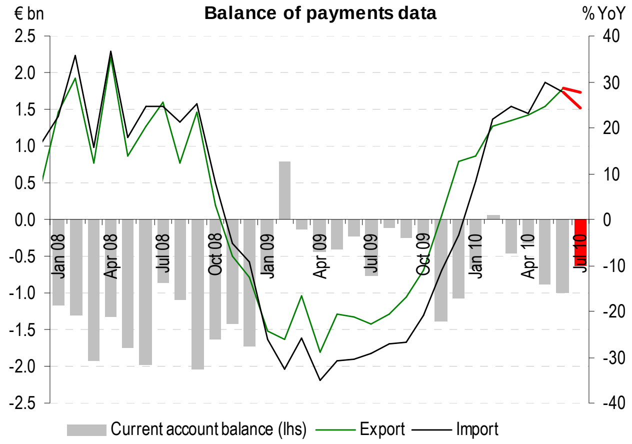
What's hot this week – Much lighter calendar of events

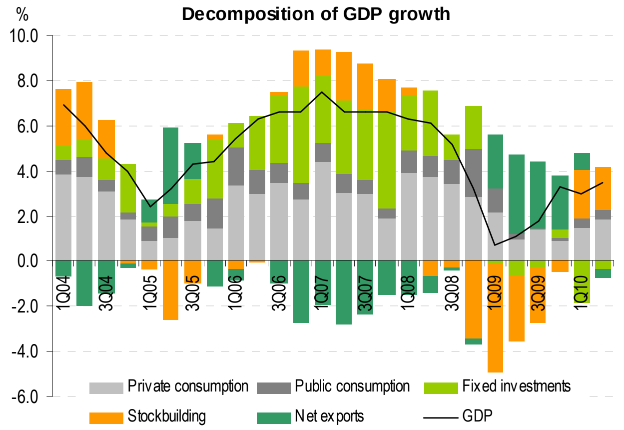


▪ This week is much less crucial in terms of new data locally and abroad. Besides, there will market holiday in the US on Monday.

▪ Domestic balance of payments for July due for release on Monday should show, according to our forecasts. lower C/A deficit than a month earlier thanks to improvement in the balances of income and transfers. At the same time. we predict only a minor deceleration in growth of exports and imports.

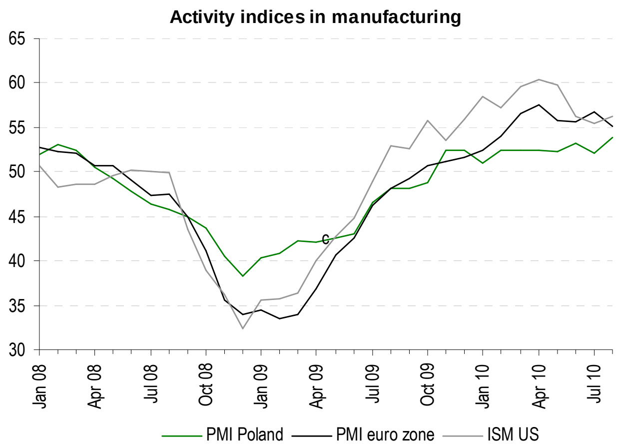
▪ Following tentative adoption of the 2011 budget draft, this week we may see more details regarding fiscal policy next year out of which the key will be information helpful to assessment of the size of general government deficit and reality of assumptions regarding the state's borrowing needs.

Economy last week – Significant positive surprises in new data



▪ GDP growth in Q2 reached 3.5%YoY vs. market consensus at 3.1-3.2%. Private consumption rose by 3%. vs. expected 2.1%. Fixed investments disappointed, but not much (a slight annual decline in Q2 rather than a slight increase) and it improved clearly as compared to Q1. Total domestic demand grew by nearly 4%YoY, the strongest since Q3 2008. The scale of the positive impact of changes in inventories and negative impact of net exports were approximately in line with our forecasts.

▪ We have been emphasizing for some time that there is a chance to achieve faster economic growth this year compared to our earlier forecast (3.2% above consensus), and after data for Q2 we revised our forecast up to 3.5%. At the same time, we remain cautious when it comes to the following year and maintain the 3.5% forecast, mainly due to risks concerning the global economy.



▪ The Polish PMI manufacturing rose to 53.8 in August, the highest level in 37 months, which indicates robust rise of activity in industry. The increase in the overall PMI was driven among others by higher number of new orders, reaching record level reached in November 2009. This was mainly due to domestic orders, while export orders were the weakest since September 2009 (possibly this was an effect of the stronger zloty). The production index reached its highest level since March 2007. The index of delays in production also increased. The employment index advanced to above the neutral level of 50 (only the third time in the past 28 months), but the pace of creating new jobs was weak.

▪ What is important, there were also positive surprises in Chinese and the euro zone's PMIs manufacturing, and the US data, including the key non-farm payrolls report.

Quote of the week – We should not be late with rate hikes

Andrzej Bratkowski. MPC member. PAP. 30 August

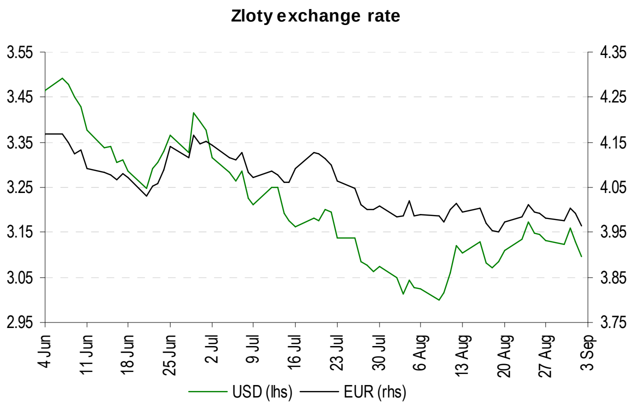
Our priority at the moment should be not to be late in order to give signals to the markets that the Council is determined to keep inflation close to the inflation target [of 2.5%]. Economic growth should be OK.

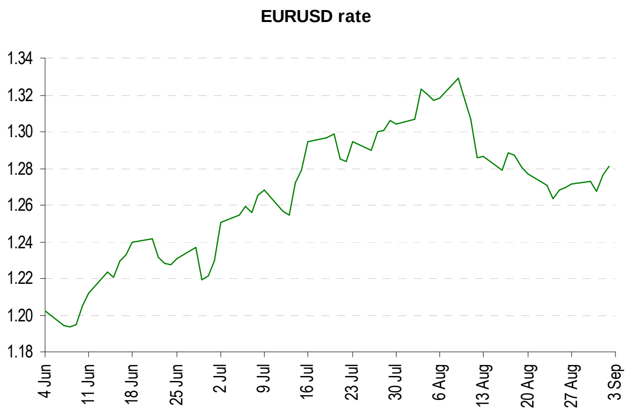
Anna Zielińska-Głębocka. MPC member. PAP. 30 August

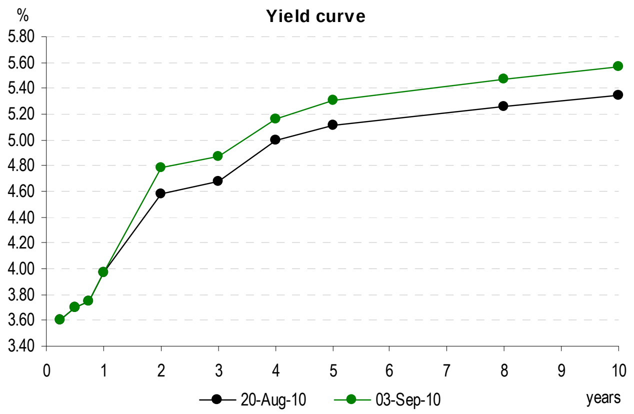
It seems to me that GDP growth this year will be at least 3.5%. but it may be 3.7-3.8%. (…) Fixed investment will most likely strengthen in the second half of the year. (…) It seems that [inflation] bottom is behind us. (…) Zloty should be stable. (…) There was vote [at the MPC meeting in August] regarding a motion to hike interest rates.

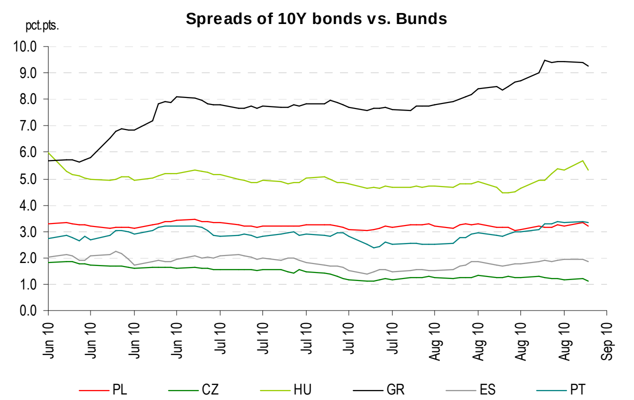
The two members of the MPC expressed clearly hawkish views in the past week, which together with the information that the Council voted on interest rate hike already at the meeting in August confirmed the scenario of the upcoming monetary policy tightening (with the first rate hike probably in October). Andrzej Bratkowski said explicitly that it is unlikely that the Council will leave interest rates unchanged this year. Together with the upcoming publication of the next local macro data, which according to our forecasts will show a clear rebound, hawkish signals from the MPC are a significant negative factor for the Polish interest rate market.

Market monitor









Strong rise in risk appetite strengthened the zloty

- The EURPLN started the past week with a substantial increase from 3.97 to 4.015 (slightly above the resistance level indicated in the previous report), which was the result of disappointment after Ben Bernanke's speech who said that the Fed will help the economy only if the situation "clearly" gets worse. In addition, he did not announce what specific actions could be taken. The zloty regained losses later in the week after better-than-expected data were received from the US. Data on Polish GDP was neutral for the market. We believe that this week the zloty may temporarily strengthen to ca. 3.90-3.92, but then a correction should be expected to around 3.96-3.98.
- Amid the deterioration of market sentiment at the start of the week. the dollar appreciated versus the euro. However, it could not reach the support at 1.26 and later during the week the scenario outlined by us, assuming continuation of increase in the EURUSD, was materialised. This was possible thanks to improving mood in the financial markets (clearly better than expected US consumer sentiment index, a surprising increase in the ISM index for the US industry, a smaller-than-expected revision of GDP growth in Q2). Information about smaller-than-expected decline in the US non-farm payrolls triggered a rapid growth in EURUSD rate. In our view, this week will not produce noticeable changes in EURUSD. A better prospect for the US economy has already been taken into account after publication of a non-farm payrolls data on Friday, while no releases of important data this week will lead to stabilisation of EURUSD. We anticipate the horizontal trend in the range of 1.26-1.30.

Better macro data drove yields higher

- On the domestic fixed income market the upward trend of the yields was continued. The correction of the latest considerable decline was the result of better than expected data on the GDP growth in Poland in the Q2. The following hawkish comments of the MPC members (Bratkowski, Zielińska-Głębocka) fuelled the expectations for the interest rates' hikes. Additional factor that was pushing domestic yields up at the long end of the curve was the sell-off significant correction in the core debt markets. Stronger expectations of monetary tightening by the MPC, Wednesday's auction of the 5Y bonds and further weakening of the concerns about the double-dip scenario in the global economy are factors which lead to continuation of upward more in yields of Polish bonds.
- The gradual improvement in sentiment on the global markets made the safe-haven assets unattractive to investors. The yields of the 10Y Bunds and Treasuries visibly recovered from the lows established at the beginning of the week. At the end of the week some stabilization was observed. as investors were awaiting for the crucial data from the US labour market. The clearly better-than-expected reading pushed the yields on the core debt markets even higher. We expect that as there are few data publications scheduled for this week the yields on the core markets may continue upward trend or stabilise.
- The spreads of the euro zone's peripheral countries versus Bunds declined slightly over the past week, mainly due to increase in yields of the German bonds. The visible drop of the CDS rates underlined weaker concerns about the fiscal condition of the euro zone's countries.

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