

# Weekly economic update

13 – 19 September 2010

The past week was pretty stable as regards market sentiment, as there were not so many macro data publications and hardly any key events. Just as we anticipated, the zloty depreciated temporarily versus the euro to 3.96, due to increase of the global risk aversion, but over the entire week the range of fluctuations was relatively narrow. This week we expect a similar scenario to come true – the increase of the global risk aversion, which may favour a decline in EURUSD and falling yields in core markets, should not trigger weakening of the zloty above the level attained last week (3.96). At the same time, we think that Polish bond market should focus this week on domestic factors, amid numerous publications of macroeconomic data for August. According to our forecasts, data will indicate significant improvement as compared to July – higher inflation, rebound in industrial and construction output, as well as wages, and continuation of strong job creation. The hawkish overtone of the data will be another argument in favour of a rate hike, which may lead to a weakening in the Polish interest rate market.

## Economic calendar

| Time CET                        | COUNTRY | INDICATOR                               | PERIOD | FORECAST |       |      | LAST VALUE |
|---------------------------------|---------|---|--------|----------|-------|------|------------|
|                                 |         |   |        | MARKET   | BZWBK |      |            |
| <b>MONDAY (13 September)</b>    |         |   |        |          |       |      |            |
| 11:00                           | EZ      | Industrial output                       | Jul    | %YoY     | 8.0   | -    | 8.2        |
| <b>TUESDAY (14 September)</b>   |         |   |        |          |       |      |            |
| 11:00                           | DE      | ZEW Index                               | Sep    | pts.     | 10.0  | -    | 14.0       |
| 14:00                           | PL      | CPI                                     | Aug    | %YoY     | 2.2   | 2.2  | 2.0        |
| 14:00                           | PL      | Money supply                            | Aug    | %YoY     | 8.6   | 8.6  | 7.8        |
| 14:30                           | US      | Retail sales                            | Aug    | %MoM     | 0.3   | -    | 0.4        |
| <b>WEDNESDAY (15 September)</b> |         |   |        |          |       |      |            |
| 11:00                           | PL      | Auction of 10Y bonds worth PLN1.5-3.5bn |        |          |       |      |            |
| 11:00                           | EZ      | HICP                                    | Aug    | %YoY     | 1.6   | -    | 1.7        |
| 14:30                           | US      | Import prices                           | Aug    | %MoM     | 0.2   | -    | 0.2        |
| 14:30                           | US      | NY Fed Index                            | Sep    | pts.     | 8.6   | -    | 7.1        |
| 15:15                           | US      | Capacity utilization rate               | Aug    | %        | 74.9  | -    | 74.8       |
| 15:15                           | US      | Industrial output                       | Aug    | %MoM     | 0.2   | -    | 1.0        |
| <b>THURSDAY (16 September)</b>  |         |   |        |          |       |      |            |
| 14:00                           | PL      | Wages                                   | Aug    | %YoY     | 4.0   | 4.5  | 2.1        |
| 14:00                           | PL      | Employment                              | Aug    | %YoY     | 1.7   | 1.8  | 1.4        |
| 14:30                           | US      | Initial jobless claims                  | week   | k        | 459.0 | -    | 451.0      |
| 14:30                           | US      | PPI                                     | Aug    | %MoM     | 0.3   | -    | 0.2        |
| 16:00                           | US      | Philly Fed Index                        | Sep    | pts.     | 1.0   | -    | -7.7       |
| <b>FRIDAY (17 September)</b>    |         |   |        |          |       |      |            |
| 10:00                           | EZ      | Current account                         | Jul    | €bn      | -     | -    | -4.6       |
| 14:00                           | PL      | PPI                                     | Aug    | %YoY     | 4.2   | 3.6  | 3.9        |
| 14:00                           | PL      | Industrial output                       | Aug    | %YoY     | 13.1  | 15.8 | 10.3       |
| 14:30                           | US      | CPI                                     | Aug    | %MoM     | 0.2   | -    | 0.3        |
| 15:55                           | US      | Flash Michigan Index                    | Sep    | pts.     | 70.0  | -    | 68.9       |

Source: BZ WBK. Dow Jones. Parkiet. Reuters

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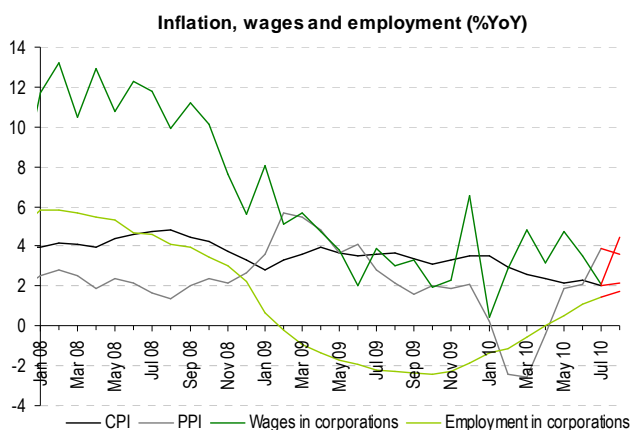
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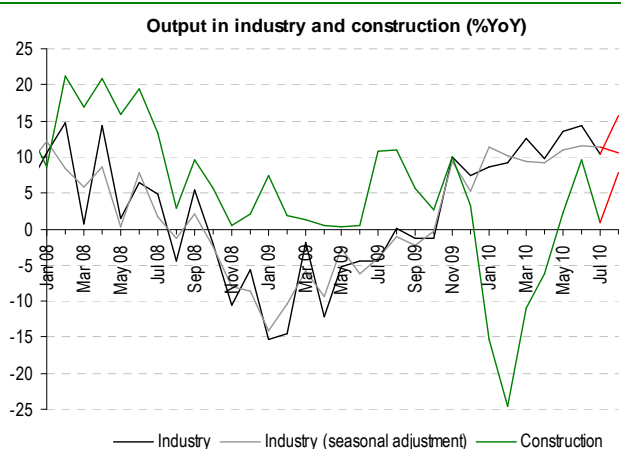
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## What's hot this week – Hawkish data in Poland

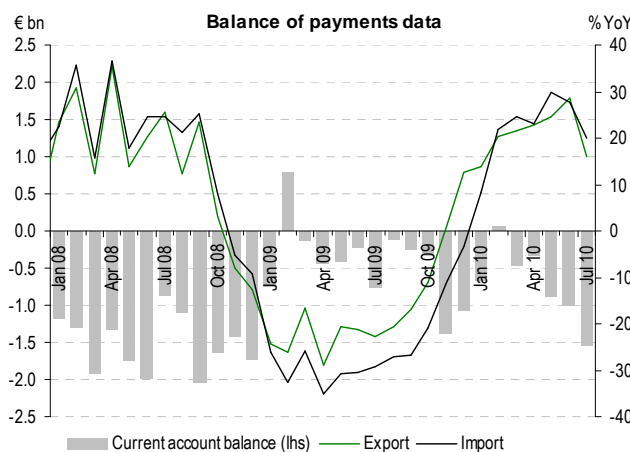


- After CPI inflation reached the bottom of 2% in July, data for August will be important hint as regards inflation path in the following months. In our opinion, which is consistent with the market consensus, inflation rose to 2.2%YoY, while the Ministry of Finance's estimate points to 2.1%. Food prices development is still the most significant risk factor amid the negative impact of bad weather conditions locally and the global trends in commodity agriculture prices (according to FAO, global food price index rose by over 5%MoM in August).
- We expect labour market data to show significant acceleration in wages after two months of relatively weak data. Also, strong employment trend should continue, which overall will suggest continuation of improvement in terms of households' disposable income. From the MPC point view, these figures may be more important than CPI.



- Another positive series of data from the Polish economy will be released at the end of the week. We forecast industrial production growth at 16%YoY. Even if number of working days is taken into account (one more than a year ago), this would represent strong expansion in manufacturing sector, based on export.
- We also expect recovery in construction output data and our forecast indicates acceleration to close 8% amid more favourable weather conditions as compared to previous month.
- After surprisingly high PPI inflation for July, we expect decrease in 12M indicator. The market consensus indicates further rise of PPI inflation, but we think that zloty strengthening observed in August lowered significantly export prices as expressed in zloty terms.

## Economy last week – Export much lower than predicted



- The current account deficit reached over €1.5bn, which was well above expectations. That was mainly due to high deficit in trade of goods, which was the consequence of the clear deceleration of the exports' growth to 16.0%YoY from 28.6%YoY in June and 22.0%YoY on average in the H1. Imports also recorded lower growth at 20.0%YoY versus 27.8%YoY in June. Additionally, the income deficit was also higher than our forecast and reached nearly €1.4bn (high dividend payments).
- There were no major surprises in current transfers balance and in services balance. It is worth to notice low FDI inflow and high inflow of portfolio capital.
- Balance of payments data was disappointing, but in our opinion one should not hurry with making any straight conclusions and we shall wait for the next data from the Polish economy.

## Quote of the week – Quite dovish NBP President

### Marek Belka, NBP President, PAP, 9 Sep

Due to the so-called statistical base the inflation rate will rise to the inflation target, or slightly above. I do not know exactly how the index will be evolving, as much depends on developments in the foreign exchange market. We keep monitoring the situation and if we see a threat to inflation, then we will act, but I think in this case there is no clear evidence that inflationary pressure is intensifying.

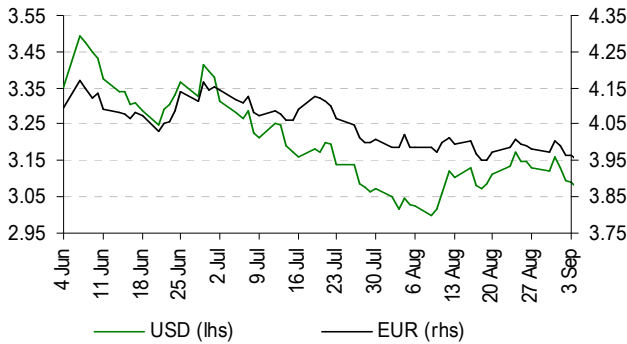
### Marek Belka, NBP President, Dziennik Gazeta Prawna, 8 Sep

An ideal policy mix is tough budgetary policy and loose monetary policy. But I would like to emphasize: there will be no automatic reaction such that when we believe that the fiscal policy is insufficiently tight, then we will change interest rates.

Recent statements of the NBP President do not suggest a particularly high propensity to tighten monetary policy anytime soon. According to Belka, inflationary impact of the VAT hike will be small and there is no clear evidence that inflationary pressure is building. Moreover, Belka assessed the draft budget for 2011 as satisfactory, though not groundbreaking. On the other hand, it is worth noting that on every occasion the NBP head point out that the MPC is monitoring the situation and if it finds that the outlook for inflation is worrying, it will take necessary action. In our opinion, the arguments for these actions will appear soon, after a series of good data showing an increase in economic activity. In October, the new NBP projection will also probably indicate a rise in inflation above target in the medium term.

**Market monitor**

**Zloty exchange rate**

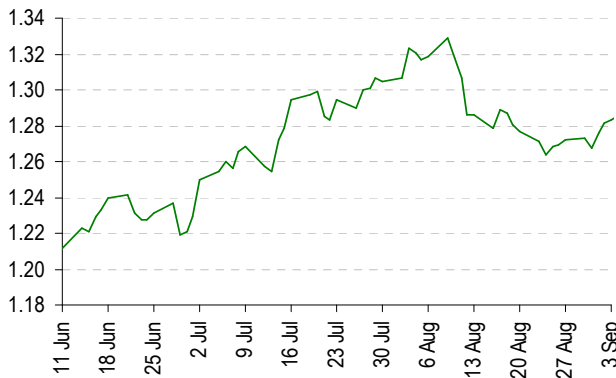


**The EURPLN and EURUSD stable**

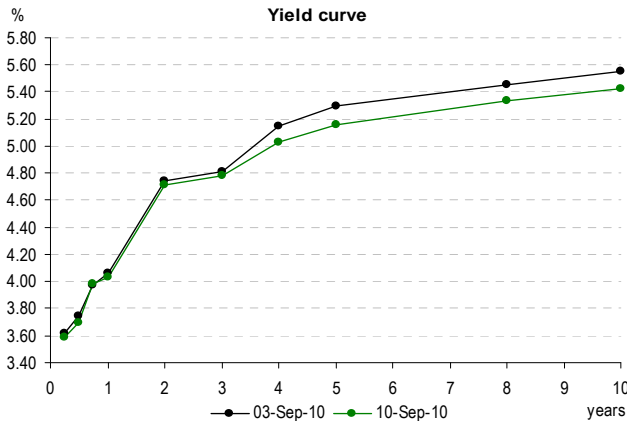
▪ The EURPLN started the week below the Friday's closing and early in the week our scenario of the zloty's appreciation to ca. 3.90-3.92 has materialised (the Monday's minimum at 3.917). The article published by *The Wall Street Journal* that suggested that during the stress-test simulations there were some cases of underestimating risk connected with the bonds of the peripheral countries of the euro zone held by the banks or even concealing the real value of these bonds that the banks owned. That triggered the rise of the risk aversion and consequently the EURPLN advanced to nearly 3.96 on Wednesday, just below our forecast. The improvement of the market sentiment that occurred later in the week (due to better than expected data from the US) supported the zloty. We expect, that this week the zloty will be under the negative pressure, but the potential for the depreciation will be limited by the resistance level at 3.96. The support is at 3.92.

▪ The US market holiday on Monday visibly limited the volatility of the EURUSD. As the worries over the stability of the European banking sector emerged, the euro depreciated versus the dollar, the EURUSD declined from 1.29 to 1.27. Later in the week the exchange rate ranged 1.265-1.275 and due to disappointing data on the US wholesale inventories rebounded from the upper band of the consolidation and headed south. All in all, during the whole week the EURUSD stayed in the horizontal trend ranging 1.26-1.30 suggested last week. We expect, that this week the market sentiment will deteriorate and consequently the EURUSD will decline below the level of support at 1.26. The next support is at 1.24.

**EURUSD rate**



**Yield curve**



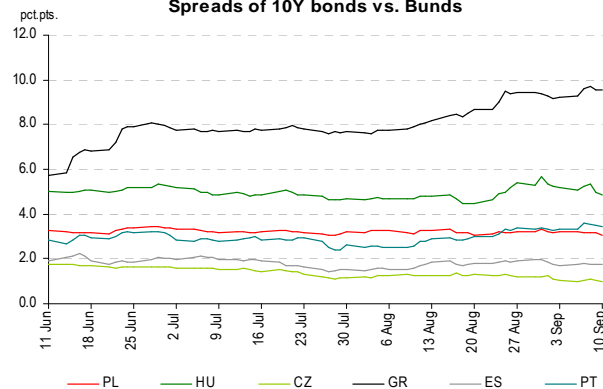
**Yield decline on the domestic debt market**

▪ Over the past week, yields on domestic debt market fell mainly in the middle and at the long end of the curve. As in the previous weeks, increase in risk aversion caused by fear of the stability the European banking system contributed to this along with decrease in yields in the core debt markets. We believe that this week the market may focus on publications of domestic data which may seem hawkish. New arguments for interest rate hikes may contribute to increase in domestic yields.

▪ After stabilization at the beginning of the week, yields on core fixed income markets have fallen (mainly 10-year Bunds), following an increase in risk aversion in the global markets. Gradual improvement in sentiment in the rest of the week contributed to the decline in demand for safe assets and as a result yields of Bunds and Treasuries began to rise. Over the entire week yields in the core debt markets fell slightly. We expect them to fall also during this week.

▪ Over the past week, Greek bond spreads versus 10-year Bunds recorded the highest increase. This was mainly the result of a surge in yields of Greek securities caused by the downward revision of GDP growth in Q2 (down to -3.7%YoY from previous estimate -3.5%YoY). The biggest drop was recorded for spreads of Hungary, which managed last week to sell bonds on the market. Yields at auction were higher than at the previous one, but the successful tender caused an increase in demand for the Hungarian securities, and thus yields decreased during the week.

**Spreads of 10Y bonds vs. Bunds**



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