

# Weekly economic update

1 – 7 August 2011

The previous week on the global market passed in sour sentiment. The risk aversion was raised by breakdown of negotiations over the US debt ceiling in the weekend and by a possible downgrade of this country's rating. In the following days the Moody's slashed the Greek rating and put the Spanish rating on watch list. Weak results of the European companies, the conclusions presented in Fed's Beige Book and disappointing flash estimates of GDP growth in the USA for Q2 deteriorated the market expectations concerning the pace of growth in the global economy. Another disappointment was delivered by results of auctions of Italian and Spanish T-bills and bonds, which drew the investors' attention to a possibility of debt crisis spilling into other European countries. That has taken its toll on the euro against the dollar and supported the prices of German bonds. The rise in risk aversion contributed to zloty weakening.

This week promises to be equally interesting. Market attention will be focused on the USA and the issue of raising the debt ceiling. Later in the week there will be release of monthly employment data in the US, which used to disappoint badly last month, and therefore may attract much attention. The market will be awaiting the press conference of the ECB President and the possible hints regarding the timing of the next interest rate hike. Domestic data on the PMI index should not affect the currency nor debt market, as global events will be the most important. Technical situation in EURPLN is favourable for the domestic currency, and if there is no next wave of risk aversion, we may see its strengthening. Bonds should remain stable. A potential for weakening at the longer end of the curve will be limited by the fact that at the bond switching auction a non-benchmark DS1021 security will be offered.

## Economic calendar

Time CET	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
<b>MONDAY (1 August)</b>							
4:30	CN	PMI – manufacturing	Jul	pts	-	-	50.1
<b>9:00</b>	<b>PL</b>	<b>PMI – manufacturing</b>	<b>Jul</b>	<b>pts</b>	<b>50.5</b>	<b>50.5</b>	<b>51.2</b>
9:53	DE	PMI – manufacturing	Jul	pts	52.1	-	54.6
9:58	EZ	PMI – manufacturing	Jul	pts	50.4	-	52.0
16:00	US	ISM – manufacturing	Jul	pts	55.5	-	55.3
<b>TUESDAY (2 August)</b>							
11:00	EZ	PPI	Jun	%YoY	5.6	-	5.7
14:30	US	Consumer spending	Jun	%MoM	0.2	-	0.0
14:30	US	Personal income	Jun	%MoM	0.2	-	0.3
14:30	US	Core PCE	Jun	%MoM	0.2	-	0.3
<b>WEDNESDAY (3 August)</b>							
9:58	EZ	PMI – services	Jul	pts	51.4	-	53.7
<b>11:00</b>	<b>PL</b>	<b>Bond switching auction</b>					
11:00	EZ	Retail sales	Jun	%YoY	-1.0	-	-1.9
14:15	US	ADP Report	Jul	k	110	-	157
16:00	US	Industrial orders	Jun	%MoM	0.6	-	0.8
16:00	US	ISM – services	Jul	pts	53.7	-	53.3
<b>THURSDAY (4 August)</b>							
12:00	DE	Industrial orders	Jun	%MoM	-1.0	-	1.8
13:00	GB	BoE decision		%	0.50	-	0.50
13:45	EZ	EBC decision		%	1.50	-	1.50
14:30	US	Initial jobless claims	week	k	405	-	398
<b>FRIDAY (5 August)</b>							
12:00	DE	Industrial output	Jun	%MoM	0.1	-	1.2
14:30	US	Non-farm payrolls	Jul	k	85	-	18
14:30	US	Unemployment rate	Jul	%	9.2	-	9.2

Source: BZ WBK, Parkiet, Reuters

**Maciej Reluga** Chief economist (+48 22) 586 8363

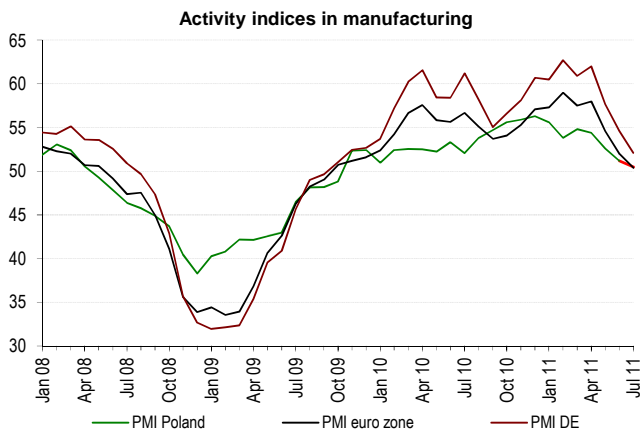
e-mail: ekonomia@bzwbk.pl

**Piotr Bielski** (+48 22) 586 8333

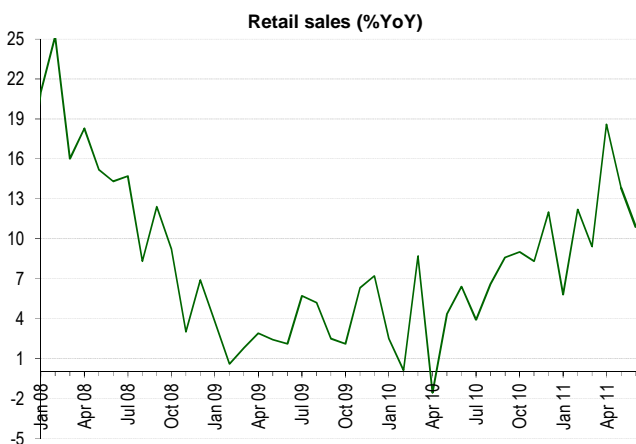
**Marcin Sulewski** (+48 22) 586 8342

**Piotr Bujak** (+48 22) 586 8341

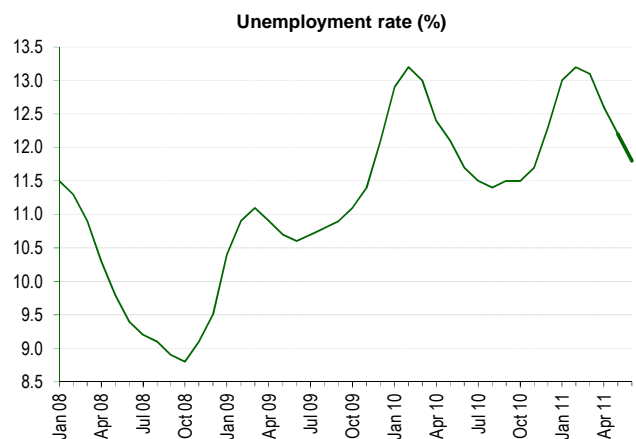
**Marcin Luzziński** (+48 22) 586 8362

**What's hot this week** – PMI indices, US debt ceiling and data, ECB press conference

- In the first part of the week the market will probably focus on the issue of raising the US debt ceiling. The second half of the week will see the ECB Governor's press conference and Friday's US labour market data. In the previous month the reading disappointed, so the investors want to confirm if that was an outlier or a harbinger of slowdown.
- The flash readings of manufacturing PMI indices for July in the euro zone and in Germany dropped again, although the scale of declines was smaller than in two previous months. We expect that the domestic PMI fell as well, although the downward tendency also slowed down. The July figures will help to assess the situation in Polish industry in the last month. Particularly, interesting will be changes in new orders (export), employment and cost pressure. However, these data will be overshadowed by the news from abroad.

**Last week in the economy** – Robust consumer demand

- The annual growth of retail sales decelerated in June in nominal terms to 10.9% from 13.8% in May. That reading was slightly weaker than expected – market consensus was at 11.8%, our forecast pointed to 12.0%. The slowdown in the annual growth can be attributed to the high base from the previous year. Analysing changes of particular categories of retail sales, we do not see any signs of a clear weakening in the upward trend of consumption demand (the increase of sales in Q2 was the highest since 2008Q2!). The data support our estimates that growth of individual consumption in Q2 2011 stayed at a pretty high level of around 4%.
- In 2011H2 we expect a stabilization of retail sales nominal growth close to 10%, which would have confirmed a vital role of consumption demand as a key driver of economic growth this year.



- The registered unemployment rate fell at end of June to 11.8% from 12.2% in May. This result is consistent with our forecast, market consensus, and the estimate and the Labour Ministry. We expect that in 2011H2 the unemployment decline will continue, which will result not only from the seasonal effect, but also from improving trend due to continued growth in labour demand.
- Detailed labour market data for June, included in the monthly Statistical Bulletin, confirmed that a marked acceleration of wage growth in corporate sector resulted mainly from the effect of wage hikes (with compensation for previous months) in the mining industry. We expect the wage pressure to strengthen in H2.
- The consumer confidence improved in July, mainly due to better expectations about the economic situation of the country and outlook for employment.

**Quote of the week** – 0% deficit in 2015?**Jacek Rostowski, Finance Minister, PAP, 26 July**

We want to narrow the finance sector deficit to 0% GDP in 2015 and to maintain it at that level until the public debt drops to 40%, which we estimate to happen in 2018.

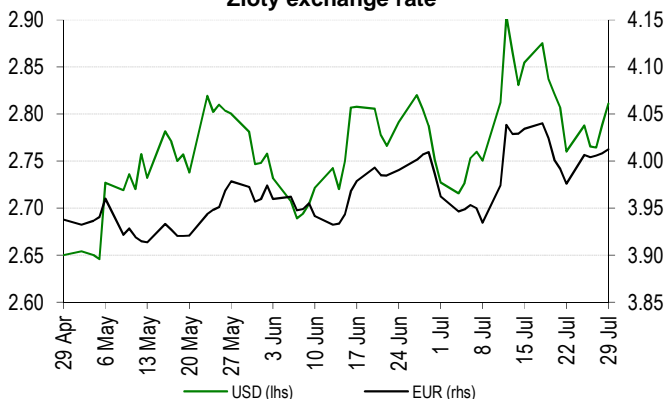
**Ludwik Kotecki, Finance Minister Deputy, PAP, 28 July**

We assume that the public debt this year according to domestic methodology will drop by 1 pp. as compared to 2010. According to ESA 95, the debt will begin to drop in the upcoming year. The public finance sector's deficit will decline by ca. 5% in 2011 and 2012. (...) The bulk of that reduction will result from spending cuts. We assume, that in 2012 the public sector's deficit will amount to 3% of GDP.

The plans of Minister Rostowski concerning the public finance seem to be very ambitious. Balancing the budget in Poland is postulated by economists for the last two decades (without significant effects). However, it has to be taken into account that in order to narrow the deficit to zero in such a short time, considerable spending cuts have to be implemented, including those aiming at reducing fixed spending (e.g. raising the retirement age). Hence, although it is theoretically possible, basing on the past experience, one may doubt if the new government will be determined and politically powerful enough to implement such measures.

Market monitor

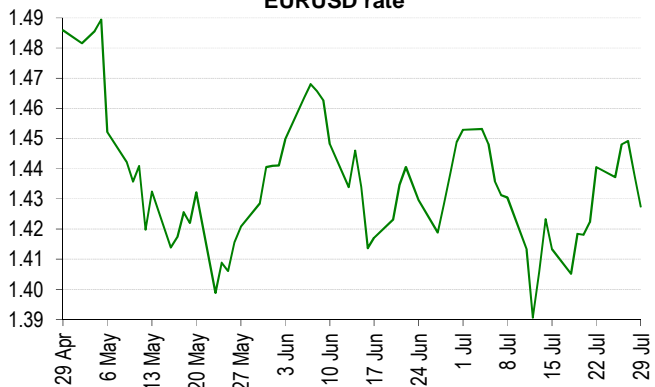
Zloty exchange rate



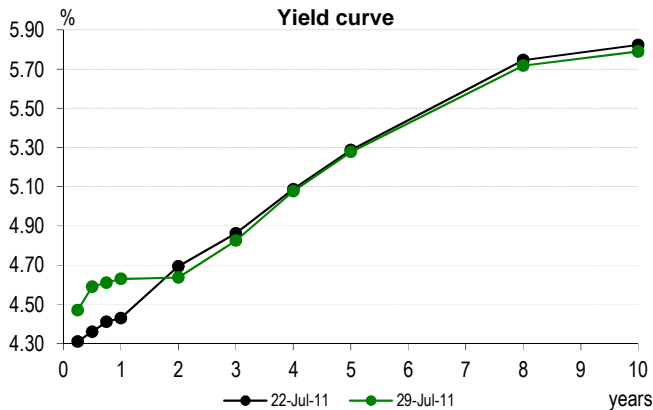
Technical analysis suggests zloty strengthening

- The zloty weakened last week versus the main currencies, amid persisting uncertainties. At some point, the depreciation against the euro slowed down, as the BGK allegedly was selling euros. Only at the beginning of the week and only for a moment the EURPLN was below the support at 3.98 indicated by us. In subsequent days, the resistance 4.0 was breached and the rate peaked at 4.028. This week, still the most important factors for the zloty will be events in the global market. The technical situation is favourable for the zloty, and this week the rate should not approach 4.03, unless a surge in risk aversion appears. This support is 3.98.
- The Hungarian forint was weakening along with the zloty, while the Czech crown was gaining. The latter was supported by increase in FinMin's GDP forecasts for 2011 and 2012, and did not suffer from the central bankers' comments about delaying perspective of interest rate hikes amid uncertainty in the euro area and predicted slowdown in the European economy.
- At the beginning of the week the dollar was under pressure versus euro as a result of impasse in talks on raising debt ceiling in the US. In subsequent days, alarming information from the euro zone peripheries started appearing (Greece's downgrade, weak bond auction of Italy, placing Spain's rating on the watch list), which pushed the EURUSD down. The issue of debt limit remains in the centre of attention, but in the following days the market may be affected by the ECB press conference and monthly data from the US labour market. This support is 1.42, the resistance 1.45.

EURUSD rate



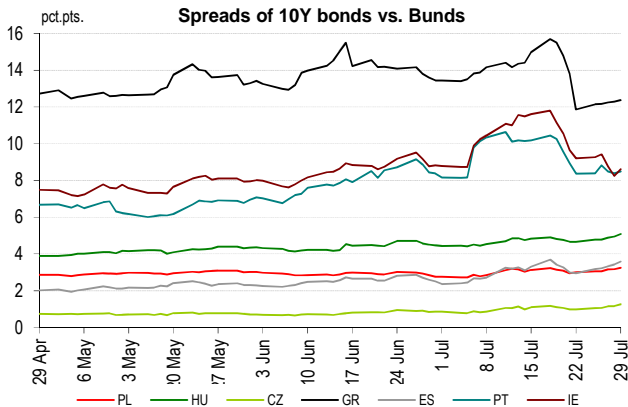
Yield curve



Yields stable amid low volatility

- On the domestic debt market the yields declined slightly, but the volatility was limited throughout the week. A slight strengthening of Polish bonds was supported mainly by falling Bunds' yields. The release of domestic PMI index should not move the market too much. We expect the low volatility to maintain in the upcoming days and the domestic market to move in line with moods in the global market. A potential for correction at the longer end of the curve will be limited by the fact that at the bond switching auction a non-benchmark DS1021 security will be offered.
- On the core debt markets the German bonds gained throughout the week due to increasing demand for safe assets. The Treasuries moved in a horizontal trend due to uncertainty about raising debt ceiling in the USA. As a result, the spread between yields of 10Y Bunds and Treasuries surged to the highest level since March 2011. At the end of the week the yields of 10Y Bunds and Treasuries amounted to 2.56% and 2.87%, respectively.
- On the core debt markets Italy, Greece and Spain came to the fore. The investors were not appeased with results of Italian bonds' auction (lowest price in 11 years), which caused a further increase of yields of Italian securities on the secondary market. Also the results of Spanish T-bills tender proved to be disappointing. Moreover, the Moody's downgraded Greece. These factors caused a weakening of euro zone peripheries debt market.

Spreads of 10Y bonds vs. Bunds



---

This publication has been prepared by Bank Zachodni WBK S.A. for information purposes only. It is not an offer or solicitation for the purchase or sale of any financial instrument. Information presented in the publication is not an investment advice. All reasonable care has been taken to ensure that the information contained herein is not untrue or misleading. But no representation is made as to its accuracy or completeness. No reliance should be placed on it and no liability is accepted for any loss arising from reliance on it. Forecasts or data related to the past do not guarantee future prices of financial instruments or financial results. Bank Zachodni WBK S.A., its affiliates and any of its or their officers may be interested in any transactions, securities or commodities referred to herein. Bank Zachodni WBK S.A. or its affiliates may perform services for or solicit business from any company referred to herein. This publication is not intended for the use of private investors. Clients should contact analysts at and execute transactions through a Bank Zachodni WBK S.A. entity in their home jurisdiction unless governing law permits otherwise. Copyright and database rights protection exists in this publication. 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>