Slightly hawkish NBP projection

This week

- **The most important event this week will be the release of data on industrial production and retails sales in Poland scheduled for today.** We forecast that industrial production dynamics rose to 10.5% YoY in October vs. 4.3% in September, due to favourable calendar effects. In turn, in our view, the nominal retail sales growth rate dropped to 8.5% YoY in October vs. 8.6% in September, due to changed timing of shopping for autumn and winter clothes (see MACROpulse of 18/10/2017). We believe that if our forecasts materialize, the aggregate impact of the data will be slightly positive for PLN and yields on Polish bonds.
- **Another important event will be the release of the November results of business surveys for major European economies scheduled for Thursday.** We expect that Composite PMI for the Eurozone dropped to 55.8 pts in November vs. 56.0 in October. The index decrease resulted, in our view, from a slight deterioration in both Germany and France. Ifo Index, reflecting the sentiment among German managers representing the manufacturing, construction, wholesale and retail trade sectors, will be released on Friday. We expect it to decrease to 116.4 pts in November vs. 116.7 pts in October. We believe that the publication of business survey results for the Eurozone will be slightly positive for PLN and prices of Polish bonds.
- **The Minutes of the November FOMC meeting will be released on Wednesday.** The markets will focus on the FED members' in-depth analyses of short- and medium-term prospects for the economic situation in the US (including primarily the expected profile of inflation) and the likely date of interest rate hikes in 2018. The release of the Minutes may be conducive to increased volatility in the financial markets; however, they are unlikely to provide new information that would alter our scenario of gradual normalization of the US monetary policy. Our base scenario assumes that at its December meeting FED will hike interest rates by 25 bp.
- **Significant hard data on US economy and business survey results will also be released this week.** We forecast that the monthly dynamics of preliminary durable goods orders dropped to 0.8% in October vs. 2.0% in September due to lower orders in the Boeing company. We expect that data on existing home sales (5.32M vs. 5.39M) will confirm the ongoing recovery in the US real estate market. We forecast that the final University of Michigan Index (98.0 pts in November vs. 100.7 pts in October and 97.8 pts in the flash estimate) will signal a slight deterioration of households' sentiment. We believe that the aggregate impact of data on the US economy on the financial market will be limited.

Last week

- **Numerous data from the US economy and business survey results were released last week.** Industrial production increased by 0.9% MoM in October vs. a 0.4% increase in September. Faster growth rate of industrial production resulted from higher production growth in manufacturing and utilities while lower output growth in mining had an opposite impact. The marked acceleration in industrial production dynamics was related to the abatement of the negative effect of Irma and Harvey hurricanes on activity in the US manufacturing. Capacity utilization rose to 77.0% in October vs. 76.4% in September. Data on retail sales were also released week and rose by 0.2% MoM in October vs. a 1.9% increase in September. Lower growth rate of retail sales resulted from lower monthly sales dynamics in most categories. The sharp increase in dynamics in September resulted from the abatement of the unfavourable effect of hurricanes (see MACROmap of 16/10/2017). Excluding cars, retail sales rose by 0.1% MoM in October vs. a 1.2% increase in September. The sustainability of the recovery in the US real estate market was indicated last week by the data on building permits (1297k in October vs. 1225k in September) and housing starts (1290k vs. 1135k). Data on CPI inflation were also released last week. It dropped to 0.1% MoM in October vs. 0.5% MoM in September (2.0% YoY in October vs. 2.2% in September). Conducive to decline of inflation were lower dynamics of fuel prices (-2.4% MoM vs. 13.1%) related to the abatement of Irma and Harvey hurricanes. Core inflation rose to 0.2% in October vs. 0.1% in September (1.8% YoY vs. 1.7%). Conducive to higher core inflation were higher dynamics of prices of rent and medical services. Last week, the NY Empire State (19.4 pts in November vs. 30.2 pts in October) and Philadelphia FED Indices (18.9 pts vs. 27.9 pts) pointed to lower growth rate of activity. The last week's data from the US economy do not alter our forecast that the annualized US GDP growth rate will not change in Q4 compared to Q3 and will amount to 3.0%.

- **In accordance with the flash estimate, Polish GDP growth rate in Q3 rose to 4.7% YoY vs. 4.0% in Q2.** The quarterly dynamics of seasonally adjusted GDP rose to 1.1% YoY vs. 0.9% in Q2, which points to a slight acceleration in economic activity growth in Q3. We believe that the main factor behind the acceleration of growth in Q3 was higher contribution of net exports, resulting from a surprising slowdown in imports. The contribution of investments has also increased. In our view this increase resulted from both higher dynamics of public investments and faster growth rate of investments of private companies and households (see MACROpulse of 14/11/2017). The contribution of consumption to GDP growth was most likely similar to that recorded in Q3 while the contribution of inventories – sold off by companies with a view to satisfying the fast growing demand – was slightly negative. The data on GDP pose an upside risk to our forecast of economic growth in 2017 (4.1%).
- **In accordance with the final data, CPI inflation in Poland dropped to 2.1% YoY in October vs. 2.2% in September, running in line with the flash estimate by GUS.** The decrease in inflation resulted from lower dynamics of fuel prices and decrease in core inflation, which dropped to 0.8% YoY in October vs. 1.0% in September. Low level of core inflation confirms the limited impact of the high growth rate of wages observed in Poland on the dynamics of the prices of consumer goods. On the other hand, higher dynamics of food prices was conducive to increase in inflation (see MACROpulse of 13/11/2017). Data on the October inflation indicate an upside risk to our short-term forecast of CPI inflation; however, we expect that inflation will slightly decrease in 2018 compared to 2017 and will thus stay markedly below the MPC inflation target. We believe that gradual increase in core inflation, related to growing wage pressure, will be offset by lower dynamics of food and fuel prices. Consequently, we maintain our scenario of the monetary policy, assuming first hike on NBP interest rates in November 2018.
- **Deficit in the Polish current account rose to EUR 100M in September from EUR 80M in August.** The current account balance decreased due to lower balances on primary and secondary income (lower from those in August by EUR 450M and EUR 138M, respectively), while higher balance on goods and services (up by EUR 486M and EUR 82M compared to August) had an opposite impact. Export dynamics dropped to 10.2% YoY in September vs. 12.1% in August, and imports dynamics declined to 5.7% YoY vs. 7.6% which was largely due to the unfavourable difference in the number of working days. We estimate that the relation of the cumulative current account balance for the past 12 months in relation to GDP rose to 0.0% in Q3 vs. -0.5% in Q2.
- **Nominal wage dynamics in the Polish sector of enterprises rose to 7.4% YoY in October vs. 6.0% in September**. In our view, the main factor behind higher wage growth in the sector of enterprises was the changed timing of bonuses paid in some branches and, to a smaller extent, the growing wage pressure resulting from improvement in the labour market (see MACROpulse of 17/11/2017). The annual employment dynamics dropped to 4.4% in October vs. 4.5% in September. Like in the last few months the increase in employment in October was limited by the growing difficulties of companies in finding skilled labour. In addition,

conducive to lower employment growth rate was the fact that some people took advantage of the entitlement to pension due to the reduction of retirement age. We estimate that real wage fund growth rate (employment times average wages) in enterprises amounted to 9.9% YoY in October vs. 8.4% in September and 8.6% in Q3, hitting the highest level since September 2008. This poses a slight upside risk to our forecast in which private consumption growth will not change in Q4 compared to Q3 and will amount to 4.7% YoY.

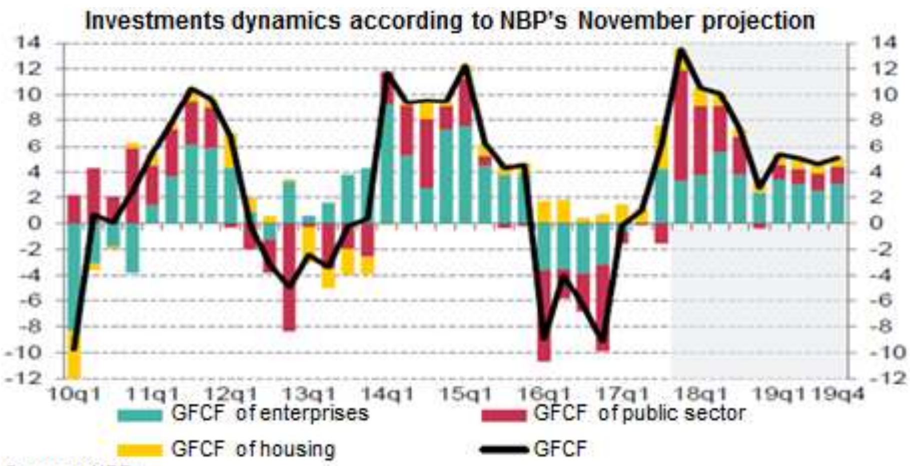
- **Flash data on GDP for major European economies were released last week.** Quarterly GDP dynamics in the Eurozone dropped to 0.6% in Q3 vs. 0.7% in Q2 (2.5% YoY in Q3 vs. 2.3% in Q2). Conducive to slower GDP growth rate within the single currency area were lower growth dynamics i.a. in France (0.5% QoQ in Q3 vs. 0.6% in Q2), Spain (0.8% vs. 0.9%), Netherlands (0.4% vs. 1.5%), and Belgium (0.3% vs. 0.5%). On the other hand, higher GDP dynamics i.a. in Germany (0.8% QoQ in Q3 vs. 0.6% in Q2) and Italy (0.5% vs. 0.3%) had a positive impact on GDP growth rate in the Eurozone. We forecast that in the whole 2017 GDP in the Eurozone will increase by 2.2% vs. a 1.7% increase in 2016, due to higher dynamics i.a. in Germany (2.2% vs. 1.9%), France (1.7% vs. 1.2%), Italy (1.5% vs. 0.9%), and Holland (3.2% vs. 2.2%).
- **ZEW index reflecting the sentiment among analysts and institutional investors regarding the economic situation in Germany rose to 18.7 pts in November vs. 17.6 pts in October**. According to the press release, conducive to improved sentiment was the continuingly high GDP growth rate in the Eurozone countries, which supports economic activity in Germany. We forecast that the quarterly GDP growth rate in Germany will decrease to 0.5% in Q4 vs. 0.8% in Q3.
- **Numerous data from China were released last week**. The dynamics of industrial production dropped to 6.2% in October vs. 6.6% in September, retail sales to 10.0% vs. 10.3%, and urban investments to 7.3% vs. 7.5%. The slightly slower growth rate of activity in the Chinese economy supports our scenario, in which the annual GDP growth rate in China will decrease to 6.7% in Q4 vs. 6.8% in Q3. Consequently we forecast that in the whole 2017 GDP in China will increase to 6.8% vs. a 6.7% increase in 2016.
- **The negotiations on forming a coalition in the German parliament composed of CDU/CSU, FDG and the Greens collapsed late Sunday night.** The FDP pulled out of the talks. In this situation there are three possible solutions. CDU/CSU can try to renew coalition with the SPD. However the SPD ruled out such option repeatedly. CDU/CSU can form a minority government. The third option is new parliamentary election. The increase in political risk in Germany is negative for EURUSD and PLN.

Slightly hawkish NBP projection

In the statement after its November meeting, the Council indicated that "taking into account the present information, including the results of the November projection, the Council judges that in the coming years inflation will run close to the inflation target". Thus the tone of the statement has slightly changed compared to the view the Council worded in October. The Council considered then that "the risk of inflation persistently running above the target in the medium term is limited". Below we discuss the most important information included in the November projection and MPC members' remarks which, in our view, are crucial from the point of view of the monetary policy outlook.

In accordance with the November NBP projection, CPI inflation will gradually increase to reach a level slightly above 2.5% in 2019 (see MACROpulse of 8/11/2017). Such profile of inflation will result, on the one hand, from a faster increase in core inflation and, on the other hand, from the abatement of the temporary factors which boosted the inflation of energy and food prices in 2017. According to the NBP, in the projection relevant horizon, core inflation will increase due to growing cost and demand pressure in the Polish economy.

Our scenario of inflation outlook differs from that presented by the NBP. In our opinion, between 2018 and 2019 inflation will stay markedly below the NBP inflation target, largely due to the expected by us sharp decrease in the dynamics of food prices. We believe that the dynamics of food prices will reach their local maximum in Q4. In subsequent quarters they will markedly decrease, due to this year's high base effects for the prices of fruit and eggs, downward phase of the cycle in the pork market, lower prices of dairy products, poultry and sugar, as well as the expected by us strengthening of PLN. Consequently, the expected by us downward, starting from Q1 2018, trajectory for the dynamics of food prices is much below the one forecast in the NBP projection. At the same time we believe that the increase in core inflation will be limited by asymmetric wage pressure. An increase in inflation resulting from growing wage pressure will be observed mainly in the sector of non-commercial goods, whereas in the sector of commercial goods it will be slowed down by strong competition pressure which limits the possibilities of raising prices of products with a view to offsetting higher costs of labour. In addition, the stabilization of oil prices with a simultaneous expected by us strengthening of PLN will limit the increase in the dynamics of fuel prices.



Source: NBP

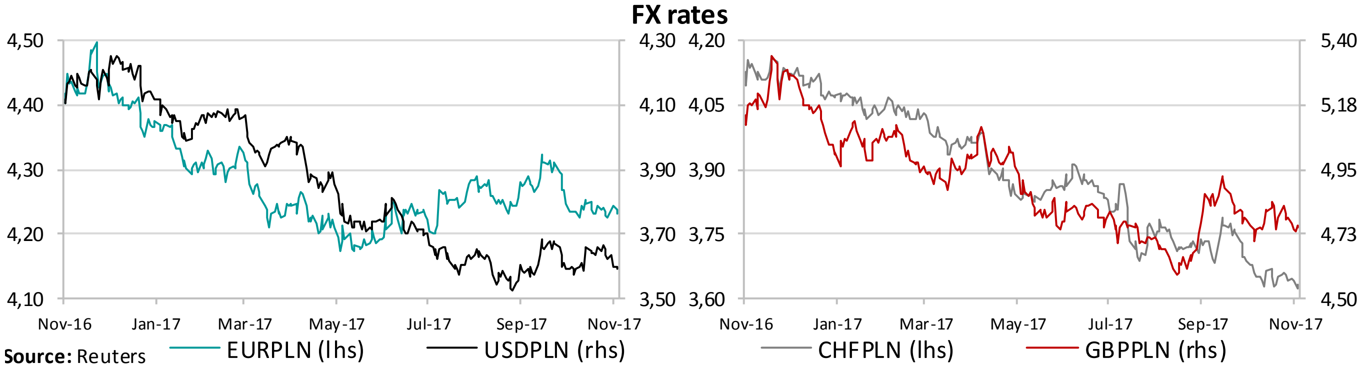
Another element of the projection which is important in the context of assessing the monetary policy outlook is the anticipated pace of investment growth. According to the NBP projection, investment dynamics amounted to ca. 6% YoY in Q3 and will increase to ca. 13% in Q4. According to the NBP, the recovery in investments in the coming quarters will be caused by fast increase in fixed capital formation in all the three segments – public investments (growing absorption of EU funds from the 2014-2020 programming period), corporate investments (growing absorption of EU funds, improved forecasts concerning demand, improved investors' sentiment, low interest rates, high capacity utilization), and households' investments (supported by good situation in the labour market and low interest rates).

The profile of investment dynamics presented in the projection is running in the short term clearly above our forecasts (3.7% in Q3 and 5.9% in Q4). We expect that only a moderate – we believe – acceleration in fixed capital formation will not be strong enough argument for the NBP to start monetary tightening in H1 2018. We believe that the likelihood of the MPC hiking interest rates in H1 2018 would substantially increase only if final data on GDP in Q3 indicated that the recovery in investments was much stronger than assumed in the November NBP projection (see MACROpulse of 14/11/2017).

The remarks of the MPC members are also significant in the context of assessing the prospects for interest rates in Poland. Ł. Hard, who shows high aversion to inflation, stated last week that a systematic and sharp increase in wages might incline the Council to hike rates at the beginning of 2018. E. Gatnar also expressed hawkish views. In his opinion, Q1 2018 is a good moment to hike rates because in his view inflation will increase faster than assumed in the November projection and will reach the inflation target in Q1 2018. In turn, other MPC members have in recent weeks changed their bias to a more dovish one. J. Kropiwnicki said last week that in his opinion there was no need to hike interest rates at least in the coming year because inflation pressure was moderate. Thus we can see a clear change in the views of J. Kropiwnicki in recent weeks, because towards the end of October he was of the opinion that no changes in monetary parameters were expected at least until the middle of next year. G. Ancyparowicz has also weakened her stance slightly saying last week that in her opinion there was no reason for considering rate hikes during the coming four quarters. On the other hand, at the conference after the October MPC meeting, G. Ancyparowicz did not anticipate any changes in the monetary policy "for the next three or even four quarters". In turn, at the conference after the November Council meeting, the NBP Governor, A. Glapiński, repeated the view expressed in recent months that NBP rates should stay at the current level until the end of 2018.

We believe that if our macroeconomic scenario materializes – namely in the conditions of a moderate wage pressure, inflation staying below the target, and only a limited recovery in investments – the MPC will leave interest rates at an unchanged level until November 2018. The Council members' remarks quoted above support this view. The data on corporate wages released last week (see above) which might indicate growing wage pressure pose a slight upside risk to our scenario. However, we believe that the main factor conducive to the sharp increase in corporate wage growth was changed timing of bonus payments in some branches. An in-depth analysis of increase in wage pressure will be possible only after seeing full data from the labour market once published in the Statistical Bulletin.

Domestic data on production and retail sales may strengthen PLN

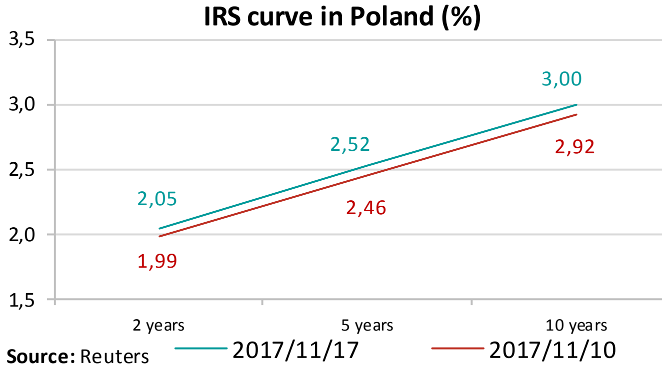


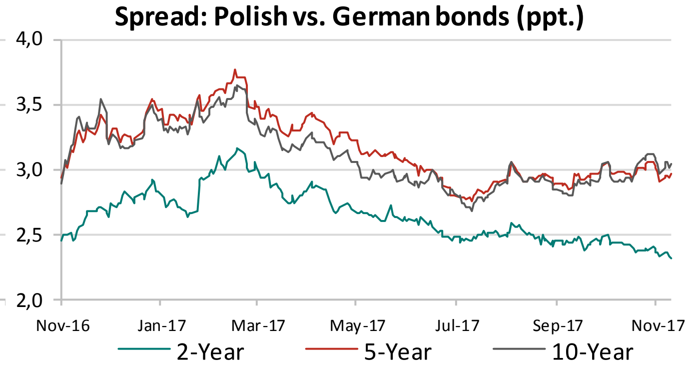
Source: Reuters

Last week EURPLN rate rose to 4.2321 (PLN weakening by 0.2%). In the first part of the week PLN was depreciating despite in-line-with-the-consensus inflation data and better-than-expected data on the Polish GDP. On Wednesday, PLN was relatively stable despite "serious concerns" expressed by the European Commission concerning the President's draft judicial reforms and numerous remarks of the members of the Monetary Policy Council (see above). Further into the week, PLN strengthened only slightly, supported by better-than-expected data on average corporate wages released on Friday. Despite slight weakening vs. EUR last week, PLN was appreciating vs. USD, due to increase in EURUSD rate which was supported by better-than-expected data on GDP in Germany and Italy.

Crucial for PLN this week will be today's reading of industrial production and retail sales. If our forecasts materialize, the data may be slightly positive for PLN. Conducive to PLN strengthening may also be the publication of preliminary results of business surveys for major European economies (PMIs and Ifo index for Germany). We expect that the release of the Minutes of the November FOMC meeting scheduled for Wednesday may contribute to increased volatility of PLN. On the other hand, increase in political tension in Germany may be negative for PLN. Data from the US (preliminary durable goods orders, existing home sales, and final University of Michigan Index) will be neutral for the market, we believe.

Publication of FOMC Minutes may increase debt market volatility





Source: Reuters

Last week 2-year IRS rates rose to a level of 2.045 (up by 6 bp), of 5-year rates to a level of 2.523 (up by 7 bp), and of 10-year rates to a level of 3.001 (up by 8 bp). Last week, IRS rates were increasing across the curve, following the German debt market. Important for IRS rates were also better-than-expected data on the Polish GDP and average wages in the corporate sector leading to their temporary increase.

This week, the Polish debt market will focus on today's publication of domestic data on industrial production and retail sales. The publication of preliminary results of business surveys for major European economies (PMIs and Ifo index for Germany) will have an opposite impact, we believe. The release of the Minutes of the November FOMC meeting scheduled for Wednesday will, in our view, support increase in market volatility. In our opinion, data from the US (preliminary durable goods orders, existing home sales, and final University of Michigan Index) will have a limited impact on IRS rates.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland														
Indicator	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-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*	4,31	4,45	4,40	4,32	4,31	4,23	4,23	4,18	4,23	4,25	4,25	4,31	4,24	**4,22**
USDPLN*	3,92	4,20	4,18	4,00	4,07	3,97	3,88	3,72	3,70	3,59	3,57	3,65	3,64	**3,58**
CHFPLN*	3,96	4,13	4,11	4,04	4,05	3,96	3,90	3,84	3,86	3,72	3,72	3,77	3,65	**3,64**
CPI inflation (% YoY)	-0,2	0,0	0,8	1,7	2,2	2,0	2,0	1,9	1,5	1,7	1,8	2,2	2,1	
Core inflation (% YoY)	-0,2	-0,1	0,0	0,2	0,3	0,6	0,9	0,8	0,8	0,8	0,7	1,0	0,8	
Industrial production (% YoY)	-1,3	3,2	2,2	9,1	1,1	11,0	-0,6	9,1	4,5	6,2	8,7	4,3	**10,5**	
PPI inflation (% YoY)	0,6	1,8	3,2	4,0	4,5	4,8	4,2	2,4	1,8	2,2	3,0	3,1	**2,9**	
Retail sales (% YoY)	3,7	6,6	6,4	11,4	7,3	9,7	8,1	8,4	6,0	7,1	7,6	8,6	**8,5**	
Corporate sector wages (% YoY)	3,6	4,0	2,7	4,3	4,0	5,2	4,1	5,4	6,0	4,9	6,6	6,0	7,4	
Employment (% YoY)	3,1	3,1	3,1	4,5	4,6	4,5	4,6	4,5	4,3	4,5	4,6	4,5	4,4	
Unemployment rate* (%)	8,2	8,2	8,2	8,5	8,4	8,0	7,6	7,3	7,0	7,0	7,0	6,8	**6,6**	
Current account (M EUR)	-14	-97	-106	2548	-514	-405	459	-297	-1114	-491	-80	-100		
Exports (% YoY EUR)	-1,0	4,3	9,0	15,1	6,4	19,7	2,5	18,5	6,5	12,4	12,1	10,2		
Imports (% YoY EUR)	1,3	5,2	9,8	16,0	10,5	19,8	3,8	20,4	13,0	12,8	7,6	5,7		

*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)	4,1	4,0	4,5	4,2	4,0	3,7	3,6	3,8	2,9	4,1	3,8
	Private consumption (% YoY)	4,7	4,9	4,7	4,7	4,6	4,3	4,3	3,9	3,9	4,7	4,3
	Gross fixed capital formation (% YoY)	-0,4	0,8	3,7	5,9	7,9	7,0	6,8	6,1	-7,9	3,2	6,7
	Export - constant prices (% YoY)	8,3	2,8	8,3	9,5	8,0	7,7	6,8	5,5	8,8	7,1	7,0
	Import - constant prices (% YoY)	8,7	6,1	8,5	11,6	10,6	10,0	10,4	8,3	7,9	8,9	9,8
GDP growth contributions	Private consumption (pp)	3,0	2,9	2,8	2,4	3,0	2,6	2,6	1,9	2,9	2,8	2,5
	Investments (pp)	0,0	0,1	0,6	1,4	0,9	1,1	1,2	1,5	-2,1	0,5	1,2
	Net exports (pp)	0,1	-1,5	0,1	-0,6	-1,1	-0,8	-1,8	-1,3	0,9	-0,6	-1,2
	Current account***	0,1	-0,5	0,0	-1,2	-1,7	-1,5	-1,7	-2,0	-0,3	-1,2	-2,0
	Unemployment rate (%)**	8,0	7,0	6,8	6,9	7,1	6,6	6,8	6,9	8,3	6,9	6,9
	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	4,9	6,0	6,4	6,7	6,6	6,5	3,8	5,0	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	4,31	4,16	4,15	4,12	4,10	4,07	4,40	4,16	4,07
	USDPLN**	3,97	3,70	3,65	3,50	3,49	3,40	3,33	3,26	4,18	3,50	3,26

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST* CA	FORECAST* CONSENSUS**
		Monday 11/20/2017				
14:00	**Poland**	**Retail sales (% YoY)**	**Oct**	**8,6**	**8,5**	**8,2**
14:00	**Poland**	**PPI (% YoY)**	**Oct**	**3,1**	**2,9**	**2,9**
14:00	**Poland**	**Industrial production (% YoY)**	**Oct**	**4,3**	**10,5**	**10,4**
		Tuesday 11/21/2017				
16:00	USA	Existing home sales (M MoM)	Oct	5,39	5,32	5,43
		Wednesday 11/22/2017				
14:30	USA	Durable goods orders (% MoM)	Oct	2,0	0,8	0,3
16:00	Eurozone	Consumer Confidence Index (pts)	Nov	-1,0		-0,8
16:00	USA	Final U. of Michigan Sentiment Index (pts)	Nov	97,8	98,0	98,0
20:00	USA	FOMC Minutes	Nov			
		Thursday 11/23/2017				
8:00	Germany	Final GDP (% QoQ)	Q3	0,8	0,8	0,8
9:30	Germany	Flash Manufacturing PMI (pts)	Nov	60,6	59,7	60,3
10:00	Eurozone	Flash Services PMI (pts)	Nov	55,0	54,9	55,2
10:00	Eurozone	Flash Manufacturing PMI (pts)	Nov	58,5	58,1	58,3
10:00	Eurozone	Flash Composite PMI (pts)	Nov	56,0	55,8	56,0
14:00	**Poland**	**MPC Minutes**	**Nov**			
14:00	**Poland**	**M3 money supply (% YoY)**	**Oct**	**5,4**	**5,5**	**5,5**
		Friday 11/24/2017				
10:00	**Poland**	**Registered unemplyment rate (%)**	**Oct**	**6,8**	**6,6**	**6,6**
10:00	Germany	Ifo busienss climate (pts)	Nov	116,7	116,4	116,5
15:45	USA	Flash Manufacturing PMI (pts)	Nov	54,6		54,9

*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

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