Poland's Economy. Financial Markets

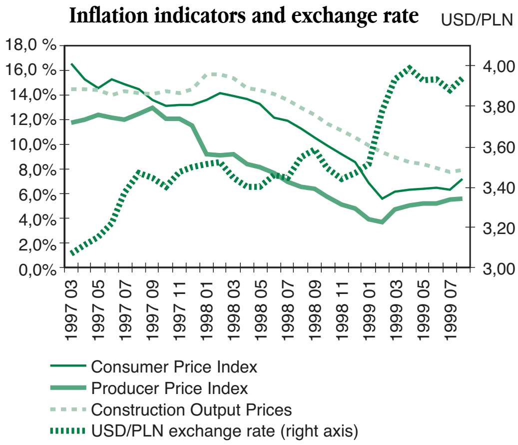
28 September 1999

No 4

Main Tendencies in the Economy:

- Prices of consumer goods and services in August 1999 increased by 0.6% month on month and 7.2% year on year. In the January-August period 1999, consumer prices increased by 5.1% vs. a 6.0% increase in the same period last year (p. 4).
- In July 1999, the current account deficit totalled USD 1,020bn after USD 1,134bn in June 1999. The trade deficit in July remained at the same level as that in June of USD 1.3bn. In the January-July period the current account deficit totalled USD 6,021bn, which means a 110% increase y/y (p. 4).
- In Q2 1999, GDP increased by 3.0% y/y vs. 1.5% GDP growth in Q1 1999. In the first half of this year GDP increased by 2.3%. If the present trends continue, gross domestic product in 1999 may grow by approx. 3.7% (p. 5).
- Industrial output in August 1999 increased by 4.9% month on month and was up 7.4% on August 1998 (p.5).
- The unemployment rate in August 1999 increased up to 11.9% after 11.8% unemployment in July. The number of the unemployed in August was 2m 144k. Average employment in enterprises in August was 5747.3k persons, reaming at the same level as in the previous month (p. 5).
- In the next two weeks the zloty may weaken below the parity rate due to high inflation which as we expect may be over 7.5% in September. The August current account deficit and September industrial output data should be positive for the zloty. We expect the zloty rate to be quite unstable in the near term and very sensitive to macroeconomic data (p. 6).
- At its meeting of 22 September the Monetary Policy Committee tightened monetary policy by increasing the intervention rate by 1 percent. Further interest rate increases cannot be ruled out. (p 8).
- Increased treasury bill and bond yields in the primary and secondary markets. Short-dated money is very expensive (p.7)
- The budget deficit is reducing but the public finances deficit may rise up to 4.0% GDP (p.9).

Arkadiusz Krześniak



In this Issue

Poland's Current Economic Situation

September witnessed a change in sentiment in the fx and money markets. Subsequent signals indicating no improvement in the current account, rising inflation and the public finances deficit had a negative impact on the market. While the zloty is likely to be quite volatile fluctuating in a relatively wide band around the parity rate in the near term, we expect the zloty to strengthen in Q1 2000.

External demand for Polish exports is still at a low level. Poland's economy seems to be facing quite serious challenges due to the increasing external imbalance, stabilisation of direct foreign investment and inflationary tendencies, which, as we believe, will emerge in Q4 1999. Relatively positive economic growth results in H1 after a very bad Q1 1999 indicate that domestic demand has not reduced and continues to be at a relatively stable level.

High retails goods sales growth continues although August saw some weakening in sales growth. Credit growth is very large - in the last year lending has increased by nearly fifty percent. It should be expected that as a result of the increased unemployment rate and reduced potential credit growth, caused by a tightened monetary policy, domestic demand may slightly decrease.

In H1 1999, the situation of enterprises was characterised by considerably deteriorated financial performance and slightly lower liquidity. It was driven by an overall reduction in domestic industrial output. Under the current foreign trade structure, Poland is more sensitive to economic cycles in EU countries and we expect this interdependence to increase in the near term. Recent business climate data for Germany are rather positive and can boost hopes that Polish exports into that market will be rebuilt, which will be helped by the appreciation of the euro relative to the zloty. However, no significant improvement in the emerging markets can be expected in the near future.

August's good industrial output results indirectly indicate that exports have improved. We expect industrial output growth to improve and sold industrial output prices to stabilise in Q4 1999.

Inflationary tendencies that will occur in Q4 may continue until early 2000. They should peter out after that period.

Tab. 1. Inflation Indicators

	04 1999	05 1999	06 1999	07 1999	08 1999	***09 1999P***
Consumer Price Index (m/m %)	0.8	0.7	0.2	-0.3	0.6	***1.0***
Consumer Price Index (y/y%)	6.3	6.4	6.5	6.3	7.2	***7.5***
Sold Industrial Output Index (m/m%)	0.6	0.5	0.1	0.5*	0.7	***0.7***
Sold Industrial Output Index (y/y%)	5.0	5.2	5.2	5.5*	5.6	***5.7***
Monthly Average FX Rate (y/y%)	17.0	15.2	13.0	12.2	10.2	-
Import Price Index in PLN (y/y%)	9.1	8.2*	4.7	-	-	-

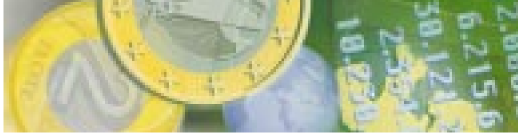
Tab. 2. Activity Indicators i

	03 1999	04 1999	05 1999	06 1999	07 1999	***08 1999***
Retail Sales Index (m/m %)	25.5	-0.9	3.1	2.1	4.2	***0.6***
Retail Sales Index (y/y%)	25.6	16.3	19.3	25.3	26.4	***25.9***
Personal Loans (y/y %)	35.2	37.4	39.4	41.1	42.8	***44.8***
Industrial Output (m/m%)	21.8	-7.0	1.2	0.1	-2.0*	***4.5***
Industrial Output (y/y %)	3.5	0.3	2.2	1.0	1.4*	***7.4***
Exports current prices (y/y %)	-7.8	-13.5	-18.8*	-21.1	-	-
Imports current prices (y/y %)	-7.9	-8.6	-9.9*	-7.2	-	-
Foreign Trade Balance (USD mio)	-904	-1036	-1031*	-1259	-	-

Tab. 3. Poland's Economy

	1996	1997	1998	***1999P***
Gross Domestic Product (y/y%) (fixed prices) of which:	6.0	6.8	4.8	***3.7***
Individual Consumption (y/y %)	8.3	6.9	4.9	***4.8***
Gross Fixed Assets Expenditures (y/y%)	19.7	21.7	14.5	***6.9***
Exports (y/y %)	12.0	12.2	1.3**	-
Imports (y/y %)	28.0	21.4	7.8**	-
Inflation (yearly average %)	19.9	14.9	11.8	***6.9***
Inflation (year on year %)	18.5	13.2	8.6	***7.5***
Unemployment Rate (year end %)	13.2	10.3	10.4	***11.8***
Current Account Balance/GDP (%)	-1.0	-3.2	-4.2	***-6.5***
Public Debt / GDP (%)	51.1	47.9	43.1	***46.0***

* - data adjustment ** - estimated data (SNA) F - forecast
y/y - year on year m/m - month on month
Source: CSO, WBK Treasury and International



Tab. 4. Foreign Exchange Rate Forecasts

	EUR/USD	USD/PLN	EUR/PLN	GBP/PLN	GBP/USD	DEM/PLN	FRF/PLN	NLG/PLN
Period								
Currently	1.0447	4.0900	4.2726	6.7597	1.6464	2.1847	0.6514	1.9388
0 - 1 month	1.04 - 1.08	4.04 - 4.13	4.26 - 4.40	6.70 - 6.83	1.63 - 1.66	2.22 - 2.27	0.66 - 0.68	1.93 - 2.01
1 -3 month.	1.05 - 1.10	3.96 - 4.09	4.28 - 4.42	6.60 - 6.73	1.63 - 1.66	2.19 - 2.23	0.65 - 0.67	1.94 - 1.99
3 - 6 month	1.08 - 1.13	3.94 - 4.04	4.30 - 4.46	6.54 - 6.67	1.62 - 1.67	2.22 - 2.26	0.66 - 0.67	1.97 - 2.01
6 - 12 month.	1.09 - 1.14	3.96 - 4.06	4.40 - 4.53	6.61 - 6.74	1.63 - 1.68	2.25 - 2.32	0.67 - 0.69	1.99 - 2.06

* - the most likely rate volatility band in a specific period
Forecast date: 27.09.1999
Note: Informational forecast based on information currently available. The Treasury and International Division cannot guarantee that exchange rates will follow the patterns as shown above.

Tab. 5. Interest Rate Forecasts

	Official Rates		Yields			Market Rates	
	Intervention	Lombard	52W T-Bills	3Y Treasury Bonds	5Y Treasury Bonds	1M WIMEAN	3M WIBOR
Period							
Currently	14.00	17.00	13.80	13.00	11.80	14.40	14.75
0 - 1 month	14.0 - 15.0	17.0 - 18.0	13.8 - 14.5	13.0 - 13.8	11.8 - 12.5	14.4 - 15.4	14.8 - 16.3
1 -3 month	14.0 - 15.0	17.0 - 18.0	13.8 - 14.3	13.6 - 13.8	11.7 - 12.0	15.4 - 16.0	16.0 - 16.2
3 - 6 month	14.0 - 15.0	17.0	12.2 - 13.5	12.1 - 13.3	10.7 - 11.5	14.2 - 15.7	14.3 - 15.8
6 - 12 month.	12.0 - 14.0	15.5 - 17.0	10.7 - 12.2	10.6 - 12.1	10.1 - 11.0	12.2 - 14.3	12.3 - 14.3

Forecast date : 28.09.1999
Note: Informational forecast based on information currently available. The Treasury and International Division cannot guarantee that interest rates will follow the patterns as shown above.

Inflation - consumer prices

Prices of consumer goods and services in August 1999 increased by 0.6% month on month and 7.2% year on year. In the January-August period 1999, consumer prices increased by 5.1% vs. a 6.0% increase in the same period last year. In August there was no deflation that occurred a year ago. The reason for a strong price increase in August was a rise in the excise duty on fuels by 10% and a much lower than in July fall in food prices that declined by a mere 0.1%. The increase in non-food goods was 1.4% and was the highest increase since the start of the year. Prices of services in August increased by 0.4%, which was driven by an increase in rentals, local transport prices and medical services. According to our estimates, in September the year-on-year inflation rise will be at least 7.5%, which translates into 0.8-0.9% m/m. This will be caused by an increase in food prices determined by stronger supply and recent protectionist tendencies as well as the lagged effect of higher fuel prices.

Inflation - producer prices

Sold industrial output prices in August increased by 0.7% month on month and 5.6% year on year. In the January-August period 1999 sold industrial output prices increased by 4.5% vs. 3.6% in the same period last year. In the processing industry prices increased in all the sectors of the industry.

Construction and installation output prices in August rose by 0.7% m/m vs. 0.3% last year. The construction and installation output prices rose by 5.7% compared to 8.1% last year.

Balance of Payments

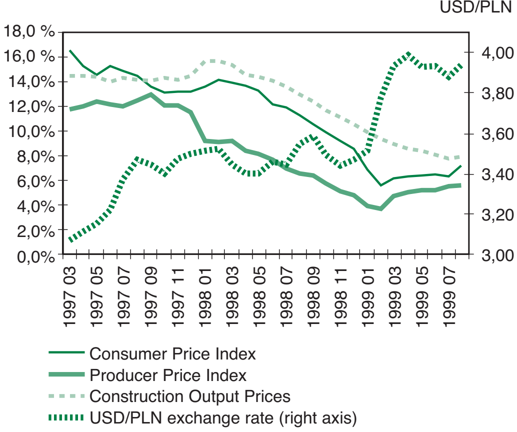
July's current account deficit data was rather negative. In July 1999, the current account deficit totalled USD 1,020bn after USD 1,134bn in June 1999. The trade deficit in July remained at the same level as that in June of USD 1.3bn. In the January-July period the current account deficit totalled USD 6,021bn, which means a 110% increase y/y.

According to the NBP, in payment terms, the trade deficit in the January-July period was USD 7.488bn, which means a 5.4% rise compared to the same period last year. In the first seven months of 1999, exports in payment terms fell by 12.6% down to USD 15.4bn whereas fell only by 7.5% down to USD 22.9bn. This means that there is still no recovery in exports.

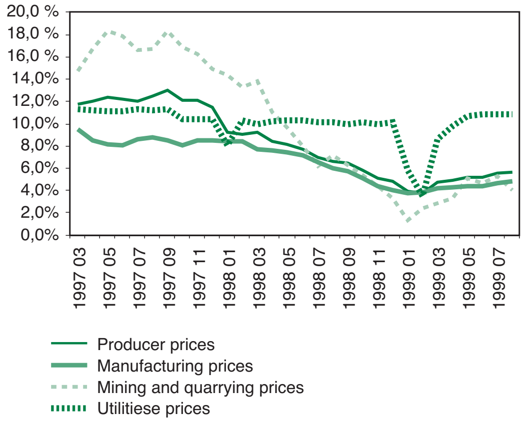
The main reason for the deteriorated current account balance is a fall in unregistered cross-border trade and a worse balance of services.

The foreign direct investment balance in the January-July was USD 2.559bn, which means a 9.4% fall y/y. In the period concerned there was a negative balance of minus USD 309m.

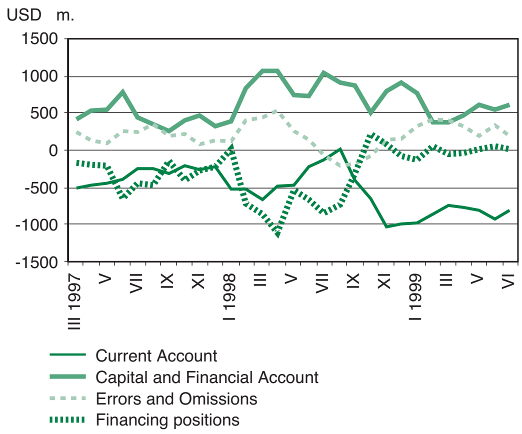
Inflation indicators and exchange rate



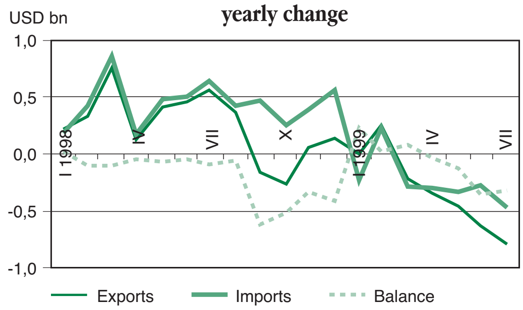
Producer Prices

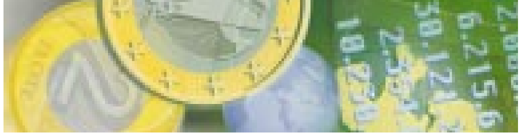


Balance of Payments (3M average)



Merchandise Trade (NBP) yearly change





GDP Growth Q1 1999

In Q2 1999, GDP increased by 3.0% y/y vs. 1.5% GDP growth in Q1 1999. In the first half of this year GDP increased by 2.3%. Gross domestic product growth in 1999 should mainly be attributed to a stable domestic demand, which grew by 4.6% in Q2 1999 after 3.2% growth in Q1 1999. In the first half of 1999 domestic demand increased by 3.9% y/y. Compared to the previous years, domestic demand growth significantly slowed down mainly due to a fall in gross fixed assets expenditures from 16.0% in H1 1998 to 6.5% in H1 1999. Gross domestic product was mainly generated in the market services sector which grew by 4.2% in H1 1999. It should be noted that there is a strong decline in gross value added in industry by 0.9% y/y, driven by a dramatic, 3% decline in Q1 1999. Given reduced capital expenditures, construction growth significantly reduced and was a mere 2.7% in H1 1999 compared to 13.0% in H1 1998. **If the present trends continue, gross domestic product in 1999 may grow by approx. 3.7%.**

Industrial Output

Industrial output in August 1999 increased by 4.9% month on month and was up 7.4% on August 1998. The industrial output increase last month can be attributed to recovery in manufacturing activities, which grew by 8.3% year on year. In the January-August 1999 manufacturing production increased by 0.9 compared to the same period last year. We expect a significant improvement in industrial output in the near term.

Construction and installation production in August rose by 6.3%, which means a 4.2% increase year on year.

Labour Market

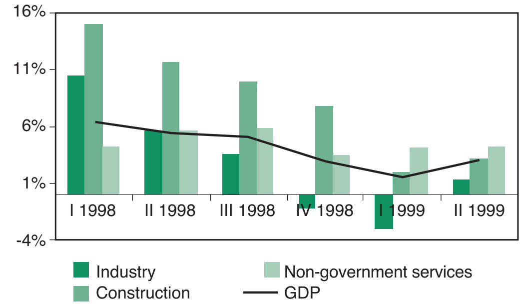
The unemployment rate in August 1999 increased up to 11.9% after 11.8% unemployment in July. The number of the unemployed in August was 2m 144k, which means an increase by 28k compared to July and an increase by 473k compared to August 1999 when the unemployment rate was 9.5%.

Average employment in enterprises in August was 5747.3k persons, reaming at the same level as in the previous month. Average employment in enterprises fell by 1.6% on an annualised basis.

The average gross salary in August was 1999 PLN 1823.29, which means a 1.6% increase m/m and a 10% increase on an annualised basis.

We do not expect a significant improvement in the labour market in the near term due to the restructuring of the economy and a continuous external demand.

Gross Domestic Product (real growth)



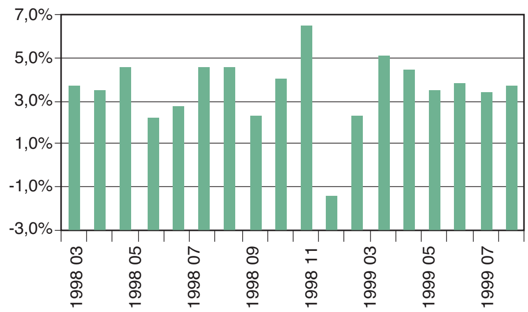
Tab. 6 Real GDP in H1 1999 (% increase y/y)

	1997	1998	Q199	Q299	H199
Total consumption	6.1	4.2	3.7	4.1	3.9
including:					
individual consumption	6.9	4.9	4.2	4.8	4.5
Gross accumulation	20.8	14.1	1.1	6.4	4.1
including:					
gross fixed assets expenditures	21.7	14.5	6.0	6.7	6.5
Domestic demand	9.3	6.5	3.2	4.6	3.9
Gross Domestic Product	**6.8**	**4.8**	**1.5**	**3.0**	**2.3**
Gross value date	6.5	4.5	1.3	2.8	2.1
including:					
- Industry	10.3	4.4	-3.0	1.3	-0.9
- Construction	13.6	10.2	2.0	3.2	2.7
- Non-govt services	4.4	4.7	4.1	4.2	4.2

Source: Central Statistical Office

Unemployment rate and employment in business sector

Real Wages Growth (y/y)



Will Privatisation Strengthen the Zloty in Q4 1999 ?

September witnessed a significant weakening of the zloty due to information that the scale of privatisation flows in Q4 1999 will be will be significantly smaller than expected. This mainly relates to information on a 25-35% TP SA privatisation tranch being deferred until Q1 2000 and information that a substantial part of this year's privatisation revenues will not be converted in the fx market in Q4 but will be used to repay Poland's foreign debt i.e. Brady bonds. In such a situation market expectations were determined by fundamental data on the current account deficit and the public finances deficit. At this stage, given the need to cover the ZUS deficit from privatisation receipts, seems that at least some of the privatisation revenues should go through the market. *The NBP Governor, Hanna Gronkiewicz-Waltz, sees the proper zloty exchange rate as being at the central parity rate*. In our opinion, this is an attempt to reduce the restrictiveness level of monetary policy by causing the zloty to depreciate. A paradox in Poland's current macroeconomic situation is the fact that changes in the banking system's net foreign assets exert a significant impact on money supply. In the light of a very likely interest rate increase, the NBP will make every effort to improve the standing of enterprises by causing the zloty to depreciate in an indirect way.

Tab. 7. Main Privatisation Transactions in 1999 and Q1 2000:

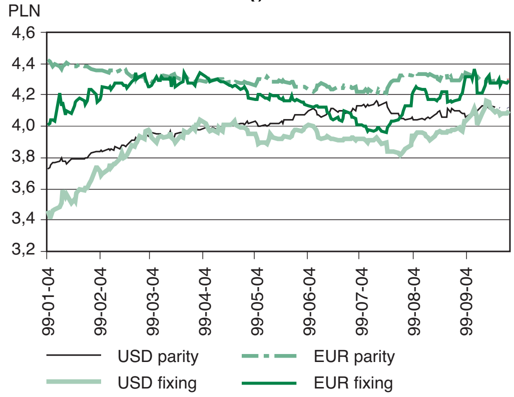
Privatisation	%	Type	Revenues	Period
Pekao S.A.	52 %	Strategic Investor	USD 1.1 bn	Completed
Bank Zachodni	80 %	Strategic Investor	USD 0.5 bn	Completed
Elektrownie PAK	20 %	Strategic Investor	USD 90 m	Completed
Polar	37 %	Strategic Investor	USD 35 m	Completed
Revenues Q1-31999	-		**USD 1.7 bn**	
PZU	30 %	Strategic Investor	USD 0.5-1 bn	4Q1999
Warta	20 %	Portfolio Investment	USD 35 m	4Q1999
Polski Koncern Naftowy	30 %	Public Officering	USD 750 m	4Q1999
LOT *	10 %	Strategic Investor	N/A	4Q1999
7 elektrociepłowni *	10-45 %	Investor /Public offering	N/A	4Q1999
Revenues Q41999	-		**USD 1.4-1.9bn**	
TP S.A.	25-35 %	Strategic Investor	USD 3.5 - 5bn	1Q2000
KGHM	10 %	Public Officering	USD 150 m	1Q2000
Revenues Q12000			**USD 3.8-5.2bn**	

Source: Reuters, WBK Treasury, WBK Central Brokerage Office
Note: The above information can be subject to change depending on what the Treasury Minister will decide. Enterprises marked with (*) may be privatised in 2000.

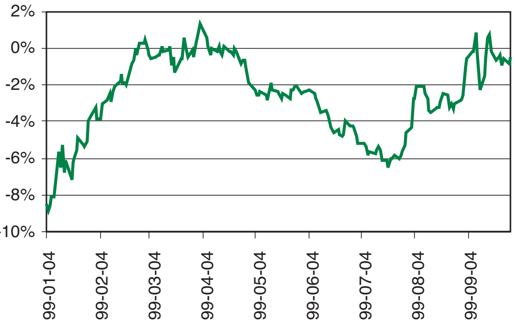
According to the Treasury Minister, Wąsacz, only PLN 8bn out of PLN 15bn planned privatisation revenues will be used to fund the budget deficit. In order to cover the ZUS's deficit, it is necessary to have an additional PLN 4bn. Approx. USD 1.7bn i.e. PLN 6.8bn has already flowed through the fx market. By the end of September, privatisation revenues will have been approx. PLN 9.4bn. Out of the remaining PLN 6bn, half will come from the privatisation of Polski Koncern Naftowy. The balancing amount i.e. USD 500-750m is likely to flow through the market in Q4 1999 as the payment for PZU. This sum may cause the zloty to deviate 1-1.5% from the parity. The recent comment by Wąsacz that privatisation revenues in 1999 will only be PLN 13bn, which may mean that the PZU payment will be made in Q1 2000,which means that the zloty will be much weaker than expected in the coming quarter. Poland's macroeconomic situation does not seem to favour the zloty. *In the next two weeks the zloty may weaken below the parity rate due to high inflation which as we expect may be over 7.5% in September.*

The August current account deficit and September industrial output data should be positive for the zloty. We expect the zloty rate to be quite unstable in the near term and very sensitive to macroeconomic data.

Exchange rates

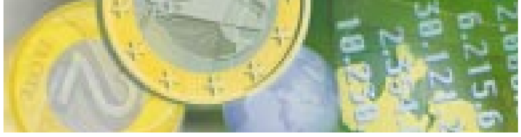


Deviation of exchange rate from central parity (weighted average of USD and EUR)



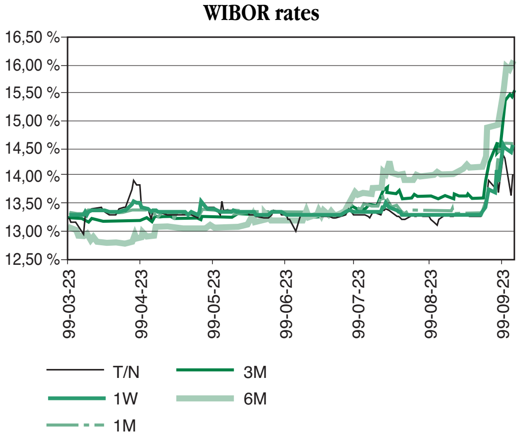
USD/PLN

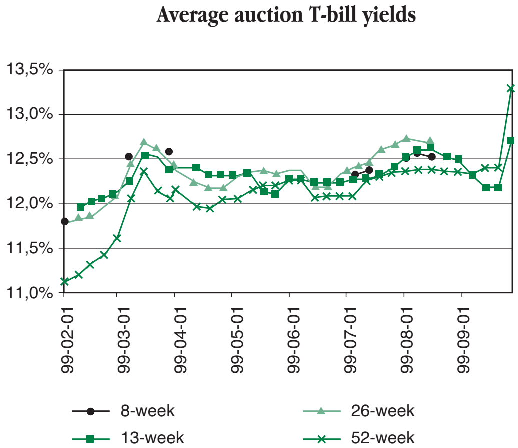
EUR/USD



Interest Rates

Over the last month the situation in the money market has considerably changed due to the combination of two factors - the approaching of the last quarter in 1999 - one before 2000 and resultant accumulation by banks as well as speculation on an interest rate increase. In early August 6M WIBOR was over 14.0% and continued to be at this level until 6 September when it reach 14.14%. A estimated Y2000 premium for 6M WIBOR was approx. 70 basis points. On 20 September, Monday, WIBOR 6M reached 15.00%. After the NBP intervention rate change, all interbank rates increased between 50 and 69 basis points. In September the liquidity of the banking system was quite substantial due to settlement of the obligatory reserve requirement resulting in strong declines in O/N and T/N terms. On 28 September O/N WIBID fell to 6.45%. On 30 September the NBP bond will be purchased due to the reduced obligatory reserve requirement. Given the purchase of the bond, PLN 13bn worst of bonds will be taken away from the market with PLN 26bn worth of NBP bills purchased. For this reason, WIBOR rates should increase in the coming weeks.





Treasury Bills

Over the last month 13-week treasury bills yields in the primary market have fallen, which was driven by increased short-term liquidity of the state treasury supported by privatisation receipts. The Finance Ministry reduced their offer and did not accept very high yield bids. The one-year treasury bill yield was subject to much smaller volatility staying at a slightly higher level since mid September. After the increase in the intervention rate, NBP bill yields considerably increased with the 13W bill yield increasing by 51 basis points and the 52W bill yield increasing by 90 basis points (360 day basis). Given the uncertain situation of the state budget and the next interest rate increase, treasury bill yields may increase even more.

Treasury Bonds

In the bond market, 2 and 3 year bond prices went down due to the change in the term portfolio structure of securities held by domestic banks due to an increase in the intervention rate and foreign investors selling short-term securities. While potential tightening of monetary policy will not have an impact on the longer end of the yield curve, we expect short-term yields to further increase.

Tab. 8. Interest Rates (WIBOR)

Maturity	Currently 28/09/99	1 Week Ago 21/09/99	1 Month Ago 26/08/99
T/N	14,02	14,04	13,22
1W	14,55	14,12	13,30
1M	14,59	14,21	13,36
3M	15,52	14,63	13,64
6M	15,98	15,00	14,00

*Tab. 9. Average Auction Treasury Bill Yields **

Date	8-W	13-W	26-W	52-W
23/08/99	-	12.70	-	12.54
30/08/99	-	12.66	-	12.52
06/09/99	-	12.49	-	12.51
13/09/99	-	12.36	-	12.57
20/09/99	-	12.36	-	12.57
27/09/99	-	12.88	-	13.48
Change 27.09-23.08	-	0.17	-	0.94

*Tab. 10. Treasury Bill Yields (secondary market) **

Date	3M	6M	9M	12M
23/08/99	12.67	12.67	12.72	12.52
30/08/99	12.52	12.57	12.62	12.47
06/09/99	12.52	12.67	12.62	12.50
13/09/99	12.57	12.62	12.72	12.52
20/09/99	12.52	13.08	13.08	13.38
27/09/99	12.98	13.69	13.89	13.69

Tab. 11. Treasury Bond Yields (Secondary Market)***

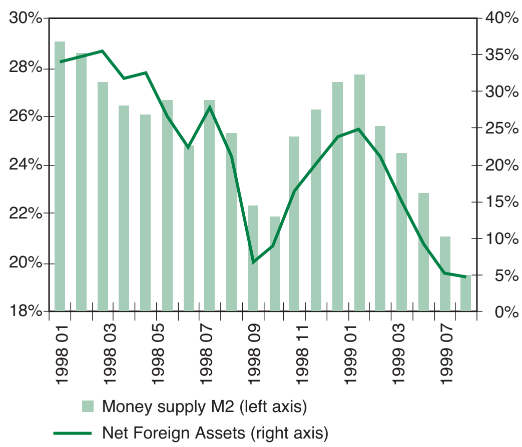
Date	2Y	3Y	4Y	5Y	10Y
23/08/99	12.77	12.34	11.79	11.36	9.31
30/08/99	12.60	12.18	11.72	11.45	9.24
06/09/99	12.62	12.35	11.88	11.45	9.52
13/09/99	12.73	12.32	11.80	11.35	9.26
20/09/99	13.35	12.64	12.66	11.82	9.87
27/09/99	13.60	12.88	12.51	11.72	9.69

* 365 day basis ** Internal Rate of Return (IRR)

Money Supply

Overall money supply (M2) was PLN 241.6bn, which means a 1.3% monthly increase and 19.7% in yearly terms. Real growth in money supply on annualised basis was 11.7%. Since the start of the year money supply increased by 9.4% in nominal terms and 4.1% in real terms. Strong personal credit growth of 44.8% continues although personal credit accounts for 19.1% of loans to the non-financial sector. Zloty deposits increased by 1.2% m/m with zloty personal deposit growth of 0.5% and business deposit growth of 3.2%. Business and personal loans increased by 2.4% m/m with personal loan growth of 4.4% and business credit growth of 1.9% m/m. Net public sector debt decreased by 7.3%. m/m. In August the money supply increase that was driven by foreign net asset growth associated with privatisation transactions was restricted by a 3% fall in domestic net assets. In effect, money supply increased by PLN 3.179bn. Net foreign assets in August increased by USD 1.078bn, up to 26,455 and were USD 1.023bn lower than those at the end of 1998.

Nominal Money Supply (y/y)



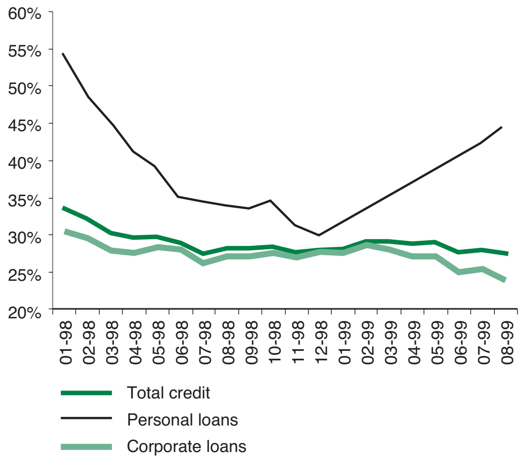
Monetary Policy in 1999

At its meeting on 22 September, the Monetary Policy Committee (MPC) increased the intervention rate by 100 basis points up to 14%, leaving the lombard and discount rates unchanged. This hike was to some extent surprising as the market had not expected any tightening of monetary policy until the next month at the earliest. It was also expected that all 3 official interest rates would be increased this year. The size of the increase was not surprising. In its rationale the MPC mainly indicated a potential threat to the 2000 inflation target (5.4-6.8% in December 2000) driven by greater inflation expectations. The MPC indicated a strong increase in CPI in August following a seasonal decrease in July and a substantial producer price increase. Another, equally important reason for tightening monetary policy, was excessively loose and inconsistent fiscal policy in 1999. The MPC called on the government to make fiscal policy more restrictive. A third reason was a threat to money supply control due to continuous excessive consumer credit growth from 30% at the end of 1998 to 45.4% at the end of August 1999. According to the MPC large consumer credit growth stimulates negative current account tendencies. A fourth reason was that the MPC indicated that in the external imbalance environment, internal demand should be limited until exports start to increase. **The MPC is planning to limit the over-liquidity of the banking sector in 2000.**

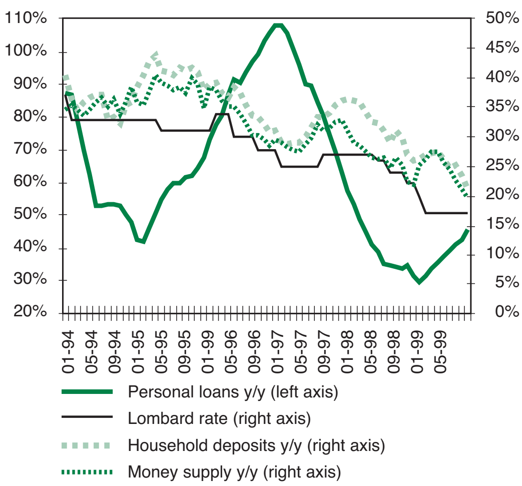
It should be expected that interest rates will be kept at high levels for a period of 5-6 months. Further increases in the prices of oil and further increases in the petrol excise, food price increases in the fourth quarter if 1999, high dynamics of the prices of services and non-food goods indicates that there are possible further inflation increases. **If fiscal policy is not tightened and inflationary threats continue one cannot ruled our further tightening of monetary policy this year.**

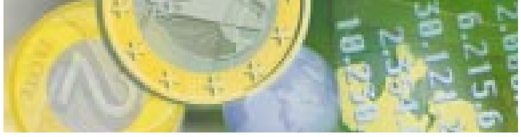
The next meeting of the MPC will be held on 20 October.

Nominal credit growth (y/y)



Monetary Conditions

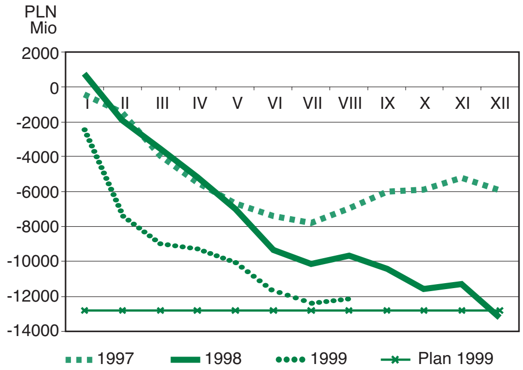




State Budget and the deficit of public finances

The budget deficit in August decreased to PLN 12.13bn from PLN 12.43bn in July, which accounts for 94.7% of the deficit planned for 1999. It was the first month this year when a budget surplus was recorded. Budget revenues in the January- August period totalled PLN 76.77bn (59.4% of plan) while expenditures totalled PLN 88.9bn, which accounts for 62.6% of the plan. According to preliminary information, in September the budget deficit will further reduce down to approx. 92-94% of this year's plan. In the face of interbank rate increases, the state treasury will be forced to seek short-term funds at a higher cost. While the budget deficit may seem to be under control, a substantial part of the budget deficit is connected with the ZUS and has been classified as a part of the public finances deficit. An estimated deficiency in the ZUS this year may range from PLN 3 to 4bn, excluding the ZUS's present debt with commercial banks of PLN 2.8bn. The deficit will covered with a through a loan from privatisation revenues, which requires a change in the public finances act. The deficit in the ZUS may total PLN 4 to 6bn this year - this means an increase in the public finances deficit this year by almost 1%, up to 4.0% compared to the planned figure of 3.0%.

State Budget Balance (cumulative)



2000 State Budget Project

It assumed in next year's state budget project that the budget deficit will be considerably reduced with real State budget revenues increasing by approx. 3.5% and real expenditures increasing by 2.6%. At the same time, it is assumed that the public finances deficit will be reduced to 2.38% of GDP in 2000. In terms of an economic equilibrium, these are very positive assumptions provided that the assumed macroeconomic parameters will be met and there occur no tensions in the budget related areas next year, which will be similar to those experienced this year. While it seems that economic growth is estimated quite optimistically, which may lead to lower direct tax revenues, under the proposed inflation assumptions there is some reserve for increased indirect tax revenues. Thus, the central budget should be met next year. A reduced current account gap next year would be a very good signal, however, it would require a significant reduction in the trade deficit, which seems to be a structural deficit in nature. What is worth noting is an increase in social fund subsidies, which account for approx. 28% of budget expenditures. The ZUS subsidy in 2000 is to be increased to PLN 14bn from PLN9.6bn planned in 1999. However, the Government assumes that there will be a smaller collection of ZUS contributions next year and that there will possibly be a loan for the ZUS of PLN 2bn. It can be surmised that the public debt services costs as assumed for 2000 of PLN 18.4bn may in reality be higher by approx. PLN 1bn. Privatisation revenues projected for 2000 will be PLN 14.4bn vs. PLN 13-15bn in 1999. According to the Finance Ministry, the planned deficit should make Poland more resistant to external shocks.

Tab. 12. Fundamental Macroeconomic State Budget Assumptions for 2000:

Assumption	Unit	1999	2000
GDP growth - fixed prices	%	4.0	5.2
Generated GDP - current prices	PLN bn	608.9	677.2
Inflation (yearly average)	%	6.8	5.7
Inflation (period end)	%	7.7	5.2
Unemployment rate (period end)	%	11.8	11.5
Current account balance (period end)	USD bn	-10.6	-10.5
Current account balance: GDP	%	6.8	6.1
Current account balance (period end)	USD bn	-14.2	-14.0
USD/PLN Foreign Exchange (yearly average)	PLN	3.8810	3.9749
Lombard rate (period end)	%	18.00	15.00
Open market operations rate (period end)	%	13.50	11.50
State Treasury revenues	PLN bn	129.3	141.5
State Treasury expenditures	PLN bn	142.1	154.1
Budget deficit	PLN bn	12.8	12.7
Budget deficit: GDP	%	2.15	1.87
Public finances deficit: GDP	%	3.00	2.38

Source: Finance Minsitry, Reuters

Foreign Trade

According to data from the Central Statistical Office, the trade deficit in the January-July period 1999 fell to USD 9.926bn vs. USD 10.3bn in the same period last year. Exports in invoice terms in the seven months of this year totalled USD 15.02bn, or down 8.7% on last year. Imports decreased by 6.6% down to USD 24.947bn. According to the NBP the trade deficit in the January-July period totalled USD 7.488bn in payment terms.

The geographical structure of foreign trade changed following the Russian crisis. Exports to Central and Eastern Europe, mainly the former USSR, decreased. In the January-August period 1999, USD-expressed exports to Central and Eastern Europe fell by 35.7% compared to the same period last year. Exports to EU countries fell marginally by 0.5% whereas exports to developed countries remained at the same level as last year. A very positive phenomenon is a 2.8% increase in exports to CEFTA countries. In the wake of the Russian crisis, total exports fell by 8.7%. Imports in dollar terms decreased by 6.6% in the period concerned with the largest fall in imports experienced in trade with developing countries by 14.0%. Imports from developed countries fell relatively moderately by 5.3%. A relatively small decrease in imports from Central and Eastern Europe (by 7.2%) should be attributed to the structure of imports from this region where fuels and raw materials play a big role.

Despite a weakened zloty at the start of the year, a fall in exports in dollar terms indicates that there is little price flexibility of demand for Polish exports, existing particularly in the trade with the EU.

An analysis of the structure and dynamics of Polish foreign trade in H1 1999 indicates that in the period concerned turnover fell in all SITC sectors. The only sector that experienced a 7.4% increase in exports was beverages and tobacco products.

An unfavourable phenomenon was an over 26% decrease in food exports compared to the same period in 1998, which can be associated with a decline in demand in the eastern markets. A very strong, nearly 23% decline exports of chemicals and chemical products, which fell by 1.2%. A 8.9% fall occurred in industrial goods classified by raw materials. A positive signal may be an insignificant 1% fall in the export of various chemical products. A positive tendency is also an increased export of machines and appliances as well as transport equipment. However, this section experienced a 1.6% fall in exports.

In relation to imports, which fell by 6.6% in dollar terms in H1 1999, there did not occur any significant changes in the commodity structure except fuels and raw materials where the percentage of imports fell by 1.4%, and food where the percentage fell by 0.4%. However, the percentage of chemicals and chemical products increased by 0.4% and the percentage of machines and appliances and transport equipment increased by 0.5%.

Tab. 13. Dynamics and Structure of Foreign Trade Turnover in I-VII 1999.

	PLN Dynamics	USD Dynamics	Structure I-VII 1998	Structure I-VII 1999
Exports	101.3	91.3	100.0	100.0
Developed countries	111.1	100.1	71.0	77.8
Including EU	110.4	99.5	65.8	71.7
Developing countries	100.6	90.2	5.9	5.9
Central and Eastern Europe	71.5	64.3	23.1	16.3
of which CEFTA	114.2	102.8	7.0	7.9
	PLN Dynamics	USD Dynamics	Structure I-VII 1998	Structure I-VII 1999
imports	103.8	93.4	100.0	100.0
Developed countries	105.4	94.7	74.1	75.2
Including EU	105.3	94.7	65.1	66.0
Developing countries	95.5	86.0	12.4	11.4
Central and Eastern Europe	103.1	92.8	13.5	13.4
of which CEFTA	106.4	95.6	6.5	6.7

Source: GUS

Strukture and changes in trade turnover according to SITC sections (USD)

Exports	**Strukture I-VI 1998**	**Strukture I-VI 1999**	**Percentage change y/y**
Total Eksports	100.0	100.0	-8.1
Food and live animals	10.4	8.3	-26.9
Beverages and tobacco	0.3	0.4	7.4
Crude materials inedible, except fuels	3.1	3.1	-7.0
Mineral fuels, lubricants and related materials	5.3	5.2	-10.0
Animal and vegetable oils, fats and waxes	0.2	0.2	-9.8
Chemicals	7.3	6.1	-22.7
Manufactured goods classified chiefly by material	25.8	25.6	-8.9
Machinery and transport equipment	27.3	29.3	-1.6
Miscellaneous manufactured articles	20.3	21.8	-1.0
Imports	Strukture I-VI 1998	Strukture I-VI 1999	Percentage change y/y
Total Imports	100.0	100.0	-6.6
Food and live animals	6.6	6.0	-15.2
Beverages and tobacco	0.6	0.6	-1.6
Crude materials inedible, except fuels	3.9	3.2	-22.8
Mineral fuels, lubricants and related materials	6.7	6.0	-16.6
Animal and vegetable oils, fats and waxes	0.7	0.4	-42.5
Chemicals	14.1	14.5	-3.8
Manufactured goods classified chiefly by material	20.1	21.0	-2.2
Machinery and transport equipment	38.2	38.7	-5.4
Miscellaneous manufactured articles	9.1	9.4	-2.7

Source: GUS

Basic Macroeconomic Data

CATEGORY	1999 January	February	March	April	May	June	July	August
Consumer price index (m/m)	1,5%	0,6%	1,0%	0,8%	0,7%	0,2%	-0,3%	0,6%
CPI non-food products (m/m)	0,6%	0,4%	0,6%	0,8%	0,6%	0,0%	-0,3%	0,7%
CPI food products (m/m)	0,2%	0,0%	0,5%	0,5%	0,6%	-0,7%	-2,3%	-0,1%
CPI services (m/m)	3,3%	1,0%	2,0%	0,9%	0,8%	0,6%	0,3%	0,4%
Consumer price index (y/y)	6,9%	5,6%	6,2%	6,3%	6,4%	6,5%	6,3%	7,2%
Consumer price index (December of the previous year=100)	1,5%	2,1%	3,1%	3,9%	4,6%	4,8%	4,5%	5,1%
Price index of sold production of industry (m/m)	0,4%	0,6%	1,1%	0,6%	0,5%	0,1%	0,5%*	0,7%
Price index of construction and assembly production (m/m)	1,6%	0,9%	0,7%	0,5%	0,6%	0,3%	0,3%*	0,7%*
Price index of sold production of industry (y/y)	3,9%	3,7%	4,7%	5,0%	5,2%	5,2%	5,5%*	5,6%
Price index of construction and assembly production (y/y)	9,8%	9,4%	9,0%	8,6%	8,4%	8,1%	7,8%*	7,9%
Sold production of industry (m/m)	-11,0%	-0,4%	21,8%	-7,0%	1,2%	0,1%*	-2,0%*	4,9%
Sold production of industry (y/y)	-5,1%	-5,6%	3,5%	0,3%	2,2%	1,0%	1,4%*	7,4%
Construction and assembly production (m/m)	-54,8%	5,7%	19,1%	10,3%	10,8%	9,6%	-0,5%*	6,3%
Construction and assembly production (y/y)	3,9%	-3,1%	1,2%	2,8%	4,2%	4,9%	-0,3%*	4,2%
Unemployment rate	11,4%	11,9%	12,1%	11,8%	11,6%	11,6%	11,8%	11,9%
Average employment in enterprise sector (thous people)	5 835	5 818	5 808	5 799	5 780	5 771	5 748	5 747
Average monthly gross salaries and wages in enterprise sector (PLN)**	1 597	1 626	1 742	1 780	1 767	1 827	1 852	1 823
The state budget balance (PLN mio)	-2 476	-7 386	-8 992	-9 299	-10 055	-11 373	-12 459	-12 132
State budget revenues (PLN mio)	9 552	17 376	27 727	37 599	46 841	56 410	65 865	76 769
State budget expenses (PLN mio)	12 029	24 762	36 719	46 898	56 896	67 783	78 323	88 901
Trade balance in a cash basis (USD mio)	-1 212	-783	- 904	-1 036	-1 031	-1 302*	-1 298	-
Exports (USD mio)	2 119	2 522	2 463	2 159	1 989	2 122*	2 149	-
Imports (USD mio)	3 331	3 305	3 367	3 195	3 020	3 424*	3 447	-
Current account balance (USD mio)	-894	-488	-844	-938	-690	-1 137*	-1 020	-
Money supply (PLN mio)	221 754	226 759	230 256	230 751	233 265	236 239*	238 460*	241 639
Gross official reserves of NBP (USD mio)	27 085	26 807	26 598	26 407	26 145	25 848	26 324	26 142
Rediscount rate	15,5%	15,5%	15,5%	15,5%	15,5%	15,5%	15,5%	15,5%
Lombard rate	17%	17%	17%	17%	17%	17%	17%	17%

* - data officially corrected