In anticipation of recovery of investments in the energy sector

This week

- **The parliamentary election in Italy was held on Sunday. According to exit polls, the election was won by a coalition of the Northern League, Forza Italia and Brothers of Italy, taking in total ca. 35%-36% of the vote**. They were followed by the Five Star Movement (31.5%) and the Democratic Party (23%). The election results, indicating that no party or coalition had an overall majority, is conducive to a slight increase in risk aversion. The fact that the party with the biggest support is the Eurosceptic Five Star Movement, which has won bigger support than in the pre-election polls, may be particularly alarming for investors. However, we believe that the negative impact of this factor on PLN and the prices of the Polish debt will be limited. Another important political event was the publication during the weekend of the results of the internal vote within SPD on the future of the coalition in Germany. Most SPD members (66%) showed readiness to create coalition with CDU/CSU. In effect, the fact that there is no need to hold early elections in Germany will be conducive to lowering of political risk. Consequently, we expect an increase in risk appetite, which will support higher EURUSD rate, stronger PLN, and increased demand for the Polish debt.
- **The most 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 results of the latest NBP projection will be presented at the same time. We expect the GDP growth and inflation profile to be revised upwards compared to the November projection. Nevertheless, we believe that the NBP Governor, A. Glapiński, will maintain his view that interest rates will remain unchanged until the end of 2018 and, most probably, also at the beginning of 2019. We believe that the NBP Governor’s remarks during the conference will be neutral for PLN and yields on Polish bonds at the short end of the curve.
- **Another important event will be the release of data on non-farm payrolls in the US scheduled for Friday.** We expect the employment to have increased by 210k in February vs. 200k in January, with unemployment rate down to 4.0% from 4.1% in January. 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 vs. 234k in January). We believe that the publication of data on non-farm payrolls in the US will be conducive to PLN weakening and higher yields on Polish bonds.
- **The ECB meeting will be held on Thursday.** In our view, the ECB the parameters of the monetary policy will be left unchanged and the conference after the meeting will not provide any new information significantly altering our scenario, in which in June 2018 the ECB will extend the expanded asset purchase program until December 2019 reducing its scale to EUR 15bn starting from September 2018. The tone of the conference will be hawkish, we believe. The latest macroeconomic projection will also be presented at the conference after the meeting. We believe that the economic growth rate and inflation profiles will not visibly change compared to the December projection. We expect that during the conference after the meeting, we may see increased volatility in the financial markets.
- **Data on the Chinese balance of trade will be released on Thursday**. We expect that its balance dropped to USD -13.9bn in February vs. USD 20.3bn in January. We forecast that, due to the impact of the Chinese New Year, export growth dropped to 1.3% YoY in February vs. 11.1% in January, while import growth dropped to 4.9% from 36.8%. The publication of data from China will be neutral for the markets.

Last week

- **Last week, the new FED Chairman, J. Powell, presented to the Congress the semi-annual report on the implementation of the monetary policy.** J. Powell's remarks indicate that FED is highly optimistic about the prospects for US economic growth and inflation meeting the target in the medium term. Contrary to market expectations, J. Powell showed quite cautious approach when speaking about the potential impact of lower taxes in USA on the outlook for economic growth and inflation. He indicated, however, that it would significantly boost demand, at least in the next few years. The March FOMC economic projections are likely to provide new information on the issue. Powell's remarks were received by the market as slightly hawkish, which led to higher yields on US bonds across the curve. Powell's remarks pose an upside risk to our scenario, in which FED will hike interest rates three times in 2018 by 25bp each time (in March, June, and September).
- **Numerous hard data and business survey results were released last week in the US.** According to the second estimate, the annualized growth rate of the US GDP in Q4 2017 was revised downwards to 2.5% vs. 2.6% in the preliminary estimate. It resulted from lower contribution of inventories (-0.70 pp in the second estimate vs. -0.67 pp in the first estimate) and government spending (0.49 pp vs. 0.50 pp). Higher contribution of investments (1.29 pp vs. 1.27 pp) had an opposite impact. The contributions of private consumption and net experts have not been revised and amounted to 2.58 pp and -1.13 pp, respectively. Thus, like in the whole 2017, the US GDP growth in Q4 was mainly driven by private consumption. Data on preliminary durable goods orders were also released last week and decreased by 3.7% MoM in January vs. a 2.6% increase in December, mainly due to lower dynamics of orders for means of transport (the effect of lower orders for aircrafts and their parts). Excluding means of transport, durable goods orders decreased by 0.3% MoM vs. a 0.7% increase in December. Especially noteworthy in the data structure is the decrease in the annual growth of orders for non-military capital goods excluding aircrafts (6.3% in January vs. 98.0% in December), being the leading indicator of future investments. Last week, a slight decrease in the growth rate of activity in the US real estate market was reflected by data on new home sales (593k in January vs. 643k in December) The ISM Index for manufacturing was also released last week and rose to 60.7 pts in February vs. 59.1 pts in January, hitting the highest level since May 2004. Conducive to the index increase were higher contributions of three of its five sub-indices (for employment, suppliers' delivery times, and stocks of goods purchased). Lower contributions of sub-indices for new orders and output had an opposite impact. The Conference Board Index was also released last week and rose to 130.8 pts in February vs. 124.3 pts in January, hitting the highest level since November 2000. The index sharp increase resulted from its higher sub-indices for both the assessment of the current situation and expectations. Improved consumer sentiment was also indicated by the University of Michigan Index which rose to 99.7 pts in February vs. 95.7 pts in January and 99.9 pts in the flash estimate. Like in the case of the Conference Board Index, the increase in the University of Michigan Index resulted from its higher sub-indices for both the assessment of the current situation and expectations. The last week's data on the US economy pose an upside risk to our forecast in which the annualized US GDP growth rate will amount to 2.3% in Q1.
- **The US President D. Trump announced that he would next week sign an order imposing global tariffs of 25 per cent on steel and 10 per cent on aluminum.** According to D. Trump's remarks, this policy is to "build back" the US steel and aluminum industry. Donald Trump also said that 'when a country (USA) is losing many billions of dollars on trade with virtually every country it does business with, trade wars are good and easy to win". Although Trump's earlier remarks suggest that higher tariffs will be mainly directed against China, the structure of the US imports of steel and aluminum indicates that the tariffs will affect other countries to a greater extent, i.a. Canada and Brazil. Donald Trump's announcement raised market concerns about the launch

of a trade war should other countries respond to the increase in US customs duties. A trade war would negatively impact the prospects for global economic growth. Donald Trump's remarks resulted in USD weakening vs. EUR.

- **According to the final estimate, the Polish GDP growth rate rose to 5.1% in Q4 vs. 4.9% in Q3, which was in line with the flash estimate.** Conducive to faster GDP growth were higher contributions of investments (2.8 in Q4 vs. 0.6 pp in Q3) and public consumption (1.0pp in vs. 2.9 pp). Lower contributions of net exports (-0.8 pp vs. 1.1 pp), private consumption (2.5 pp vs. 2.9 pp), and inventories (-0.4 pp vs. 0.0 pp) had an opposite impact. Thus, as we expected, investments were the main source of Polish GDP growth in Q4. In our view, the sharp increase in fixed capital formation should be attributed mainly to faster increase in public investments and, to a smaller extent, to the recovery in corporate investments (see MACROpulse of 28/2/2018).
- **Polish manufacturing (PMI) dropped to 53.7 pts in February vs. 54.6 pts in January.** The indicator decreased due to lower contributions of 4 out of its 5 sub-indices (for new orders, stocks of goods purchased, output, and employment). Higher contribution of the sub-index for suppliers' delivery times had an opposite impact. Especially noteworthy in the data structure is a further increase in production backlogs despite a slower growth rate of orders (see MACROpulse of 1/3/2018. This results from the record high capacity utilization in Polish manufacturing, as signaled by numerous business surveys. The companies are trying to increase capacity utilization through increase of employment. This is shown by a continuingly high value of the employment sub-index (52.8 pts in February vs. 53.1 pts in January). In our view, the increase of employment in subsequent months will be more and more limited by the growing difficulties of companies in finding skilled labour. This will be conducive to higher corporate investments enabling to make the production technology less labour intensive and thus to increase productivity.
- **According to flash estimate, inflation in the Eurozone dropped to 1.2% YoY in February vs. 1.3% in January.** Conducive to decrease in inflation were lower dynamics of food prices. In our view, both total inflation and core inflation in the Eurozone will continue to stay at a low level (below 1.5% YoY) in the horizon of next two years. This supports our scenario, in which in June 2018 the ECB will extend the expanded asset purchase program until December 2019 reducing its scale to EUR 15bn starting from September 2018.
- **China CFLP manufacturing PMI dropped to 50.3 pts in February vs. 51.3 pts in January.** On the other hand, the Caixin PMI recorded an increase, rising to 51.6 pts in February vs. 51.5 pts in January. The index increase resulted from higher contributions of two of its five sub-indices (for new orders and stocks of goods purchased). Lower contributions of the sub-indices for employment, output, and supply delivery times) had an opposite impact. Noteworthy is the continuing sharp increase in total orders, including export orders. This supports our forecast of recovery in global trade. However, the protectionist actions initiated by D. Trump (see above) pose a substantial risk to further increase in global trade turnover.

In anticipation of recovery of investments in the energy sector

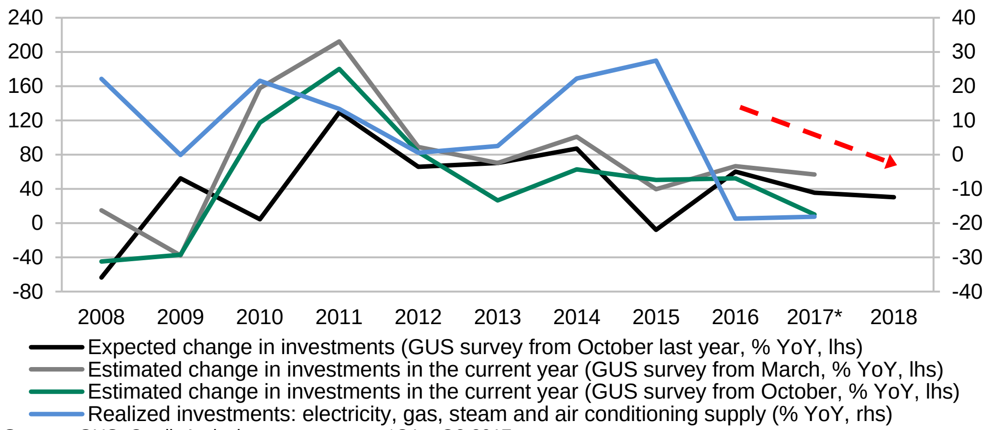
The future profile of fixed capital formation in energy sector is important from the point of view of assessing the prospects for total corporate investments. In 2006 the investments of companies employing at least 50 persons in the category "generation and supply of electricity, gas, steam, and hot water" represented 28.3% of fixed capital formation in industry and 18.2% of the expenditures of all 50+ companies. Below we present the likely profile of investments in the energy sector in 2018.

Future outlays on fixed assets in the energy sector are difficult to forecast precisely due to lack of centralized information about investment plans of companies in this sector. According to the binding laws, every two years the Energy Regulatory Office collects information about investment plans of energy suppliers in the horizon of 15 years. However, these data are not available to public. Thus, in order to estimate the future fixed capital formation of energy companies, we have used documents published by major companies of this sector (growth strategies, investment plans) and press releases. However, most companies do not provide information about specific profile of expenditures in the coming years, publishing only the aggregate value of outlays on fixed assets in the horizon of several years. Assuming, to simplify, that these expenditures will be spread evenly between the respective years, we can expect a stable flow of new investments amounting to ca. PLN 17 bn per year in most energy companies at least until 2020. This value is close to the levels observed in 2016 and 2017 (see the table).

Investments of the key players in the Polish energy industry

Company	2016	2017	Investment plans	On average (per year)
		PLN bn		
Polska Grupa Energetyczna (PGE)	7,5	n/d	34,0 (2016-2020)	6,6 (2017-2020)
Tauron	3,5	3,5	18,0 (2016-2020)	3,7 (2018-2020)
ENERGA	1,6	0,8*	20,6 (2016-2025)	2,3 (2018-2025)
ENEA	2,7	3,1*	26,4 (2018-2025)	3,3 (2018-2025)
Polskie Sieci Elektroenergetyczne (PSE)	n/d	1,5	12,3 (2018-2027)	1,2 (2018-2027)

* Q1 – Q3 2017
Source: Companies' press releases, Credit Agricole



Source: GUS, Credit Agricole *Q1 – Q3 2017

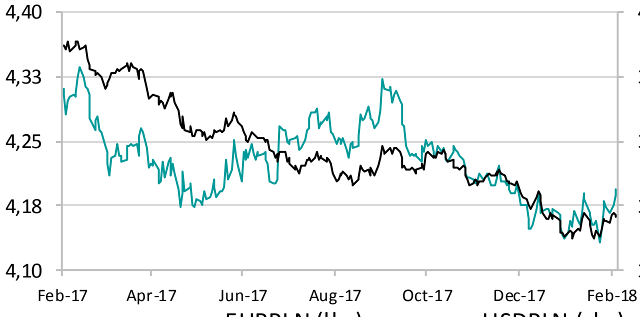
Another source of information on the expected profile of energy companies is GUS business survey. The questionnaire includes i.a. a question about the change expected by the companies in investment outlays (in the category "energy") next year compared to the current year and the value of investments completed in the current year compared to the previous year. The business sentiment indicator from the investment survey is calculated using the method of weighted average of all replies of individual companies to this question (index weighted by revenue from sale of products, goods and materials). Historically, these indicators pointed to a moderate correlation with the dynamics of investments of 50+ energy companies. Conclusions concerning the dynamics of the actually realized investments should not be drawn directly on the basis of the values of the leading and diagnosing indicators but taking into consideration their trends. According to the results of the GUS survey carried out in October 2017, the energy companies anticipate a slight decrease in the dynamics of outlays on fixed assets in 2018 as compared to 2017, which would signal a further deceleration in the investment activity of energy companies compared to 2017 – between Q1 and Q3 2017, the investments of energy companies decreased by 18.1% compared to the similar period of the previous year. Considering the above-mentioned press information (pointing to good investment sentiment) as well as low base effects, we expect the materialization of a less pessimistic scenario from the one suggested by the business surveys.

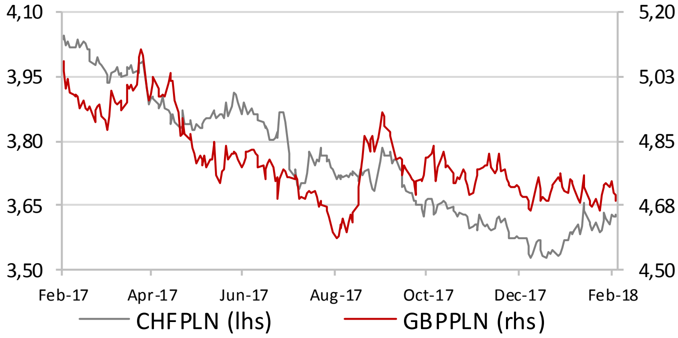
We believe that the value of energy investments in 2018 will not change substantially compared to 2017.

The stabilization of fixed capital formation of energy companies means that their dynamics will run close to zero, which will be conducive to an increase in the growth rate of investments of all 50+ companies by 2.7 pp in 2018 compared to 2017. The above-outlined scenario supports our forecast of recovery in total investments in 2018 (7.1% YoY vs. 5.2% in 2017).

Data from the US labour market negative for PLN

FX rates



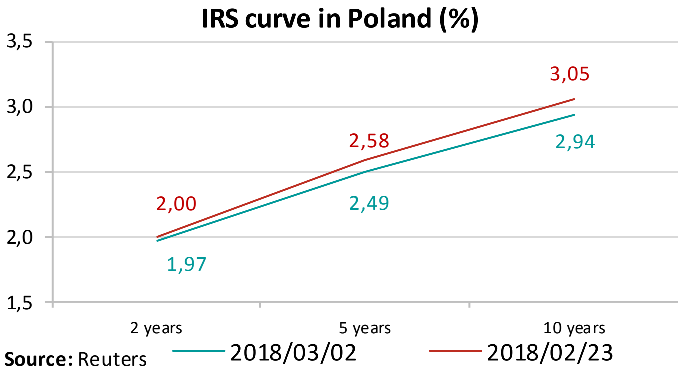


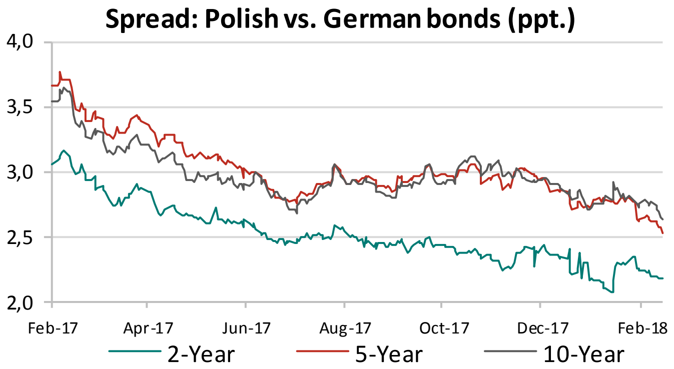
Source: Reuters

Last week EURPLN rate rose to 4.1944 (PLN weakening by 0.5%). On Monday and Tuesday PLN was relatively stable in anticipation of J. Powell's Tuesday testimony to the Congress. It was received by the market as hawkish which was conducive to PLN weakening further into the week. The depreciation of PLN was also supported by D. Trump's announcement concerning the introduction of customs duties on the US imports of steel and aluminum which increased concerns about the launch of a trade war and decreased demand for risky assets. This was reflected by higher VIX Index. Higher risk aversion supported PLN depreciation also vs. USD and CHF.

Today, PLN appreciation may be supported by the reported during the weekend SPD readiness to create a coalition in Germany with CDU/CSU. On the other hand, we believe that the results of the parliamentary elections in Italy will have a limited impact on PLN. Crucial for PLN this week will be the data on non-farm payrolls in the US. If our higher from the market consensus forecast materializes, they may result in PLN depreciation. On Thursday during the press conference after the ECB meeting, we may see an increased volatility of PLN. Data on the Chinese balance of trade will be neutral for PLN, we believe. The Wednesday's MPC meeting and the publication of the latest economic projection by the NBP will also be neutral for PLN.

IRS continue to decrease following the German debt market





Source: Reuters

Last week the 2-year IRS rates dropped to a level of 1.965 (down by 3 bp), 5-year rates to a level of 2.490 (down by 9 bp), and 10-year rates to a level of 2.940 (down by 11 bp). Last week IRS rates continued to sharply decrease across the curve following the German debt market. The decrease was not stopped by the hawkish tone of the testimony of the FED Chairman, J. Powell, to the Congress or D. Trump's announcements concerning the imposition of customs duties on the US imports of steel and aluminum.

Today, the IRS rates decline may be supported by the reported during the weekend SPD readiness to create a coalition in Germany with CDU/CSU. On the other hand we believe that the results of the parliamentary elections in Italy will be neutral for the market. This week the market will focus on the publication of the data on non-farm payrolls in the US. We believe that it may be conducive to higher IRS rates. On Thursday during the press conference after the ECB meeting we expect an increased volatility of IRS rates. The Wednesday's MPC meeting and the publication of the latest economic projection by the NBP will not be market moving.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland														
Indicator	Feb-17	Mar-17	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-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*	4,31	4,23	4,23	4,18	4,23	4,25	4,25	4,31	4,24	4,20	4,18	4,15	4,17	**4,17**
USDPLN*	4,07	3,97	3,88	3,72	3,70	3,59	3,57	3,65	3,64	3,53	3,48	3,34	3,42	**3,42**
CHFPLN*	4,05	3,96	3,90	3,84	3,86	3,72	3,72	3,77	3,65	3,59	3,57	3,59	3,62	**3,56**
CPI inflation (% YoY)	2,2	2,0	2,0	1,9	1,5	1,7	1,8	2,2	2,1	2,5	2,1	1,9	**1,6**	
Core inflation (% YoY)	0,3	0,6	0,9	0,8	0,8	0,8	0,7	1,0	0,8	0,9	0,9	**1,0**	**1,0**	
Industrial production (% YoY)	1,2	11,0	-0,5	9,3	4,4	6,3	8,9	4,3	12,4	9,2	2,8	8,6	**8,3**	
PPI inflation (% YoY)	4,5	4,8	4,2	2,4	1,8	2,2	3,0	3,2	3,0	1,8	0,3	0,2	**0,4**	
Retail sales (% YoY)	7,3	9,7	8,1	8,4	6,0	7,1	7,6	8,6	8,0	10,2	6,0	8,2	**8,0**	
Corporate sector wages (% YoY)	4,0	5,2	4,1	5,4	6,0	4,9	6,6	6,0	7,4	6,5	7,3	7,3	**7,3**	
Employment (% YoY)	4,6	4,5	4,6	4,5	4,3	4,5	4,6	4,5	4,4	4,5	4,6	3,8	**3,6**	
Unemployment rate* (%)	8,4	8,0	7,6	7,3	7,0	7,0	7,0	6,8	6,6	6,5	6,6	6,9	**6,9**	
Current account (M EUR)	-514	-405	350	-264	-892	-203	189	120	297	272	-1152	**1885**		
Exports (% YoY EUR)	6,4	19,7	3,2	19,2	7,2	13,3	11,5	10,0	15,5	14,9	2,1	**11,7**		
Imports (% YoY EUR)	10,5	19,8	4,6	21,7	14,5	13,2	7,8	7,5	14,8	15,7	10,9	**15,5**		

*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)	4,1	4,0	4,9	5,1	4,7	4,3	4,2	3,9	4,6	4,3	3,0
Private consumption (% YoY)	4,7	4,9	4,8	4,9	5,2	4,2	4,1	4,3	4,8	4,4	3,6
Gross fixed capital formation (% YoY)	-0,5	0,9	3,3	11,3	9,2	9,5	7,6	4,7	5,2	7,1	3,1
Export - constant prices (% YoY)	9,6	3,1	7,6	6,8	7,5	6,5	6,6	6,0	6,7	6,6	5,0
Import - constant prices (% YoY)	9,7	6,0	5,7	9,2	8,1	7,8	7,5	7,0	7,7	7,6	6,0
GDP growth contributions: Private consumption (pp)	2,9	2,9	2,9	2,5	3,4	2,5	2,4	2,1	2,8	2,6	2,1
GDP growth contributions: Investments (pp)	0,0	0,1	0,6	2,8	1,1	1,5	1,3	1,2	1,0	1,3	0,6
GDP growth contributions: Net exports (pp)	0,4	-1,3	1,1	-0,8	0,0	-0,4	-0,2	-0,3	-0,2	-0,2	-0,3
Current account***	0,1	-0,4	0,2	0,1	-0,1	-0,1	-0,4	-0,4	0,1	-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	0,0
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	1,8	1,9	2,0	1,3	2,0	1,7	1,8
Wibor 3M (%)**	1,73	1,73	1,73	1,72	1,72	1,72	1,72	1,72	1,72	1,72	1,97
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	4,17	4,14	4,12	4,10	4,18	4,10	4,15
USDPLN**	3,97	3,70	3,65	3,48	3,42	3,37	3,30	3,25	3,48	3,25	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 03/05/2018				
10:00	Eurozone	Services PMI (pts)	Feb	56,7	56,7	56,7
10:00	Eurozone	Final Composite PMI (pts)	Feb	57,5	57,5	57,5
10:30	Eurozone	Sentix Index (pts)	Mar	31,9		31,0
11:00	Eurozone	Retail sales (% MoM)	Jan	-1,1		0,3
16:00	USA	ISM Non-Manufacturing Index (pts)	Feb	59,9	58,9	59,0
		Tuesday 03/06/2018				
16:00	USA	Factory orders (% MoM)	Jan	1,7	1,0	-1,3
		Wednesday 03/07/2018				
11:00	Eurozone	Final GDP (% YoY)	Q4	2,7	2,7	2,7
11:00	Eurozone	Revised GDP (% QoQ)	Q4	0,6	0,6	0,6
14:15	USA	ADP employment report (k)	Feb	234		190
	Poland	**NBP rate decision (%)**	**Mar**	**1,50**	**1,50**	**1,50**
		Thursday 03/08/2018				
	China	Trade balance (bn USD)	Feb	20,3	-3,1	-5,3
8:00	Germany	New industrial orders (% MoM)	Jan	3,8		-2,1
13:45	Eurozone	EBC rate decision (%)	Mar	0,00	0,00	0,00
		Friday 03/09/2018				
2:30	China	PPI (% YoY)	Feb	4,3	3,8	3,8
2:30	China	CPI (% YoY)	Feb	1,5	2,0	2,5
8:00	Germany	Industrial production (% MoM)	Jan	-0,6		0,5
8:00	Germany	Trade balance (bn EUR)	Jan	21,4		21,0
14:30	USA	Unemployment rate (%)	Feb	4,1	4,0	4,0
14:30	USA	Non-farm payrolls (k MoM)	Feb	200	210	190
16:00	USA	Wholesale inventories (% MoM)	Jan	0,0		
16:00	USA	Wholesale sales (% MoM)	Jan	1,2		

*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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