

# MACROscope

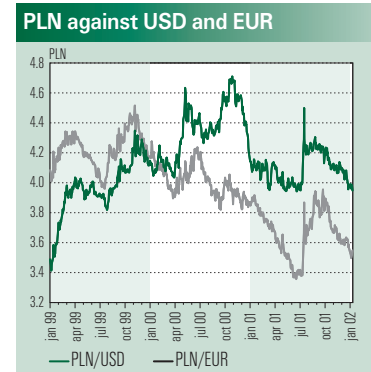
## Polish Economy and Financial Markets

January 2002

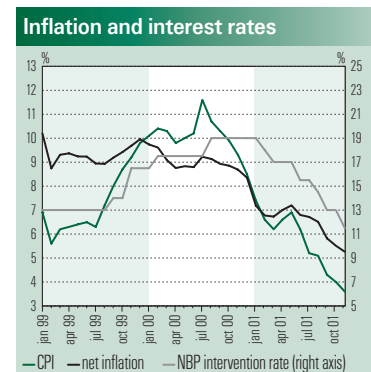
N° 30

### Poland at crossroads in 2002

- A true man is recognised by his output and not by the way he starts, the leader of the Left Democratic Alliance (SLD), Leszek Miller, used to say before he became Prime Minister. However, it seems that in the difficult situation, in which the Polish economy is in 2002, the beginning of the government actions will be equally important as the end itself. For politicians, the miserable economic situation means a fall in popularity and actually, in December, all institutions carrying out opinion polls informed about a considerable growth in the percentage of people unsatisfied with the government actions. Therefore, it is no wonder that politicians intend to generate a quick economic revival (thus, the pressure on the central bank in order to reduce interest rates and depreciate the zloty), however, it surprises that long-term costs of such policy become completely ignored (inflation growth, loss of prestige and investors' trust). Most probably, year 2002 will commence with the parliamentary debate on the role of monetary policy, in the course of which debate, an attempt will certainly be made to change the mandate of the central bank. If the independence of the central bank is limited, then, even if the President' probably vetos it, a considerable weakening of the zloty can be expected. Therefore, if the government and the parliament will start badly in January, then, even a better end of the year may not allow to achieve the target, i.e. to create the basis for a permanent and balanced economic growth.
- After the GDP growth of 0.8% in Q3 2001 and poor November figures, the revival in Q4 was symbolic and related to consumption rather than investment. The November data showed that the Polish economy was still in the same trend, i.e. showed slow economic growth, yet, at the same time more balanced. i.e. with lower inflation (3.6% y/y) and lower current account deficit (4% GDP). However, we do not share the pessimism of government forecasts and some of the MPC members, and expect a slight GDP revival in Q4 (to 1.3% y/y). In 2002, the economic growth will accelerate slightly, however, it will take place with higher inflation and higher current account deficit.
- In January, the expectations of further interest rate reductions will certainly come back. FRA contracts will not price off the interest rate reduction in January, mainly due to increasing difference between WIBOR rates and the intervention rate resulting from liquidity fluctuations in the banking system. However, it seems that a great number of analysts and dealers expect a cut. We do not share these expectations, moreover, the political pressures may be followed by the stiffening of the council's stance. However, the MPC might decide to reduce interest rates if the zloty strongly appreciated in January, which we do not expect to occur.



Source: NBP, Reuters



Source: NBP, CSO

**In this issue:**

- Special focus ..... **2**
- What awaits us in the New Year?*
- Economic update ..... **3**
- Central bank watch ..... **8**
- Government and politics ..... **13**
- Market monitor ..... **16**
- International review ..... **19**
- Economic calendar ..... **21**
- Statistics & forecasts ..... **22**

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Financial market		on 28 December 2001	
NBP deposit rate.....	<b>7.00</b>	WIBOR 3M .....	<b>11.91</b>
NBP intervention rate.....	<b>11.50</b>	Yield on 52-week T-bills.....	<b>10.45</b>
NBP lombard rate.....	<b>15.50</b>	Yield on 5-year T-bonds.....	<b>9.45</b>
		PLN/USD.....	<b>3.9601</b>
		PLN/EUR.....	<b>3.4963</b>
		EUR/USD.....	<b>0.8875</b>

## What awaits us in the New Year?

- Politicians will decide on the central bank's role
- Government and Parliament will accept the public finance rehabilitation and economic revival plan
- It will turn out whether Poland will put an end to negotiations with the European Union
- There will be a battle between politicians and financial markets over an equilibrium level of the zloty fx rate
- Economic growth rate will improve, inflation and the current account deficit will deteriorate, the unemployment will increase

Year 2002 will be very important for the Polish economy, investors and companies for at least four reasons. Firstly, the parliament will decide on the status of the central bank. Secondly, the government and parliament will decide on the shape of the public finance rehabilitation and economic revival plan, the first step of which is the 2002 budget draft. Thirdly, it will turn out whether Poland will finalise negotiations with the European Union and be accepted in the Union in the first group of countries, probably in 2004. Fourthly, a battle most probably will take place between financial markets and politicians to determine where the rate of balance for the zloty is.

### January: what statutes for the central bank?

In January, the parliament will probably decide on the shape of the NBP act amendment. The already accepted change reducing remuneration may be followed by the change increasing the number the Council members or adding to the Council objectives the provision about support for the economic growth and fighting unemployment. Politicians, blinded with the intention to accelerate the economic growth immediately, lost a longer-term view. Luckily, the central bank gained an ally in the person of President Kwasniewski, who suggested vetoing the changes in the NBP act if they violated the Constitution or were contradictory with the European Union law.

### February: economic revival plan

According to announcements of the finance minister, in the middle of February, the government will present the public finance rehabilitation and economic revival plan. Until now, the government made the first step, a small one, but in the right direction, preparing the 2002 budget and a package of budget-related acts. However, a number of solutions in the 2002 budget

is of temporary nature and it will be just „Belka's plan" and political support for this plan, ensured by Prime Minister Miller, on which the possibility of avoiding the public finance crisis and generating a quicker and more balanced economic growth will depend.

### Autumn: will Poland finalise negotiations with the EU?

Probably in autumn 2002, it will turn out whether Poland will close all the negotiation chapters and become a member of the first group of countries accepted in the EU as early as in 2004. The decision will be dependent on both the politics and economy. For example, taking political decisions on depriving the NBP of independence, introducing import tax, lack of consensus in the issue of the sale of land or subsidised lending for farmers may diminish Poland's chances for the membership in the first group. On the other hand, if the public finance rehabilitation plan will not succeed and the Polish economy instead of accelerating will slow down in 2002, the escalating unemployment and budget deficit may also bury our chances for quick membership in the EU.

### Q1 2002: what rate of balance for the zloty?

PLN 5 per one dollar. This is, undoubtedly, a dream of some of the politicians who, quite rightly, perceive the only chance for economic revival in the weak zloty. Unfortunately, politicians do not see that when this short period of "life on the devaluation stimulus" will come to an end, there will be a long "inflation hangover". However, financial markets want a strong zloty, which will ensure gains on high yield government securities. Therefore, it can be expected that financial markets and politicians will start a battle, which will result in a new equilibrium level of the zloty fx rate. As the NBP act will be the politicians' tool in this struggle, we emphasise increasing risk of considerable zloty weakening in Q1 2002.

### What will the year 2002 be like?

In line with our forecasts, the year 2002 will be both better and worse, depending on a ratio. We expect some acceleration in the economic growth from 1.3 to 2%, however, at the same time the growth in unemployment from 17.3 to 18.5%, inflation from 3.7 to 5% and the current account deficit from 4.2 to 5.5% GDP. Thus, the growth will be quicker but less balanced, however, the main challenge for the government, apart from the negotiations with the EU, will be a deteriorating situation on the labour market.

## Economic update

- Growth in Q3 2001 slightly lower than in Q2. Beginning of revival only in the second half 2002.
- November statistics confirmed our suppositions – for the time being no light at the end of the tunnel
- Inflation in November hit the bottom, a rebound possible at the beginning of 2002
- Run away from Belka's tax resulted in erosion of the deposit base in banks

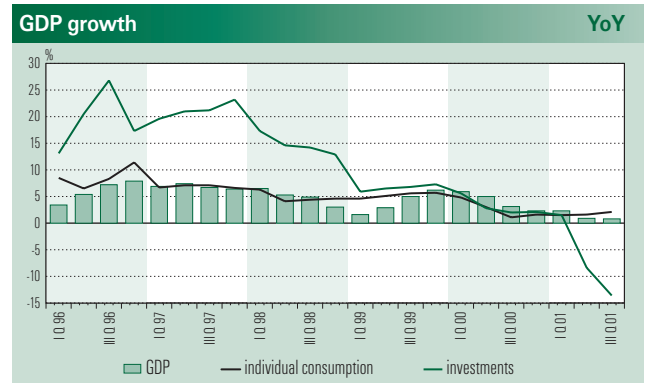
### GDP grew in Q3 by 0.8% y/y, a collapse in investments

The third quarter was the weakest this year in terms of the economic growth. GDP grew by 0.8% y/y against 2.3% in Q1 and 0.9% in Q2. The slowdown was due to a deep fall in investments into fixed assets, which decreased by 13.6% y/y after a fall of 8.4% in Q2. In addition, there was a further reduction in stock, however, much slower than in the two previous quarters, which may imply that accumulation (capital expenditure in fixed assets plus stock) is approximating the bottom.

Individual consumption is quite good, raising by 2.1% y/y in Q3 against 1.5% and 1.6% in Q1 and 2, respectively. Enlivening in individual consumption most probably reflects once-off transfers for the Third Reich workers and indexation of pensions. In addition, a sudden disinflation process increased a purchasing power of salaries and pensions in Q3.

In the quarters to come, it is difficult to expect a real economic growth revival, although some improvement of statistical ratios will probably occur. It will result from, e.g. a once-off deep fall in stock in Q1 2001. Assuming that such a fall will not be repeated in the following year, the GDP growth rate in Q1 2002 will be overestimated by high dynamics of the gross accumulation, an element of which is a change in stock volumes. However,

the actual improvement of the economic activity will be noticeable only in the second half of the year, when the effect of domestic interest rate cuts, effected from the beginning of 2001, will be fully reflected by the economy, and signs of the economic situation revival in the countries of the European Union and the USA will also emerge.



Source: CSO

### November statistics confirmed our suppositions – lack of economic revival for the time being

The November statistical data confirmed our suppositions made a month ago that unusually favourable figures on the economic situation in October constituted a once-off deviation from the trend rather than the beginning of a new one.

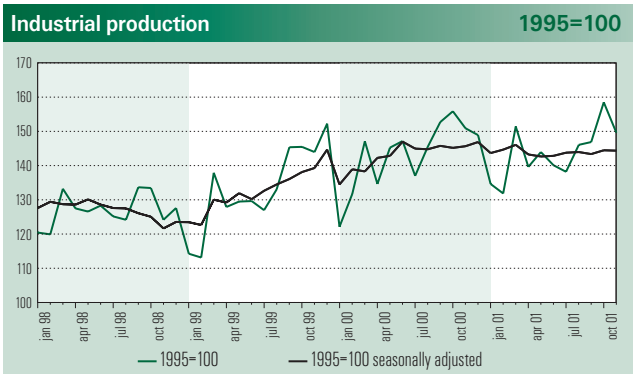
Industrial output decreased in November both on an annual and monthly basis by 0.8% and 5.5% respectively, after a growth by 1.4% y/y and 7.7% m/m in October. This means that the data confirmed the results of economic surveys, which this month once again showed in harmony the lack of improvement in the business sector. A slump in the industry sector is well illustrated by the sold industrial output index, cleansed from seasonal fluctuations and impact of once-off factors (see graph), published by the Central Statistical Office (GUS). The analysis of this index clearly shows that the output volume, apparently higher in the last months (particularly in October), does not result from the actual trend change but from once-off distortions, e.g. due to more business days.

In November, the manufacturing industry output decreased by 2.2%, which may reflect not only low domestic demand, but also substantial slowdown in the EU. In consequence, deterioration in exports should be expected, if not this month, then, in the following ones.

### GDP growth real, YoY

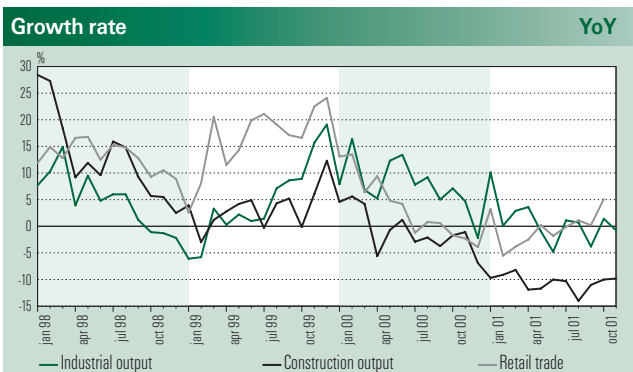
	I Q	2000			2001		
		II Q	III Q	IV Q	I Q	II Q	III Q
GDP	105.9	105.0	103.1	102.3	102.3	100.9	100.8
Total consumption	104.1	102.7	101.2	101.6	101.2	101.3	101.8
Individual consumption	104.8	103.0	101.1	101.6	101.5	101.6	102.1
Public consumption	101.2	101.6	101.4	101.4	100.1	100.2	100.6
Accumulation	110.4	105.7	101.6	101.7	86.9	87.5	85.8
Investments	105.4	102.8	102.0	102.1	101.5	91.6	86.4
Change in inventories	206.5	149.6	93.4	90.3	-229.1	-137.0	71.1
Value added	105.7	104.8	102.9	102.2	102.1	100.8	100.6
industry	109.6	109.1	106.0	102.3	103.3	98.7	98.5
construction	104.1	100.7	97.7	97.6	94.8	92.0	91.8
market services	105.2	104.8	103.1	104.0	103.5	103.7	104.1

Source: GUS, BZ WBK



Source: CSO

Also data on retail sales were not so impressive in November as a month earlier. In nominal terms, retail sales rose by 2.4% y/y and dropped by 6.4% m/m against the rise by 5.8% y/y and 6.0% m/m in October. The deepest deterioration fell on the sales figures of furniture, audio and video equipment, household appliances, liquid and gas fuel as well as on vehicles and their spare parts. This information, to some extent, may reflect the fact that in November households, willing to block as much funds as possible in a run away from „Belka’s tax” on interest income, made increased savings in long-term instruments at the expense of current consumption.



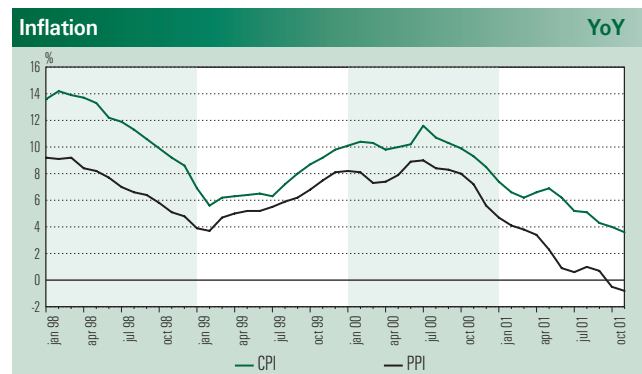
Source: CSO

### November inflation hit the bottom

In November, the inflation data once again surprised the market. CPI increased only by 0.1% m/m and 3.6% y/y, when the market expectations pointed to ca. 3.9% y/y. Such positive result was mainly due to another significant fall in fuel prices (–1.9% m/m, –15% y/y) and exceptionally low growth in food prices (0.2% against 0.4% indicated by preliminary estimates of the CSO). Nevertheless, prices of other commodities and services also grew quite slowly as a result of continuing low demand.

At the same time, in November, the deflation of producer prices deepened. PPI reduced by 0.4% m/m and by 0.8% y/y. It is worth highlighting that the prices of the sold output were under a strong

influence of fuel prices, which dropped by 5.6% m/m. In the period January-November, the coke and crude oil manufacturing products output was cheaper by 15.6% than a year ago. The share of this sector of ca. 6% in the PPI basket accounts for 1% deflation, when in the period January-November, the producer prices increased on average by 0.1%. This clearly implies that we should not be optimistic with regard to inflation and producer prices in 2002, which will grow due to the lack of fuel prices deflation and the weaker zloty.



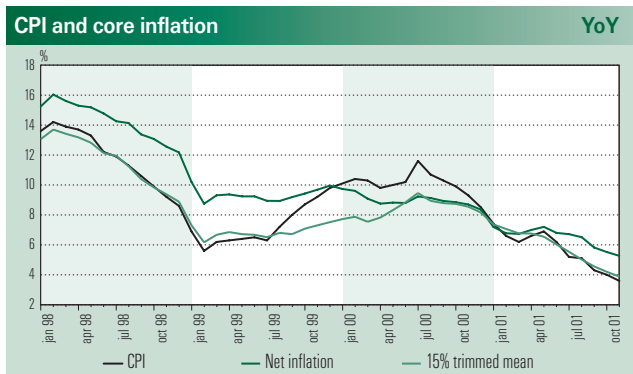
Source: CSO

We continue with our forecast that the consumer price index reached a local minimum in November (which, in principle, is also in line with the central bankers’ expectations, see pg. 10-11). In December, CPI should slightly rebound to ca. 3.7%, however, a stronger inflation growth will most probably occur in Q1 2002. This year, the “January effect” will be probably quite moderate with the growth of consumer prices on a monthly basis only slightly exceeding the all-time low 0.8% from last year. Main factors of the CPI rise in January are as follows: higher excise tax on fuel and cigarettes, higher fees for electricity as well as cold and hot water, and maybe also some growth in fuel prices as a result of the last cut in extracting limits by the OPEC. The inflation index will also go up due to reduction in discounts for bus and railway tickets from the beginning of the New Year.

Relatively good January figures should not evoke too much optimism as a great part of the inflation impulse was moved into another month. In February, we will notice the effect of higher VAT rates and a new excise on electricity. There is a possibility that it will additionally accumulate with long expected revaluation of gas tariffs and with a more active policy of the agriculture minister. The beginning of the year is important for developments on the food market due to the so-called “pigs’ low” and it is possible that meat prices will grow this year. If the activities

around the central bank will additionally weaken the zloty, we might witness a sudden reversal of the existing strong disinflation trend as early as at the end of Q1 2002.

We expect that at the end of 2002, the inflation rate will go up to ca. 5% y/y (provided that the scenario, assumed by us, of interest rate cuts, see pg 8, will materialise).



Source: CSO, NBP

### All core inflation measures went down

In November, all core inflation measures went down though this fall was smaller than 0.4% of the CPI fall (from 4% to 3.6%). All five core inflation measures calculated by the NBP ranged 3.0-5.3% against 3.2-5.5% a month earlier. Two ratios, which are most carefully watched by the MPC, the net inflation and 15%-trimmed average were higher than the main inflation rate. This confirmed the opinion of the MPC presented in the statement from the December meeting that the inflation fall in November was a result of temporary factors – low fuel and food prices, which may go up the following year.

### Slower salaries growth, employment is falling

In November, salaries rose seasonally by 2.2% m/m, and the growth on annual basis diminished to 6.6% from 7.8% in October. Employment is still falling. In November, the number of the employed in the

business sector decreased by 0.5% m/m and was lower by 4.3% than in November 2000. In November, the nominal wage bill was higher by 2% than a year ago, which gives a fall of 2% in real terms.

### Money supply rose in November by 0.4% m/m

Personal deposits grew in the last decade of November, which implies that a run away from Belka's tax at the end of November took a form of transfers between various types of banking deposits rather than the outflow of money into bonds and investment funds. However, there was some outflow and in the whole month, personal deposits decreased by PLN 1.8bn. It can be supposed that a considerable part of household savings, held so far in banking accounts, was placed in products guaranteeing a long-term protection against interest tax, e.g. treasury bonds or units of trust or investment funds. This can be proved by a clear-cut rise of business zloty deposit balances in the banking system as well as the lack of extraordinary growth in retail sales in November, signifying that money withdrawn from banks was not spent on current consumption.

### Business and household loans remain poor, their volume has hardly changed in the last three months.

The next data on December consolidated balance sheet for the banking system will be important. Just before Christmas, the media informed about higher interest in loans displayed by Poles (a number of banks are said to have run short of loan application forms). This might mean, contrary to what appears, a not too favourable consequences for individual demand if this process was an after-effect of households blocking excessive funds in "anti-tax" deposits in November and accordingly, losing their current liquidity. In this situation, possible acceleration of lending activity just before Christmas was rather a once-off phenomenon, after which, there can be further fall in consumer demand (e.g. in order to repay loans drawn for the purchase of presents).

		30.11	20.11	10.11	31.10	20.10	10.10	30.9
MoM (%)		0.4	-0.5	0.2	1.4	0.1	0.4	0.9
Money	in PLN bn	325.88	323.10	325.70	325.04	320.83	322.67	320.66
National currency		274.95	271.71	273.23	272.70	270.65	272.09	269.58
Cash in circulation		36.65	36.76	37.46	36.65	36.59	37.25	36.58
Zloty deposits total		238.31	234.94	235.77	236.05	234.06	234.85	233.00
personal		171.11	170.67	172.99	172.91	171.67	173.28	172.65
corporate		67.19	64.27	62.78	63.14	62.39	61.56	60.36
FX depos	in PLN bn	50.93	51.39	52.47	52.35	50.18	50.58	51.09
FX depos	in US\$ bn	12.46	12.52	12.90	12.77	12.23	12.16	12.06
Net foreign assets	in PLN bn	132.08	130.24	139.95	140.44	137.95	134.16	140.09
Net foreign assets	in US\$ bn	32.31	31.73	34.42	34.27	33.63	32.26	33.07
Lending to non-financial sector		225.45	226.32	223.69	224.89	223.50	224.10	225.90
to households		54.73	54.63	53.69	54.27	54.15	53.78	54.12
to corporates		170.71	171.69	169.99	170.62	169.34	170.31	171.78
Credit to general government		60.4	59.00	53.62	52.86	50.22	58.02	53.56

Source: NBP, Reuters, BZ WBK

### Low current account deficit in November, upward revision of October

Current account deficit was in October lower than expected and amounted to only USD 217m. Simultaneously, the central bank revised the October data from USD 672m to USD 838m.

Lower than expected current account deficit was mainly due to lower imports (exports were USD 2.6bn, in line with expectations) and higher than expected

Balance of payments in November				USD m
	11'01	10'01	11'00	YoY (%)
Current account balance	-217	-838	-445	-51.2
Exports	2 574	2 778	2 651	-2.9
Imports	3 524	3 953	3 512	0.3
Unclassified transactions	637	557	295	115.9
Direct investments (net)	320	1 256	539	-40.6
Portfolio investments (net)	222	268	316	-29.7
Other investments (net)	-3 234	-558	-509	535.4

Source: NBP, BZ WBK

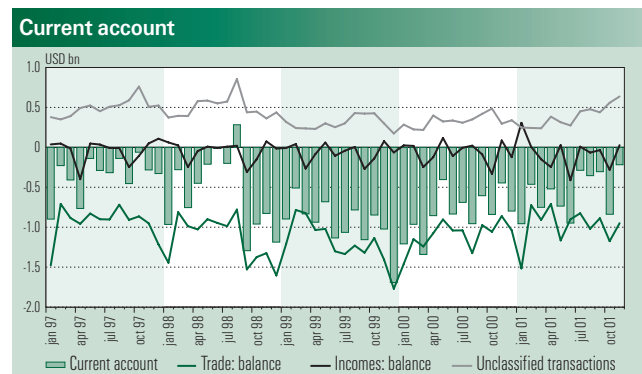
surplus in unclassified transactions. The position of unclassified transactions is a total of two elements: the difference between the purchase and sales of foreign currencies in foreign exchanges agencies and changes of banking accounts denominated in foreign currencies. In November monetary statistics, no significant growth in fx deposits was recorded, at the same time, press releases imply that households with savings in DEM, francs and other currencies, which will be converted into EURO, hurried to foreign exchange agencies to exchange cash in these currencies into PLN. We do not know what part of the surplus of unclassified transactions is related to this factor and what to the reviving border trade with the former Soviet Union countries, or more and more numerous groups of workers from Poland looking for jobs abroad. However, it seem that the EURO factor can be significant and we do not rule out the possibility that in December the surplus can reach almost USD 1bn.

One should not be too much excited about the data on low deficit. First of all, part of the improvement is not real and reflects transfer of cash in foreign currency from stockings to the registered flows. Secondly, for the first time since April 2000, exports dropped on an annual basis (fall in September

resulted from the distortion in payments after the terrorist attack of 11 September).

Capital account of the balance of payments showed a substantial capital outflow related to earlier purchase of the Paris Club debt to Brasil by Poland. However, it did not have impact on exchange rate and the zloty kept firming up despite quite a big deficit of the whole balance of payments. Generally, we might think of the Brasil transaction as of an intervention of the central bank, strengthening the zloty. Actually, the zloty rate regime is not a liquid rate regime in a handbook meaning of this notion, in which fx domestic reserves remain unchanged.

Low deficit in the current account may facilitate



Source: NBP, BZ WBK

the strengthening of the zloty at the beginning of January.

### Budget deficit reached 95% of plan in November

After 11 months of 2001, the budget deficit reached 95% of the annual plan in line with the budget amendment introduced by the Lower House in July this year. Budget revenues were PLN 127.8bn, i.e. 83.8% of the plan. Expenditures amounted to PLN 155.5bn, i.e. 85.6% of the plan (before the second amendment). The deficit rose to PLN 27.68bn.

A key issue is the revenue side of the budget. Recent forecasts of the finance ministry indicated PLN 141.5bn revenues for the whole 2001, which is PLN 11bn less than assumed in the revised budget. This would imply a shortage in the budget of PLN 2.5bn in relation to the planned level, even taking account of the expenditure freeze of PLN 8.5bn,

### Estimated revenue shortage after corresponding month

PLN m

2001	I	II	III	IV	V	VI	VII	VIII	IX	X	XI
Total	8 472	10 708	12 901	10 612	13 254	8 685	8 782	9 712	9 570	10 147	11 246
Indirect taxes	13 806	5 973	7 516	6 785	6 060	7 276	6 343	5 898	6 142	5 795	5 280
CIT	-553	702	2 493	2 038	1 523	1 851	2 578	2 661	2 762	2 822	3 191
PIT	1 056	2 337	2 407	588	1 962	1 872	1 804	1 923	1 943	2 008	2 028
Budget Entities Income	-10 846	-744	-2 925	-1 573	1 509	51	40	658	-211	212	963
Import tariffs	289	584	734	685	815	778	758	762	769	722	742

Source: BZ WBK calculations

made in October. Although minister Marek Belka said earlier that some savings might be achieved due to lower than the earlier assumed foreign debt cost (mainly due to the strong zloty) and moreover, additional income from NBP profits can be expected, some other expenditure cuts might turn out necessary in order to achieve the target of PLN 29.1bn (or PLN 33bn after the second amendment). This will probably mean "creative budgeting" rather than real expenditure reduction, with transfer of some of payments to the beginning of 2002. It is difficult to imagine some effective expenditure cuts in the last weeks of a year – probably most of budget units have already spent their planned expenditures.

The picture painted by the November data does not look more promising than in the previous month. Although there is some improvement, as far as collection of direct taxes and PIT is concerned (annual variance grew in both cases), shortages estimated in other areas are increasing, i.e. business taxes, budget unit income and customs duties (see table).

We estimate that if the situation in December is not significantly different from the current trend, budget revenues for the whole 2001 will be lower by ca. PLN 11bn, which confirms the finance ministry forecasts.

That is why it looks that the finance ministry will have to find some additional PLN 2.5bn savings in order to close the planned budget deficit.

However, looking at expenditures in November, it is difficult to notice any clear signals of freezing October expenditure. After 11 months, the growth in budget expenditures speeded up to 12.8% y/y from 11.4% in the previous two months. This data is supported by sudden growth in donations to Social Insurance Fund (FUS) and the Labour Fund, as well as general subventions for local government units.

Very little room is left for December expenditures, assuming that the revenues will reach PLN 141.5bn. In this case, December expenditures should not

exceed PLN 15.15bn (excluding the repayment of commitments introduced in the second amendment), in order to fit in the planned deficit level, which implies a fall of  $-0.4\%$  m/m. And this is a really difficult challenge as the monthly expenditure growth in December was always at a two digit level in previous years, usually closer to 20% rather than 10%.

Summing up, we see few chances for the deficit level to fit in the planned amount without resorting to creative budgeting. Probably, some payments will be transferred to the beginning of 2002 and / or a sudden cut in government subsidies will be made in December, leading to accumulation of budget units indebtedness at the end of 2001. The effect of such actions would be positive for quantitative image of the budget deficit, but catastrophic for the economic deficit and budget liquidity at the beginning of 2002. Indeed, recent information from the finance ministry implies that the supply of treasury securities in Q1 2002 will be record-breaking.

Budget revenues and expenditures growth											(YoY, cumulative)
2001	I	II	III	IV	V	VI	VII	VIII	IX	X	XI
<b>Revenues</b>	5.9	3.5	1.9	3.7	1.6	5.5	5.5	4.8	5.0	4.6	3.9
Indirect taxes	-5.6	1.5	-0.6	0.2	1.3	-0.1	1.1	1.7	1.4	2.0	2.6
CIT	15.2	-8.6	-18.8	-15.5	-13.2	-16.6	-20.5	-20.2	-20.5	-20.4	-21.9
PIT	6.4	0.1	-1.7	7.9	1.1	1.0	1.4	1.3	1.5	1.6	1.9
Budget Entities Income	191.9	46.1	65.3	52.6	25.5	37.8	37.8	32.3	40.1	36.3	29.4
Import tariffs	-12.7	-18.8	-20.4	-19.3	-21.3	-20.6	-20.1	-20.2	-20.4	-19.4	-19.9
<b>Expenditures</b>	41.4	32.9	22.9	22.2	18.2	15.3	14.1	12.2	11.4	11.4	12.8
Domestic debt serv.	75.5	16.4	37.9	33.6	29.3	21.9	18.5	11.9	11.6	12.5	12.5
Foreign debt serv.	40.0	31.2	-43.1	3.9	5.3	1.5	2.2	2.4	-7.6	-12.4	-11.9
Labour fund subs	133.6	123.5	250.5	318.1	286.6	241.9	205.9	185.0	161.5	145.1	154.7
KRUS subsidy	31.0	22.5	17.7	19.5	16.1	11.8	16.0	13.7	13.7	12.9	12.7
FUS subsidy	171.0	138.3	81.3	61.8	63.1	48.9	45.6	34.4	32.2	31.1	42.0
Local govt. subsidies	11.4	11.1	9.9	16.5	16.3	15.2	14.8	13.5	13.0	12.8	13.9

Source: BZ WBK calculations

## Central bank watch

- No rate reduction in December resulted in further sharpening of attacks on the MPC
- Another rate reduction expected in March... although an earlier cut cannot be ruled out .

### Rates without changes, the central bank under siege

In line with our expectations, and with the financial market anticipations, the Monetary Policy Council did not reduce interest rates at the December meeting. In the formal communication, the MPC presented a list of arguments for and against the rate reduction. The members admitted that inflation was below expectations, and the loan demand and economic activity remained low. However, at the same time, they pointed to a sudden drop in personal deposits in November, higher inflation expectations of personal customers and higher than expected economic deficit. The MPC also stated that a sudden drop in inflation to 3.6% in November from 4.0% in October partially results from factors, which may be temporary, such as low food and fuel prices (according to the MPC, food and fuel account for 58% of the inflation fall).

Just after the MPC meeting, the zloty started firming up quickly. As it could be expected, politicians, for whom it is a priority now to weaken the zloty by some 15-20%, reacted immediately. Representatives of the government coalition thoroughly criticised the lack of a rate cut. At the end of December, proposed changes to the NBP act, prepared by PSL and UP, were submitted to the Lower House. They assume increasing the number of MPC members by 6 and completing the central bank's policy by objectives to support economic growth and reduce the unemployment.

### Time for male talk, i.e. the MPC with their backs to the wall

The government announced that before it gives their opinion on the draft of legislative changes by UP-PSL, they would like to meet with the MPC not later than on 12 January in order to discuss possible ways of reviving economic growth. According to the Deputy Prime Minister, Marek Pol, it was to be a really „male talk“.

Regardless of whether the following rate cuts are currently justified or not on the economic ground, we are of the opinion that the growing pressure of the government on the MPC is harmful for reaching a reasonable compromise on this issue. It draws the central bank into a political game and creates a

situation, in which, regardless of what the actual MPC decision will be, it will be viewed as inappropriate and politically motivated. If the Council reduces rates just after the meeting with Leszek Miller cabinet, everybody will notice the submission to the government pressures, even if deteriorating economic situation would justify such a decision. However, maintaining rates at the unchanged level can also be assessed as lack of professionalism, proving that „personal factors“ and caring for their own image is more important for central bankers than economic arguments.

### Another reduction earliest in March...

At present, forecasts of further interest rate changes are burdened with uncertainty not only with regard to the development of the economic situation, but also further developments of political coup on the central bank. Currently, the financial market expects a rate fall of 100-150 bp in January, possibly in February 2002. And although, in our opinion this option cannot be entirely ruled out, in the base scenario we assume that the MPC headcount will remain unchanged in Q1 2002, and the rate cut will take place in March or at the beginning of Q2.

It seems that finally, changes in the NBP act should not be put in place as SLD certainly realises that this type of actions may put obstacles in the way of our integration with the European Union. Probably this is the reason why SLD will not support the PSL-UP proposal in parliamentary votings. Even if it does not happen (for example, as a result of striking a bargain between SLD and PSL: land for the central bank), one can expect that President will be the guarantor of the MPC independence. In the case of the parliament accepting the changes, President most probably will send the proposal to the Constitutional Tribunal.

Economic arguments will rather speak for refraining from another rate cut until the end of Q1 2002. Economic activity should not deteriorate further (although there should not be any clearer revival until the end of Q2), inflation most probably will rebound in the first months of the year, inclination of households to save may diminish along with banking deposit interest rate reductions and the introduction of capital gains tax. An open attack of politicians may lead to further sharpening of the MPC members stance – they may refrain from interest rate reduction in order to emphasise their independence from political pressures.

### ...unless earlier

However, this scenario is associated with distinctive threats. The first one – probably the most important one – is the zloty exchange rate. Appreciation on



such a scale as has occurred in the last few weeks seems impossible to be continued, and this is both for economic and political reasons. If the growing economic risk (growth in current account deficit and inflation) or political risk (coup on the MPC) will not manage to weaken the zloty, the central bank may have no other choice but reduce interest rates in order to cut a speculative play of the foreign capital. It will be the so much easier to take and justify the decision on the reduction, if this is in accordance with the market consensus.

Another risk factor is the legislative initiative intending to change the MPC headcount. The support for limitation of the central bank's independence is very broad in the parliament, and although we do not consider it a very probably scenario, the proposal may, however, gain the support of the majority. Newly appointed Council members would certainly pass rate reductions as quickly as possible. However, it seems that if the parliament chose an option to increase the number of Council members, the process of selecting new members would take some time, for example, as a result of the President's decision to check the compliance of this provision with the Constitution.

#### **Scale of reductions in 2002 will not be large**

As so far, the economy has not yet fully experienced the effects of previous interest rate reductions (by 7.5% in total from the beginning of 2001). However, the impact of these reductions, though with delay, will finally start to be noticeable. Most probably, it will overlap with a gradual improvement of global economic situation, including our main trading partners, inflation rebound due to non-monetary factors and maybe weakening of the zloty. Therefore, the MPC must be particularly careful with further loosening of the monetary policy. Reducing rates until the moment when clear economic revival signs are visible may cut them to the level threatening macroeconomic stabilisation and result in the necessity to return to the cycle of restricting the policy in the near future.

It seems that the MPC realises this threat, which is visible in the contents of announcements and comments of the Council members in the last months. Therefore, we expect that during the whole 2002, the main NBP rates will not drop deeply. We forecast that the referential rate will be reduced by 2.5%, to 9% at the end of 2002. The cut of the lombard rate can be slightly deeper, narrowing in that way the range of fluctuations of inter-bank market rates along with reducing interest rates to a one-digit level and

continuing reduction of over-liquidity of the Polish banking system.

# Comments of the Monetary Policy Council members

In their December commentaries, the Monetary Policy Council members tried to highlight their independence in taking decisions on interest rates. Even "friendly" members of the MPC (Ziółkowska, Rosati) protested with determination against the government pressures on the Council. Simultaneously, the Council rejects accusations of not supporting economic growth, addressed to them by the government. The MPC members explain to their critics that after a few reductions of interest rates, one should patiently wait to see their effects. Another reason for the Council abstaining from further rate reductions is concerns about inflation rebound next year. The quoted commentaries of the MPC members allow us to conclude that another interest rate cut is possible not earlier than at the end of Q1 2002. Representatives of the MPC also commented the current data on inflation and economic growth, formulating at the same time their forecasts for the future.

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**WHO? WHAT MEDIA? WHEN?**
**QUOTE**

Dariusz Rosati, MPC member,  
 Radio Zet, 5 Dec

"This kind of statements create market expectations. Yesterday PM's speech caused zloty appreciation. (...) It's obvious, because market expects that because of these threats MPC could lower the rates, and if there is a perspective of rate cut the capital flows to Poland and zloty appreciates immediately. It's not helpful to our exporters. It shakes the foreign exchange market and is definitely unnecessary in our situation, because zloty is already strong enough. (...) This kind of comments are unnecessary because they create difficult situation for MPC. Even if it wanted to lower the rates, doing this would make the impression that it bends over political calls. (...) In its decisions the MPC takes into account essential issues, solid analysis of [economic] situation, and even if one can have objections to MPC decisions, political issues will at no chance be taken into consideration in making interest rate decisions."

PAP, Rzeczpospolita, 17 Dec

"Inflation figure is a surprise for me. I thought that inflation would inch up since November. Market expected 3.9-4.0%, and similar were MPC's forecasts. It means that the situation is more disinflationary than we thought and in conjunction with low demand data it creates new situation. It looks like we are entering the classical recession and the demand didn't react to interest rates cuts. On the other hand we have to be cautious and consider that these rate cuts made so far may fire up at some time. (...) In December 2001 inflation shouldn't exceed 4% and the maximum inflation rebound in 1H02 should amount to 4.5-5.0%."

"After CSO figures I am more comfortable about recession possibility. I estimate that economic growth in 4Q01 and 1Q02 should amount to 0.5-1.0% and it will be bigger in second half of 2002, which will imply GDP growth in 2002 at above 2%. (...) This year GDP growth will probably reach 1.5%."

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Janusz Krzyzewski, MPC member,

PAP, 6 Dec

"Interest rates should remain flat for several months, also to let MPC members judge the risk of inflation rebound next year."

PAP, 17 Dec

"The 0.8% figure is less troublesome. It's better than some people expected, but in general it's bad. (...) In 4Q01 GDP growth might be slightly better than in 3Q01 and it could amount to some 1%. I expect economic growth in 4Q01 to stabilise or to increase slightly."

"One should not expect significant growth in Poland separately from growth in other countries. Significant growth can be expected in second half of next year."

PAP, 19 Dec

"There are no fundamental reasons for the zloty to weaken. Even possible limited worsening of the current account deficit compared with a giant treasury papers issues will not weaken the zloty".

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Wiesława Ziolkowska, MPC member,

Gazeta Wyborcza, 7 Dec

"I wasn't appointed to this post to surrender to the pressure of whatever Prime Minister and whatever government. MPC independence is guaranteed in the constitution. (...) The government seeks the scapegoat in MPC. Maybe PM's comments result from political game with PSL. Wish it wasn't at MPC's reputation expense. Although this pressure is more harmful to PM's reputation than that of MPC."

Puls Biznesu, 7 Dec

"One who expects the rate cut today, might be presumed unaware of macroeconomic consequences of such decisions like 300bp rate cut practically in one month or interest income tax introduction. Some banks already have interest rate on deposits below inflation rate. Further rate reductions could trigger dangerous fall in households' propensity to save, therefore disabling the return to long-run balanced growth path."

"PM said many times that public institutions should not communicate through media. I wish he applied this rule with regard to MPC. (...) Discussion in media is a good way of persuasion for those with little economic knowledge. It's definitely not the right way to promote economic growth."

"GDP fall is possible, not only in 1Q02 but also in 2Q02."

PAP, 17 Dec

"Polish foreign reserves exceed USD28bn and ensure Poland's solvency, and they will prevent us from Argentinean scenario for sure."

PAP, 19 Dec

"In 4Q01 GDP growth will reach 0.3-0.4%, and 1% in the full year"

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Cezary Jozefiak, MPC member,

Życie, 6 Dec

"There are gossips that the draft of changes [to central bank law] is already reconciled between coalition members. For me further expectations for rate cuts, after they've been reduced considerably in whole year, sound ridiculous."

Puls Biznesu, 7 Dec	<p>“Such hard pressure – in spite of two rate cuts in 30 days – ensure that the gossips about limiting central bank independence may not be anecdotal only. The government wants to gain control over monetary policy. I think we should wait for effects of MPC past decisions. Now any further decisions must be cautious.”</p> <p>“The basis for MPC decisions will be the expected development in savings and inflation expectations in Poland during next few months.”</p>
PAP, 11 Dec	<p>“This year we’ve cut the rates by 750bps, of which 300bps in last two months, and now I hear that MPC doesn’t want to co-operate with government to stimulate economic growth. (...) This means that they will exploit every opportunity to change the central bank law in a way to let government influence interest rates. This would have fatal consequences not next year, but in future years.”</p>
Reuters, 12 Dec	<p>“In economy that has inflation rate still higher than in countries it tries to converge, and that still has significant external imbalance, such procedure [increasing domestic demand] implies the risk of inflation impulse. (...) As regards domestic demand stimulation, I would prefer if it was like in the US, i.e. through lowering taxes.”</p>
PAP, 13 Dec	<p>“Exchange rate is also the result of the harmony between fiscal and monetary policies. If there is no such harmony, the problem arises if one should try to rescue by interventions this, what is a consequence of other factors.”</p>

Leszek Balcerowicz, NBP governor;

Reuters, 19 Dec	<p>“Zloty strength in recent two days was probably caused by shallow FX market, in which one transaction could trigger a series of transactions and lead to a transitory appreciation. (...) Secondly, also forint and koruna has appreciated amid recent Laeken UE summit results suggesting that 10 countries may be admitted to the EU. (...) Please note, that if we have large deficit, and large treasury papers issues it invites portfolio capital and this appreciates the zloty. If someone is worried about the zloty strength, he should also be worried about the shape of the public finances”</p>
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## INFORMATION ON THE MEETING OF THE MONETARY POLICY COUNCIL ON 18-19 DECEMBER 2001

The Monetary Policy Council held its meeting on December 18-19, 2001. The Council was submitted the materials prepared by the Management Board and departments of the NBP and information and analytical materials prepared by the Ministry of Finance, banks and research institutes. On this basis, the Council discussed inflation; tendencies in the area of money supply, lending and interest rates; external conditions and the situation in the balance of payments, real sector of the economy and in public finance sector.

### I. Inflation, inflation expectations.

1. The consumer price index on the twelve-month scale lowered from 4.0% a month before to 3.6%. However, 58% of this drop are justified by the factors that may be temporary, i.e. changes of foodstuffs and fuel prices.
2. In November this year, the sold industrial output prices were lower by 0.4% than in October this year (a month before they lowered by 0.6%). The biggest price drop has been noted in the production of coke and the petroleum refining products (by 5.6%). As compared to November 2000, the industrial output prices lowered by 0.8%.
3. In the survey made at the beginning of December this year, the future inflation expectations of individuals worsened. The percentage of the most pessimistic individuals forecasting that the prices will grow faster than currently increased by 6.2 percentage points (to 20.0%). The remaining groups of the surveyed with more optimistic expectations decreased.

***The inflation rate expected by bank analysts at the end of the year lowered from 4.2% a month before to 4.0%. The inflation expected in the 11-month horizon lowered by 0.1 percentage point and amounted to 4.7%.***

***In November this year, the growth pace of consumer goods and services prices decreased on the twelve-month scale. However, it mainly resulted from factors that may be temporary - changes of foodstuffs and fuel prices. The sold industrial output prices were lower than a month before and lower than a year before.***

***In December this year, the future inflation expectations of individuals worsened. The inflation expectations of bank analysts were subject to further decrease.***

### II. Money supply, loans, interest rates.

1. The nominal growth pace of total money supply (M2) on the twelve-month scale lowered from 13.1% in October to 11.9% in November this year.
2. In November this year, the total amount of household savings at banks decreased by PLN 1.8 billion as compared to October this year. PLN-denominated deposits placed by businesses increased by PLN 4.1 billion. The dynamics of PLN-denominated deposits placed by individuals on a twelve-month scale lowered from 19.0% in September and 16.8% in October to 13.4% in November this year.
3. In November this year, the annual dynamics of total lending lowered from 8.7% a month before to 8.1%. The drop of the dynamics has been noted in case of both the loans to households (from 16.4% to 15.9%) and to businesses (from 6.4% to 5.9%).

***For the first time since 1997 a monthly drop of PLN-denominated deposits of individuals has been noted. First of all, it is a result of the introduction of bank placements income tax. In order to escape from the taxation, individuals transferred their resources to the other forms of saving (bonds and investment funds). As a result of banks' actions to counteract the money outflow from the banking system, the savings placed at banks have been shifted to long-term placements. In November this year, the total amount of funds held by businesses at banks increased.***

***The demand for loans is still at a low level. In November, the dynamics of total money supply decreased.***

### III. External conditions.

1. There are maintained the forecasts indicating that the boom in the world economy will probably take place in the second half of 2002. In the 4th quarter this year the GDP drop is possible for both the United States and the euro zone.
2. The forecasts for the petroleum prices on the world markets did not change.

**There are maintained the forecasts indicating that the boom in the world economy will take place in the second half of 2002. It means worse outlooks for the Polish exports. At the same time, it is a factor that reduces the inflation pressure. Since the last meeting of the Council, stable are also forecasts for petroleum prices on the world markets.**

#### **IV. Balance of payments, exchange rate.**

1. Within the period January-October this year, the current account deficit amounted to USD 6.0 billion and was lower by USD 2.7 billion than in the same period last year. Exports were bigger by 10.5% than within the period January- October 2000, while the dynamics of imports amounted to 2.6%.
2. In November this year, the exchange rate of the zloty strengthened against both the euro (the average exchange rate amounted to PLN 3.64 as compared to PLN 3.74 in October this year) and the dollar (PLN 4.09 as compared to PLN 4.13 a month before).

**The improvement of the current account balance indicates the strengthening of the external balance of the Polish economy. The observed strengthening of the exchange rate of the zloty mainly results from the inflow of foreign capital invested in Treasury securities.**

#### **V. Supply, demand, situation on labor market and income.**

1. In the 3rd quarter this year, the Gross Domestic Product was lower by 0.8% than in the 3rd quarter last year. In real terms, the domestic demand was lower by 2% than a year before what was mainly caused by the drop of gross investments in fixed assets by 13.6%. Faster than in the 2nd quarter was the growth of individual consumption (2.1% as compared to 1.6%). The negative net export decreased to PLN 4.8 billion from PLN 7.7 billion in the 2nd quarter and PLN 10.1 billion a year before.
2. In November this year, the sold industrial output was lower by 0.8% than a year before. The construction and assembling production was lower by 9.8% than a year before.
3. The employment in the enterprise sector lowered in November this year by 0.5% as compared to October this year and it was lower by 4.3% than a year before.
4. Within the period January-November this year, average wages in the enterprise sector were bigger by 7.3% in nominal terms and by 1.6% in real terms than within the same period last year.

**A low level of economic activity has been maintained. Within latest months, due to the drop of inflation, the growth pace of wages in real terms in the enterprise sector accelerated.**

#### **VI. Situation in public finance sector.**

**The economic deficit of public finance sector in 2001 will be bigger than it was forecasted before and it will amount to approximately 5.2% GDP.**

**Since the last meeting of the Monetary Policy Council, the evaluation of the situation in public finance sector in 2002 has not been changed: the project of the budget for 2002 raises concern about its impact on a future economic growth and the possibility of the improvement of fiscal and monetary policies scheme.**

**Some legal solutions contained in the budget-related acts which decide on the final shape of the budget for 2002 constitute a step in the right direction. However, their scale is not sufficient for a permanent solution of public finance sector problems.**

**The enactment of budget-related acts by the Sejm should be treated as a confirmation of earlier information on the shape of the state budget for 2002.**

#### **VII. Decision of the Monetary Policy Council.**

1. The Monetary Policy Council wishes to remind that in 2001 it cut the interest rates by 7.5 percentage points in total. The full results of cuts, especially these made in October and November by 3 percentage points in total, have not been revealed yet.
2. At the same time, there are maintained sources of uncertainty:
  - Situation in public finance sector in 2002 and 2003. The enactment of some budget-related acts by the Sejm increases the probability that the budget for 2002 will be consistent with the project of the government. However, this information has already been taken into consideration by the Monetary Policy Council.
  - Savings income tax impact on the tendency to save. The introduction of tax on bank placements income will put the level of deposit interest closer to the level of inflation what may lead to a drop of tendency to save.
  - The scale of necessary structural reforms that will be made.
3. The new data that appeared since the last meeting of the Monetary Policy Council are of different nature. On one hand:
  - Consumer price index lowered to 3.6%, however, a considerable part of this drop is justified by factors that may be temporary, i.e. changes of foodstuffs and fuel prices;
  - Sold industrial output prices were lower than a month before and lower than a year before;
  - The dynamics of money supply and lending decreased;
  - The forecasts of economic situation worldwide and petroleum prices did not change;
  - A low level of economic activity is maintained.

On the other hand:

- Future inflation expectations of individuals worsened;
- For the first time since 1997, a monthly drop of PLN-denominated deposits of individuals took place that mainly resulted from the enactment of the act introducing bank placements income tax; the decline of deposits was not prevented by banks offering long-term placements;
- The economic deficit of public finance sector in 2001 will be bigger than it was expected earlier.

**Considering the 3 mentioned above reasons, the Monetary Policy Council decided to maintain the parameters of monetary policy at the actual level, i.e. maintain the basic interest rates of the NBP and the neutral position in monetary policy.**

#### **VIII.**

**According to the Guidelines of Monetary Policy for 2002, the Monetary Policy Council made a decision to lower the obligatory reserve ratio from the level of 5% to 4.5%. This decision will not result in the increase of banking sector liquidity as very soon the Management Board of the NBP will make a decision on the liquidation of possibility to hold the obligatory reserve in vault cash by banks. This decision constitutes an element of adjustment to the standards of the European System of Central Banks.**

**At the same time, the Council adopted the Financial Plan of the National Bank of Poland for 2002 that provides for the exchange of NBP bonds issued due to the cut of obligatory reserve ratio in 1999 into market interest bonds.**

#### **IX.**

**The next meeting of the Monetary Policy Council will be held on January 28-29, 2002.**

## Government and politics

- The first success on the way towards a new 2002 budget: first budget-related acts adopted
- The public opinion polls held in December indicate a drop in the trust in the Government
- It is still an open issue, whether the loss of popularity will weaken the Government's drive to reform the public finance sector and labour market

### The Parliament has adopted budget-related acts

In mid-December the Lower House of the Parliament adopted, without any significant amendments, budget-related acts tabled by the Government. Within a few days the package of acts was also adopted by the Upper House of the Parliament) and signed by the President, which made it possible for the acts to become effective at the beginning of the new year. The acts introduce stricter criteria that have to be met in order to be entitled to social benefits, they freeze teachers' salary, reduce or eliminate some subsidies, freeze finances allocated for the health care. The total savings of this package are estimated at ca. PLN 8bn, and expenditures arising from social benefits has been reduced by PLN 2.5bn.

It seems that Prime Minister Leszek Miller is capable of ensuring political support for Finance Minister Belka's economic program. The first step in the right direction has already been taken; the next important date is February, when Marek Belka will propose a medium-term plan for reviving the economy.

Economists love making comparisons, therefore I would like you to consider the following facts. According to the Chinese calendar, the year of 2002 will be a year dedicated to a horse, and the last year dedicated to a horse was 1990. In that year Prime Minister **Mazowiecki** supported the Finance Minister **Balcerowicz** who introduced a reform plan which was a foundation for healthy economic development for the following years. It seems likely now that Prime Minister **Miller** will similarly support Finance Minister **Belka** who is also introducing a reform plan, so the year of a horse can once again be a time of economic growth.

Still, one word of warning seems indispensable here. Some savings provided for in the package of budget-related acts are only temporary. For example, the rise of teachers' salary has been postponed till next year, and similarly the freeze of finances allocated for the health sector will be the implemented only in 2002. Therefore, similar

problems can revive next year, if Belka's medium-term plan fails to reform social spendings and budget subsidies. The plan can also fall through if it is not accompanied by a faster pace of privatization, especially in such sectors as mining, metallurgy, railway, power industry.

### December polls – the Government's decreasing popularity

According to Demoscope (Public Opinion Research Agency), 44% of pollees did not approve the Government's actions in December which translates into a 14% increase in the social discontentment in comparison to November. 32% of pollees approved the Government's policy (a 1% decrease). 29% of respondents were against the Prime Minister Leszek Miller (a 4% increase) whereas 45% of respondents approve his actions (a 2% decrease). Social support for President Kwasniewski also decreased: 67% of pollees declared their approval of Kwasniewski (a month ago: 75%).

According to the OBOP institute (Public Opinion Research Center), in December the support rate for the Government declined to 30%, and the percentage of people dissatisfied with the Government sprang up to 38% (!). In November 33% of pollees approved the Government and 15% were against it.

The CBOS institute (Social Opinion Research Center) reports that the governing parties' popularity is rapidly decreasing. SLD-UP is supported by 39% of pollees, whereas a month ago the percentage of supporters was 45% (the parties had a 41% vote in September elections). The support for PSL dropped from 8% in November and 9% in September elections to 7%.

It is clear right now that post-election "honeymoon" has come to an end. The drastic decrease in the Government's popularity is probably a result of a very controversial decision to introduce interest income tax adopted in November. The support for the Government is likely to decrease even further due to the latest unpopular decisions to cut social expenditures and freeze salaries in the public sector. Now we can only wait and see whether the Government will continue its policy and introduce painful but necessary reforms. The main unresolved issue is whether such a decline in popularity will weaken the Government's drive to reform public finance and labour market. It is obvious that short-term political interests will lead to quite different decisions, as elections for local governments will probably be held in spring. Answers to all these questions will be found in the Minister Belka's medium-term plan which is to be presented in mid-February.

# Statements delivered by members of the Government

In their speeches members of the Government first of all touched upon the issue of the Monetary Policy Council and came up with proposals to limit its independence (increasing the number of its members, additional objectives). The Finance Minister, despite his disapproval of the MPC decision, is against such type of proposals.

WHO? WHAT MEDIA? WHEN?	QUOTE
Leszek Miller, PM PAP, 4 Dec	"There is a solid foundation, also in budget draft, for interest rate reduction. If MPC doesn't do that, the conflict between MPC and the government will arise, and only parliament could resolve this conflict." "It can't be that an important institution responsible for adequate economic policy may consider itself released from the responsibility and from the participation in public finance recovery process."
Polish Radio 3, 7 Dec	"To prop up the economy, to improve living conditions of millions of Polish households, we need pro-growth stimulus and we need lower interest rates for that. If that stimulus is not delivered then it means that we have a conflict between the MPC and the cabinet, which can be only resolved by parliament. (...) It is a question of a path that will be chosen by the parliament. But we cannot tolerate a stalemate [between the central bank and the government], which hurts the economy."
Marek Belka, deputy PM, finance minister, PAP, Reuters, RMF FM, 3 Dec	"In budget assumptions the revenue from interest income tax was much lower than PLN2bn, which we estimated when considering this solution. We didn't know how efficient will be banks' offer of so-called 'anti-tax' deposits. (...) Today we can say that long-term deposits captured some one twentieth of total banking deposits and the budget revenue shortfall because of this will not be significant. Therefore PLN1.35bn is underestimated and we can safely increase this number."
PAP, 4 Dec	"In 1Q02 the government will present the overall economic programme for the present parliament tenure. It will present whole complex of measures aimed at stimulating economy. The budget presented today is the first step on this right path."
PAP, 6 Dec	"Import tax as a part of the budget means immediate pressure to spend the extra revenues, which would imply that whole public finance strategy that this government is starting, would disappear. (...) It would be possible to introduce import tax as an extraordinary measure in case of emergency, but outside the budget."
Reuters, PAP, 12 Dec	"We will acquire missing funds [privatisation revenue] on capital market. If I had trouble, I would hesitate with second budget amendment. Budget liquidity is secured. We wouldn't have pursued earlier repayment of liabilities, if we didn't have enough funds." "The result of backing off VAT increase in construction was that our tax revenue projections, initially cautious, became less conservative. (...) Although we introduced some offsetting solutions, this creates some pressure on revenue side of budget next year. The safety margin narrowed." "Although budget liquidity is not endangered, situation will be more difficult because in 1Q02 the demand for capital on Polish market will have to increase, which would probably stop extremely fortunate downward trend of market yields." "Repayment of liabilities due will make budget liquidity situation more difficult around the turn of the year. (...) We plan to make it in such way that budget liquidity is not endangered."
PAP, 13 Dec	"There is huge sucking for Polish papers on international markets. Our unofficial rating is much better than that granted by rating agencies. (...) Poland is regarded as future EU member and the country that experiences difficult moments but has solid foundation as regards the solvency." "At the moment there's big scarcity of Polish [foreign currency] papers on the market and paradoxically, the bigger the supply would be, the easier it would be to place them. We are far from the moment when the problems with demand on Polish papers could arise. (...) So far markets demand more papers, because when there's too little of them, they are illiquid. Therefore meanwhile we would have a rent allowing placing Polish papers safely and probably under improving conditions. (...) For Polish foreign currency papers European market is natural. It's important that Polish papers have liquidity. (...) " "We would have to make massive foreign debt restructuring. (...) It takes place already, the example being early repayment of Brazilian debt or Brandy bonds buy backs. (...) I think this [massive debt restructuring] may happen after EU decisions that will probably be made until the end of next year. Therefore I don't rule out that it would happen before Poland's accession to EU, before 2004. (...) The operation will partially include the shift of payments to future years, but it will bring about the increase of current debt servicing costs, while at present interest payment costs are relatively low." "We have to assume that Polish economy wouldn't grow at the rate equal to statistical error during next years. Public debt amounting to 51% of GDP is nothing terrible. It would be terrible if public debt in relation to GDP increased very quickly for several years. (...) If it happens that we have zero growth, then indeed we could easily be in trouble. I don't forecast such situation to happen." "Zloty devaluation by several percent would give some oxygen to exporters. One could expect some weakening next year. Looking at past years after very sharp appreciation there is relaxation and one should expect this right now. There will be no huge privatisation flows any more. (...) Short-term capital will have no speculative incentives for treasuries purchase." "After introducing euro in cash, there might be psychological effect of euro strengthening against US dollar. We wish it happened very much. It would be very positive from polish exporters' point of view."

- "I'm afraid that if next year there will be some rebound and CPI inflation rate will start to grow slowly from 4% or even 3.5% to 4.5-5.0%, the MPC will tighten monetary policy although inflation will be still within the target. (...) I think that in case of inflation rebound it should be allowed to rise freely to 5%. (...) In regard to medium-term inflation target, we fulfilled the plan two years before the schedule. Now the problem is to keep CPI from falling to 3%, because we have clear downward trend. From producers' point of view we have deflation. (...) If next year there is economic recovery, inflationary impulse will be gentle, or there will be none."
- PAP, 19 Dec "It's not standard situation when Polish economy grows at 0%, 0.5% or even 1.5% a year. Economy like ours, catching up economy, where labour efficiency grows, have foundations for 4-5% growth."  
„This is a bad decision because economic data supports rate cut. Economy is on the verge of recession. We experience deflation of producer prices.”  
„It is not a surprise for the finance ministry. There is hope that rate cut decision will be made next month.”  
„There is a tendency in Sejm to limit the Council independence. Such proposal may be backed by majority in present circumstances. [...] Today's decision gives an argument to persons supporting such proposals.”
- PAP, 21 Dec “Definitely, I am a defender of MPC's independence. However I don't say I never criticise its decisions. This is one of the institutions that is an achievement of our transformation and we should protect it.”  
“I am sure that even if we increase a headcount of the MPC by six new persons, the present members will consolidate and have majority. Moreover, it is not guaranteed that new ones will be against present policy.”  
“International reply will be stronger than the weight of this issue. I think we will back off from the idea, but with some political and reputational losses.”  
“MPC mainly looks into the future, while the government must consider the fact that present economic situation is bad and if it does not improve there will be serious results for society and EU accession.”
- 
- Wieslaw Kaczmarek, treasury minister,  
PAP, 5 Dec “Public offer of PZU S.A. will be crucial for privatisation revenues in 2002. Common sense dictates that 5-10% of PZU should be offered.”
- 
- Halina Wasilewska-Trenkner, finance deputy minister,  
PAP, 6 Dec “We estimate that introducing excise tax on electricity will cause the year-average inflation to rise by 0.3-0.4 pct. point at most. It will happen if producers pass all the excise tax to final customers. If not, the impulse will be weaker.”
- 
- Jaroslaw Kalinowski, deputy PM, agriculture minister;  
Reuters, PAP, 12 Dec “The best solution would be to make changes in monetary policy and to impose the import tax at the same time. But the government will analyse this issue further and it will make appropriate decisions.”  
“PSL doesn't believe that MPC will start to co-operate with government on economic improvement. (...) Therefore legislative changes are necessary, I mean the central bank charter amendment, which would allow for change of central bank objectives, to make NBP responsible for growth and unemployment.”  
“At present zloty exchange rate is not determined by economic developments but by external investment funds, which benefit because Poland has the highest interest rates in the world. (...) We think that central bank law amendment should aim at making exchange rate real. This would allow our economy to rebound from the bottom.”  
“There must be such change in monetary policy to weaken the zloty. (...) Today US dollar should cost almost 5 zloty.”  
“PSL is not going to cancel any constitutional guarantees for MPC.”
- 
- Stanislaw Stec,  
SLD deputy, deputy chairman of the Public Finances Commission;  
Gazeta Wyborcza, 14 Dec “The zloty is too strong, which ruins our exports. (...) It would be enough, if MPC cuts one-off interest rates by 4-5 percentage points announcing at the same time that rates will stay at this level for next 6 months. Then the zloty will weaken. (...) We will have to win this war against MPC and change the NBP bill. The central bank's task should be not only to care about inflation but also to support the government's economic policy. (...) Exchange rate would be determined by the government which will announce the target range. (...) This level would be consulted with the NBP.”

## Market monitor

- Polish zloty continued its appreciation trend in December
- A big supply of bonds accompanied by a significant foreign investors' appetite for Polish assets can contribute to the continuation of the trend
- Politicians are against strong zloty and they have a few potential ways to weaken it
- Let us not expect that the Monetary Policy Council will yield to the pressure and will cut interest rates low enough to lead to Polish zloty's devaluation
- Politicians will be left with two options: either changing the NBP act or attempting to change the exchange rate regime.

### FX market

December was another month of Polish zloty's appreciation against EURO and dollar. As it has been presented in the grid below, the depreciation during holidays and slight stabilization in September were followed by similar in scale appreciation of the zloty, measured by average monthly exchange rate.

Changes of foreign exchange rate %			
month	USD/PLN	EUR/PLN	EUR/USD
July	5.6	6.3	0.7
August	1.3	6.0	4.7
September	-0.6	0.6	1.1
October	-2.0	-2.5	-0.6
November	-1.1	-3.1	-2.0
December	-1.2	-2.2	0.6

*Negative values mean nominal appreciation, calculations on basis of monthly average rates.*

Source: NBP, BZ WBK

It is worth noticing that the exchange rate appreciation is accompanied by a slow-down in economic growth but also by the macroeconomic stabilization. It seems then, that what foreign investors pay attention to, when deciding on the purchase of Polish assets, is the improvement in the current account and the decrease in inflation, rather than the decelerating dynamics of GDP. Indeed, it seems that the expectations of new interest rate cuts resulting from the macroeconomic stabilization (which has been confirmed by MPC decisions) have been in the past and will be in the current month the main factor attracting portfolio capital. If the appetite for Polish assets remains big, and a big supply of Treasuries (PLN5.4bn in T-bills and PLN5.5-6.5bn in bonds) will meet with big interest from foreign investors, we can expect an increased pressure for the strengthening of zloty. In fact, we

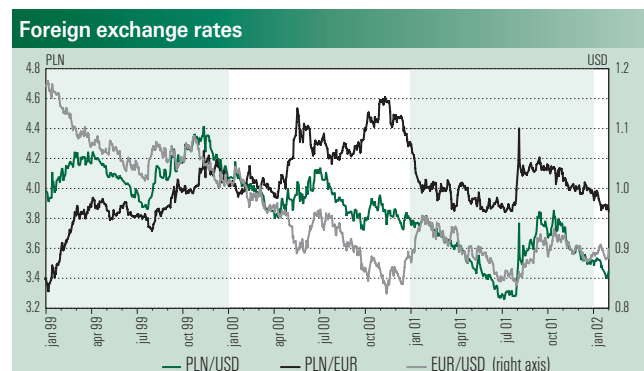
saw the first "heads of the oncoming herd" at the beginning of January.

There is no doubt that politicians will try to find a "an electric shepherd" who will not only stop the herd, but also turn it back – make the zloty depreciate. The shepherd is to be embodied by radical interest rate cuts. According to investors' estimates, only the cut by 3-4% would allow for zloty's depreciation down to Belka's level, that is to PLN 4.25 per 1 dollar.

The exchange rate proposed by Kalinowski – PLN 4.90 per 1 dollar could be set by decreasing the intervention rate by additional 2% to the level of 6%.

Since, as we believe, the Central Bank will fulfil its obligation – defined in the Constitution – of controlling inflation (see the relevant article in the Constitution and the NBP act below) and bringing the inflation rate to the level lower than 4% in 2003, the interest rate cut which could bring about zloty's devaluation will not take place. Politicians will be left with two options. SLD can support the change of the NBP act proposed by PSL and UP, or try to provoke the change in the exchange rate policy. If the first happened, investors would perceive the change in the NBP act as Poland's loss of chance to access the EU in the first round, and they would sell assets on a large scale, which would consequently lead to devaluation. President Kwasniewski could relegate the amendment of the NBP act to the Constitutional Tribunal, which, after a few months, would probably find it inconsistent with the Constitution, so no changes in legislation would be introduced, and Polish zloty would remain weak throughout the whole time.

If there was an attempt to change the exchange rate policy, the Government could conclude that NBP act determines the exchange rate policy and consequently, would not consider the MPC opinion as binding as well as could try to oblige the NBP to intervene in the exchange rate policy. As can be seen, the scenario can take on different forms, but most of them might bring about the weakening of zloty in the following months.



Source: BZ WBK



### The Republic of Poland's Constitution Art.227

The central bank of Poland is the Polish National Bank. It has the sole right of issuing money as well as of establishing and implementing monetary policy.

### The NBP act; Art. 3

1. The basic task of the NBP is maintaining the stability of prices while supporting the Government's economic policy as long as it does not interfere with the NBP's basic task.

### The NBP act; Art.24

1. The NBP implements FX policy established by the Cabinet in consultation with MPC.

2. The rules of setting the exchange rate of zloty against foreign currencies are established by the Cabinet in consultation with the RPP.

### Money and Treasuries Market

In December the situation in the money market improved slightly in comparison to November, however, the volatility of market rates was higher than so far. In the first decade of the month, one-day WIBOR remained slightly lower than the intervention rate ranging from 10%-11.5%, and banks had liquidity surpluses in their current accounts (over the obligatory reserve level), which resulted from the central bank's scaling down open market operations. Later on, beginning with December 11, daily WIBOR increased even up to 15% on December 18 while the liquidity in the bank sector decreased, which very quickly led to the increase in the long-term (1M and longer) WIBOR. Probably, the banks found themselves short of funds due to slightly higher than usual tax charges, and negative experiences in November gave rise to unrest. Things calmed down when PLN 2bn returned to the banking system on December 20, as a result of the repurchase of the NBP-bills. In the third decade of the month, WIBOR was almost the same as during the first 10 days, and certain fluctuations resulted from a big number of non-business days in this period. At the end of

December, long-term WIBOR was 40bp-70bp lower than at the end of November.

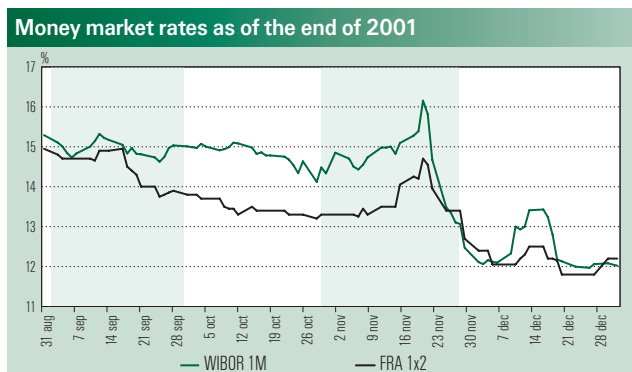
### T-bills offered in January (PLN m)

Date of auction	13-week	26-week	52-week	Total
07.01.2002	100	-	1200	1300
14.01.2002	100	-	1200	1300
21.01.2002	100	-	1300	1400
28.01.2002	-	100	1300	1400
<b>Total</b>	<b>300</b>	<b>100</b>	<b>5000</b>	<b>5400</b>

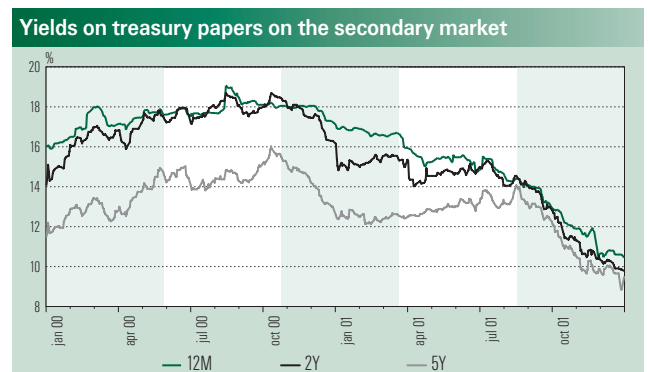
Source: Finance Ministry

Fluctuations in the money market lead to the destabilization of the derivatives market. It is best exemplified by FRA 1x2. This derivative is a type of speculation on the MPC decision to be taken at the nearest meeting. Currently, most analysts are expecting a decrease in interest rates by ca. 100bp at the end of January. However, FRA 1x2 is equal to 1m WIBOR, as there is a fear on the market that despite the decreased central bank's rates, market rates will not decrease owing to new liquidity problems.

In December the value of T-bills supplied in tenders totalled PLN5.3bn against PLN3.8bn in November. Concurrently, the sales were higher than supply and totalled PLN6.2bn. The Finance Ministry decided to enlarge the T-bills pool, taking advantage of relatively good market conditions, in order to increase its liquidity for Q1 2002, as well as to plug the whole that was created due to the failure to generate projected income from privatization in 2001. In December 13-week T-bills worth PLN300m, 26-week T-bills worth PLN293m, 39-week T-bills (offered for the first time in 2 years) worth PLN2.1bn and 52-week T-bills worth PLN3.6bn were sold. As a result of the cut in interest rates at the end of November, the average yield on 26- and 52-week bills was 95bp down on the previous month. The yield on 13-week bills which were not offered in November decreased in December by 203bp against October. The supply-demand ratio in tenders deteriorated: from 3.47 to 2.55, as a result of a significant increase in the supply of T-bills.



Source: BZ WBK



Source: BZ WBK

In the secondary market the yield on T-bills was not stable in December, however its oscillations did not exceed 40bp. At the end of the month yield on bills slightly decreased and on December 31 it was lower than at the end of November by 10 to 50 bp.

At the tender of T-bonds held on December 5 there was a relatively small decrease in average yield. The yield on 2-year Treasuries (OK 1203) was 10.2% against the yield of 10.40% on November 7, whereas the yield on 5-year bonds (PS 1106) was 9.68% against the yield of 9.76% a month earlier. The decrease in yield was not significant in comparison

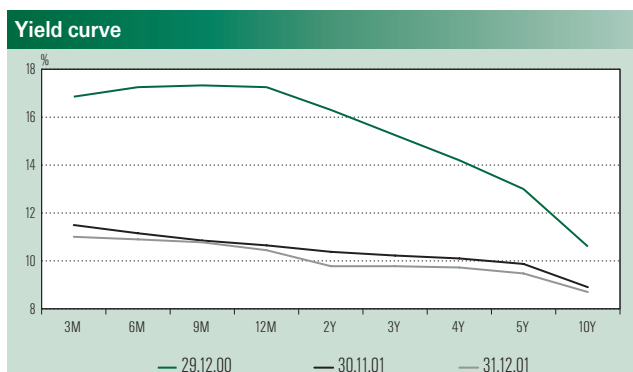
In December the yield on bonds on the secondary market was decreasing throughout most of the month. Only around December 10 there was a temporary increase in yield, when some foreign investors withdrew from the Polish market after successive attacks on the MPC and negative events in Argentina. Finally, the yield decreased against the end of November and the drop ranged between 20bp and 60bp. Moreover, in the 2Y-5Y sector the yield curve flattened even further.

The Finance Ministry announced its intention to sell PLN5.5bn-PLN6.5bn's worth of 2.5-year and 10-year wholesale bonds.

T-bond auctions in 2002				
Month	1st auction		2nd auction	
	date	T-bonds	date	T-bonds
January	09.01	OK1203, PS1106	16.01	DS1110
February	06.02	OK1203, PS1106	13.02	DZ0811
March	06.03	OK1203, PS1106	20.03	DS1110
April	03.04	OK0404, PS1106	10.04	DZ0811
May	08.05	OK0404, PS0507	-	-
June	05.06	OK0404, PS0507	12.06	DZ0811
July	03.07	OK0404	17.07	DS1110
August	07.08	OK0804, PS0507	14.08	DZ0811
September	04.09	OK0804, PS0507	18.09	DS1110
October	02.10	OK0804, PS0507	09.10	DZ0811
November	06.11	OK0804, PS1107	20.11	DS1112
December	04.12	OK1204	11.12	DZ0811

Source: Finance Ministry

to the central bank's cut in interest rates at the end of November, as this MPC decision was discounted much earlier. The supply was smaller than in record-breaking November and the value of both types of bonds totalled PLN1.2bn. The tender in December was more successful than the one in November (when the demand was smaller than supply). In December the demand-supply ratio was 2.1 and 2.3 and all the offered Treasuries were sold. Quite unsuccessful, however, was the tender of 10-year bonds (DZ 0811) held on December 12. Out of the total offer worth PLN500m, the demand covered only PLN246m and PLN90m's worth of treasuries was sold. Such a tender indicates that the market found this derivative unattractive.



Source: BZ WBK

## International review

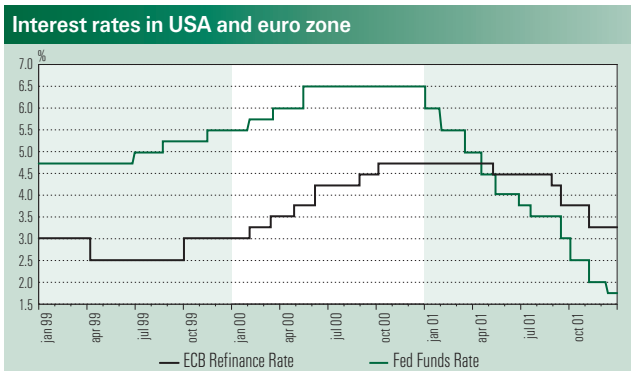
- Fed cuts rates further, ECB waits
- Introduction of the euro
- Improvement of activity and sentiment indicators.

### Fed cut interest rates by 25 bps

On 11 December US Federal Open Market Committee cut rates by 25 basis points. Federal funds rate now amounts to 1.75% - the lowest level since July 1961. Moreover in a statement issued after the meeting Fed assessed that "risks are weighted mainly toward conditions that may generate economic weakness in the foreseeable future", what suggests that easing monetary policy cycle might not be over yet.

The 25 bps rate cut was consistent with market expectations and had been discounted in asset prices, so analysts did not expect that it would influence market trends. Nevertheless, the euro strengthened after that cut.

In contrary to Fed, the ECB did not change the rates its December and January meetings. The last cut took place on 8 November. Since that time the refinancing rate is at the level of 3.25%. The next interest rate reduction is expected after inflation rate drops below 2%. According to preliminary figures it fell to 2% in December from 2.1% last month.



Source: FED, ECB

### Introduction of the euro



From the beginning of 2002, in the twelve member countries of the EMU, euro banknotes and coins were introduced into trading. The operation was carried out quite efficiently though the final assessment one would need to make a bit later. For some time (different for various countries, usually 2 months), euro will function parallel to the national money. Later, it will become the only payment means in the countries of the euro zone. The introduction of

the common European currency to cash trading will be the success of a few years' efforts aimed at the full monetary integration of the European states.

### Improvement of activity and sentiment indicators

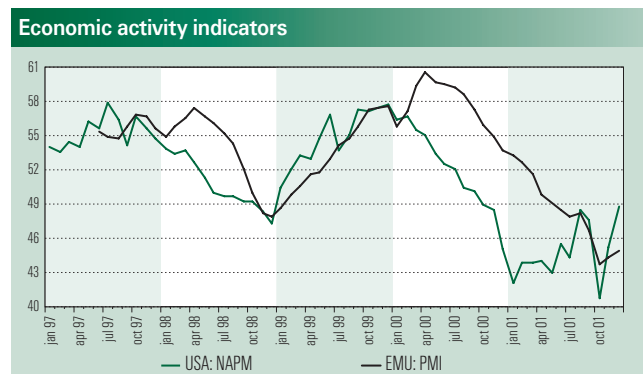
Eurozone PMI index (measuring economic activity in manufacturing sector) increased in December to 44.1 from 43.6 last month. It is the second consecutive growth of PMI index from the record-low level of 42.9 reached in October. But the index still remains below 50, what means that Eurozone industry is not expanding. These figures were consistent with expectations (at about 44.2 points).

Eurozone PMI index of economic activity in services sector increased to 49.2 in December from 46.9 in November. The figure was stronger than expected (47.4). The index came close to the level of 50, which makes the borderline between the development and depression. Positive factor is the optimism growth concerning future economic developments in Europe. Expectations index increased by 3.2 points to 58.9, which was the highest level in 4-month time.

December ISM index (former NAPM), i.e. American equivalent for European PMI, increased to 48.2 from 44.5 recorded in November. The result was much stronger than expected – average expectations ranged around 45.5.

ISM non-manufacturing index also increased in December. It reached 54.2 compared to 53.1 in November. The figure was much better than expected 49.7.

Increase of activity indicators for two major world



Source: REUTERS

economies may indicate their gradual recovery from economic stagnation.

IFO index reflecting German business sentiment increased in November for the first time since July, reaching 84.9 (compared to 84.7 last month). What is interesting, the expectation component also increased, which is usually a leading indicator of recovery. Slight increase in November does not mean

the trend reversion in German economy, although the perspectives improve – said Gernot Nerb, economist at IFO institute.

### **Other macroeconomic events**

ECB expects sluggish growth in eurozone in 4Q01 and in early 2002. However ECB monthly report suggests that growth recovery should be expected later in 2002 as lower inflation will contribute to rising consumer confidence. ECB expects next year eurozone growth between 0.7 and 1.7% and inflation to fall below 2%.

Euro zone inflation pressure still weakens. EMU CPI in November reached 2.1% against 2.4% in October. The prices declined 0.1% MoM. The Italian final CPI decreased to 2.4% YoY – the lowest level since April 2000. French inflation fell to 1.3% YoY. German PPI in November rose 0.1% YoY – the lowest level since September 1999.

Eurozone industrial production declined in October by 1.4% MoM and 2.7% YoY. The figures confirm that European economy still heads South.

US PPI in November fell 0.6% MoM and were down 1.1% YoY. US retail sales fell 3.7% MoM following a revised 6.4% MoM rise in October. Both PPI and retail sales were lower than market consensus.

US trade deficit in October was higher than expected and reached US\$29.43bn in comparison with US\$19.02bn in September, and was highest since April. Imports rose US\$11bn to 106.75bn and exports inched up US\$0.5bn to US\$77.3bn, which may still be partly affected by payments disruptions after the September 11 terrorist attack.

Durable goods orders in the US fell in November 4.8%MoM following 12.5% collapse in October. Markets expected 4.6% decline.

IFO economic institute said that economic slowdown in Germany was not over. IFO expects that the bottom will be reached in 2Q02. In 2001 German GDP is expected to rise 0.5% YoY and in 2002 0.6% YoY. IFO called on ECB to cut rates by a further 50bps, but expects that ECB will do just 25 bps early next year.

IMF released its "World Economic Outlook". It paints two possible scenarios for global growth. In optimistic scenario global growth next year will remain flat 2.4%, lowest since 1993, with US economy slowing to 0.7% from 1% this year, Euroland slowing to 1.2% from 1.5% and Japan contracting by 0.4%. Yes, it was an optimistic scenario. In pessimistic one global growth will fall to 1.7%, US economy will inch up 0.2%YoY and eurozone will grow on at 0.6% rate. In

this scenario Japan is in severe recession contracting 2.4%.

According to ECB eurozone current account deficit was in EUR0.1bn surplus in October comparing with EUR1.3bn deficit in September and EUR6.4bn deficit in October 2000. Trade surplus in the Euro area amounted to EUR9.6bn comparing with EUR2.3bn in October 2000.

In line with expectations OPEC countries decided to reduce the oil output from 1 January 2002 by 1.5m b/d with an aim to increase the oil prices. This reduction will be valid for a period of six months. After this decision OPEC controlling 60% of the oil market will produce 21.7m b/d, i.e. 19% less than in early 2001. Non-OPEC countries also decided to trim down output (Russia, Mexico, Norway, Oman and Angola) by 0.46m b/d. Next OPEC meeting will take place on 15 March.

**Data release calendar**

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
MPC meeting	28-29	-	-	-	-	-	-	-	-	-	-	-
CPI	15	15 <sup>a</sup>	15 <sup>b</sup>	15	15	17	15	16 or 19	16	15	15	16
PPI	18	19	18	18	20	19	17	20	18	17	20	18
Industrial output	18	19	18	18	20	19	17	20	18	17	20	18
Gross wages, employment	15	14	14	15	17	18	12	14	13	14	18	13
Trade	about 50 working days after reported period											
Balance of payments	31	28	29	30	-	-	-	-	-	-	-	-
Money supply	14	14	14	12	-	-	-	-	-	-	-	-
NBP balance sheet	7	7	7	5	-	-	-	-	-	-	-	-
Business climate indices	7 <sup>c</sup> & 22 <sup>d</sup>	20	20	18	20	19	18	20	19	18	20	19
Food prices, 1-15	-	8 <sup>d</sup> & 27 <sup>e</sup>	27	26	27	27	26	27	27	25	27	30
Food prices, 16-30	3	8	8	5	7	6	5	6	6	7	6	6

a) preliminary data; b) final data (January, February); c) December 01; d) January 02; e) February 02

Source: CSO, NBP

**What's hot this month**

Monday	Tuesday	Wednesday	Thursday	Friday
<b>31 December</b>	<b>1 January</b> <i>New Year's Day</i>	<b>2</b> EMU: PMI (Dec) USA: ISM (ex NAPM, Dec)	<b>3</b> EMU: ECB meeting ITA: Inflation preliminary (Dec)	<b>4</b> EMU: Inflation preliminary (Dec) EMU: Unemployment (Nov) USA: Unemployment (Dec)
<b>7</b> POL: T-bills auction (PLN 1,3bn)	<b>8</b> GER: Industrial orders (Nov) EMU: Economic sentiment (Dec) EMU: Producer prices (Nov) EMU: Retail sales (Oct)	<b>9</b> POL: T-bond auction (OK1203 and PS 1106) GER: Unemployment (Dec)	<b>10</b> GER: Industrial output (Nov) FRA: Inflation preliminary (Dec) EMU: GDP (3Q)	<b>11</b> USA: Producer prices (Dec)
<b>14</b> POL: T-bills auction (PLN 1,3bn)	<b>15</b>	<b>16</b> POL: T-bond auction (DS1110) USA: Inflation (Dec)	<b>17</b> EMU: ECB meeting	<b>18</b>
<b>21</b> POL: T-bills auction (PLN 1,4bn) POL: Unemployment (Dec) EMU: Foreign trade (Nov)	<b>22</b> EMU: Inflation final (Dec) EMU: Industrial output (Nov)	<b>23</b>	<b>24</b>	<b>25</b>
<b>28</b> POL: MPC meeting POL: T-bills auction (PLN 1,4bn) GER: IFO business climate (Dec, Jan) EMU: Money supply (Dec)	<b>29</b> POL: MPC meeting USA: Fed meeting	<b>30</b> USA: Fed meeting	<b>31</b> EMU: Inflation preliminary (Jan)	<b>1 February</b> EMU: Economic sentiment (Jan) USA: Unemployment (Jan)

Source: Finance Ministry, Reuters

**Monthly indicators**

	unit	Dec-00	Jan-01	Feb-01	Mar-01	Apr-01	May-01	Jun-01	Jul-01	Aug-01	Sep-01	Oct-01	Nov-01	Dec-01	Jan-02	Feb-02
GDP	% YoY	2.4	-	-	2.3	-	-	0.9	-	-	0.8	-	-	1.2	-	-
Industrial output	% YoY	-2.2	10.1	0.1	2.9	3.6	-0.9	-4.8	0.9	0.4	-3.8	1.6	-0.8	-0.8	-0.9	0.1
Retail sales	% YoY	3.2	10.9	-0.2	0.1	1.9	4.3	0.2	1.5	3.0	1.3	5.8	2.4	-	-	-
Unemployment rate	%	15.1	15.7	15.9	16.1	16.0	15.9	15.9	16.0	16.2	16.3	16.4	16.8	17.4	18.1	18.4
Gross wages**	% YoY	7.5	9.9	7.7	7.9	5.2	8.8	4.9	8.0	6.9	6.2	7.8	6.6	6.0	5.9	6.2
Exports (acc. to NBP)	USD m	2 759	2 430	2 392	2 614	2 559	2 472	2 477	2 556	2 616	2 287	2 778	2 574	2 700	2 187	2 187
Imports (acc. to NBP)	USD m	3 797	3 946	3 116	3 522	3 269	3 638	3 379	3 382	3 635	3 176	3 953	3 524	4 000	3 600	3 060
Trade balance (acc. to NBP)	USD m	-1 038	-1 516	-724	-908	-710	-1 166	-902	-826	-1 019	-889	-1 175	-950	-1 300	-1 413	-873
Current account	USD m	-816	-956	-463	-751	-520	-737	-948	-287	-354	-304	-838	-217	-515	-894	-374
Budget deficit	PLN bn	-15.4	-5.1	-12.0	-15.1	-18.4	-20.4	-18.7	-19.4	-21.0	-21.8	-24.6	-27.7	-33.0	-8.0	-15.0
Inflation	% YoY	8.5	7.4	6.6	6.2	6.6	6.9	6.2	5.2	5.1	4.3	4.0	3.6	3.7	3.9	4.4
Producer prices	% YoY	5.6	4.7	4.1	3.8	3.4	2.3	0.9	0.6	1.0	0.7	-0.5	-0.8	0.0	0.8	1.1
Money supply	% YoY	11.7	14.6	14.6	14.9	14.0	13.5	8.0	13.5	14.6	14.3	13.0	11.9	11.6	11.8	11.9
Deposits	% YoY	15.5	17.5	17.1	16.8	16.1	15.5	9.1	15.4	16.3	15.5	13.7	12.3	12.1	12.1	12.2
Credits	% YoY	17.3	16.1	15.6	14.6	12.7	11.3	5.0	11.6	11.7	10.7	8.7	8.1	8.5	8.2	8.2
USD/PLN	PLN	4.3143	4.1108	4.0925	4.0599	4.0175	3.9807	3.9705	4.1859	4.2459	4.2185	4.1332	4.0943	4.0144	4.00	4.05
EUR/PLN	PLN	3.8802	3.8648	3.7689	3.6952	3.5904	3.4856	3.3894	3.5998	3.8218	3.8450	3.7425	3.6389	3.5829	3.60	3.65
Intervention rate*	%	19.0	19.0	19.0	17.0	17.0	17.0	15.5	15.5	14.5	14.5	13.0	11.5	11.5	11.5	11.5
WIBOR 3M	%	19.67	18.97	18.61	18.01	17.17	17.22	16.88	16.01	15.35	14.73	14.01	13.91	11.83	11.80	11.80
Lombard rate*	%	23.0	23.0	23.0	21.0	21.0	21.0	19.5	19.5	18.5	18.5	17.0	15.5	15.5	15.5	14.0
Yield on 52-week T-bills	%	18.01	17.23	16.97	16.85	15.80	15.67	15.61	15.38	14.61	14.01	12.64	11.80	10.86	9.9	9.8
Yield on 2-year T-bonds	%	17.20	15.68	15.48	15.60	14.59	14.92	15.22	15.13	14.40	13.57	11.36	11.00	10.70	9.2	9.1
Yield on 5-year T-bonds	%	13.93	13.08	12.92	13.33	13.47	13.38	13.29	13.85	13.50	12.92	11.32	10.13	9.91	9.1	8.9
Yield on 10-year T-bonds	%	11.50	10.44	10.23	10.68	10.61	11.30	11.74	11.87	11.97	11.57	10.31	9.19	8.92	8.3	8.2

\* at the end of period \*\* in corporate sector

Source: CSO, NBP, BZ WBK

**Quarterly and yearly**

	unit	1997	1998	1999	2000	2001P	2002P	2003P	10 2001	20 2001	30 2001	40 2001	10 2002	20 2002
GDP	% YoY	6.8	4.8	4.1	4.0	1.3	2.0	3.5	2.3	0.9	0.8	1.2	2.5	1.5
Industrial output	% YoY	11.5	3.5	3.6	6.8	0.5	2.4	3.4	4.1	-0.9	-1.2	-0.1	-1.0	1.0
Real retail sales	% YoY	6.8	2.6	4.0	1.0	0.4	-	-	-3.1	-0.2	1.2	3.5	-	-
Unemployment rate*	%	10.3	10.4	13.1	15.1	17.4	18.5	18.8	16.1	15.9	16.3	17.4	18.5	18.1
Real gross wage	% YoY	5.9	3.3	4.7	1.0	2.5	0.5	1.5	2.5	0.8	2.5	4.0	1.5	1.0
Exports (acc. to NBP)	USD m	27 229	30 122	26 347	28 256	30 455	31 886	34 000	7 436	7 508	7 459	8 052	6 758	6 868
Imports (acc. to NBP)	USD m	38 549	43 842	40 727	41 424	42 540	44 242	47 000	10 584	10 286	10 194	11 477	10 118	10 183
Trade balance (acc. to NBP)	USD m	-11 320	-13 720	-14 380	-13 168	-12 085	-12 355	-13 000	-3 148	-2 778	-2 735	-3 425	-3 360	-3 315
Current account	USD m	-4 309	-6 862	-11 558	-9 946	-6 900	-8 000	-9 150	-2 170	-2 205	-945	-1 570	-2 086	-1 434
Current account	% of GDP	-3.0	-4.3	-7.4	-6.3	-3.9	-4.5	-5.0	-4.9	-5.2	-4.2	-3.9	-3.8	-3.5
Budget deficit*	PLN bn	-5.9	-13.2	-12.5	-15.4	-33.0	-40.0	-	-15.0	-18.8	-21.9	-33.0	-20.0	-28.0
Inflation	% YoY	14.9	11.8	7.3	10.1	5.5	4.1	4.5	6.7	6.6	4.9	3.8	4.3	3.9
Inflation*	% YoY	13.2	8.6	9.8	8.5	3.7	5.0	4.0	6.2	6.2	4.3	3.7	4.4	3.8
Producer prices	% YoY	12.2	7.3	5.7	7.8	1.7	1.8	2.5	4.2	2.2	0.8	-0.4	1.0	1.6
Money supply	% YoY	30.3	25.8	23.2	14.9	13.2	10.0	11.0	14.7	11.8	14.1	12.2	11.6	11.0
Deposits	% YoY	33.0	28.8	24.7	17.0	14.8	10.0	10.5	17.1	13.6	15.7	12.7	11.9	11.0
Credits	% YoY	44.6	29.3	28.3	23.0	11.2	13.8	15.0	15.4	9.7	11.3	8.4	8.6	10.0
USD/PLN	PLN	3.2808	3.4937	3.9675	4.3465	4.0939	4.2	4.5	4.0876	3.9895	4.2168	4.0805	4.05	4.20
EUR/PLN	PLN	3.7055	3.9231	4.2270	4.0110	3.6685	3.8	4.0	3.7765	3.4884	3.7551	3.6549	3.65	3.80
Intervention rate*	%	23.50	15.50	16.50	19.00	11.50	9.0	9.0	18.00	15.50	14.50	11.50	10.0	9.0
WIBOR 3M	%	23.93	21.34	14.73	18.78	16.04	10.4	9.2	18.53	17.09	15.37	13.24	11.3	9.6
Lombard rate*	%	27.00	20.00	20.50	23.00	15.50	12.0	12.0	22.00	19.50	18.50	15.50	14.0	13.0
Yield on 52-week T-bills	%	23.44	18.59	12.95	17.77	14.77	9.4	9.2	17.02	15.70	14.67	11.72	9.8	9.3
Yield on 2-year T-bonds	%	23.47	18.08	12.41	17.37	13.91	8.7	8.6	15.59	14.91	14.37	10.83	9.1	8.6
Yield on 5-year T-bonds	%	21.03	15.83	10.87	14.00	12.59	8.6	8.5	13.12	13.38	13.43	10.45	9.0	8.5
Yield on 10-year T-bonds	%	-	-	9.60	11.79	10.74	7.9	7.8	10.46	11.22	11.81	9.48	8.2	7.8

\* at the end of period

Source: CSO, NBP, BZ WBK



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