Decline in foreign orders in Polish manufacturing

This week

- **August data on business sentiment in Polish manufacturing have been released today (see below).** PMI dropped to 51.4 pts in August vs. 52.9 pts in July, running significantly below the market consensus (53.0 pts) and our forecast (53.5 pts). The average value of the Polish PMI in July-August period (52.1 pts) stood significantly below its average value in Q2 (53.8 pts), which poses a slight downside risk to our forecast of GDP dynamics in Q3 (4.8% YoY vs. 5.1% in Q2). We will present our latest macroeconomic scenario in the next MACROmap.
- **Another important event this week will be the meeting of the Monetary Policy Council scheduled for Wednesday.** We expect that the MPC will decide to leave interest rates at an unchanged level. The issues of lower-than-expected investment growth in Q2 2018 and estimated higher-from-consensus core inflation in August (see below) are likely to be raised during the conference in the context of the impact of these data on the monetary policy outlook. In our view, the NBP Governor, A. Glapiński, will repeat his view at the conference that interest rates will remain unchanged at least until the end of 2019. We believe that the text of the statement after the Council meeting and the remarks of the NBP Governor during the conference will be neutral for PLN and prices of the Polish debt.
- **Important data from the US will also be released this week.** Data from the labour market will be published on Friday. We expect that non-farm payrolls growth amounted to 195k in August vs. 157k in July, with unemployment falling down from 3.9% to 3.8% in August. 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 190k in August vs. 219k in July). The ISM index for manufacturing will be released on Tuesday. In our view it dropped to 57.8 pts in August vs. 58.1 pts in July, in line with the results of regional business surveys. We believe that the publication of data from the US will be neutral for PLN and prices of Polish bonds.
- **The results of business surveys in Chinese manufacturing have been released in recent days.** The CFLP PMI rose to 51.3 pts in August vs. 51.2 pts in July while the Caixin PMI, released today, dropped to 50.7 pts in August vs. 50.8 pts in July. The decline in Caixin PMI resulted from lower contributions of three of its five sub-indices (for new orders, employment, and suppliers' delivery times). Higher contributions of the sub-indices for output and inventories had an opposite impact. Especially noteworthy in the index structure is the decline in the sub-index for new orders (50.6 pts in August vs. 51.6 pts in July) to the lowest level since May 2017. At the same time, the new export orders sub-index has slightly increased to 48.8 pts in August vs. 48.4 pts in July, nonetheless staying below the 50 pts threshold dividing expansion from contraction of activity. Thus, the data structure indicates weaker internal demand with slower pace of the decrease in new export orders. Slower decline in new export orders signals that customs duties imposed by the US on Chinese exports have so far had a limited impact on their dynamics. Therefore we maintain our forecast in which the Chinese GDP growth rate will decrease to 6.6% in 2018 vs. 6.9% in 2017. Our forecast is supported by the measures planned by the Chinese government to stimulate domestic demand. They include increase in tax allowance, lower corporate tax, increased lending, and launch of new structural investments. The main risk to our scenario is possible further escalation of protectionist measures in global trade.

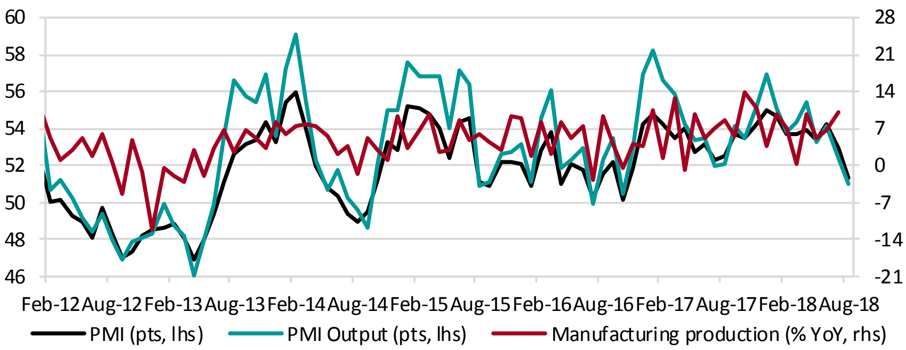
Last week

- **The GDP growth rate stood at 5.1% YoY in Q2 vs. 5.2% in Q1, running in line with the flash estimate released earlier**. Seasonally-adjusted quarterly GDP increased by 1.0% QoQ vs. a 1.6% increase in Q1. Conducive to the decline in the annual economic growth rate were lower contributions of inventories (0.2 pp in Q2 vs. 1.9 pp in Q1), investments (0.7 pp vs. 0.9 pp), and private consumption (2.9 pp vs. 3.0 pp). Higher contributions of new exports (0.5 pp vs. -1.2 pp) and public consumption (0.8 pp vs. 0.6 pp) had an opposite impact. Thus consumption remained the main driver of economic growth. A big surprise in the data structure are the data on investment dynamics which dropped to 4.5% YoY in Q2 vs. 8.1% YoY in Q1. The reason for the strong deceleration in total investments in Q2 was the way in which military investments are treated in the national accounts, which boosted public investments dynamics in Q1 and was responsible for their decline in Q2 (see MACROpulse of 31/8/2018). Despite the surprising decline in investment dynamics in Q2, we expect that their growth will accelerate in H2 boosted by fast increase in public investments excluding local governments and higher dynamics of investment outlays of small and medium-size enterprises. At the same time, the data on consumption in Q2 suggest that its growth in H2 is likely to be faster than we expected. Consequently, there is a slight upside risk to our forecast of economic growth both in H2 and in the whole 2018 (5.0%).

- **According to the flash estimate, CPI inflation in Poland has not changed in August compared to July and amounted to 2.0% YoY, running in line with market expectations and above our forecast (1.9%)**. GUS has published partial data on inflation structure, including information about inflation rate in the categories “food and non-alcoholic beverages”, “energy”, and “fuels”. Conducive to a decrease in total inflation were lower dynamics of prices of food (2.1% YoY in August vs. 2.2% in July) and fuels (15.3% YoY vs. 18.0%), while higher dynamics of energy prices (2.2% YoY vs. 1-8% in July), resulting from the rise in gas prices, had an opposite impact. We estimate on this basis that core inflation rose to 0.9% YoY in August vs. 0.6% in July. The August data do not alter our forecast of average inflation in 2018 (1.6% vs. 2.0% in 2017).
- **Significant hard data from the US economy and business survey results were released last week.** According to the second estimate, the annualized US GDP growth rate amounted to 4.2% in Q2 vs. 4.1% in the first estimate. The upward revision resulted from higher contributions of investments (1.07 pp in the second estimate vs. 0.94 pp in the first estimate), net exports (1.17 pp vs. 1.06 pp), government spending (0.41 pp vs. 0.37 pp), and inventories (-0.97 pp vs. -1.00 pp), which have more than offset a lower contribution of consumption (2.55 pp vs. 2.69 pp). The second estimate has confirmed that private consumption was the main source of the US GDP growth in Q2 while in Q1 it was investments. The results of consumer sentiment surveys were also released last week. The Conference Board Index rose to 133.4 pts in August vs. 127.9 pts in July, hitting the highest level since October 2000. The index increase resulted from both its higher sub-index concerning the assessment of the current situation and expectations. On the other hand, the final University of Michigan Index pointed to a slight deterioration of consumer sentiment, decreasing to 96.2 pts in August vs. 97.9 pts in July and 95.3 pts in the flash estimate. Its decrease 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 decrease to 3.0% in Q3 2018.
- **According to the flash estimate, inflation in the Eurozone dropped to 2.0% YoY in August vs. 2.1% in July, running in line with our forecast equal to market expectations**. The decrease in inflation resulted from lower price dynamics in the categories: “energy”, “industrial goods”, and “services”, while the growth rate of the prices of food and non-alcoholic beverages has not changed compared to the previous month. We expect that in subsequent quarters, the annual inflation rate within the single currency area will continue to range between 1.9% and 2.1%. Q2 2019 will see a decline in inflation, supported by high base effect from the year before, and inflation will reach 1.4% YoY in Q4 2019. We also forecast that core inflation in the Eurozone will not exceed 1.4% in the next two years. This is in line with our scenario, in which the first hike of the ECB interest rates (deposit rate) will take place in September 2019, while the main interest rate will be hiked in December 2019.
- **Ifo Index reflecting the sentiment among German managers representing the manufacturing, construction, and services rose to 103.8 pts in August vs. 101.7 pts in July, hitting the highest**

level since February 2018. The index increased due to higher sub-indices for both the assessment of the current situation and expectations. Sector-wise, improved sentiment was recorded in all the four segments covered by the survey (services, manufacturing, construction, and trade). The improvement in Germany in August had been signaled earlier by the PMI Composite published two weeks ago (see MACROmap of 27/8/2018). However, considering the PMI structure which pointed to slower pace of activity in German manufacturing, including slower growth of new orders, it is highly likely that the economic slowdown in Germany observed from the beginning of 2018 is not over yet. We forecast that the quarterly GDP growth rate in Germany will not change in Q3 compared to Q2 and will amount to 0.5%.

Decline in foreign orders in Polish manufacturing



Source: Markit. GUS

Polish manufacturing PMI dropped to 51.4 pts in August vs. 52.9 pts in July, running significantly below our forecast (53.5 pts) and the market consensus (53.0 pts). Conducive to the index decline were lower contributions of all its five sub-indices (concerning output, total new orders, employment, suppliers' delivery times, and stocks of goods purchased).

Especially noteworthy is the decline in the sub-index concerning new export orders significantly below the 50 pts threshold dividing expansion from contraction of this category. A decline in export orders in monthly terms has already been observed in recent months (in March and in May) but in July this decline was the strongest since July 2014. We believe that the decrease in foreign demand was related to the slowdown in global trade observed in recent months, which was limiting exports in the Eurozone, including Germany. This view is supported by the downward tendency recorded from the beginning of 2018 in export orders in German manufacturing. We believe that the protectionist measures implemented in recent months in global trade did not have any substantial impact on the exports of goods from Poland. At the same time it should be pointed out that the sub-index concerning total new orders - taking into account the decrease in foreign orders – continues to signal a quite fast increase in domestic demand.

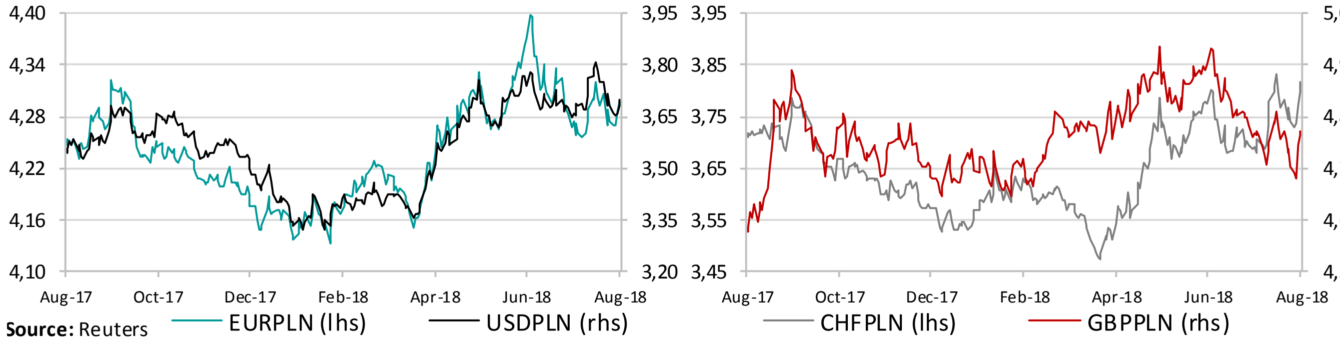
According to Markit, slower growth of orders has contributed to a slowdown of output growth. Interestingly, output slowed down despite the resumption of work in car factories after the holiday break in July (see MACROpulse of 1/8/2018). Given slower inflow of new orders, the companies were using production capacities to reduce production backlogs (which have dropped for the first time since April 2018) and to increase stocks of final products (which increased for the first time since January 2017).

Important in the context of assessing the prospects for growth of activity in Polish manufacturing is the future output indicator reflecting the companies' expectations concerning production volumes in the next 12 months. It has slightly decreased in August 2018 but stayed at a relatively high level. The surveyed companies reported that the good production outlook was related to the launch of new products and investments in machinery. This is in line with our scenario in which the recovery in corporate investments recorded in Q2 (see MACROmap of 27/8/2018) will contribute towards an increase in production capacities and future output.

The average value of the Polish PMI between July and August (52.1 pts) stood significantly below its average value in Q2 (53.8 pts), which poses a slight downside risk to our forecast of GDP dynamics in Q3 (4.8% YoY vs. 5.1% in Q2). However, considering the tendencies outlined above, we expect that the August decline in PMI was temporary. In subsequent months the increase in manufacturing activity will be limited by the slowdown in foreign trade but the acceleration in domestic demand (supported by fast increase in investments and consumption, see MACROpulse of 31/8/2018) will offset this negative trend. In effect, we assess the downside risk to our all-year forecast of GDP growth in 2018 (5.0% YoY) as limited. We will present our latest macroeconomic scenario in the next MACROmap.

Currency crisis in Turkey negative for the PLN

FX rates



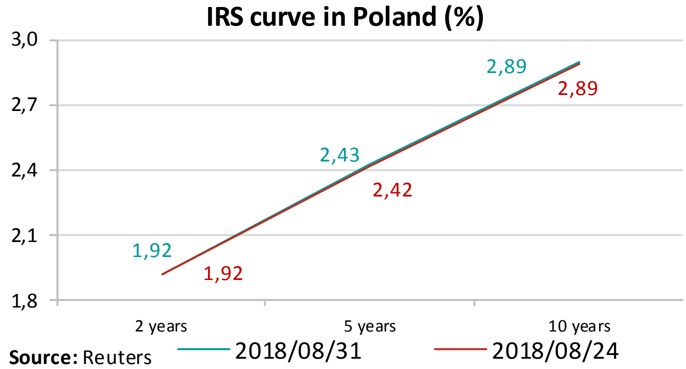
Source: Reuters

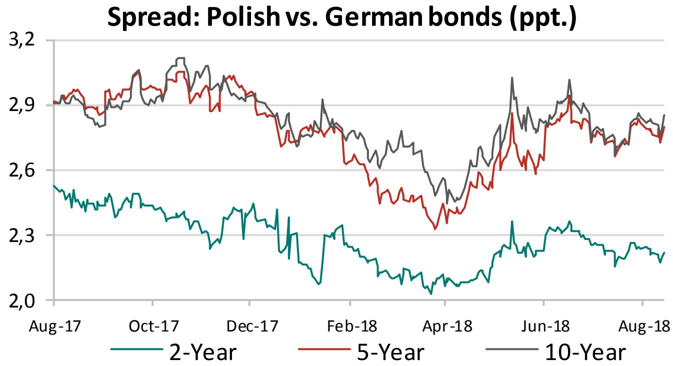
Last week, the EURPLN exchange rate rose 4.2935 (PLN weakening by 0.4%). On Monday and Tuesday EURPLN was stable and oscillated around 4.27. Wednesday saw a visible increase in risk aversion with intensification of the currency crisis in Turkey, after Moody's downgraded the rating of 20 Turkish financial institutions, pointing to a growing risk to the financial sector in the context of its excessive debt in foreign currencies. Consequently, Wednesday and Thursday saw PLN weakening. On Friday there was a correction. Domestic data on GDP and flash inflation had a limited impact on the market.

Due to the nature of the last week's weakening of PLN, which resulted mainly from higher risk aversion, PLN was also depreciating vs. other major currencies. In effect, last week, PLN depreciated vs. CHF (by 1.9%), GBP (by 1.6%), and USD (by 0.6%). PLN was relatively strongly depreciating vs. GBP, due to a decrease in EURGBP after the EU chief Brexit negotiator, M. Barnier, said that EU was prepared to offer the United Kingdom "unprecedented close relations" but would not agree to solutions weakening the single market. These remarks were received as a lower likelihood of the implementation of a hard Brexit scenario.

Today's results of business surveys for Polish manufacturing are slightly negative for PLN. On the other hand, the China manufacturing Caixin PMI published during the night is neutral for PLN. Crucial for PLN this week will be the US non-farm payrolls data. If our forecast that is close to the market consensus materializes, the data will not have any substantial impact on PLN. We believe that the manufacturing ISM Index will also be neutral for PLN as well as the MPC meeting scheduled for Wednesday.

Market will focus on data from the US labour market





Source: Reuters

Last week, 2-year IRS rates have not changed compared to the level from two weeks ago and amounted to 1.92, 5-year rates rose to 2.43 (up by 1 bp), and 10-year have not changed compared to the level from two weeks ago and amounted to 2.89. Monday through Wednesday saw an increase in IRS rates across the curve, following the German market. This increase was particularly strong on Wednesday due to higher risk aversion caused by the intensification of the currency crisis in Turkey. Thursday saw a correction. On Friday IRS rates were relatively stable and domestic data on GDP and flash inflation had a limited impact on the curve.

Today's reading of PMI for Polish manufacturing may be conducive to an decrease in IRS rates. This week the market will focus on the US non-farm payrolls data. We believe that they will be neutral for IRS rates. In our view, the manufacturing ISM Index will also have a limited impact on the market. The MPC meeting will not have any substantial impact on the yield curve, we believe.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland														
Indicator	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-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*	4,25	4,31	4,24	4,20	4,18	4,15	4,17	4,21	4,24	4,31	4,37	4,27	4,28	**4,27**
USDPLN*	3,57	3,65	3,64	3,53	3,48	3,34	3,42	3,42	3,51	3,69	3,74	3,66	3,68	**3,62**
CHFPLN*	3,72	3,77	3,65	3,59	3,57	3,59	3,62	3,58	3,54	3,74	3,78	3,69	3,80	**3,65**
CPI inflation (% YoY)	1,8	2,2	2,1	2,5	2,1	1,9	1,4	1,3	1,6	1,7	2,0	2,0	**1,9**	
Core inflation (% YoY)	0,7	1,0	0,8	0,9	0,9	1,0	0,8	0,7	0,6	0,5	0,6	0,6	**0,6**	
Industrial production (% YoY)	8,9	4,3	12,4	9,2	2,8	8,6	7,3	1,7	9,3	5,2	6,7	10,3	**5,5**	
PPI inflation (% YoY)	3,0	3,2	3,0	1,8	0,3	0,2	-0,1	0,5	1,0	3,0	3,7	3,4	**3,2**	
Retail sales (% YoY)	7,6	8,6	8,0	10,2	6,0	8,2	7,9	9,2	4,6	7,6	10,3	9,3	**9,0**	
Corporate sector wages (% YoY)	6,6	6,0	7,4	6,5	7,3	7,3	6,8	6,7	7,8	7,0	7,5	7,2	**6,7**	
Employment (% YoY)	4,6	4,5	4,4	4,5	4,6	3,8	3,7	3,7	3,7	3,7	3,7	3,5	**3,5**	
Unemployment rate* (%)	7,0	6,8	6,6	6,5	6,6	6,9	6,8	6,6	6,3	6,1	5,9	5,9	**5,9**	
Current account (M EUR)	311	218	206	54	-847	1955	-782	-785	-90	169	-240	**-290**		
Exports (% YoY EUR)	13,4	11,5	15,8	15,5	2,6	12,1	5,9	-1,6	8,9	2,7	9,0	**11,9**		
Imports (% YoY EUR)	8,7	8,9	15,4	15,9	10,9	16,7	8,1	1,4	11,1	1,5	10,2	**11,0**		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland											
Indicator	2018				2019				2017	2018	2019
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)	5,2	5,1	4,8	4,7	4,4	3,8	3,3	3,0	4,6	5,0	3,7
Private consumption (% YoY)	4,8	4,9	4,6	4,5	4,0	3,5	3,6	3,4	4,8	4,6	3,7
Gross fixed capital formation (% YoY)	8,1	4,5	9,4	9,1	4,9	3,4	2,5	2,1	3,4	8,9	3,2
Export - constant prices (% YoY)	1,1	6,9	5,5	4,7	7,0	5,5	5,3	4,9	8,2	4,3	5,7
Import - constant prices (% YoY)	3,5	6,5	4,5	5,3	6,2	5,8	5,4	5,1	8,7	4,3	5,7
GDP growth contributions											
Private consumption (pp)	3,0	2,9	2,7	2,3	2,6	2,1	2,1	1,7	2,7	2,7	2,1
Investments (pp)	0,9	0,7	1,6	2,2	0,6	0,6	0,4	0,5	0,6	1,5	0,6
Net exports (pp)	-1,2	0,5	0,8	-0,1	0,6	0,1	0,2	0,0	0,1	0,2	0,2
Current account (% of GDP)***	-0,2	0,0	-0,1	-0,6	-0,9	-0,9	-0,8	-0,9	0,2	-0,6	-0,9
Unemployment rate (%)**	6,6	5,9	5,7	6,0	6,4	5,9	5,7	6,0	6,6	6,0	6,0
Non-agricultural employment (% YoY)	1,4	1,0	1,0	0,8	0,5	0,3	0,2	0,1	1,9	1,0	0,3
Wages in national economy (% YoY)	6,2	7,1	7,0	7,1	7,6	7,0	6,7	6,6	5,3	6,9	7,0
CPI Inflation (% YoY)*	1,5	1,7	1,9	1,1	1,3	1,3	1,2	1,5	2,0	1,6	1,3
Wibor 3M (%)**	1,70	1,70	1,70	1,70	1,70	1,70	1,70	1,78	1,72	1,70	1,78
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
EURPLN**	4,21	4,37	4,27	4,24	4,23	4,20	4,18	4,15	4,18	4,24	4,15
USDPLN**	3,42	3,74	3,62	3,50	3,44	3,36	3,27	3,19	3,48	3,50	3,19

* quarterly average
** end of period
***cumulative for the last 4 quarters
**** revised forecast will be published on 10/09/2018

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST*	
					CA	CONSENSUS**
		Monday 09/03/2018				
3:45	China	Caixin Manufacturing PMI (pts)	Aug	50,2	50,6	50,6
9:00	**Poland**	**Manufacturing PMI (pts)**	**Aug**	**52,9**	**53,5**	**53,0**
9:55	Germany	Final Manufacturing PMI (pts)	Aug	56,1	56,1	56,1
10:00	Eurozone	Final Manufacturing PMI (pts)	Aug	54,6	54,6	54,6
		Tuesday 09/04/2018				
11:00	Eurozone	PPI (% YoY)	Jul	3,6		3,9
15:45	USA	Flash Manufacturing PMI (pts)	Aug	54,5		
16:00	USA	ISM Manufacturing PMI (pts)	Aug	58,1	57,8	57,6
		Wednesday 09/05/2018				
10:00	Eurozone	Services PMI (pts)	Aug	54,4	54,4	54,4
10:00	Eurozone	Final Composite PMI (pts)	Aug	54,4	54,4	54,4
11:00	Eurozone	Retail sales (% MoM)	Jul	0,3		-0,2
	Poland	**NBP rate decision (%)**	**Sep**	**1,50**	**1,50**	
		Thursday 09/06/2018				
8:00	Germany	New industrial orders (% MoM)	Jul	-4,0		1,8
14:15	USA	ADP employment report (k)	Aug	219		190
14:30	USA	Initial jobless claims (k)	w/e	213		214
16:00	USA	Factory orders (% MoM)	Jul	0,7	-0,7	-0,6
16:00	USA	ISM Non-Manufacturing Index (pts)	Aug	55,7	56,6	56,5
		Friday 09/07/2018				
8:00	Germany	Industrial production (% MoM)	Jul	-0,9		0,2
8:00	Germany	Trade balance (bn EUR)	Jul	19,3		19,5
11:00	Eurozone	Final GDP (% YoY)	Q2	2,2		2,2
11:00	Eurozone	Revised GDP (% QoQ)	Q2	0,4	0,4	0,4
14:30	USA	Unemployment rate (%)	Aug	3,9	3,8	3,9
14:30	USA	Non-farm payrolls (k MoM)	Aug	157	195	190

*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

Jakub BOROWSKI
Chief Economist
tel.: 22 573 18 40

jakub.borowski@credit-agricole.pl

Krystian JAWORSKI
Senior Economist
tel.: 22 573 18 41

krystian.jaworski@credit-agricole.pl

Jakub OLIPRA
Economist
tel.: 22 573 18 42

jakub.olipra@credit-agricole.pl