Is the peak of the upward cycle in the Eurozone already behind us ?

This week

- **The most important event this week will be the FOMC meeting scheduled for Wednesday.** We expect that after the rate hike in March, the Federal Reserve will maintain the status quo in the monetary policy this week. The markets will focus on possible changes in the tone of the statement, taking into account D. Trump's remarks concerning protectionist measures in international trade. We believe that statement after the meeting will be consistent with our scenario, in which there will be three more 25 bp interests rate hikes in current year (in June, September and December). Supportive to our assessment are better than expected data on US GDP in Q1 (see below) that were published last week. In our view, the publication of the statement after the FOMC meeting may contribute towards increased volatility in the financial markets.
- **Important data from the US will also be released this week**. Data from the labour market will be released on Friday. We expect non-farm payrolls to have increased by 195k in April vs. 103k in March, with unemployment rate decreasing to 4.0% from 4.1% in March. Before the Friday's reading some additional information on the labour market will be provided by the ADP report on private sector employment (the market expects an increase by 200k in April vs. 241k in March). The ISM index for manufacturing will be released on Tuesday and, in our view, it dropped to 58.3 pts in April vs. 59.3 pts in March, running in line with the results of regional business surveys. The April Richmond FED index published last week, which ran significantly below market consensus (-3.0 pts vs. 15.0 pts in March), poses a downside risk to our forecast. We believe that the publication of US data will be neutral for PLN and prices of Polish bonds.
- **Significant data from the Eurozone will be released this week.** We expect that the quarterly GDP dynamics in the Eurozone have not changed in Q1 compared to Q4 2017 and amounted to 0.6%. Lower than expected flash estimate of French GDP (0.3% QoQ in Q1 vs. 0.7% in Q4 2017) published last week poses a downside risk to our forecast. In addition, we forecast that HICP inflation has not changed in April compared to March and amounted to 1.3%. We believe that the publication of data from the Eurozone will not be market moving.
- **The April China manufacturing PMIs (Caixin and CFLP) will be released this week.** The CFLP index, released today, dropped to 51.4 pts vs. 51.5 pts in March. We forecast that Caixin PMI decreased to 50.7 pts vs. 51.0 pts in March. This data will be crucial in terms of assessment of global trade tendencies (see below). We expect that the results of business surveys in China, pointing to a slight deterioration of sentiment in manufacturing, will be neutral for the markets.
- **The April data on business sentiment in Polish manufacturing will be released on Wednesday.** We expect that PMI dropped to 52.9 pts vs. 53.7 pts in March, which will be consistent with the deterioration of sentiment observed in GUS surveys. Our forecast is also supported by decrease of sub-index for new orders (total and export) of German and Eurozone PMI indices that was recorded in April. Our forecast is below the market consensus (53.2 pts), therefore its materialization will be conducive to PLN weakening and higher prices of Polish bonds.
- **Flash data on the April inflation in Poland will be released on Wednesday. In our view, it rose to 1.5% vs. 1.3% in March.** We expect that the higher dynamics of fuel prices have been partly offset by lower core inflation. Our forecast is in line with the consensus, therefore its materialization will be neutral for PLN and yields on Polish bonds.

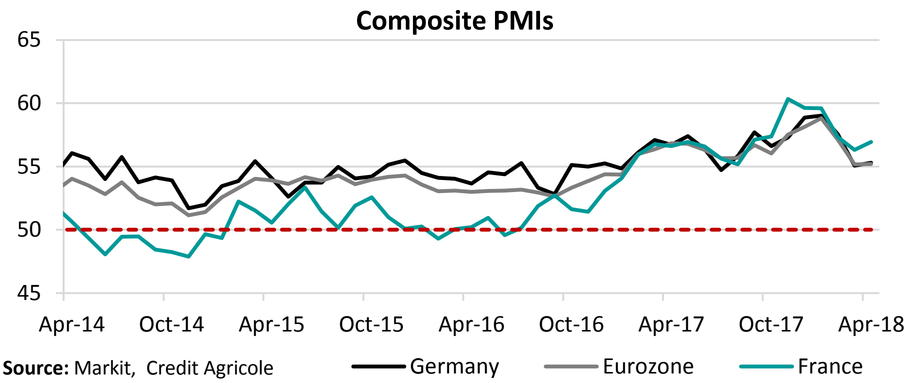
Last week

- **According to the flash data, the Composite PMI (for manufacturing and services) in the Eurozone has not changed in April compared to March and amounted to 55.2 pts.** The Composite PMI stabilized due to an increase in its sub-index for business activity in services and a decrease in its sub-index for output in manufacturing. The data pose a substantial risk to our forecast, in which the GDP growth rate in the Eurozone will not change in 2018 compared to 2017 and will amount to 2.4% (see below).

- **The ECB meeting was held last week.** The ECB maintained the existing monetary policy parameters. According to the statement, the ECB expects that interest rates are likely to stay at the current level for an extended period of time, significantly exceeding the horizon of the asset purchase program (forward guidance). The provision saying that the asset purchase program would last until September 2018 or longer, if necessary, was left unchanged. On the other hand, the fragment saying that changes in foreign exchange rate posed a downside risk to economic growth was deleted. During the conference after the meeting, the ECB Governor, M. Draghi, said that "the monetary policy per se was not discussed". On the other hand, there was a discussion on factors which substantially affect this policy. Mr Draghi pointed to the slowdown of the economic growth observed from the beginning of the year. However, he emphasized that it might result from temporary factors like adverse weather conditions, strikes and different timing of Easter holiday. In effect, he expects that economic growth will remain strong and will continue to be wide ranging. Nevertheless, before next decisions in the monetary policy he would like to wait for further data in order to have broader overview of the situation. During the conference, Mr Draghi also emphasized the risk related to protectionism, which, by adversely affecting market participants' sentiment, might hamper economic recovery. We maintain our scenario, in which in June 2018 the ECB will extend the asset purchase program until December 2018, reducing its scale to EUR 15bn starting from September 2018. However, we do not rule out that the high uncertainty stemming from the currently observed slowdown of economic growth may prompt the ECB to wait with this decision until July.
- **Important hard data on the US economy and business survey results were released last week.** In accordance with the flash estimate, the annualized GDP growth rate decreased to 2.3% in Q1 2018 vs. 2.9% in Q4 2017, running above market expectations (2.0%). The decrease resulted from lower contributions of private consumption (0.73 pp in Q1 vs 2.75 pp in Q4 2017) investments (0.76 pp vs. 1.31 pp) and government expenditures (0.20 pp vs. 0.51 pp). Higher contributions of net exports (0.20 pp vs. -1.16 pp) and inventories (0.43 pp vs -0.53 pp) had an opposite impact. Hence, the main source of US GDP increase in Q1 2018 were investments, while since Q3 2013 it had been consumption. Especially noteworthy in the data structure is a marked increase in inventories, which in our opinion might indicate a peak of growth cycle in US economy. Labour cost index rose by 0.8% QoQ in Q1 2018 vs. 0.6% in Q4 2017, which was above market expectations (0.7%). Previous such high increase in labour costs index was recorded in Q1 2017 and previously in Q4 2007.
- **Preliminary data on durable goods orders were also released last week and increased by 2.6% MoM in March vs. 3.5% in February.** The decrease in their monthly dynamics resulted from lower dynamics of orders for military aircrafts and parts. Excluding means of transport, the monthly growth rate of durable goods orders dropped to 0.0% in March vs. 0.9% in February, due to lower dynamics of orders for machinery, metals and electric equipment. Especially noteworthy in the data structure is the high growth rate of the annual dynamics of orders for non-military capital goods, excluding aircrafts (7.0% in March vs. 7.2% in February), which is a leading indicator for future investments. The ongoing recovery in the US real estate market was confirmed by data on new home sales (694k in March vs. 667k in February) and existing home sales (5.60M in March vs. 5.54M in February). Business survey results were also released last week. The Conference Board Index rose to 128.7 pts in April vs. 127.0 pts in March. The index increase resulted from higher values of its sub-indices for both the assessment of the current situation and expectations. On the other hand, the University of Michigan Index pointed to deterioration of sentiment, decreasing to 98.8 pts in April vs. 101.4 pts in March and 97.8 pts in the flash estimate. Its fall resulted from lower sub-indices for both the assessment of the current situation and expectations. We forecast that the annualized US GDP growth rate will rise to 3.1% in Q2 2018.

- **Retail sales in Poland rose by 9.2% YoY in March vs. a 7.9% increase in February**. The sales in constant prices rose by 8.8% in March vs. 7.7% in February. The increase in real retail sales resulted mainly from higher sales in the category "food, beverages and tobacco products" and "retail sales in non-specialized stores". Higher retail sales growth rate in these categories resulted from a different configuration of Easter holiday. It should be pointed out that higher pace of sales growth was mainly the effect of the shift of Easter shopping from April to March while their dynamics in a majority of categories have gone down. On the one hand, this could have been the effect of the unfavourable difference in the number of working days (in March 2018 the number of working days was one day lower than in 2017, while in February 2018 it was the same as the year before). On the other hand, we cannot exclude a negative impact of the Sunday trade ban on sales in these categories (see MACROpulse of 23/4/2018). Between January and March 2018 the average growth rate of retail sales in constant prices amounted to 8.5% YoY vs. a 7.5% increase in Q4 2017, which supports our upward-revised forecast, in which the private consumption growth rate rose to 5.4% YoY in Q1 vs. 5.0% in Q4 2017 (before the revision we assumed an increase at a level of 5.2% YoY).
- **Last week GUS revised the data on national accounts for 2016-2017**. According to the final estimate, GDP in 2016 rose in real terms by 3.0%, as compared to 2015, vs. the earlier-published increase by 2.9%. Real GDP growth in 2017 has not changed and amounted to 4.6%. On the other hand, the quarterly profile of economic growth has changed, i.a. the annual GDP growth rate was raised in Q1 2017 from 4.1% to 4.4% and in Q4 it was reduced to 4.9% from 5.1%. The most significant change is the modified estimate of investment dynamics in Q4 2017 from 11.3% YoY down to 5.4%. It has lowered the forecasted by us profile of dynamics of gross fixed capital formation in 2018 (down to 5.6% YoY vs. previously forecasted 7.1% and 3.4% observed in 2017). At the same time, due to the better-than-expected data from the labour market in Q1, we have increased our forecast of consumption (up to 4.6% YoY vs. 4.8% in 2017). As a result, our GDP forecasts for Q1 2018 (4.7%) and the whole 2018 (4.3%) have remained unchanged.

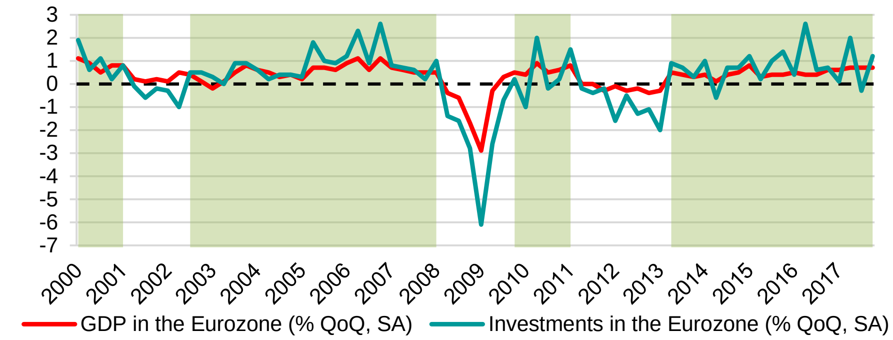
Is the peak of the upward cycle in the Eurozone already behind us ?



Source: Markit, Credit Agricole

According to the flash data, the Composite PMI (for manufacturing and services) in the Eurozone has not changed in April compared to March and amounted to 55.2 pts. The Composite PMI stabilized due to an increase in its sub-index for business activity in services and a decrease in its sub-index for output in manufacturing.

Especially noteworthy in the data structure is the decline in the indicator for new export orders in manufacturing, which dropped to 53.7 pts in April vs. 54.8 pts in March, hitting the lowest level since October 2016. At the same time, it has declined for a fifth month in a row. Between January and March a decrease in the indicator for new export orders has also been observed in the case of Chinese manufacturing PMI, which, in total, may signal a slowdown in global trade. This view is supported by the latest forecasts of the International Monetary Fund, in which the dynamics of global trade (the average dynamics of imports and exports) will decrease to 5.3% in 2018 vs. 5.4% in 2017. A fuller assessment of the global trade outlook will be possible only after the publication of the April PMI for Chinese manufacturing scheduled for 2 May.



Source: Eurostat, Credit Agricole

The situation in global trade is crucial for the investment outlook in the Eurozone. The current investment cycle in the Eurozone, namely a period in which the quarterly investment dynamics have not decreased for at least two consecutive quarters, has lasted for 19 quarters now (Q2 2013 – Q4 2017). Such a long investment cycle was last recorded in the period from Q3 2002 to Q1 2018 when it lasted for 23 quarters. Possible deterioration of global trade outlook combined with increased uncertainty related to the US protectionist policy will be conducive to higher risk premium expected by investors (higher expected rate of return on investment). As a result, it will be negative for investment dynamics in global trade and, consequently, for economic growth in the Eurozone. In addition, investments will also be limited by the expected by us further increase of interest rates in the US (in 2018 we assume three more hikes of interest rates by 25 bp each). Hence, we see a significant downside risk to our forecast, in which the GDP growth rate in the Eurozone will not change in 2018 compared to 2017 and will amount to 2.4%.

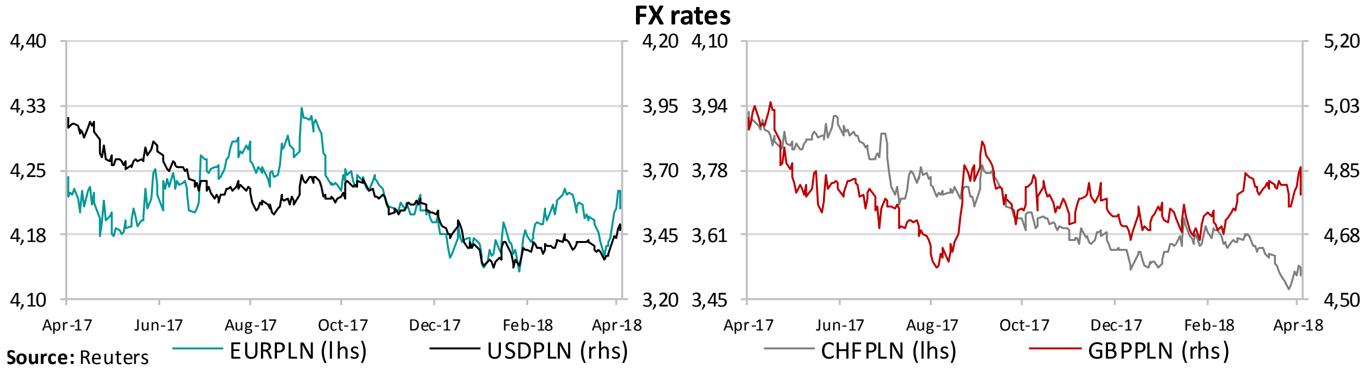
Geographically, an increase in the growth rate of economic activity was recorded both in Germany and in France. In both these cases the upturn resulted from higher sub-indices for business activity in services and for output in manufacturing. On the other hand, a deterioration of sentiment was recorded in other Eurozone economies covered by the survey, where the activity growth rate plummeted to the lowest level in 18 months. It resulted from lower activity in both manufacturing and services.

From the point of view of future business climate in Poland, especially noteworthy is the situation in German manufacturing. The PMI for this sector dropped to 58.1 pts in April vs. 58.2 pts in March. Its decrease resulted from lower contributions of four of its five sub-indices (for employment, new orders, supplier's delivery times, and stocks of goods purchased), while higher contribution of the sub-index for output had an opposite impact. Like in the case of data for the whole Eurozone, especially noteworthy in the index structure is the decrease in the sub-index for new export orders (55.4 pts in April vs. 55.8 pts in March) which has decreased for a fourth consecutive month.

Additional information on the situation in German manufacturing was also provided last week by Ifo Index, reflecting the sentiment among German managers representing manufacturing, construction, and wholesale and retail trade, which dropped to 102.1 pts in April vs. 103.3 pts in March (revised downwards from 114.7 pts due to a change in the methodology of the indicator calculation – see MACROmap of 23/4/2018). The index decline resulted from lower values of its sub-indices for both the assessment of the current situation and expectations. Sector-wise, the deterioration of sentiment was recorded in three of the four sectors (manufacturing, trade, and services); in turn, sentiment in construction has improved.

The decreasing rate of export orders growth in German manufacturing signals a high likelihood of weaker demand for goods manufactured in Poland and used in the production of final products (so-called intermediate goods). This supports our forecast, in which the dynamics of Polish exports will decrease to 6.6% in 2018 vs. 8.2% in 2017. Combined with the revised data on investments and GDP growth in Q4 2017 (see above), we notice a downside risk to our forecast of the Polish GDP growth rate in 2018 (4.3% vs. 4.6% in 2017).

Higher volatility of EURPLN due to FOMC meeting

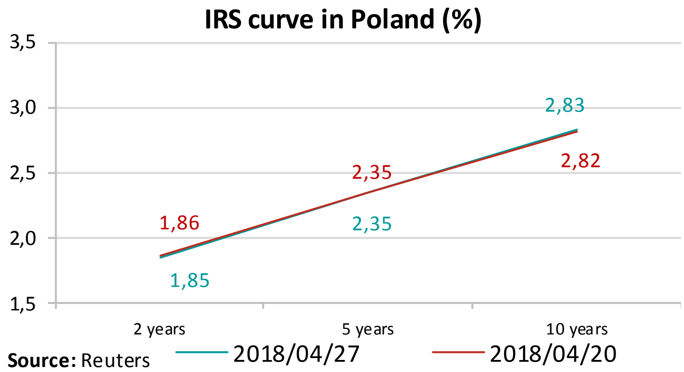


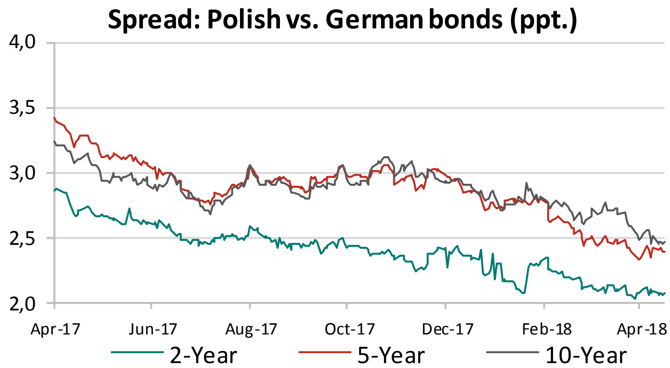
Source: Reuters

Last week EURPLN rate rose to 4.2053 (PLN weakening by 0.8%). Last week saw a marked capital outflow from Europe to the US. It led to depreciation of EUR against USD, as well as weakening of PLN and other currencies from the region against EUR and USD. It indicates that cyclical factor (interest rate spread between the US and the Eurozone) is beginning to influence the exchange rate stronger than fundamental factors (deficit in US balance of payments and surplus in Eurozone balance of payments). Thus, due to the simultaneous increase in the EURPLN rate and the decline in the EURUSD rate, PLN lost the most against USD last week (PLN weakening by 2.1%).

This week we expect low turnover in the exchange market due to the May holidays. The FED meeting scheduled for Wednesday might be conducive to higher volatility of PLN. The data from the US (non-farm payrolls and ISM for manufacturing), Eurozone (flash estimates of GDP in Q1 and inflation), China (Caixin PMI index for manufacturing) and flash inflation reading in Poland in our opinion will have limited impact on Polish FX rate. On the other hand, Polish PMI index for manufacturing might have negative effect on PLN.

Low liquidity in the market due to the May holidays





Source: Reuters

Last week the 2-year IRS rates dropped to a level of 1.85 (down by 1 bp), 5-year rates stayed at the level from two weeks ago and amounted to 2.35, and 10-year rates increased to a level of 2.83 (up by 1 bp). Throughout last week IRS rates were changing following the German market. In the first part of the week an increase was observed, which was a continuation of an upward trend started two weeks ago. In Thursday and Friday there was a correction. As a result, IRS interest rates returned to levels near

Friday’ closing two weeks ago. On Friday there was a debt auction at which the Ministry of Finance sold PLN 4.0bn of 2-, 5-, 6-, 10, and 30-year bonds with demand amounting to PLN 5.2bn. The auction had a limited impact on IRS rates.

This week we expect low turnover in the debt market due to the May holidays. The market focus will be on FOMC meeting scheduled for Wednesday, which might be conducive to higher volatility of IRS rates. However, the results of business surveys in Polish manufacturing may contribute to decline in IRS rates. We believe that data from US (non-farm payrolls and ISM for manufacturing), the Eurozone (flash estimates of GDP in Q1 and inflation) and other Polish data (flash inflation reading) will be neutral for IRS rates.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18
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*	4,23	4,18	4,23	4,25	4,25	4,31	4,24	4,20	4,18	4,15	4,17	4,21	**4,21**	**4,20**
USDPLN*	3,88	3,72	3,70	3,59	3,57	3,65	3,64	3,53	3,48	3,34	3,42	3,42	**3,47**	**3,48**
CHFPLN*	3,90	3,84	3,86	3,72	3,72	3,77	3,65	3,59	3,57	3,59	3,62	3,58	**3,51**	**3,53**
CPI inflation (% YoY)	2,0	1,9	1,5	1,7	1,8	2,2	2,1	2,5	2,1	1,9	1,4	1,3	**1,5**	
Core inflation (% YoY)	0,9	0,8	0,8	0,8	0,7	1,0	0,8	0,9	0,9	1,0	0,8	0,7	**0,6**	
Industrial production (% YoY)	-0,5	9,3	4,4	6,3	8,9	4,3	12,4	9,2	2,8	8,6	7,3	1,9	**7,8**	
PPI inflation (% YoY)	4,2	2,4	1,8	2,2	3,0	3,2	3,0	1,8	0,3	0,2	-0,1	0,3	**0,7**	
Retail sales (% YoY)	8,1	8,4	6,0	7,1	7,6	8,6	8,0	10,2	6,0	8,2	7,9	9,2	**8,2**	
Corporate sector wages (% YoY)	4,1	5,4	6,0	4,9	6,6	6,0	7,4	6,5	7,3	7,3	6,8	6,7	**7,1**	
Employment (% YoY)	4,6	4,5	4,3	4,5	4,6	4,5	4,4	4,5	4,6	3,8	3,7	3,7	**3,7**	
Unemployment rate* (%)	7,6	7,3	7,0	7,0	7,0	6,8	6,6	6,5	6,6	6,9	6,8	6,6	**6,2**	
Current account (M EUR)	284	-202	-902	-296	311	218	436	278	-699	2072	-1017	**-620**		
Exports (% YoY EUR)	3,3	19,1	7,2	15,0	13,4	11,5	15,8	15,5	2,6	11,7	5,7	**-1,1**		
Imports (% YoY EUR)	5,0	21,5	14,3	14,6	8,7	8,9	15,4	15,9	10,9	16,3	8,3	**2,1**		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

	Indicator	2017				2018				2017	2018	2019
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
	Gross Domestic Product (% YoY)	4,4	4,0	5,2	4,9	4,7	4,3	4,2	3,9	4,6	4,3	3,0
	Private consumption (% YoY)	4,5	4,9	4,7	5,0	5,4	4,4	4,3	4,2	4,8	4,6	3,6
	Gross fixed capital formation (% YoY)	1,4	1,3	3,6	5,4	6,5	6,0	5,5	5,0	3,4	5,6	3,1
	Export - constant prices (% YoY)	11,2	4,5	9,2	8,2	7,5	6,5	6,6	6,0	8,2	6,6	5,0
	Import - constant prices (% YoY)	11,1	8,0	7,0	8,9	8,1	7,8	7,5	7,0	8,7	7,6	6,0
GDP growth contributions	Private consumption (pp)	2,8	2,9	2,8	2,5	3,5	2,6	2,6	2,1	2,7	2,7	2,1
	Investments (pp)	0,2	0,2	0,6	1,4	0,8	1,0	0,9	1,2	0,6	1,0	0,6
	Net exports (pp)	0,5	-1,5	1,3	0,0	0,0	-0,4	-0,2	-0,3	0,1	-0,2	-0,3
	Current account (% of GDP)***	0,2	-0,4	0,3	0,3	-0,1	-0,1	-0,4	-0,4	0,3	-0,4	-0,6
	Unemployment rate (%)**	8,0	7,0	6,8	6,6	6,6	6,0	6,2	6,5	6,6	6,5	6,5
	Non-agricultural employment (% YoY)	2,1	2,4	1,8	1,3	1,2	0,7	0,4	0,3	1,9	0,6	0,2
	Wages in national economy (% YoY)	4,1	5,0	4,9	7,1	6,8	6,1	6,4	6,8	5,3	6,5	6,5
	CPI Inflation (% YoY)*	2,0	1,8	1,9	2,3	1,5	1,5	1,6	1,1	2,0	1,4	1,7
	Wibor 3M (%)**	1,73	1,73	1,73	1,72	1,70	1,70	1,70	1,70	1,72	1,70	1,95
	NBP reference rate (%)**	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,75
	EURPLN**	4,23	4,23	4,31	4,18	4,21	4,19	4,18	4,17	4,18	4,17	4,15
	USDPLN**	3,97	3,70	3,65	3,48	3,42	3,41	3,34	3,31	3,48	3,31	3,19

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST* CA	FORECAST* CONSENSUS**
Monday 04/30/2018						
3:00	China	Caixin Manufacturing PMI (pts)	Apr	51,5	51,5	51,3
10:00	Eurozone	M3 money supply (% MoM)	Mar	4,2		4,1
14:00	Germany	Preliminary HICP (% YoY)	Apr	1,5	1,5	1,5
14:30	USA	Real private consumption (% MoM)	Mar	0,0		
15:45	USA	Chicago PMI (pts)	Apr	57,4		57,9
Tuesday 05/01/2018						
15:45	USA	Flash Manufacturing PMI (pts)	Apr	56,5		
16:00	USA	ISM Manufacturing PMI (pts)	Apr	59,3	58,3	58,4
Wednesday 05/02/2018						
3:45	China	Caixin Manufacturing PMI (pts)	Apr	50,2	50,7	50,8
9:00	**Poland**	**Manufacturing PMI (pts)**	**Apr**	**53,7**	**52,9**	**53,2**
9:55	Germany	Final Manufacturing PMI (pts)	Apr	58,1	58,1	58,1
10:00	**Poland**	**Flash CPI (% YoY)**	**Apr**	**1,3**	**1,5**	**1,5**
10:00	Eurozone	Final Manufacturing PMI (pts)	Apr	56,0	56,0	56,0
11:00	Eurozone	Preliminary GDP (% QoQ)	Q1	0,6	0,6	0,4
14:15	USA	ADP employment report (k)	Apr	241		203
20:00	USA	FOMC meeting (%)	May	1,75	1,75	1,75
Thursday 05/03/2018						
11:00	Eurozone	Preliminary HICP (% YoY)	Apr	1,3	1,3	1,3
11:00	Eurozone	PPI (% YoY)	Mar	1,6		2,1
14:30	USA	Initial jobless claims (k)	w/e	232		225
16:00	USA	ISM Non-Manufacturing Index (pts)	Apr	58,8	58,9	58,2
16:00	USA	Factory orders (% MoM)	Mar	1,2	1,4	1,4
Friday 05/04/2018						
10:00	Eurozone	Services PMI (pts)	Apr	55,0	55,0	55,0
10:00	Eurozone	Final Composite PMI (pts)	Apr	55,2	55,2	55,2
11:00	Eurozone	Retail sales (% MoM)	Mar	0,1		0,5
14:30	USA	Unemployment rate (%)	Apr	4,1	4,0	4,0
14:30	USA	Non-farm payrolls (k MoM)	Apr	103	195	195

*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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