Positive business sentiment in the Eurozone continues

This week

- **Parliamentary elections in Germany took place on Sunday.** According to the initial official results, the election was won by CDU/CSU coalition with 33.0% of votes, followed by SPD (20.5%), AfD (12.6%), FDP (10.7%), the Left (9.2%) and the Greens (8.9%). Considering the poll results and SPD announcement that it intends to move to opposition, a coalition of CDU/CSU, FDP and the Greens seems to be the most likely scenario. These parties present a similar pro-European approach, therefore no significant change should be expected in the German foreign policy. The main risk is the future fiscal policy. This view is supported by the statement of an executive member of the FDP, A. Hahn, who suggested that the FDP would join the coalition only if given the position of the minister of finance. We believe that despite a worse-than-expected result of CDU/CSU and the necessity of establishing broader coalition, no significant changes in German economic or foreign policy should be expected. Nevertheless, the surprising results of the parliamentary elections in Germany may contribute to a slight weakening of PLN in the short term.
- **Important hard data from the US and business survey results will be released this week**. The final estimate of GDP in Q2 will be released on Thursday. We expect that the annualized economic growth rate rose to 3.1% vs. 3.0% in the second estimate, i.a. due to higher contributions of inventories and net exports. We forecast that the monthly dynamics of preliminary durable goods orders rose to 1.5% in August vs. -6.8% in July due to higher orders in the Boeing company. We expect that data on existing home sales (5.95M in August vs. 5.71M in July) will point to the ongoing recovery in the US real estate market. Business survey results will also be released this week. We forecast that the Conference Board Consumer Confidence Index (120.0 pts in September vs. 122.9 pts in August) as well as the final University of Michigan Index (96.0 pts in September and 95.3 pts in the flash estimate) will signal a slight deterioration in households' sentiment. We believe that the publication of the US data will have a limited impact on the market.
- **Ifo Index reflecting the sentiment among German managers representing the manufacturing, construction, wholesale and retail trade sectors was released today.** It decreased to 115.2 pts in September vs. 115.7 pts in August which was slightly below the market consensus (116.0 pts). In our opinion the reading is neutral for the market.
- **The flash estimate of HICP inflation for the Eurozone will be released on Friday**. We expect that the annual inflation did not change in September compared to August and amounted to 1.5% YoY. We believe that the data will be neutral for PLN and prices of Polish bonds.
- **Data on the September inflation in Poland will be released on Friday.** In our view it rose to 2.0% YoY vs. 1.8% in August, largely due to higher dynamics of food prices. Our forecast is in line with market expectations. Therefore, we believe that the data will not have a significant impact on PLN and yields on Polish bonds.

Last week

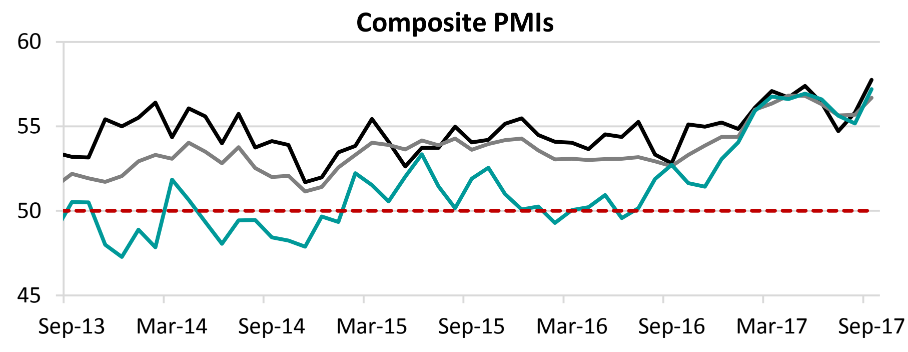
- **FOMC meeting was held last week.** As we expected, the target range for the Federal Reserve funds has been left at an unchanged level [1.00%; 1.25%]. At the same time, FED announced that the reduction of its balance-sheet would start from October 2017. It will consist in a gradual tapering of the reinvesting of proceeds obtained from its assets maturing in accordance with the schedule presented at the conference after the June meeting (see MACROmap of 19/6/2017). Thus, at the beginning, the monthly limits on the value of funds that will not be reinvested will be fixed at a level of USD 6bn for treasury bonds and at USD 4bn for MBS (mortgage-backed securities). Every three months the limits will be increased by USD 6bn and USD 4bn, respectively, until they reach the target level (USD 30bn and USD 20bn, respectively, per month) after one year's time. As we expected, the FED chair, J. Yellen, emphasized at the conference after the meeting that interest rates level was the main tool of the US monetary policy. However, she indicated that the quantitative easing program would continue being a tool of the current monetary policy and that FED might consider suspension of the balance-sheet reduction in the event of a significant deterioration of the economic outlook. Noteworthy in the statement after the meeting is the view that, although negative for the economic activity in the short term, the losses resulting from Harvey and Irma hurricanes would not have a substantial impact on the medium-term GDP growth rate in the US. At the same time, through higher fuel prices, they might contribute to a temporary increase in inflation. New macroeconomic projections by FOMC members were presented at the conference after the meeting. As compared to the June projection, the median expected GDP growth rate in 2017 slightly rose (2.4% vs. 2.2%). The expected growth rate in subsequent years has not changed and amounts to 2.1% in 2018, 1.9% in 2019, 1.8% in 2020 and 1.8% in the long term. The expected unemployment rate has been slightly lowered. Now the median expectations for Q4 2017 amount to 4.3% (4.3%), 4.1% in Q4 2018 and 2019 (4.2%), and 4.2% in Q4 2020. On the other hand the estimate of natural unemployment rate has been left unchanged at 4.6%. Noteworthy is also a slight downwards revision of the expected PCE inflation profile. Now the median expectations for 2017 amount to 1.5% (1.7%), 1.9% in 2018 (2.0%), 2.0% in 2019, and 2.0% in 2020. Thus, the median expectations of FOMC members indicate that the inflation target will be reached no sooner than in 2019 while in the June projection it was to take place in 2018. The profile of federal funds interest rate expected by FOMC members has been left at a level similar to the June projection. Now the median expectations concerning the amount of interest rates as at the end of 2017 amount to 1.4% (1.4%), 2.1% at the end of 2018 (2.1%), 2.7% at the end of 2019 (2.9%), 2.9% at the end of 2020 and 2.8% in the long term (3.0%). The September FOMC economic projection supports our scenario in which FED will hike interest rates by 25bp in December 2017. However, we believe that the incoming data on inflation will not be sufficient justification for the monetary tightening scale in 2018 expected in the September projection (by 75bp). Therefore, we forecast that the scale of interest rate hikes in 2018 will be lower from FOMC members' expectations and will amount to 50bp.

- **Composite PMI Index (for manufacturing and the services sector) in the Eurozone rose to 56.7 pts in September from 55.7 pts in August.** The index increased due to higher values of its sub-indices for both business activity in services and output in manufacturing. The average value of PMI Composite amounted to 56.0 pts in Q3 vs. 56.6 pts in Q2, which supports our forecast assuming that GDP growth rate in the Eurozone will slightly drop to 0.5% QoQ in Q3 vs. 0.6% in Q2 (see below).
- **Hard data from the US economy and business survey results were released last week.** The data on building permits (1300k in August vs. 1230k in July), housing starts (1180 vs. 1190), and existing home sales (5.35M vs. 5.44M) pointed to continuing rebound in the real estate market. Philadelphia FED Index was also released last week and rose to 23.8 pts in September vs. 18.9 pts in August, suggesting increased economic activity in the district within the domain of Philadelphia Fed (comprising western part of Philadelphia, southern part of New Jersey and Delaware). We forecast that the annualized US GDP growth rate will drop to 2.8% in Q3 vs. 3.1% in Q2.
- **The dynamics of industrial production in Poland rose to 8.8% YoY in August vs. 6.2% in July**. Conducive to the acceleration in output growth in August was the abatement of the effect related to longer than last year holiday breaks in car factories in July 2017. In addition, industrial production in August was supported by continuing increase in new export orders in manufacturing and orders from construction companies (see MACROpulse of 19/9/2017). The construction-assembly production growth rose to 23.5% YoY in August vs. 19.8% in July. Seasonally-adjusted construction production dropped month-on-month by 0.8%. Its annual seasonally-adjusted growth rate (22.6%) was the fastest since January 2012, namely since the

construction boom related to EURO 2012. The high against the backdrop of recent quarters growth rate in all segments of the construction-assembly production point to a wide range of the recovery in both private and public investments. This supports our forecast, in which the growth rate of gross fixed capital formation will amount to 3.0% YoY in Q3 vs. 0.8% in Q2.

- **Nominal dynamics of retail sales in Poland increased to 7.6% YoY in August vs. 7.1% in July.** Real retail sales growth rose to 6.9% YoY in August vs. 6.8% in July. The slight acceleration in sales in August was mostly due to their higher growth in the category "food, beverages, and tobacco products" and "sales in non-specialized stores". The stabilization of total sales growth in fixed prices supports our scenario that in the coming months the annual sales dynamics will gradually decrease, due to last year's high base effects related to the disbursement of funds under the Family 500+ scheme. Nevertheless we forecast that private consumption growth will stay in subsequent quarters at a level of 4.0% YoY or higher, supported by the improving situation in the labour market (including the expected by us faster increase in real wages), high households' propensity to pay for current expenses using accumulated savings and reduced retirement age (see MACROmap of 11/9/2017).
- **Nominal wage dynamics in the Polish corporate sector rose to 6.6% YoY in August vs. 4.9% in July, hitting the highest level since January 2012.** In our view, the strong acceleration in the wage growth rate in August was largely due to the low base effects from the year before resulting from changed timing of bonuses paid in mining. The annual employment dynamics rose to 4.6% in August vs. 4.5% in July. The factor behind higher employment growth rate were the low base effects from the year before in the sector "information and communication" (see MACROpulse of 18/9/2017). We estimate that real wage fund dynamics (employment times average wages) in enterprises amounted to 9.6% YoY in August vs. 7.8% in July and 7.9% in Q2. It has been its highest growth rate since September 2008. In subsequent quarters we expect improvement in the labour market and weak decline in the annual employment growth. Given the continuing strong demand for labour, this will be conducive to a gradual increase of wage pressure in the Polish economy. We forecast that the wage growth rate in the national economy will increase to 5.2% YoY in 2017 vs. 3.8% in 2016 and will reach 6.5% in 2018.

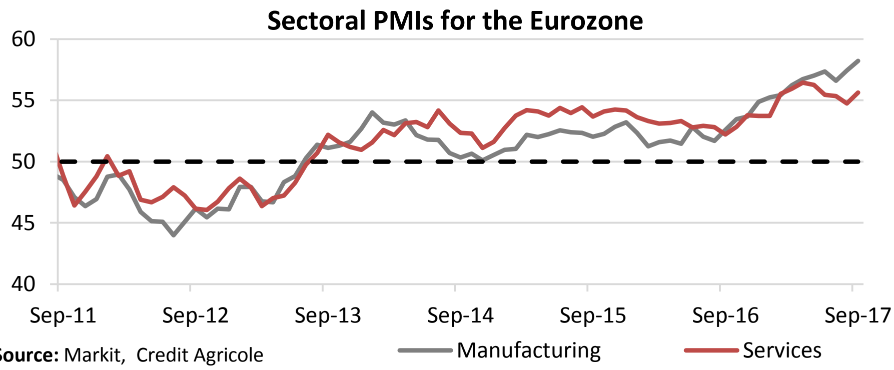
Positive business sentiment in the Eurozone continues



Source: Markit, Credit Agricole

The Composite PMI (for manufacturing and services) in the Eurozone rose to 56.7 pts in September from 55.7 pts in August. Thus, it is only slightly below its six-year high recorded in April and May (56.8 pts). The increase in Composite PMI occurred due to an increase in both its sub-index for business activity in services and for output in manufacturing. The average value of the Composite PMI amounted to 56.0 pts in Q3 vs. 56.6 pts in Q2, which supports our forecast assuming a slight decrease in the GDP growth rate in the Eurozone in Q3 (0.5% QoQ vs. 0.6% in Q2).

Positive business sentiment in the Eurozone continues



Source: Markit, Credit Agricole

Although improved sentiment in the Eurozone was recorded for both manufacturing and services, noteworthy is the continuing disproportion in the growth rate of activity in these sectors. The recovery in the Eurozone manufacturing is supported by a sharp increase in internal and foreign orders. Increasingly stronger signals of insufficient capacities are also observed. Suppliers' delivery times in the Eurozone manufacturing in August have been the longest since April 2011, which signals that companies are behind in executing orders. This supports higher investments in increasing production capacities, including increase in employment. Consequently the sub-index for employment in the Eurozone manufacturing rose to 56.8 pts in September vs. 55.5 pts in August, reaching the highest value in the survey history.

Geographically, the improvement of sentiment in the Eurozone occurred due to faster growth rate of economic activity in both Germany (57.8 pts in September vs. 55.8 pts in August – the highest level since April 2011) and in France (57.2 pts vs. 55.2 pts – the highest level since May 2011). The increase in the PMI indices for Germany and France resulted from higher sub-indices concerning both output in manufacturing and business activity in services. Other Eurozone countries covered by the survey recorded a decrease in the growth rate of economic activity.

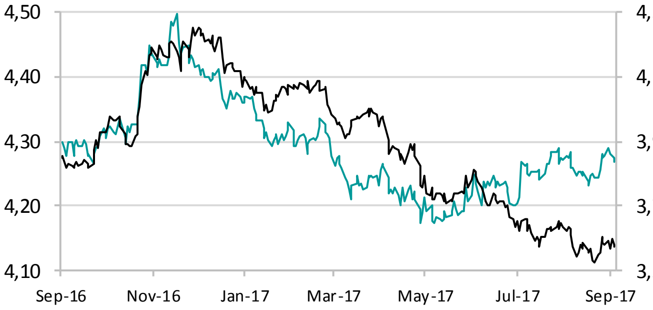
From the point of view of assessing future business climate in Poland, especially noteworthy is the situation in German manufacturing. The German manufacturing PMI rose to 60.6 pts in September vs. 59.3 pts in August, hitting the highest level since April 2011. In the index structure noteworthy is an increase in the output sub-index (61.8 pts in September vs. 60.1 pts in August – the highest level since April 2011), accompanied by continuing high against the historical backdrop levels of sub-indices for new orders (60.5 pts vs. 60.3 pts) and new export orders (58.9 pts vs. 61.0 pts).

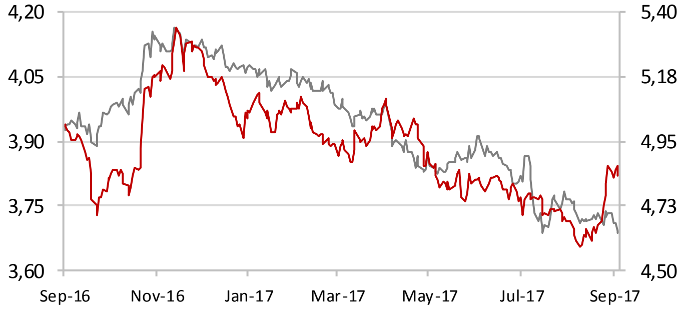
Additional information on the situation in German economy was also provided last week by the ZEW index reflecting the sentiment among analysts and institutional investors regarding the economic situation in Germany which rose to 17.0 pts in September vs. 10.0 pts in August. According to the press release the improvement in sentiment resulted from a significant increase in lending and recovery in corporate and government investments.

The marked improvement in the Eurozone manufacturing, in Germany in particular, signals a high likelihood of stronger demand for goods manufactured in Poland and used in the production of final goods (so-called intermediate goods). This is in line with our forecast in which the annual dynamics of Polish exports will increase to 8.0% in Q3 2017 vs. 2.8% in Q2 and will reach 10.0% YoY in Q4. At the same time, the growing demand for intermediate goods made in Poland in the conditions of high capacity utilization supports higher fixed capital formation in Polish manufacturing. This supports our forecast of higher investment growth rate in Q3 (3.0% YoY vs. 0.8% in Q2).

Results of elections in Germany may weaken PLN

FX rates



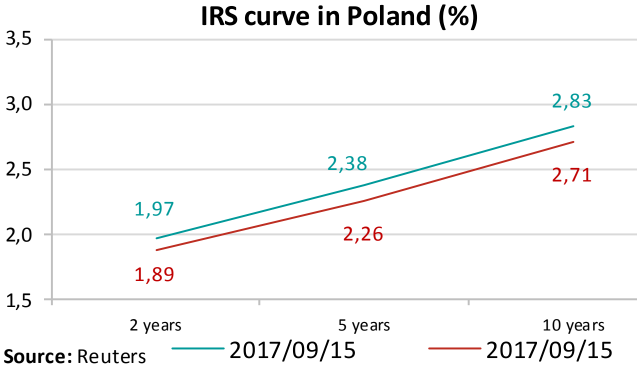


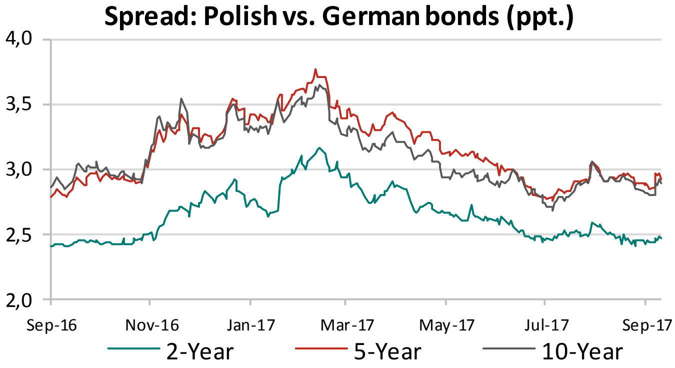
Source: Reuters

Last week EURPLN rate dropped to 4.2677 (PLN strengthening by 0.2%). On Monday PLN continued the depreciation from two weeks before coming close to a level of 4.30 for EUR. On Tuesday PLN started appreciating and remained within a weak upward trend until the end of the week. PLN strengthening was helped by the Tuesday's readings of better-than-expected domestic data on industrial production and retail sales. Conducive to its appreciation was also a decrease in global risk aversion, reflected by lower VIX index. On Thursday PLN was temporarily depreciating in reaction to the Wednesday's FOMC meeting which decided to start the reduction of the FED balance-sheet and presented the latest macroeconomic projections at the press conference (see above). The better-than-expected results of business surveys in the Eurozone published on Friday also had a temporary negative impact on PLN. Also noteworthy last week is the drop of CHFPLN rate to the lowest level since 15 January 2015 when CHF significantly appreciated in reaction to SNB decision to exit the policy of keeping 1.20 floor on EURCHF rate (see MACROmap of 19/1/2015). The PLN appreciation against CHF last week occurred due to the abovementioned decline in EURPLN rate and CHF depreciation vs. EUR. The increase in EURCHF is supported by the growing differences between the prospects for the ECB and the SNB monetary policies (see MACROmap of 7/8/2017).

Today we may see a slight weakening of PLN in reaction to the results of the parliamentary elections in Germany. Crucial for PLN this week will be numerous data from the US (final GDP estimate in Q3, preliminary durable goods orders, new home sales, Conference Board Index, and final University of Michigan Index). However, the data will have a limited impact on the market, if our forecasts that are close to the market consensus materialize. Preliminary data on inflation in Poland and in the Eurozone will also be neutral for PLN.

Higher IRS rates following core markets





Source: Reuters

Last week the 2-year IRS rates rose to a level of 1.965 (up by 8 bp), 5-year rates to a level of 2.375 (up by 12 bp), and 10-year rates to a level of 2.830 (up by 13 bp). In the first part of the week IRS rates were increasing across the curve following core markets in anticipation of the Wednesday's FOMC meeting. The Federal Reserve decision to start the process of reducing the FED balance-sheet and the latest economic projections presented at the press conference were received by the market as hawkish. Consequently, Thursday and Friday saw further increase in IRS rates across the curve.

This week the Polish debt market will focus on numerous data from the US (final GDP estimate in Q3, preliminary durable goods orders, new home sales, Conference Board Index, and final University of Michigan Index). However, we believe that their aggregate impact on IRS rates will be limited. Preliminary estimates of inflation in Poland and in the Eurozone as well as results of parliamentary elections in Germany will also be neutral for the Polish debt market, we believe.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17
NBP reference rate (%)	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50
EURPLN*	4,36	4,29	4,31	4,45	4,40	4,32	4,31	4,23	4,23	4,18	4,23	4,25	4,25	**4,23**
USDPLN*	3,91	3,82	3,92	4,20	4,18	4,00	4,07	3,97	3,88	3,72	3,70	3,59	3,57	**3,55**
CHFPLN*	3,97	3,93	3,96	4,13	4,11	4,04	4,05	3,96	3,90	3,84	3,86	3,72	3,72	**3,68**
CPI inflation (% YoY)	-0,8	-0,5	-0,2	0,0	0,8	1,7	2,2	2,0	2,0	1,9	1,5	1,7	1,8	
Core inflation (% YoY)	-0,4	-0,4	-0,2	-0,1	0,0	0,2	0,3	0,6	0,9	0,8	0,8	0,8	0,7	
Industrial production (% YoY)	7,5	3,2	-1,3	3,2	2,2	9,1	1,1	11,0	-0,6	9,1	4,5	6,3	8,8	
PPI inflation (% YoY)	-0,1	0,2	0,6	1,8	3,2	4,0	4,5	4,8	4,2	2,4	1,8	2,2	3,0	
Retail sales (% YoY)	5,6	4,8	3,7	6,6	6,4	11,4	7,3	9,7	8,1	8,4	6,0	7,1	7,6	
Corporate sector wages (% YoY)	4,7	3,9	3,6	4,0	2,7	4,3	4,0	5,2	4,1	5,4	6,0	4,9	6,6	
Employment (% YoY)	3,1	3,2	3,1	3,1	3,1	4,5	4,6	4,5	4,6	4,5	4,3	4,5	4,6	
Unemployment rate* (%)	8,4	8,3	8,2	8,2	8,3	8,6	8,5	8,1	7,7	7,4	7,1	7,1	7,0	
Current account (M EUR)	-729	-858	172	99	-219	2342	-599	-529	-160	-298	-932	-878		
Exports (% YoY EUR)	9,3	3,1	-0,6	5,7	5,1	14,3	5,7	15,1	1,4	16,2	8,7	10,7		
Imports (% YoY EUR)	10,7	3,5	3,6	6,3	7,1	16,0	8,9	16,8	3,3	21,4	15,0	12,5		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

Indicator	2017				2018				2016	2017	2018
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)	4,0	3,9	4,3	4,2	4,0	3,7	3,6	3,8	2,7	4,1	3,8
Private consumption (% YoY)	4,7	4,9	4,2	4,5	4,6	4,3	4,3	3,9	3,8	4,6	4,3
Gross fixed capital formation (% YoY)	-0,4	0,8	3,0	5,5	7,9	7,0	6,8	6,1	-7,8	3,0	6,7
Export - constant prices (% YoY)	8,3	2,8	8,0	10,0	8,0	7,7	6,8	5,5	9,0	7,3	7,0
Import - constant prices (% YoY)	8,7	6,1	9,0	11,6	10,6	10,0	10,4	8,3	8,9	8,9	9,8
GDP growth contributions: Private consumption (pp)	3,0	2,9	2,5	2,3	3,0	2,6	2,6	1,9	2,3	2,7	2,5
GDP growth contributions: Investments (pp)	0,0	0,1	0,5	1,3	0,9	1,1	1,2	1,5	-1,6	0,5	1,2
GDP growth contributions: Net exports (pp)	0,1	-1,5	-0,3	-0,4	-1,1	-0,8	-1,8	-1,3	0,3	-0,6	-1,2
Current account***	0,1	-0,5	-0,7	-1,2	-1,7	-1,5	-1,7	-2,0	-0,2	-1,2	-2,0
Unemployment rate (%)**	8,1	7,1	7,0	7,3	7,6	6,8	6,9	7,3	8,3	7,3	7,3
Non-agricultural employment (% YoY)	2,1	2,4	1,9	1,0	0,3	0,1	0,1	0,1	1,9	1,9	0,2
Wages in national economy (% YoY)	4,1	5,0	5,6	6,0	6,4	6,7	6,6	6,5	3,8	5,2	6,5
CPI Inflation (% YoY)*	2,0	1,8	1,9	1,8	1,5	1,9	1,6	1,5	-0,6	1,9	1,6
Wibor 3M (%)**	1,73	1,73	1,73	1,73	1,73	1,73	1,90	1,98	1,73	1,73	1,98
NBP reference rate (%)**	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,75	1,50	1,50	1,75
EURPLN**	4,23	4,23	4,23	4,16	4,15	4,12	4,10	4,07	4,40	4,16	4,07
USDPLN**	3,97	3,70	3,55	3,41	3,40	3,35	3,31	3,26	4,18	3,41	3,26

* quarterly average
** end of period
***cumulative for the last 4 quarters

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST*	
					CA	CONSENSUS**
		Monday 09/25/2017				
10:00	Germany	Ifo busienss climate (pts)	Sep	115,9	116,3	116,0
		Tuesday 09/26/2017				
15:00	USA	Case-Shiller Index (% MoM)	Jul	0,1		0,2
16:00	USA	Richmond Fed Index	Sep	14,0		
16:00	USA	New home sales (k)	Aug	571	595	584
16:00	USA	Consumer Confidence Index	Sep	122,9	120,0	120,0
		Wednesday 09/27/2017				
10:00	Eurozone	M3 money supply (% MoM)	Aug	4,5		4,6
14:30	USA	Durable goods orders (% MoM)	Aug	-6,8	1,5	1,0
		Thursday 09/28/2017				
11:00	Eurozone	Business Climate Indicator (pts)	Sep	1,09		1,11
14:00	Germany	Preliminary HICP (% YoY)	Sep	1,8	1,9	1,8
14:30	USA	Initial jobless claims (k)	w/e	284		265
14:30	USA	Final GDP (% YoY)	Q2	3,0	3,1	3,0
		Friday 09/29/2017				
12:00	Eurozone	Preliminary HICP (% YoY)	Sep	1,5	1,5	1,6
14:00	**Poland**	**Flash CPI (% YoY)**	**Sep**	**1,8**	**2,0**	**2,0**
14:30	USA	Real private consumption (% MoM)	Aug	0,2		
15:45	USA	Chicago PMI (pts)	Sep	58,9		59,0
16:00	USA	Final U. of Michigan Sentiment Index (pts)	Sep	95,3	96,0	95,3

*The forecasts of macroeconomic indicators for Poland were prepared by Credit Agricole Bank Polska S.A. The forecasts of foreign indicators were prepared by Crédit Agricole Corporate and Investment Bank
** Reuters

MACRO MAP

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