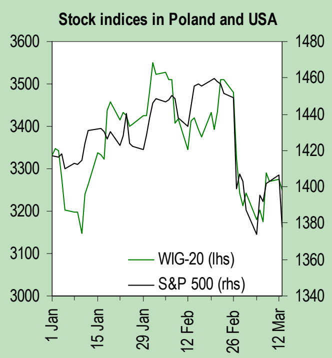
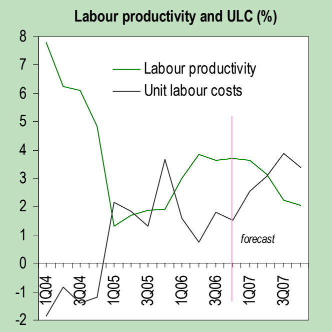
Bank Zachodni WBK

MACROscope

Polish Economy and Financial Markets

March 2007





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Spring-time correction

- **We are in the middle of period of increased volatility in world financial markets, caused by concerns over prospects for US economy.** Polish currency proved to be quite resilient to sell-off that swept through emerging markets amid rising global risk aversion and flee to safe assets. Nevertheless, current situation (particularly in the stock market) remains uncertain and one cannot exclude further correction of the zloty if new data from the US economy confirm a risk of recession. Still, in the base case scenario we predict that after a period of turbulence and some weakening in Q1 (EURPLN should not exceed 3.95 though), next months will see a recovery (end-year forecast at 3.75).

- **In line with expectations, the Monetary Policy Council left interest rates unchanged in February, for the 12th straight month.** The statement released after the meeting was little changed as compared to the version from the preceding month, however those small changes were important in our opinion as they had tightened the MPC's hawkish language. Interestingly, the market interpreted it quite differently, focusing on rather dovish comments of NBP president, and expectations for rate hikes moved forward in time. Meanwhile, in our view a risk of rate hikes has increased. New economic data will be key for future MPC decisions, especially figures concerning inflation and the labour market.

- **Data for the first month of 2007 showed that economic expansion gains strength and is accompanied by gradual increase in inflationary pressure.** As a result, we revised upwards our GDP growth forecasts for this year. Currently we predict that economic growth in 1Q07 will accelerate to 6.7% while earlier we expected a slowdown to 6% from 6.4% posted in 4Q06. In the subsequent quarters GDP growth should slightly moderate and in the whole year it would amount to 5.7%.

- **In the *Special focus* section we try to estimate the supply of Polish treasuries in the primary auctions in particular quarters of this year.** We assumed that budget deficit is going to be realized in the amount of PLN28.5bn, the off-budget spending may amount to PLN17.7bn (proceeds from privatization at 50% of the plan), the value of maturing bonds this year is going to be much smaller than last year (PLN39bn), T-bills issue is going to be limited (25.8bn), similar as the foreign financing (9.03bn). The gross borrowing needs in the domestic market may equal to PLN101.8bn. Taking into consideration the switch auctions we estimate the Ministry of Finance may decide to offer bonds worth PLN58bn at primary auctions and PLN26bn at switch tenders (PLN18bn of bonds maturing this year).

Financial market on 28 February 2007:

NBP deposit rate	2.50	WIBOR 3M	4.22	USDPLN	2.9699
NBP reference rate	4.00	Yield on 52-week T-bills	4.07	EURPLN	3.9175
NBP lombard rate	5.50	Yield on 5-year T-bonds	5.02	EURUSD	1.3220

This report is based on information available until 12.03.2007

Special focus

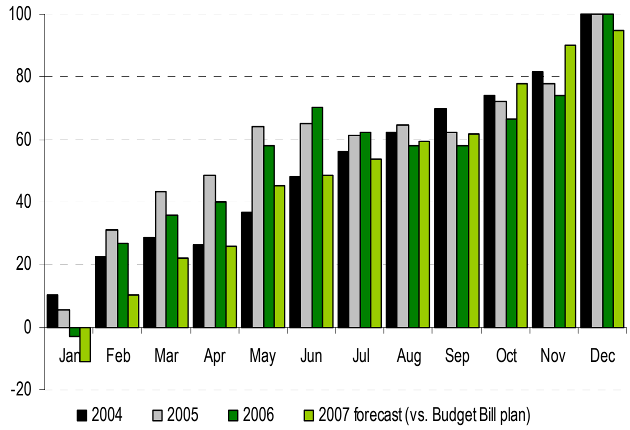
Supply of treasuries in 2007 on the domestic market

This article will be an attempt to estimate a quarterly supply of treasuries in Poland vis-à-vis domestic borrowing needs of the Finance Ministry. The latter are primarily driven by the size of budget deficit, unbudgeted allocations, which are an indicator of a net borrowing needs, and the volume of treasuries maturing this year being total an indicator of gross borrowing needs. Thus calculated bottom line adjusted by net foreign debt financing shows our gross domestic borrowing needs. Maturity terms of treasuries may not dovetail into a time breakdown of borrowing needs, while differences are an effect of tactics pursued by the Finance Ministry to minimise the cost of public debt.

According to the Budget Act of 2007, the current budget deficit is planned to reach PLN30bn, i.e. slightly below the plan for 2006, but much above the deficit of PLN25.08bn reached last year. A much lower than expected deficit in the previous year was partially eased by a higher revenue and lower expenditure. It seems that the previous year's deficit might have been even lower, however some of the revenue streams from 2006 are to be recognised this year, among others to mitigate the risk of running into excessive spending, especially in the context of higher budget expenditure and reduction of a so-called tax wedge, i.e. contributions to the disability fund to be lowered by 3%. This year's budget deficit seems to be unchallenged then, given quick economic growth, higher revenues, controlled spend and taking of some of the last year's revenue streams to this year's book. We believe that despite lower contributions to the disability fund, which according to the MF's estimates may cost PLN9bn annually (we estimate that the second half of the year may bring ca. PLN3bn) the budget deficit may again be lower versus the forecast. **PLN28.5bn** is our projected figure, based on continuation of a strong growth of Polish economy.

On top of providing for the deficit, the Finance Ministry must ensure funds to be allocated to Open Pension Funds as part of the pension reform underway, investments co-funded by EU and advances. Obligations payable towards the Open Pension Funds this year are marginally lower than last year, though above the last year's forecast and stand at ca. PLN14.5bn. These obligations are lodged to the Funds' accounts on a relatively regular basis, hence we based our schedule of payments on an average for the last three years. Other payables which add up to borrowing needs represent mainly PLN1.1bn worth of advances for Export Credit Insurance Corporation, Compensation Fund (PLN300m) and up front funding towards tasks co-funded by EU (deficit of PLN2.78bn, expenditure of PLN13.97bn, revenue PLN11.20bn).

Budget deficit performance (% of full-year realisation)



Source: Ministry of Finance, BZWBK.

One of the domestic revenue streams to be earmarked for additional off-budget expenditure, i.e. allocations to the open pension funds in particular, comes from privatisation, which is planned to yield PLN3bn. This figure is much lower than last year's plan at PLN5.5bn, but still shows outperformance at PLN0.6bn. We believe that 2007 can witness a greater animation in the government's initiatives on this issue. Revenues from privatisation this year are estimated to top PLN1.5bn. The Budget Act sets the balance of privatisation revenues and subsequent spending at PLN12.28bn. According to our forecast that will be a negative balance of PLN13.8bn.

Our estimates also show that the additional borrowing needs driven by off-budget spending will be PLN17.7bn in the red. This means that with a deficit at PLN28.5bn, the net borrowing needs is **PLN46.2bn.**

To calculate the gross borrowing needs, the above figure must be increased by payables on account of maturing T-bills (PLN25.8bn) and treasury bonds (PLN39bn), which adds up to ca. **PLN64.8bn.** A slightly higher figure of PLN68.7bn found in the last draft of the Budget Bill does not factor in T-bonds bought back on last year's November and December auctions. For this reason, the gross debt requirement in an optimistic scenario amounts to PLN**110.9bn.**

The domestic gross borrowing needs are financed by domestic and international issues of treasuries.

One of the foreign sources of funding is revenue from PLN13.53bn worth of treasury bonds issued abroad and partially from bank loans of PLN3.45bn from European Investment Bank. The main expenditure item recognised on foreign accounts are repayments of bank debt owed to the Paris Club. Poland's debt owed to creditors grouped around the Paris Club, which matures this year, amounts to ca. PLN6.67bn, however the schedule of repayments as arranged by the Finance Ministry has not been revealed. A net foreign debt is planned to reach **PLN9.03bn.** We also assume that the balance of foreign debt will remain consistent over subsequent months. Last year, the Ministry of Finance limited deficit funding via bonds sold on international markets, while the actual debt funding in 2006 was at PLN6.9bn versus PLN20.5bn planned.

The maturing marketable treasuries in 2007 (PLN billon)

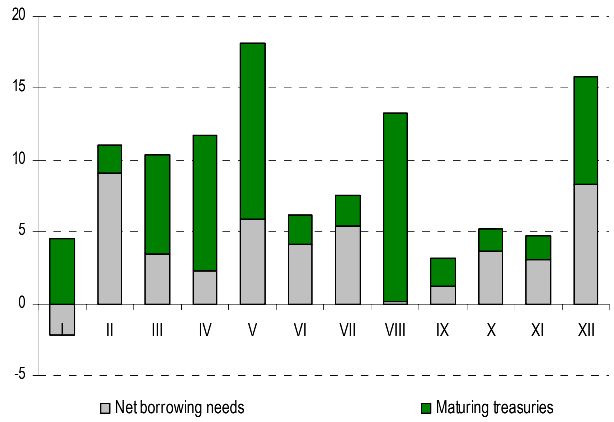
	T-bills	market bonds	Marketable treasuries	
			monthly	quarterly
January	4.3	0.20	4.49	
February	2.0	0.00	2.00	*13.35*
March	2.3	4.56	6.86	
April	2.0	7.39	9.39	
May	2.0	10.22	12.22	*23.61*
June	2.0	0.00	2.00	
July	2.0	0.08	2.08	
August	2.0	11.07	13.07	*17.15*
September	2.0	0.00	2.00	
October	1.6	0.00	1.60	
November	1.6	0.00	1.60	*10.66*
December	2.0	5.46	7.46	
Total	**25.8**	**38.96**	**64.76**	**64.76**

Source: Ministry of Finance, BZWBK.

The remaining shortage of own funds is financed via domestic treasuries and saving bonds. The balance of the latter ones reduces the existing deficit only by PLN 0.16 bln. Taken into account foreign debt and saving bonds, domestic debt requirements to be covered with treasuries represent a figure of **PLN101.8bn.**

As per the adopted strategy, the Ministry of Finance plans to extend an average maturity term of the issued treasuries. For the reason above, the volume of T-bill issues as short-term debt instruments ought to be limited gradually. **PLN25.8bn** worth of T-bills mature this year. We believe that as per the strategy adopted, the Finance Ministry decides to issue T-bills only to cover that amount. The outstanding amount is slightly higher than the Budget Bill's assumption of PLN23.4bn representing the issue of short-term bills in December, last year. The issue of T-bills should rather be spread evenly over the whole year. Slightly lower issues of T-bills may be observed amid relatively lower bond yields, while larger volume issues might occur towards the year's end and when the market is expecting interest rate increases.

Gross domestic debt requirement in 2007 (PLN billon)



Source: Ministry of Finance, BZWBK.

The schedule of T-bonds in 2007.

Issue (in bln PLN)	Bond type						
Month	2L	5L	10L	20L	10L change	12L CPI	Changes
January		2,9	1,8				1,3
February	1,0	1,5			2,4		3,7
March	1,0	√		√			
April	√	√	√				
May		√			√	√	
June	√	√					
July	√		√				
August	√				√	√	
September	√	√		√			
October	√	√	√				
November	√	√			√	√	
December	√						

Source: Ministry of Finance, BZWBK.

Thus, we estimate that the total of bond issues will add up to **PLN76bn.** However, the above figure would need to be adjusted by a possible, earlier redemption of treasuries maturing next year on switch tenders close of 2007. Last year, the Ministry of Finance redeemed ca. PLN20.3bn worth of bonds maturing in 2006 and ca. PLN7.1bn worth of bonds maturing in 2007. We believe that due to a lower volume of bonds maturing this year as compared to the last year and the next year, interest paid on bonds subject to switch auction trading this year, total value of bonds redeemed may be slightly below 70%, against 74% in the previous year. We are estimating that the Finance Ministry will decide to redeem ca. **PLN8bn** worth of bonds maturing in 2008, representing slightly over 30% of all bonds redeemed via auctions. Hence, a total value of T-bonds issued this year may amount even up to **PLN84bn** (the total debt requirement would grow from **PLN101.8bn** to **PLN109.8bn.**). The remaining bonds issued via switch auctions on account of redeeming bonds which mature this year, are used to "smooth out" the supply of bonds on ordinary auctions and is estimated at 17% of all bonds issued, i.e. **PLN18.0bn.** Hence, the value of bonds to be offered at primary auctions may add up to **PLN58bn,** while the total value of domestically issued treasuries may amount to ca. **PLN83.8bn** (last year it was PLN75.3 and 97.8bn respectively).

This year the Finance Ministry may decide to issue fewer treasuries than last year in view of, among others, smaller value of domestic treasuries maturing this year. A discernible risk attaching the volume of issuance is low revenue from privatisation.

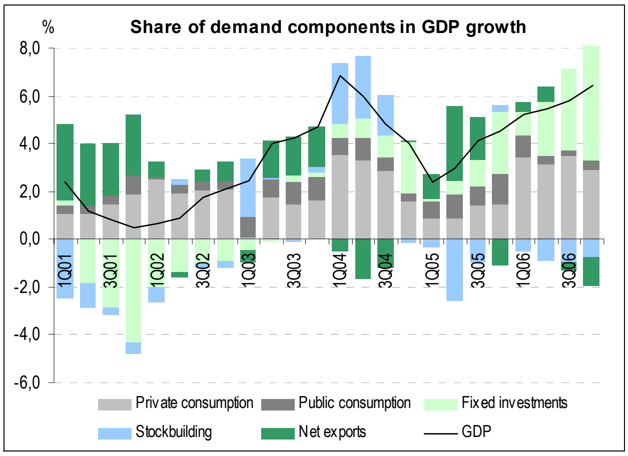
Bearing in mind the schedule of bond auctions published on the web site of the Finance Ministry, we have adopted a forecast of issuances broken down by subsequent quarters. It seems that this year the Ministry of Finance may smooth out the supply of treasuries eligible for ordinary auctions over the year, more than before among others due to lower value of bonds to be issued and amid substantial issuances at switch auctions.

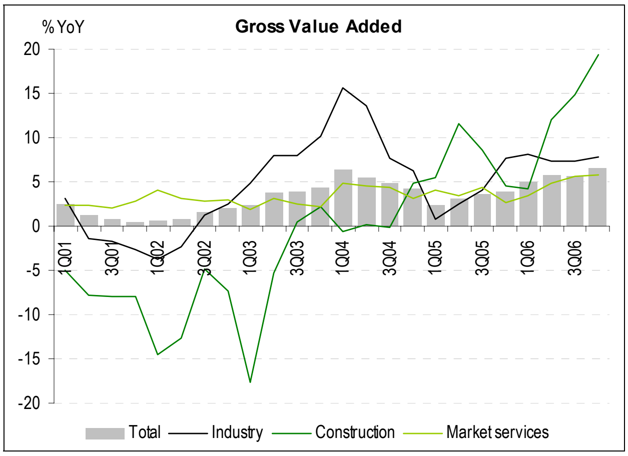
A forecast of bond issuance in 2007 (PLN billion)

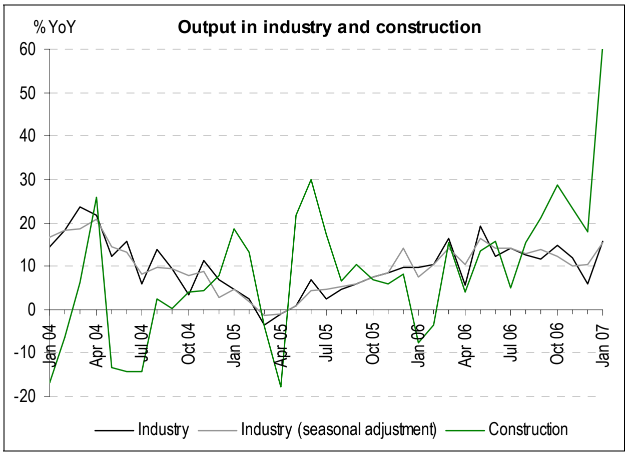
	Supply of treasuries		Ordinary auctions		Switch auctions		Total
	min	max	T-bills	Bonds	Bond redemption	Bond redemption	
Q1	18.3	21.7	5.6	**15.0**	7.5	0,0	**28,1**
Q2	20.0	30.0	6.0	**15.7**	5.6	0,0	**27,3**
Q3 .	15.0	24.0	6.4	**12.4**	3.8	0,0	**22,6**
Q4	19.0	24.0	7.8	**13.4**	1.1	8,0	**30,3**
Total	72.3	99.7	25.8	**56.5**	18.02	8,0	**108,3**
Grand total			**25.8**	**82.3**	**100.3**	**108.3**	

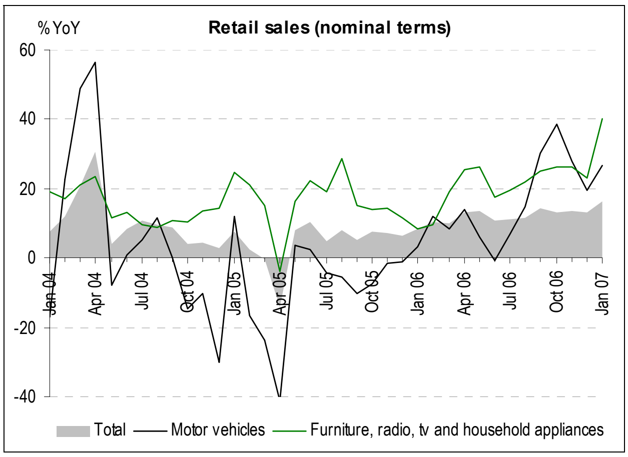
Source: BZ WBK

Economic update









Source: CSO, own calculations

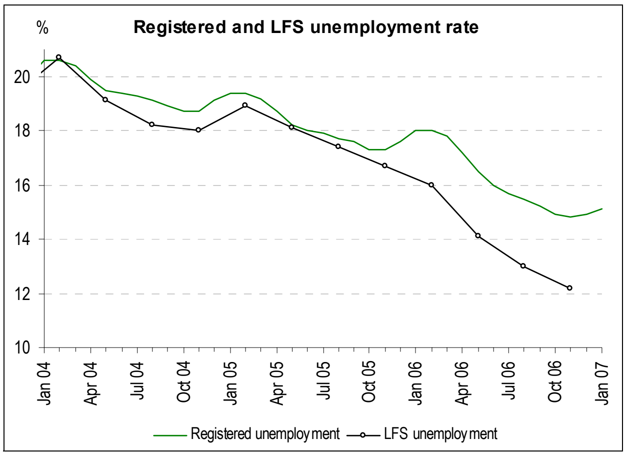
Confirmation of very good ending of 2006…

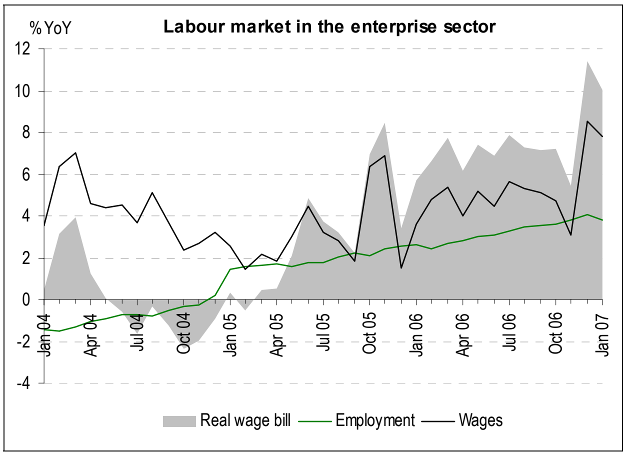
- GDP growth amounted to 6.4%YoY in the final quarter of last year and appeared slightly lower than estimates at 6.5% based on the preliminary data for the whole 2006. GDP growth for 2006 as a whole was confirmed at 5.8%. There were no revisions of the GDP growth in the first three quarters of 2006.
- Rise in private consumption in Q4 amounted to 5.2%YoY and fixed investment growth reached 19.3%YoY Domestic demand grew by as much as 7.7%YoY. Net exports' contribution was more negative than we estimated and amounted to -1.2pp.
- The seasonally adjusted GDP growth amounted to 1.9%QoQ in 4Q06, which has been the highest growth pace for many years, even exceeding the high growth pace that was recorded during the pre-accession boom in 1H04.
- The supply side of the national accounts showed the strongest increase in the construction sector (19.3%YoY), though economic expansion was also visible in other sectors. In industry the value added increased by 7.8%YoY, in market services by 5.8%YoY and in non-market services by 3.9%YoY. The agriculture sector was the only one with an annual decrease in value added.
- All in all, the data did not differ much from earlier estimates. Therefore, they confirmed the picture of economic situation known before. We are still facing acceleration in economic growth, and its structure is still favourable, suggesting no major threats for general macroeconomic balance. While GDP data did not change our forecasts, the earlier released economic activity indicators for January (see below) made us to revise the predicted path of GDP growth this year. We revised GDP growth in 1Q07 up from 6% to 6.7% and our forecast of economic growth in 2007 as a whole was revised up to 5.7% from 5.4%.

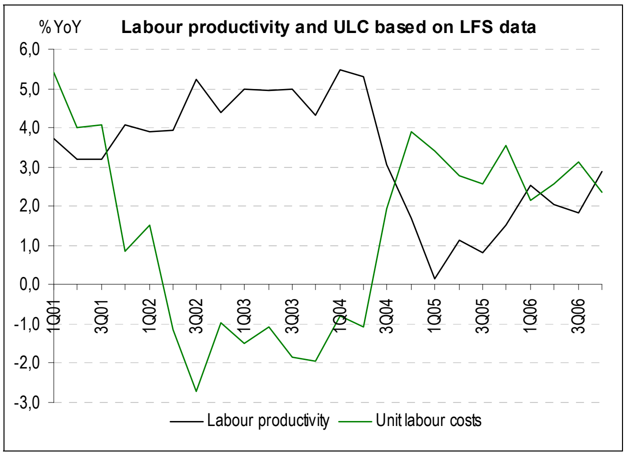
…and strong beginning of 2007

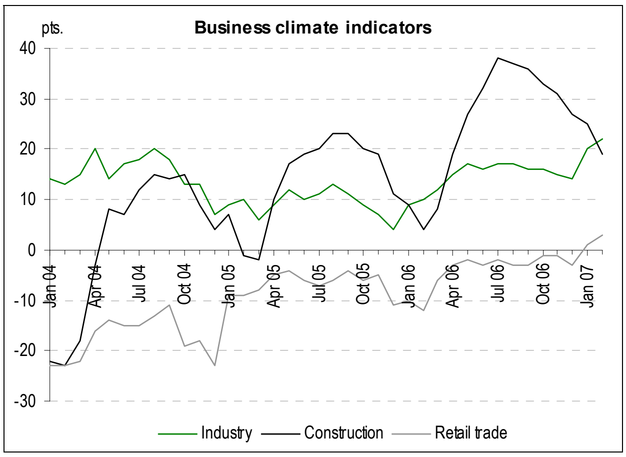
- Industrial production in January rose by 15.6%YoY, beating market expectations pointing to ca. 12%YoY rise. The seasonally adjusted growth in industrial output was also high and amounted to 15.5%YoY, significantly above the average for the previous year at 12.1%.
- In manufacturing, output surged by 19.2%YoY and this was the best result since the boom before the Poland's entry to the EU. This suggests the continuation of robust exports growth, confirming at the same time the fact that the slowdown in exports that was noted in December (see below) was a one-off event.
- Besides, construction output soared 60.8%YoY. To some extent, it was connected with very favourable weather conditions, allowing for continuation of construction works. Nevertheless, the data suggested that the breakdown of economic growth remains favourable, with large contribution of fixed investment.
- Retail sales rose in nominal terms by 16.5%YoY in January (seasonal fall by 24.3%MoM). In real terms retail sales rose by 16.2% (seasonal fall by 24.4%MoM).
- A solid growth was observed in all components of retail sales, but the most dynamic increase took place in case of durable goods (sales of furniture and electronic equipment up by 40%YoY, motor vehicles by 26.5%YoY). This means that consumers are in very positive moods, which is in line with results of various opinion polls and leading indicators. Optimistic moods of consumers translate into strong growth in consumption demand.
- After publication of January's economic activity indicators the Ministry of Finance said it estimated GDP growth in the first quarter of this year in a range of 6.5-7%, which is consistent with our forecast.

Economic update









Source: CSO, own calculations

Unemployment seasonally up, but downward trend lasts

▪ The registered unemployment rate amounted to 15.1% in January (below the preliminary estimate of the Ministry of Labour and Social Policy at 15.2%). The rate rose from 14.9% in December, however it resulted mainly from seasonal factors. In annual terms the fall in the unemployment rate accelerated to 2.9pp and it was the fastest pace since December 1997. The number of unemployed declined by 17.5%YoY and amounted to 2.366m.

▪ The results of LFS survey for Q4 are yet more optimistic. They showed that the unemployment rate in the last quarter of the previous year amounted to only 12.2%, which pointed to a record high fall by 4.5pp in annual terms. The fact that the higher and higher number of Poles find job supports estimates assuming that private consumption growth remains above 5%.

Good data on wages and employment

▪ Despite sharp fall in unemployment, the LFS data were not so negative for inflation prospects. Namely, they showed that the employment growth decelerated from 3.8%YoY in 3Q06 to 3.6%YoY in 4Q06. According to our estimates, this means an acceleration in productivity growth in 4Q06 - to 2.9%YoY from 1.8% in 3Q06 and time deceleration in unit labour costs to 2.3%YoY from 3.1% in 3Q06 (as compared to 2.4% in 1H06).

▪ Let's remind that the same trends – higher productivity gains and lower growth rate of unit labour costs - were suggested by monthly data on employment (up 3.8%YoY) and wages (a rise of 7.8%YoY) in the enterprise sector.

▪ In total, wage bill in the enterprise sector grew 11.9%YoY in nominal terms and 10%YoY in real terms.

▪ The risk for inflation prospects from the labour market still exists. Though the relation between wage growth and productivity has recently improved, this may well change in the following months. This was suggested by the breakdown of January's wage growth, which showed this was not driven by one-off payments in the mining sector, but the significant increase in salaries was also observed in the manufacturing sector (by 8.5%YoY). As in our opinion the manufacturing output is likely to decelerate in the forthcoming months (from close to 20% growth in January), the relationship between wage growth and productivity may also deteriorate.

▪ We expect that in the economy as a whole productivity growth will be maintained at a high level, but growth in unit labour costs may accelerate as a result of stronger increase in salaries. This will cause increase in inflationary pressure, but this should be gradual as other factors (globalisation effects, strong zloty) will work in the opposite direction.

Enterprises remain optimistic

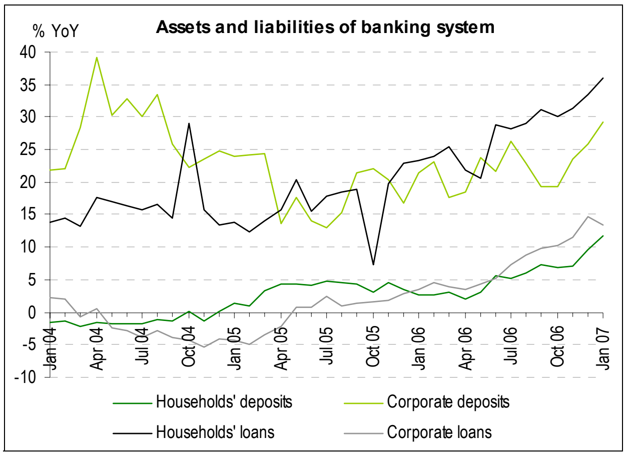
▪ Business climate indicators for February published by the CSO showed continuation of positive tendencies observed in previous months.

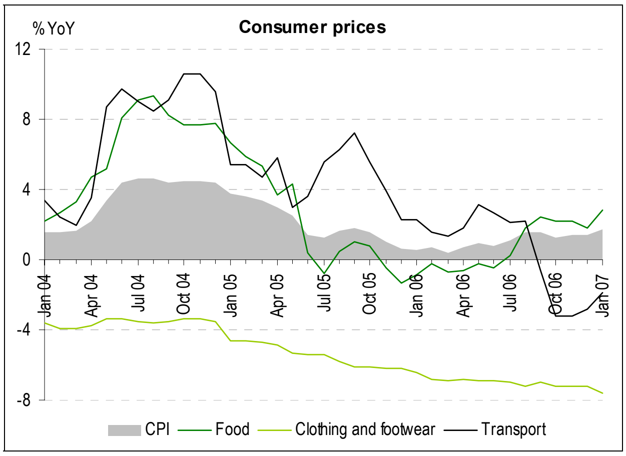
▪ Although index for construction saw another seasonal fall, in annual terms there was improvement in builder's moods by 15pp, on a similar scale as in previous months.

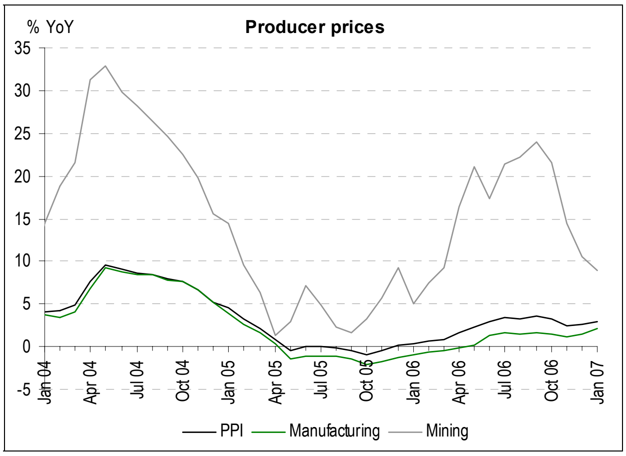
▪ Indicators for industry and retail trade improved on the month and there was acceleration in their growth in annual terms.

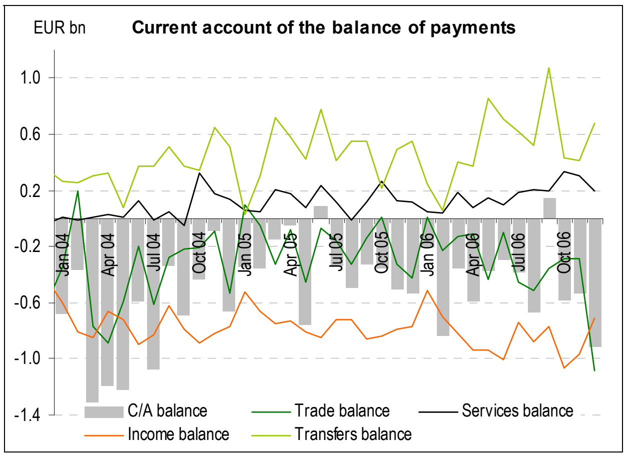
▪ Changes in indices and generally upbeat tone of firms' opinions on current and expected demand, financial situation, planned changes in employment indicate that positive tendencies in the Polish economy are continued. Rising confidence of enterprises should positively affect their investment activity.

Economic update









Source: CSO, NBP, own calculations

Monetary statistics reflect strong economic expansion

▪ Money supply in January rose 19.4%YoY against 15.6%YoY rise in December, reaching the highest pace of growth since mid-2000.

▪ Total deposits growth accelerated to 18.4%YoY from 15%YoY, also reaching the highest level since mid-2000. The acceleration concerned both households deposits (to 11.6%YoY) and enterprise deposits (to 29.2%YoY).

▪ Total loans increased 25%YoY. Growth in corporate borrowing remained at two-digit levels (13.4%YoY) and growth in households' borrowing accelerated to 35%YoY, the highest level since 2000.

▪ All in all, the data confirmed that the Polish economy experiences strong expansion. Further strong rise in loans will surely be closely watched by the MPC.

No surprises in CPI, slightly worrying PPI

▪ Preliminary inflation data for January released by the Central Statistical Office showed rise in consumer prices by 1.7%YoY (as compared to 1.4% in December). What is interesting, the influence of excise tax increases (tobacco and alcohol) was not visible at the beginning of the year, while fuel prices fell (the CSO did not release the detailed data on fuel prices but total transport costs fell by as much as 0.7%MoM in January). The excise tax increase is able to be seen in consumer prices in the following months.

▪ Also, one should remember that January's provisional data will be revised next month after the CSO recalculates the CPI basket, though we do not expect major changes in that respect.

▪ Overall, the January inflation data confirmed our expectations for the next months - the inflation rate is going to rise further in February and March, though this increase will be probably quite moderate (in March CPI may rise up to 2.2%YoY, which is still below the target). In the following months of Q2 and Q3 inflation should stabilize or even slightly decline. What is more, the net inflation should stay at low level (according to our estimates in January it remained unchanged at 1.6%, and may stay below 2.5% till the year-end).

▪ Annual growth in PPI accelerated in January to 2.9% from 2.6% in December. On a monthly basis, after five months of producer price decline (on average by 0.4%), January saw 0.5% rise, which was connected mostly, as usual at the beginning of the year, with hikes in energy prices. However, there was also rise in prices in manufacturing (0.2%MoM and 2.1%YoY). Thus, the annual price growth in manufacturing accelerated from a moderate 1.5%YoY in December to the highest level since early 2005. In our opinion continuation of the tendency will be important hawkish argument for the MPC.

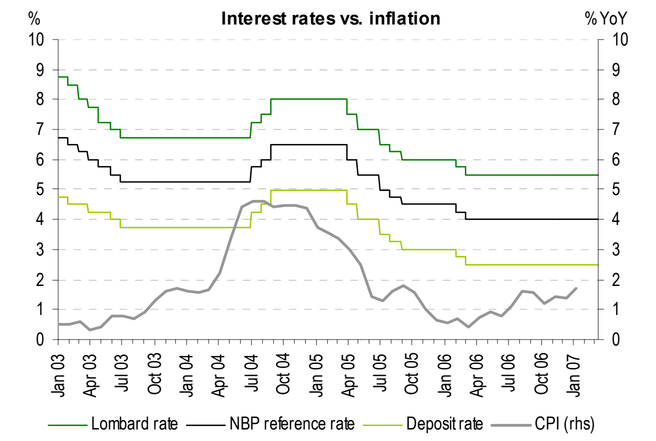
One-off deceleration in exports growth

▪ Current account deficit in December reached as much as €915m, mainly due to wide trade gap of €1.08bn.

▪ Interestingly, wider than expected trade gap was not caused by forecasted import acceleration (in fact import growth in December proved to be lower than predicted and reached 17%YoY), but by significant export deceleration. In annual terms exports rose by merely 8.3%YoY, while in previous months of 2006 it was above 21%YoY on average. At the moment, it is hard to decide whether this is a change in upward trend of the Polish exports. High output growth in January suggests that December's slowdown in exports growth was a one-off.

▪ Cumulated 12-month C/A deficit at the end of 2006 reached 2.1% of GDP which means it remains relatively low. Moreover, it is entirely financed by FDI inflow (above €1bn in December).

Central bank watch

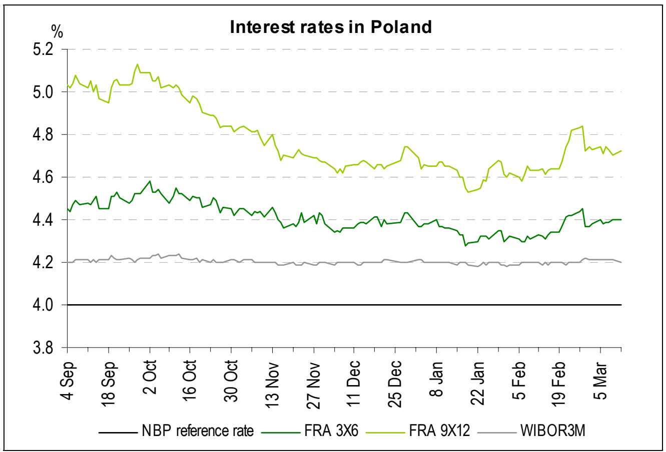


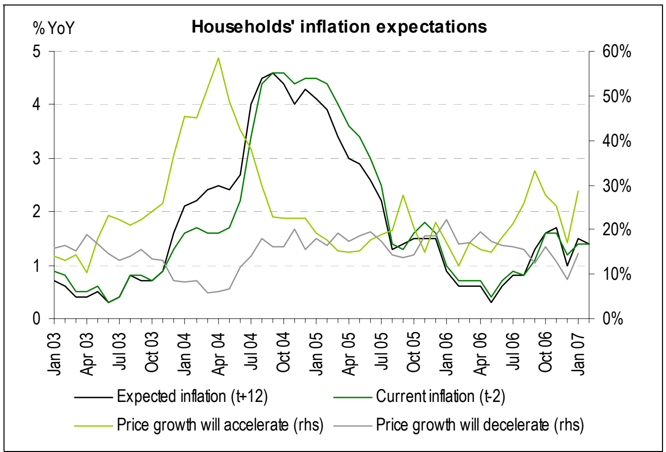
Fragments of MPC statement, 28 February 2007

In the Council's assessment, in the short term CPI inflation will be considerably lower than in the January projection. The core "net" inflation may also prove markedly lower than in the projection.

In the medium term the growth of wages may gradually increase, leading to higher inflation. The Council believes that this increase in inflation will be probably moderate provided that the strong productivity growth and low growth of external prices are sustained, the latter being associated with globalisation and the ensuing increased competition in the market of internationally traded goods and services.

The Council judged that the current level of NBP interest rates makes it possible for inflation to be kept close to the target of 2.5% in the medium term. However, maintaining inflation close to target and thus creating conditions for sustainable long-term economic growth may require monetary policy tightening. Future decisions of the Council will depend, to a large extent, on whether rising economic activity proves more permanent. It will also depend on other economic developments in Poland and in the world and also on their impact on the inflation outlook in Poland.





Source: NBP, Reuters

Restrictive bias does not mean rate hike

- The Monetary Policy Council delivered no surprise in February, keeping main reference unchanged at 4.0%.
- The official communiqué was little changed as compared to the January's version, but in our opinion the small differences were quite important, as they signalled further sharpening of MPC's tone, increasing chances for rate hikes.
- Prospects for interest rates outlined by the MPC in the statement was largely unchanged – current level of interest rates allows for keeping inflation close to target in the medium run, however inflation stabilisation at the target level could still require monetary tightening in future.
- In our view, it should be interpreted as maintaining restrictive bias in monetary policy.
- While in the preceding month, the Council wrote that its future decisions will depend on the new data, this time it added that an important factor will be also whether "rising economic activity will be of persistent nature". Thus, it seems that there is some shift towards more hawkish view, which is connected with possibility of faster closing of output gap.
- On the other hand, in the economic scenario assumed by us, negative impact of rising unit labour costs on inflation will be counterbalanced by other factors and should not produce a significant risk for the inflation target. Therefore, in our base scenario we assume that a rate hike will take place only at the beginning of 2008. However, if new data from the labour market do surprise once more, one should remember that the Monetary Policy Council has been sending a signal about its readiness to kick off with rate hikes for the third straight month, which seems to be overlooked by some market analysts at the moment.

The market misinterpreted MPC signals

- FRA market strengthened following the last MPC decision and its justification (FRA 6x9 fell by almost 10 bp), which shows a significant drop in discounted likelihood of interest rate hikes.
- We think that a direction of change in market expectations is at odds with MPC's intentions, as the Council has adopted more hawkish tone, signalling a rise (rather than fall) in risk that interest rate hikes may be needed soon.
- On the other hand, a correction took place after earlier significant (excessive) rise in rates, returning them back to rational levels – a 25 bp rate hike in the 3-month horizon is now priced in with ca. 50% probability.

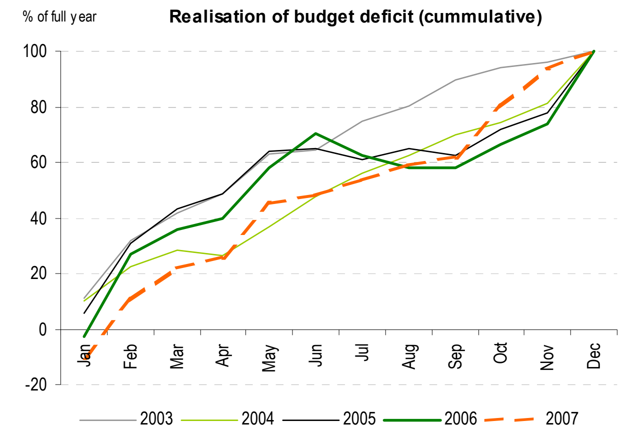
Inflationary expectations stay low

- February saw a decline in households' inflationary expectations to 1.4% from 1.5% in the preceding month. This reduction took place despite stabilisation of current inflation (which strongly affects expectations measure) at 1.4%, which suggests an improvement in a structure of poll results.
- One should anticipate that together with a rise in observed inflation at the start of 2007 there will be also a rise in inflationary expectations of households. However, if it is not coupled with significant deterioration in a structure of poll answers, it should not be necessarily a reason for concern for the MPC, as in the later part of the year a stabilisation of CPI is predicted, which should keep inflationary expectations in curbs.

Central bank watch

Comments of the central bank representatives	Our remarks
Andrzej Sławiński, MPC member **Radio PiN, 20 February** One of our allies is globalisation which decreases enterprises' possibility to transfer costs into prices. The second ally is surprisingly high productivity growth. However, there is also the central bank which should slowly start to think about monetary tightening so that inflation behave properly. In my opinion inflation will increase gradually and slowly, so I do not see a need for large changes in rates. **Bloomberg, 20 lutego** The January wage increase [stronger than expected] raised the probability of a pre-emptive hike in interest rates to buy insurance against higher consumer prices. **Jan Czekaj, MPC member** **Reuters, 15 February** I do not exclude a possibility that some factors will appear, which will force the MPC to hike rates [this year]. **Stanisław Nieckarz, MPC member** **Reuters, 15 February** If the balance of risks for inflation in the medium term moves towards higher than today's inflationary pressure as a result of higher labour costs or weaker zloty, a rate hike may be necessary at the start of 2008. **Andrzej Wojtyna, MPC member** **Rzeczpospolita, 10 February** For me the key factor is relation between rates of growth in wages and productivity. […] This [rate hike in 1H07] may happen.	Comments of majority of MPC members indicate that they expect an increase in inflation rate, but on a limited scale and gradual. This is consistent with our view. Among factors that should counteract higher inflation there are e.g. effects of globalisation and fast rise in labour productivity. However, one should also account for the fact that in the statements of central bank representatives warning signals appear more and more frequently, indicating a possibility of monetary policy tightening in the case of such developments that could threaten inflation perspectives get more persistent. While this is not a surprise in the case of those MPC members who represent very hawkish views, one cannot overlook a fact that recently a new element emerged, i.e. such comments started appearing also in interviews with those central bankers who consistently declare no need to make urgent changes in monetary policy. We think that at this moment, such comments are still just a rhetoric aimed more at keeping inflation expectations low rather than a real portent of swift rate hikes. However, we cannot ignore what the majority of MPC members say. Focusing on importance of the labour market data, they emphasise a possibility of rate hikes, which is well in line with the restrictive bias they informally adopted. While we maintain our view on flat interest rates throughout this year, in our opinion the risk of a hike has recently increased. Thus, we are somewhat surprised that market consensus is changing towards later start of monetary tightening.
Jan Czekaj, MPC member **Interfax, 28 February** You are not reading it [the statement] right. There is a sentence about economic activity. [...] If you have growth of 6.5-7.0%, then that probably means the gap is closing. [...] If GDP accelerates more, then we will act. **Marian Noga, MPC member** **Reuters, 7 March** In my opinion the financial markets did not interpret our last message too well. Apart from a statement that in the short run inflation will be lower than expected, there was a sentence that monetary tightening may be necessary.	We think the financial market is misinterpreting recent MPC communiqués, overlooking hawkish statements and focusing only on soft (dovish) comments of NBP president. Meanwhile, the MPC has been signalling straight in the last few months that a likelihood of rate hike has been rising and if relations between labour productivity and wages get worse and the Council gets more certainty about persistence of economic revival, then the rates may go up. Comments of Jan Czekaj and Marian Noga confirmed our feeling that the MPC's intention at the time of writing its last communiqué was to send a signal to the market about the Council's higher vigilance and growing probability of rate hikes. So, if this try was unsuccessful in channelling market expectations, perhaps the MPC will decide that next communiqués will have to be even more straightforward and more hawkish.
Marian Noga, MPC member **Reuters, 7 March** The Council sees risks and in my opinion should tighten its policy already now to prevent inflation topping not only 2.5%, but 3.5%. There is a risk and this is why we must act now. As time passes, the risk rises that the council will be too late with monetary tightening. Taking two small steps now would be less painful for the economy and would give better effect than killing prices later when they get out of control. **Halina Wasilewska-Trenkner, MPC member** **PAP, 6 March** We should act in advance, recongnise signs of inflation growth and react timely. [...] If the MPC waits too long with a rise in interest rates if it delays until the second half of 2007, this may be too late and sharp monetary tightening might have to be needed.	A few members of the MPC would like to hike rates already now. We should remember, however, that these are opinions of members, who used to vote in favour of hikes already in the fourth quarter (and lost), using the same line of reasoning. As the time showed, the argumentation was not entirely convincing. By now, a belief that monetary tightening should be applied right now is still in minority among MPC members. It seems that an important factor that could influence opinions of "mainstream" Council members would be a release of new Inflation report in April. After publication of last report, the MPC members signalled that in the next quarters they will pay more attention to alternative models of inflation forecasting, other than ECMOD that was a core of inflation projections until recently. If the results of other models updated and analysed this time, and/or results of base model after introduction of some corrections in the assumptions, confirm that there is a risk of breaching inflation target in the medium run, then it could tip the scales in favour of rate hikes.

Government and politics

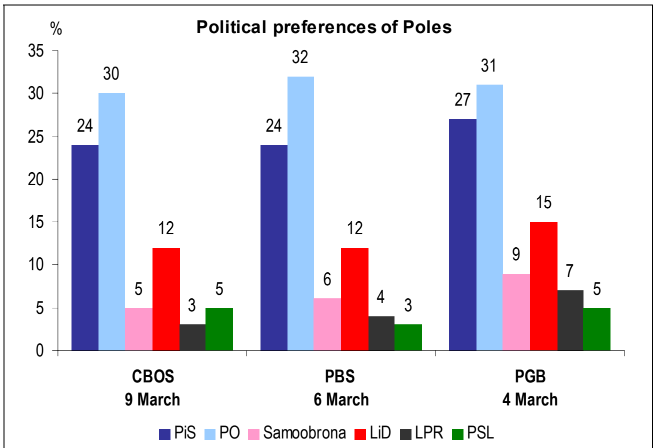


Schedule of revenues and spending realisation in 2007

	revenues	spending	deficit	deficit (cumulative)
January	22.3	19.2	3.09	3.09
February	15.8	22.0	-6.23	-3.13
March	17.1	20.6	-3.47	-6.61
April	21.2	22.3	-1.12	-7.72
May	17.7	23.5	-5.82	-13.55
June	18.5	19.4	-0.96	-14.50
July	18.3	19.8	-1.55	-16.06
August	20.2	21.9	-1.70	-17.76
September	19.7	20.5	-0.79	-18.55
October	20.3	25.8	-5.46	-24.01
November	19.5	23.6	-4.11	-28.12
December	18.4	20.3	-1.88	-30.00

Disability pension contribution – the Ministry of Finance's plans

	current plan	previous plan
mid-2007	reduction by 3 pp to 10%	-
2008	reduction by 4 pp do 6%	reduction by 3 pp to 10%
2009	-	reduction by 3 pp to 7%



Source: BZWBK, Ministry of Finance, opinion polls

Budget surplus in January

- The Ministry of Finance informed that in January the central budget recorded the surplus of PLN3bn (revenues at PLN22.3bn and expenditures at 19.2bn), as compared to PLN1.4-1.5 expected previously.
- Such a positive result was driven mainly by very high revenues (increase by 14.6%YoY), out of which indirect taxes performed extremely good with the highest monthly inflow of PLN17.5bn (rise by 77%YoY). Most likely, it was at least partly driven by moving some of last year's revenues into 2007.
- It seems that very high economic growth this year will make execution of the budget quite easy. Let's remind that budgetary macroeconomic assumptions showed GDP growth of 4.6%.

… and realisation should be no problem in 2007 as a whole

- The Ministry of Finance presented also the full-year plan of execution of the budget deficit as well as revenues and expenditures. This shows that all three elements are expected to be in line with the budget plan.
- We think that in case of budget deficit there is even a chance for lower figure, as this will be connected with higher revenues (although this will be partly spent on lowering disability pension contribution) and a possibility of lower spending, similarly as it was observed in the previous year.
- The forecasted path of budget deficit will of course affect, to some extent, the planned schedule of supply of government's treasuries on the primary market this year. We describe this issue in this months' *Special focus*.

Tax wedge reduction – faster, stronger

- Better execution in the budget, will result in earlier than previously assumed reduction in disability pension contribution.
- This year's reduction will concern the part of the contribution paid by employees, which amounts to 6.5 percentage points, while the next step in reduction planned for 2008 will be equally distributed between employees and employers.
- According to the Ministry of Finance, reduction in tax wedge by one percentage point in contribution would cost the budget almost PLN3bn. As a result, financial consequences of tax wedge cut in the middle of this year will amount to PLN3.4bn in 2007, while cumulative effect of 2007 and 2008 cuts will represent PLN19-20bn cost for the next year's budget.
- Unfortunately, this changes will not be accompanied by reduction in spending growth.

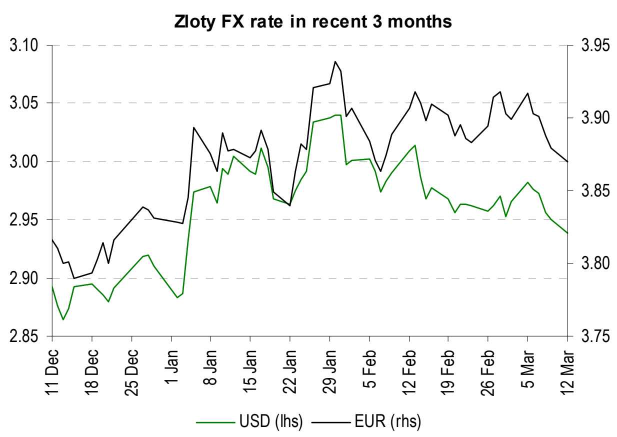
No changes in politics

- Opinion polls showing Poles' political preferences did not change much recently – Civic Platform leads with above 30% support, PiS has some 25%, while left-wing LiD is third with small two-digit support. The remaining parties show different results depending on the poll, but it is hard to say that breaking parliament threshold of 5% would be easy in their case.
- Though it makes no much sense, some polls appeared, which take into account possibility of new political parties. If ex-PM Marcinkiewicz forms a party with PO's Rokita, they could count on 8% support, while ex-PO leader together with ex-president Kwaśniewski could reach as much as 21%.
- As for now, another conflicts within the ruling coalition were head off and early elections do not seem a likely option.

Government and politics

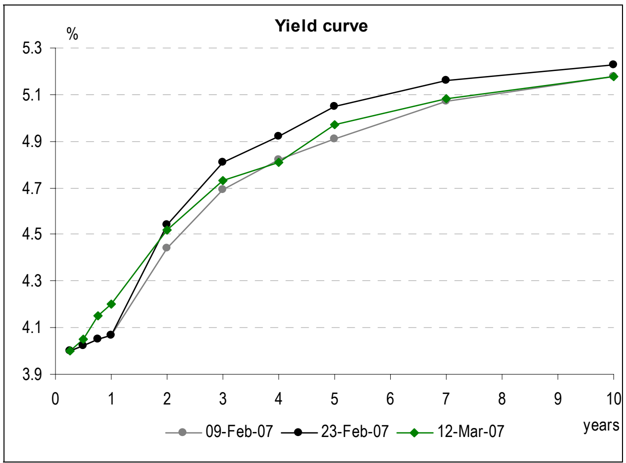
Comments of government representatives and politicians	Our remarks
Joaquin Almunia, EU monetary policy commissioner **Reuters, 27 February** I would recommend the Polish authorities to make use of the period of high economic activity (…) to take steps needed towards a considerable reduction of excessive deficit. We do not suggest any detailed solutions. We indicate only that no steps were undertaken until now, to reduce the excessive deficit. **Zyta Gilowska, deputy PM, finance minister** **Reuters, 21 February** Everything suggests that the year of 2006 will end with much better result than we previously forecasted. I would not be surprised if the deficit was around 3.5 percent of GDP in 2006 and this would mean that our assumption of fiscal deficit below 3.5% in 2007 cannot be questioned. And the European Commission still tries to question this. The assumption of maintaining high GDP growth within next 5-6 years is based on several factors e.g. funds from the European Union, transfers of money from Poles working abroad. **Katarzyna Zajdel-Kurowska, deputy finance minister** **Reuters, 23 February** The risk that we will not fulfil the recommendation of the European Commission is small. What is more, if the deficit is close to 3% of GDP the Commission will allow to exclude costs of pension system reform (…) ,which will decrease the deficit by 1.2% of GDP. Forecasts for this year are based on very conservative assumptions and if the situation on the foreign exchange market is favourable, and there are circumstances to assume this as we have very good macroeconomic situation and strong capital inflow, we can have public debt increase much slower.	Very good performance of the Polish economy results in even more optimism among the Ministry o Finance's representatives. Although we have also recently raised, similarly as majority of market participants, the forecast of GDP growth this year, it seems the ministry is the most optimistic. They said economic growth this year may exceed 6%. And the finance minister mentioned figures as high as 7-8% as a possible outcome. The European commission has also changed forecasts for Poland. From this point of view, it is interesting that the criticism as regards too optimistic assumptions of GDP growth presented in the Polish convergence Programme, was replaced by the revision in growth forecast to some 6%. As the situation in the Polish economy is as positive, the EU commissioner changed the main line of reasoning. While the Polish authorities expect high revenues driven by positive economic climate to help in bringing the fiscal deficit down to the level recommended by the Commission, Almunia sees to major steps taken in order to lower fiscal imbalance. What is interesting, both sides may be right. It may turn out that reduction in fiscal deficit will be in line with the Convergence Programme's assumptions despite no additional steps by Polish cabinet. This would be purely the result of higher revenues. The problem is, however, that the Ministry of Finance already found some ways to spend additional revenues. Fortunately, these resources would not be spend on increasing budget expenditures (well, minor coalition partners of PiS would not have problem with that), but will be used to lower tax burden in the economy. PIT Act accepted by the parliament last year assumes lowering taxes for individuals starting 2009. Additionally, the planned reduction in tax wedge should take place earlier than previously expected. Disability pension contribution was supposed to fall by 6 percentage point (3 pp in 2008 and 3 in 2009), while today's plan is to bring it down by 7 pp (3 pp in mid-2007 and 4 in 2008). Unfortunately, this move would be mainly aimed at lowering contribution paid by employees (and private consumption growth is high).
Zyta Gilowska, deputy PM, finance minister **PAP, 26 February** I am very sceptical about annual indexation. Technical costs of such operation are very high and the record-low inflation in 2006 as well as low inflation expected for 2007 (as shown by our analysis) makes the increase in pensions and disability pensions very low on net basis, I would say this would be irritatingly low. I do not know why minister Kalata assumes such high indexation, as the main factor responsible for this i.e. high inflation does not exist right now. It is quite contrary – average inflation for 2006 was at 1% last year and it was the lowest level since the beginning of 70s. If we add the expected 2% in 2007, this is still too low for indexation. Minister Kalata should have know that the aim of indexation is not to change the system, but to adjust the level of payments to real value of money. **Anna Kalata, labour minister** **Reuters, 17February** In June, we will present the cabinet with a bill amendment increasing the minimum wage. We want to do it after consultations in Three-Party Committee, as we do not want this change, if launched too quickly, to lower the profitability of Polish companies. However, the increase of minimum wage to 50-60% of average wage is very much needed to stop emigration.	It is hard to find more controversial proposals than those presented recently by the Labour Ministry. Of course, representatives of Self-Defence could even return to the pre-election proposal to equal the minimum wage with the average wage in the economy (quite hard to make mathematically), but we do not think that sharp increase in the minimum wage is the best idea to stop emigration of Poles to work abroad. What this should be? Well, we hope the next idea would not be to make the Polish minimum wage dependant on average wage in Ireland or United Kingdom. Equally controversial is the proposal as regards the indexation of pensions. The Ministry of Labour and Social Affairs will probably force the idea of making the indexation each year and additionally to take into account not only the inflation rate, but also 20% of increase in average wage in the economy. It is not surprising that the Ministry of Finance is against such idea. And this is not only connected with the fact that additional money would be needed in the budget, as according to the labour minister, Anna Kalata, the idea would cost above PLN4bn in 2008. simply, with low inflation rate the annual indexation makes no sense. Anyway, the Labour Ministry has recently become a bank of bad ideas for the Polish economy. Besides the above-mentioned plans, which would lead to lower competitiveness of the Polish economy, we saw also the idea that public Social Security Office could manage money in the private second pillar of pension system. Fortunately, recent comments of other government's representatives seem to lower this risk.
Jacek Krzyślak, director of research department in the Ministry of Finance **Reuters, 1 February** Inflation results are in line with our expectations. The highest impact was connected with food prices increase (by 1.3 percentage point) as well as with higher housing prices, including energy prices. We should also notice that fuel prices fell despite higher excise tax. We expect that 12M CPI inflation in the first quarter will be below 2%.	Indeed the January's inflation was in line with expectations of the Ministry of Finance (and ours). As this was not the first time the ministry was right, the average (median) of market expectations has been recently in line with the ministry's assumptions. However, we think that forecasts presented recently by director Krzyślak may be too optimistic, as regards the inflation level in the first quarter. . We expect 12M CPI inflation to reach 2.2%in March, though of course the inflation path in 2007 will to some extent depend on the new basket, which will be announced in mid-March.

Market monitor



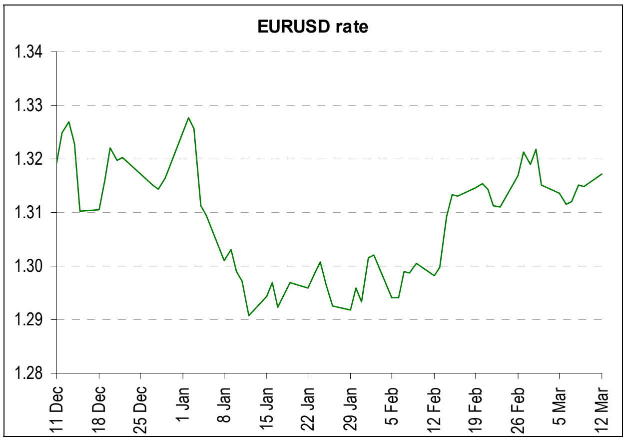
Zloty stable despite emerging markets sell-off

- Since the release of our last report zloty remained quite stable and fluctuated in a tight range (3.88-3.93 against the euro). At the end of February there was a quite significant weakening in the emerging markets in reaction to rising fears of slowdown of US economy. This contributed to a significant drop of stock indices in the stock markets as well as yen and Swiss franc strengthening (limiting „carry trades"). However zloty remained quite stable.
- Further rise of fears of the situation in United States (low economic growth amid fears of inflation) may contribute to international markets nervousness, which may increase risk and thus emerging markets aversion. It seems however that good data from the Polish economy will still support the zloty and we do not expect a serious sudden weakening.



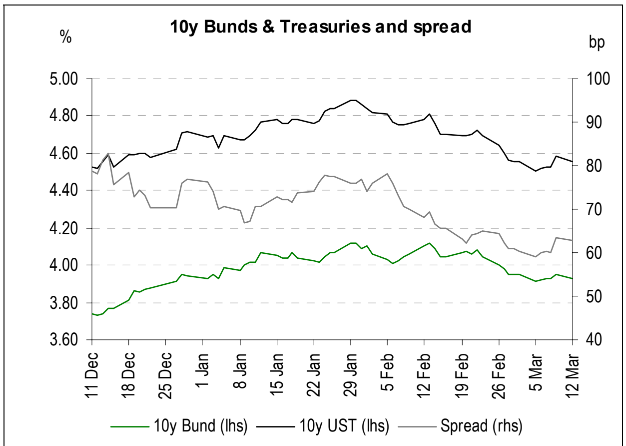
Slight rise in yields

- During most of the February bonds yields rose by ca. 4-10 bp, and the yield curve slightly flattened. In the same time there was a substantial strengthening in the core markets. Despite higher and higher number of MPC comments on the possible interest rate hike the Council's statement was perceived as a less hawkish than expected, which along the weaker than expected Q4 GDP data slightly supported the short end of the curve. The sell-off in the emerging markets did not significantly influence the Polish debt market.
- After substantial strengthening in the core markets there may be some correction amid fears over US inflation. This may negatively affect the longer end of the yield curve. On the other hand the rising domestic inflation may have a negative impact on the short end of the curve. Until then the Council members may sharpen their hawkish statements.



Dollar weakens after softer data from US

- In the second part of February the dollar weakened above 1.31 vs. the euro on weaker data from US economy (retail sales, industrial production, labour and housing market). The US central bankers comments on expected fall of inflation and weak Ifo resulted in dollar's recovery. Further weak data from US (revised Q4 GDP, retail sales) contributed to another dollar's depreciation. Calming Bernanke's comments and ISM index slightly improved the moods.
- Amid heavy influence of housing market slowdown on other sectors of US economy the greenback may be still under pressure. All the more business climate in the euro zone is expected to remain positive. We expect that in several weeks the EURUSD rate may rise even to 1.33.

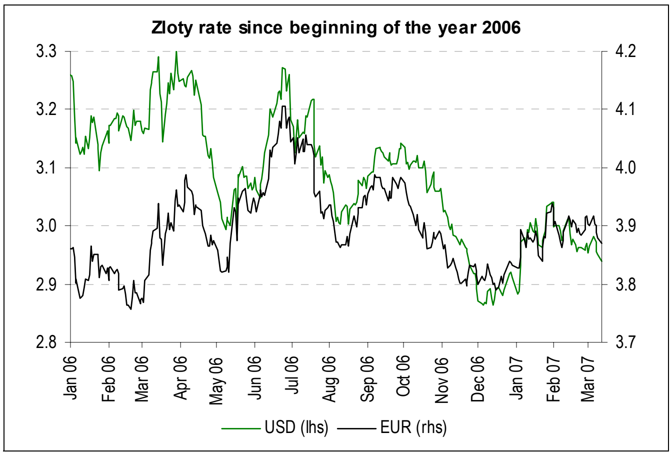


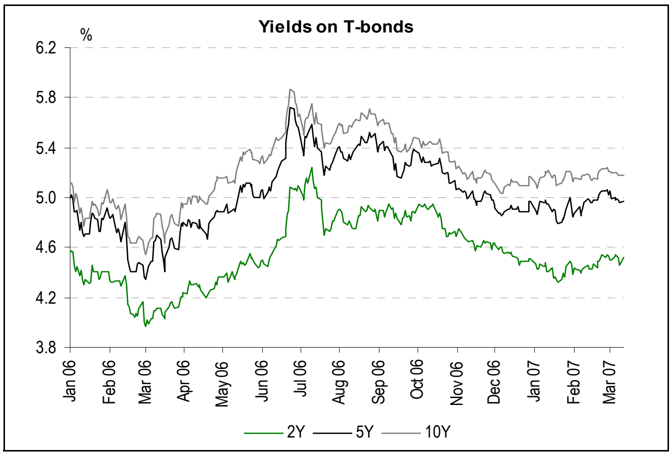
Yields fall after significant bonds weakening

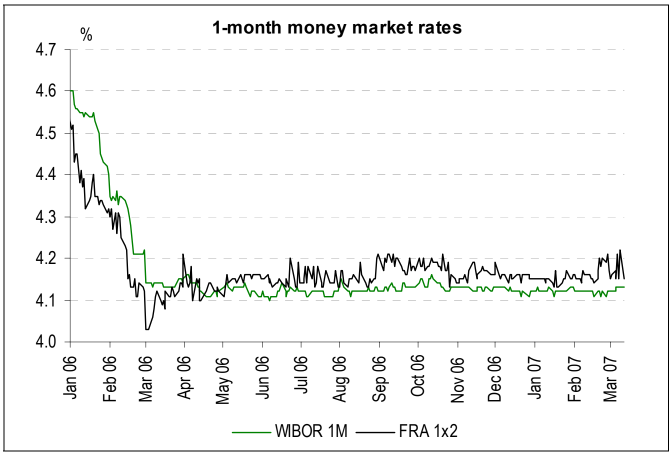
- During last month the core bond markets experienced significant strengthening most of all due to weak data from the US economy and fears of potential recession in US. These factors resulted in the rise of risk aversion and flight to quality. In the last days the situation slightly stabilised. Ultimately yields of 10Y Treasuries fell since the mid-February by 25 pb, and 10Y Bunds by 14 bp.
- We hold our opinion that amid economic slowdown in United States and assuming the falling inflation scenario Fed may decide to cut the interest rates in the second part of this year. In our view the interest rates in the euro zone are going to rise to 4% and any further moves will depend on the situation in the US economy and its influence on global markets as well as further economic data from the EA13 countries.

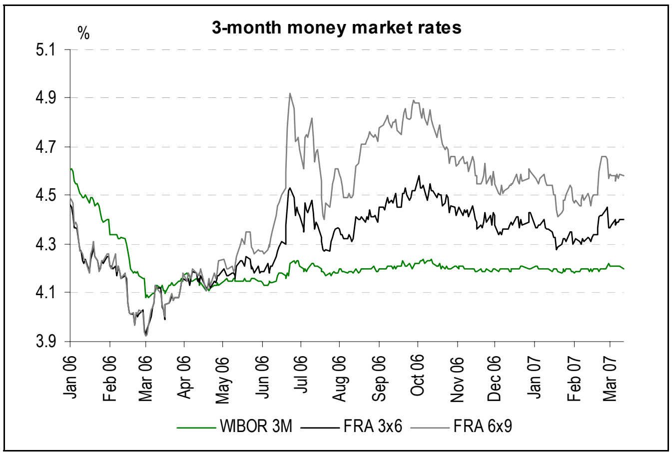
Source: Reuters, BZ WBK

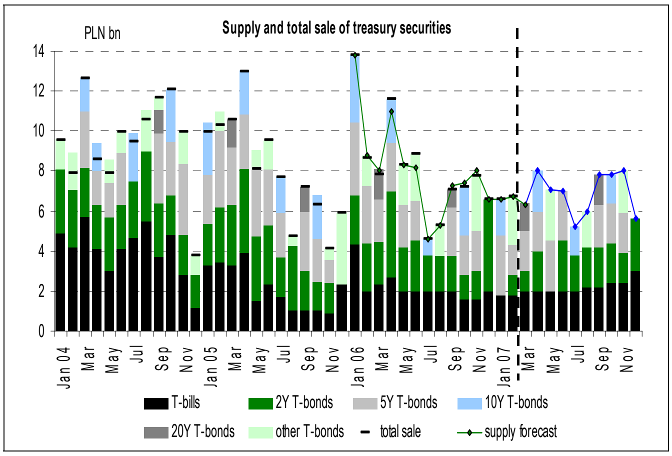
Market monitor











Treasury bill auctions (PLN m)

	OFFER / SALE	
Date of auction	52-week	Total
08.01.2007	900 / 900	900 / 900
22.01.2007	900 / 900	900 / 900
Total January	**1 800 / 1 800**	**1 800 / 1 800**
05.02.2007	900 / 900	900 / 900
19.02.2007	900 / 900	900 / 900
Total February	**1 800 - 1 800**	**1 800 / 1 800**
05.03.2007	1 000 / 1 000	1 000 / 1 000
19.03.2007	1 000 - 1 200	1 000 – 1 200
Total March*	**2 000 - 2 200**	**2 000 - 2 200**

* estimations based on Ministry of Finance preliminary information

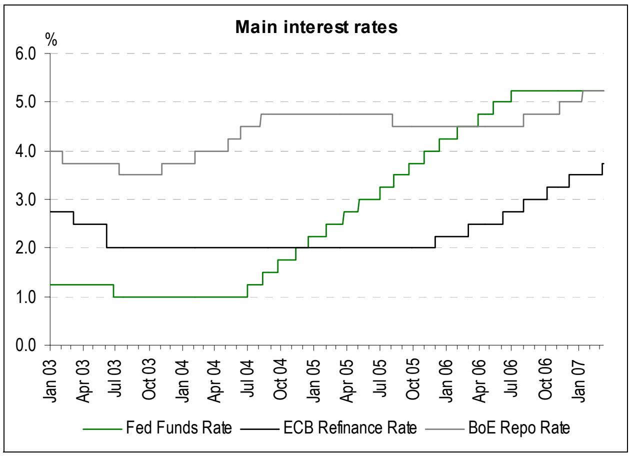
Treasury bond auctions in 2007 (PLN m)

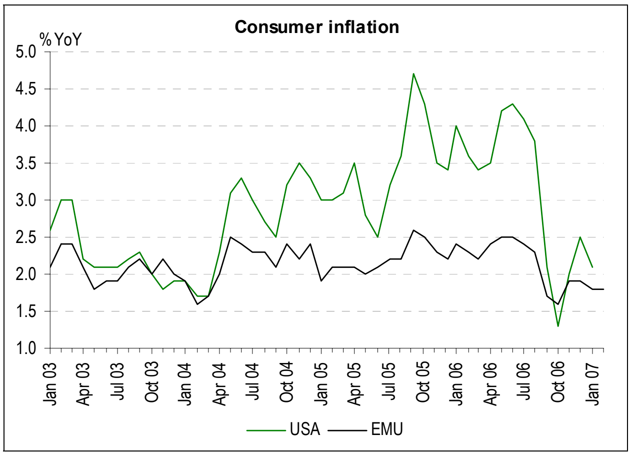
month	First auction				Second auction				Third auction			
	date	T-bonds	offer	sale	date	T-bonds	offer	sale	date	T-bonds	offer	sale
January	-	-	-	-	10.01	DS1017	1 800	1 800	17.01	PS0412	3 000	3 000
February	07.02	OK0709	1 000	1 000	14.02	WZ0118 | IZ0816	2400 | 0	2400 | 0	21.02	PS0412	1 500	1 500
March	07.03	OK0709	1 000	1 000	14.03	WS0922	1 400	-	21.03	PS0412	1 000 - 2 000	1 000 - 2 000
April	04.04	2Y	-	-	11.04	10Y	-	-	18.04	5Y	-	-
May	-	-	-	-	09.05	10Y WIBOR | 12Y CPI	-	-	16.05	5Y	-	-
June	06.06	2Y	-	-	-	-	-	-	20.06	5Y	-	-
July	04.07	2Y	-	-	11.07	10Y	-	-	-	-	-	-
August	01.08	2Y	-	-	08.08	10Y WIBOR | 12Y CPI	-	-	-	-	-	-
September	05.09	2Y	-	-	12.09	20Y	-	-	19.09	5Y	-	-
October	03.10	2Y	-	-	10.10	10Y	-	-	17.10	5Y	-	-
November	07.11	2Y	-	-	14.11	10Y WIBOR | 12Y CPI	-	-	21.11	5Y	-	-
December	05.12	2Y	-	-	-	-	-	-	-	-	-	-

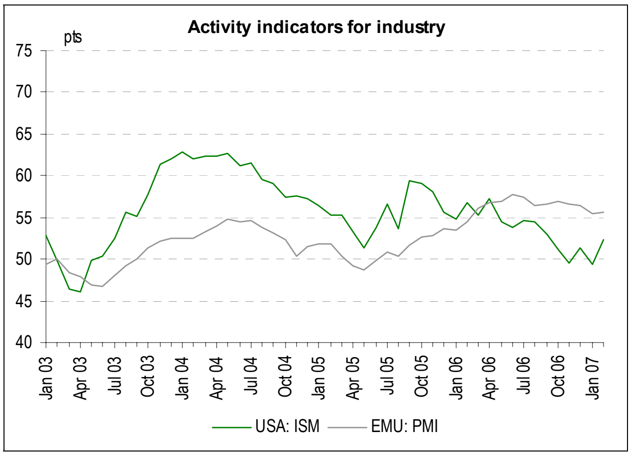
* with supplementary auction

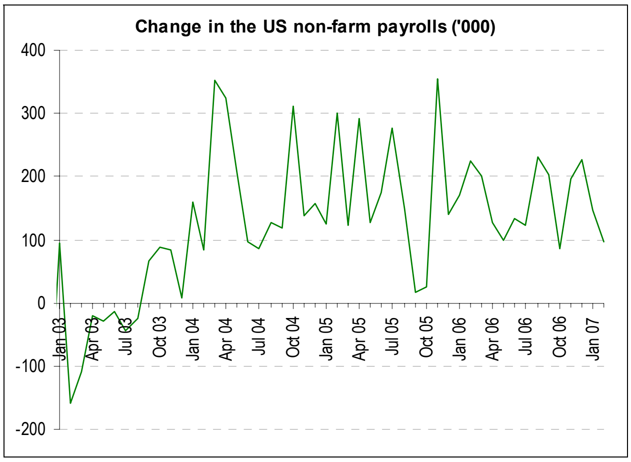
Source: Ministry of Finance, Reuters, BZ WBK

International review









Source: Reuters, ECB, Federal Reserve

Rate hike in the euro zone

- Although the Fed's communiqué expressed the view of falling inflation, the later released FOMC minutes included some wording suggesting uncertainty in this issue. Alan Greenspan expressed his fears on possibility of recession at the end of this year, though Ben Bernanke maintained his view that US economy may be stronger than everybody expects.
- European Central Bank raised main interest rates by 25 bp to 3.75%, which was in line with expectations. According to European central bankers' view, the level of official rates is "moderate" ("low" in the previous statements). Such change in wording may suggest that the ECB considers further monetary tightening in the euro zone, though the cycle may be close to the end.

US core CPI still high

- US CPI inflation for January rose by 0.2%MoM against market consensus of 0.1%MoM. On annual basis CPI inflation fell from 2.5% in December to 2.1%, which was similar to monthly data moderately above expectations that stood at 2.0%. Core inflation index, excluding food and energy prices, rose by 0.3%MoM and 2.7%YoY against market average forecast at 0.2% and 2.6%, respectively. PPI fell in January by 0.6%MoM)+0.2%YoY, while analysts expected a fall by 0.5%MoM. The core index rose by 0.2%MoM and 1.8%YoY.
- Euro zone's inflation rate measured by HICP index reached 1.8%YoY in January against earlier estimate and expectations 1.9%. According to preliminary data fro February the inflation in the EA13 amounted to 1.8%YoY, while the market expected a rise to 1.9%YoY.

Manufacturing ISM above 50, downward revision of US GDP

- ISM index for the US manufacturing sector appeared much higher than forecasted (50) as it rose to 52.3 from 49.3 amid rise of all components. On the other hand non-manufacturing ISM declined from 59.0 to 54.3 against market consensus at 57.5.
- Manufacturing PMI index in the euro zone rose in line with expectations from 55.5 in January to 55.6 in February. PMI services index fell from 57.9 to 57.5 against forecasted 57.7.
- The figure of US GDP growth in 4Q06 was revised downwards from 3.5%YoY to 2.2% against expectations at 2.4%. This was mainly caused by change in inventories, though consumption and investments growth rates were also lowered. GDP deflator was revised to 1.6% from 1.5%, while core deflator PCE was down to 1.9% from 2.1%.
- The Q4 GDP data from the EA12 showed a rise by 0.9%QoQ and 3.3%YoY, which was in line with expectations.

No serious weakening in the labour market

- ADP report that showed a notable fall in the US non-farm employment in the private sector from 121k in January to 57k in February. Actually the non-farm payrolls in American economy rose in February by 97k in line with expectations. Although it was the lowest increase in more than two years, at the same time data for two preceding months have been revised upwards quite substantially, by 55,000. The data from the labour market met with quite positive reception, as they did not confirm the most pessimistic forecasts heralding severe slowdown in economic activity in the US. Unemployment rate declined to 4.5% in February against predicted 4.6%.
- Unit labour costs in United States in Q4 rose by 6.6% after revision from 1.7%. In turn, labour productivity was revised down from 3.0% to 1.6%.

Economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
12 March US: Federal budget (Feb)	**13** GER: ZEW Index (Mar) US: Retail Sales (Feb) US: Foreign trade prices (Feb)	**14** ***POL: Auction of 20Y bonds*** ***POL: CPI (Jan & Feb)*** ***POL: Money supply (Feb)*** ***POL: Balance of payments (Jan)***	**15** ***POL: Wages and Employment (Feb)*** EMU: Final HICP (Feb) US: PPI (Feb) US: Net capital flows (Jan) US: Philadelphia Fed index (Mar)	**16** US: CPI (Feb) US: Capacity utilization (Feb) US: Industrial output (Feb) US: Preliminary Michigan (Mar)
19 ***POL: Treasury bills auction*** ***POL: PPI (Feb)*** ***POL: Industrial Output (Feb)*** US: Home sales (Jan)	**20** JP: BOJ meeting – decision US: House starts (Feb)	**21** ***POL: Auction of 5Y bonds*** USA: Fed meeting – decision	**22** ***POL: Business climate (Mar)*** US: Home sales (Feb)	**23** ***POL: Retail sales (Feb)*** ***POL: Unemployment (Feb)*** US: Preliminary Michigan (Mar)
26 JP: BOJ minutes US: New homes sales (Feb)	**27** ***POL: MPC meeting*** GER: Ifo Index (Mar) USA: Consumer confidence (Mar)	**28** ***POL: MPC meeting – decision*** EMU: M3 money supply (Feb) US: Durable goods orders (Feb)	**29** ***POL: Switch auction*** US: Final GDP (Q4) US: Final PCE (Q4)	**30** ***POL: Balance of payments (Q4)*** EMU: Business climate (Mar) EMU: Preliminary HICP (Mar) USA: Core PCE (Feb) USA: Chicago PMI (Mar) US: Final Michigan (Mar)
2 ***POL: Treasury bills auction*** EMU: Non-manufacturing PMI (Mar) US: Non-manufacturing ISM (Mar)	**3** USA: Pending homes (Feb)	**4** ***POL: Auction of 2Y bonds*** EMU: Manufacturing PMI (Mar) USA: ADP report (Mar) US: Manufacturing ISM (Mar) US: Factory orders (Feb)	**5** ***POL: Switch auction***	**6** US, DE, GB: Market holiday US: Non-farm payrolls (Mar) US: Unemployment (Mar) US: Wholesale inventories (Feb)
9 DE, GB: Market holiday	**10** JP: BOJ meeting – decision	**11** ***POL: Auction of 10Y bonds***	**12** EMU: GDP (Q4) EMU: Industrial production (Feb) EMU: EBC meeting - decision US: Foreign trade prices (Mar)	**13** ***POL: CPI (Mar)*** ***POL: Money supply (Mar)*** ***POL: Balance of payments (Feb)*** US: Trade balance (Feb) US: PPI (Mar) US: Preliminary Michigan (Apr)

Source: CSO, NBP, Finance Ministry, Reuters

MPC meetings and data release calendar for 2007

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
MPC meeting	30-31	27-28	27-28	24-25	29-30	26-27	24-25	28-29	25-26	30-31	27-28	18-19
GDP*	-	-	2	-	31	-	-	30	-	-	30	-
CPI	15	15[a]	14[b]	13	15	13	13	14	13	15	14	13
Core inflation	22		23[b]	23	23	22	23	23	24	22	23	21
PPI	19	19	19	20	21	20	19	20	19	18	20	19
Industrial output	19	19	19	20	21	20	19	20	19	18	20	19
Retail sales	29	23	23	-	-	-	-	-	-	-	-	-
Gross wages, employment	16	15	15	18	17	19	17	16	15	16	16	15
Unemployment	29	23	23	-	-	-	-	-	-	-	-	-
Foreign trade	about 50 working days after reported period											
Balance of payments*	2	-	30	-	-	-	-	-	-	-	-	-
Balance of payments	16[c]	12	14	13	18	-	-	-	-	-	-	-
Money supply	12	14	14	13	14	-	-	-	-	-	-	-
NBP balance sheet	5	7	7	6	7	-	-	-	-	-	-	-
Business climate indices	23	22	22	23	23	22	23	23	24	23	23	21

* quarterly data, [a] preliminary data, January, [b] January and February, [c] November 2006, [d] January, [e] February

Source: CSO, NBP

Economic data and forecasts

Monthly economic indicators

		Feb 06	Mar 06	Apr 06	May 06	Jun 06	Jul 06	Aug 06	Sep 06	Oct 06	Nov 06	Dec 06	Jan 07	Feb 07	Mar 07
Industrial production	%YoY	10.2	16.4	5.7	19.1	12.2	14.3	12.6	11.6	14.8	12.0	5.9	15.6	12.7	10.5
Retail sales [c]	%YoY	10.2	10.1	13.2	13.7	10.7	11.0	11.5	14.5	13.3	13.6	13.3	16.5	15.9	15.9
Unemployment rate	%	18.0	17.8	17.2	16.5	16.0	15.7	15.5	15.2	14.9	14.8	14.9	15.1	15.0	14.9
Gross wages [b c]	%YoY	4.8	5.4	4.0	5.2	4.5	5.6	5.3	5.1	4.7	3.1	8.5	7.8	6.5	6.2
Employment [b]	%YoY	2.4	2.7	2.8	3.0	3.1	3.3	3.5	3.5	3.6	3.8	4.1	3.8	3.8	3.9
Export (€) [d]	%YoY	19.2	28.2	9.8	32.5	16.9	19.4	21.8	16.6	23.6	21.9	8.3	17.6	10.2	11.2
Import (€) [d]	%YoY	22.0	23.9	10.1	29.9	17.2	23.6	23.7	19.2	27.5	20.6	17.0	18.7	13.2	14.1
Trade balance [d]	EURm	-229	-130	-108	-439	-103	-450	-518	-356	-283	-287	-1080	-71	-465	-378
Current account balance [d]	EURm	-839	-356	-597	-374	-300	-387	-668	143	-587	-531	-915	-196	-835	-543
Current account balance [d]	% GDP	-1.8	-1.9	-2.1	-1.9	-2.0	-2.0	-2.1	-1.9	-2.0	-2.0	-2.1	-2.1	-2.1	-2.1
Budget deficit (cumulative)	PLNbn	-6.7	-9.0	-10.0	-14.6	-17.7	-15.6	-14.5	-14.5	-16.6	-18.5	-25.1	3.1	-3.1	-6.6
Budget deficit (cumulative) [e]	% realisation	26.7	35.8	40.0	58.2	70.4	62.3	57.9	57.8	66.3	73.9	100.0	-10.3	10.4	22.0
CPI	%YoY	0.7	0.4	0.7	0.9	0.8	1.1	1.6	1.6	1.2	1.4	1.4	1.7	1.9	2.2
PPI	%YoY	0.7	0.9	1.7	2.3	3.0	3.5	3.3	3.6	3.2	2.5	2.6	2.9	3.2	3.2
Broad money (M3)	%YoY	11.7	9.8	9.6	10.1	11.9	13.0	12.9	13.0	12.3	14.4	15.6	19.4	17.5	17.3
Deposits	%YoY	10.8	9.1	8.6	8.9	11.4	12.3	12.0	11.6	11.4	13.1	15.0	18.4	17.5	17.2
Loans	%YoY	13.5	13.6	12.2	12.4	16.0	16.7	18.0	19.2	19.5	20.7	23.4	25.0	23.1	22.6
USD/PLN	PLN	3.18	3.23	3.20	3.05	3.17	3.15	3.05	3.12	3.09	2.97	2.88	2.98	2.98	2.98
EUR/PLN	PLN	3.79	3.88	3.92	3.90	4.02	4.00	3.90	3.97	3.90	3.82	3.81	3.88	3.90	3.91
Reference rate [a]	%	4.25	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00
Lombard rate [a]	%	5.75	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50
WIBOR 3M	%	4.26	4.12	4.14	4.15	4.17	4.19	4.19	4.21	4.22	4.20	4.20	4.20	4.20	4.20
Yield on 52-week T-bills	%	3.97	3.87	3.95	4.02	4.20	4.30	4.35	4.44	4.35	4.29	4.20	4.14	4.07	4.20
Yield on 2-year T-bonds	%	4.20	4.10	4.28	4.44	4.75	4.95	4.85	4.87	4.84	4.65	4.54	4.41	4.46	4.55
Yield on 5-year T-bonds	%	4.60	4.59	4.80	5.00	5.33	5.37	5.41	5.31	5.24	5.01	4.91	4.90	4.97	5.05
Yield on 10-year T-bonds	%	4.78	4.78	5.02	5.26	5.54	5.55	5.61	5.48	5.39	5.18	5.10	5.16	5.18	5.25

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates

[a] at the end of period [b] in corporate sector [c] in nominal terms [d] balance of payments data on transaction basis [e] 2005 - % of Dec, 2006 - % of plan

Quarterly and annual economic indicators

		2004	2005	2006	2007	1Q06	2Q06	3Q06	4Q06	1Q07	2Q07	3Q07	4Q07
GDP	PLNbn	923.2	980.7	1 050.9	1 132.9	240.9	251.7	258.6	299.7	261.9	272.4	276.6	322.0
GDP	%YoY	5.3	3.5	5.8	5.7	5.2	5.5	5.8	6.4	6.7	6.0	5.2	5.1
Domestic demand	%YoY	5.9	2.4	5.9	6.3	4.8	4.8	6.1	7.7	6.9	6.8	5.8	5.9
Private consumption	%YoY	4.0	1.9	5.2	5.4	5.2	4.9	5.5	5.2	5.8	5.3	5.2	5.2
Fixed investments	%YoY	6.3	6.5	16.7	13.6	7.7	14.8	19.8	19.3	25.0	15.0	12.0	10.0
Industrial production	%YoY	12.3	4.0	12.5	9.8	12.4	12.1	12.3	10.7	13.0	10.5	8.1	7.6
Retail sales (real terms)	%YoY	7.1	1.5	11.9	13.3	9.0	11.8	13.8	12.6	15.8	14.9	12.3	10.2
Unemployment rate [a]	%	19.1	17.6	14.9	13.0	17.8	16.0	15.2	14.9	14.9	13.7	13.0	13.0
Gross wages (real terms) [c]	%YoY	0.8	1.2	4.2	4.5	4.3	3.9	4.1	4.5	4.8	4.7	5.0	3.6
Employment [c]	%YoY	-0.8	1.9	3.2	3.5	2.6	3.0	3.4	3.8	3.8	3.6	3.4	3.1
Export (€) [b]	%YoY	22.3	17.8	19.9	14.1	23.3	19.5	19.3	18.2	12.8	15.5	14.5	13.5
Import (€) [b]	%YoY	19.5	13.4	21.5	16.0	23.3	19.0	22.2	21.7	15.2	17.5	15.5	16.0
Trade balance [b]	EURm	-4 552	-2 242	-3 970	-6 435	-352	-646	-1 322	-1 650	-914	-1 212	-1 759	-2 550
Current account balance [b]	EURm	-8 670	-4 130	-5 602	-6 768	-1 396	-1 266	-907	-2 033	-1 574	-1 527	-1 039	-2 628
Current account balance [b]	% GDP	-4.3	-1.7	-2.1	-2.3	-1.9	-2.0	-1.9	-2.1	-2.1	-2.1	-2.1	-2.3
Budget deficit (cumulative) [a]	PLNbn	-41.5	-28.6	-25.1	-30.0	-9.0	-17.7	-14.5	-25.1	-6.6	-18.0	-21.0	-30.0
Budget deficit (cumulative) [a]	% GDP	-4.5	-2.9	-2.4	-2.6	-	-	-	-	-	-	-	-
CPI	%YoY	3.5	2.1	1.0	2.0	0.6	0.8	1.4	1.3	1.9	2.0	1.7	2.3
CPI [a]	%YoY	4.4	0.7	1.4	2.5	0.4	0.8	1.6	1.4	2.2	2.2	1.8	2.5
PPI	%YoY	7.0	0.7	2.5	2.4	0.9	3.0	3.6	2.6	3.1	2.1	1.7	2.9
Broad money (M3) [a]	%YoY	8.7	10.5	15.6	12.1	9.8	11.9	13.0	15.6	17.3	15.1	13.5	12.1
Deposits [a]	%YoY	8.1	9.4	15.0	14.3	9.1	11.4	11.6	15.0	17.2	17.1	16.6	14.3
Loans [a]	%YoY	2.9	11.8	23.4	18.2	13.6	16.0	19.2	23.4	22.6	21.4	20.2	18.2
USD/PLN	PLN	3.65	3.23	3.10	2.94	3.19	3.14	3.10	2.98	2.98	2.89	2.96	2.94
EUR/PLN	PLN	4.53	4.02	3.90	3.85	3.83	3.95	3.96	3.85	3.89	3.84	3.88	3.80
Reference rate [a]	%	6.50	4.50	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00
Lombard rate [a]	%	8.00	6.00	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50
WIBOR 3M	%	6.21	5.29	4.21	4.30	4.29	4.15	4.20	4.20	4.20	4.20	4.20	4.20
Yield on 52-week T-bills	%	6.50	4.92	4.18	4.20	4.02	4.06	4.37	4.28	4.14	4.15	4.20	4.30
Yield on 2-year T-bonds	%	6.89	5.04	4.57	4.63	4.23	4.49	4.89	4.67	4.47	4.60	4.60	4.85
Yield on 5-year T-bonds	%	7.02	5.25	5.03	5.07	4.67	5.04	5.36	5.05	4.97	5.00	5.00	5.30
Yield on 10-year T-bonds	%	6.84	5.24	5.22	5.27	4.83	5.27	5.55	5.22	5.20	5.20	5.20	5.50

Source: CSO, NBP, Finance Ministry, BZ WBK own estimates

[a] at the end of period; [b] balance of payments data on transaction basis [c] in corporate sector

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