The “Family 500+” scheme has sustainably improved consumer sentiment

This week

- **US business survey results will be released today.** We forecast that non-manufacturing ISM index rose to 55.3 pts in July vs. 55.1 pts in June, consistently with the results of regional business surveys. Thus, we will see deepening differences between the sentiment in manufacturing and in services (see below). We believe that the reading will not be market moving.
- **Data on the Chinese balance on trade will be released on Thursday.** The market expects that it decreased to USD 37.5bn in July vs. USD 51.0bn in June. According to the consensus, export dynamics dropped to -2.2% YoY in July from -1.3% in June, while import dynamics decreased to -7.6% YoY from -7.3% in June. We believe that the publication of data on the Chinese trade balance will be overshadowed by Donald Trump’s decision of last week to impose new tariffs on goods imported from China at the beginning of September (see below) and therefore will be neutral for the financial markets.

Last week

- **The most important event last week was FOMC meeting.** In accordance with our expectations and the market consensus, FED reduced the target range for federal funds by 25bp to [2.00%; 2.25%]. At the same time, FED said that it would end the reduction of its balance in August, namely two months earlier than originally announced. FED pointed to the deterioration of global economic outlook and to limited inflationary pressure in the US as the motivation for its decision. During the press conference after the meeting, the FED Chairman, J. Powell, said that the interest rates cut was the continuation of the monetary policy easing in H1 2019. He added that the cut did not mean a start of an easing cycle in the US monetary policy. Thus, the tone of the conference after the meeting was less dovish than expected which resulted in USD appreciation vs. EUR and higher yields on US bonds. The statement repeated the view that that FED would be taking adequate actions in order to sustain the economic recovery, strong labour market and ensure inflation staying close to the FED symmetric target (2%). In our view, this provision is a gateway to further monetary easing in the US. We assume in our baseline scenario that FED will cut interest rates by subsequent 25 basis points in September, anticipating further deterioration in the US, and in 2020 will make two more cuts of 25bp each. The market is now pricing in that FED will cut interest rates by further 50bp in total until the end of 2019.
- **Significant data from the US were released last week.** Non-farm payrolls in the US rose by 164 in July vs. a 193k increase in June (downwardly revised from 224k), running close to the market expectations (a 162k increase) and our forecast (165k). The highest increase in employment was recorded in education and health service (+66.0k), professional and business services (+38.0k), and financial activities (+18.0k). The highest decrease in employment was recorded in information (-10.0k), mining and logging (-5.0k), and retail trade (-3.6k). The unemployment rate did not change in July compared to June and amounted to 3.7%, staying markedly below the natural unemployment rate indicated by FOMC (4.2% - see MACROmap of 24/6/2019). The annual dynamics of average hourly earnings rose to 3.2% in July vs. 3.1% in June. Despite higher dynamics of earnings, the wage pressure in the US economy continues to be low. The results of business surveys in the US were released last week. The ISM index for manufacturing decreased to 51.2 pts in July vs. 51.7 pts in June, running below the market expectations (52.0 pts) and our forecast (51.3 pts) and hitting the lowest level since August 2016. The index decrease resulted from lower contributions of the sub-indices for suppliers’ delivery times, inventories, and new orders. A marked improvement of consumer sentiment was indicated by the Conference Board Index which rose to 135.7 pts in July vs. 124.3 pts in June, running clearly above the market

expectations equal to our forecast (125.0 pts). The index increase resulted from higher values of its sub-indices for both the assessment of the current situation and expectations. According to the statement, an important role in the improvement of consumer sentiment was played by better assessment of the current tendencies and the outlook for the US labour market. The final University of Michigan index also pointed to greater optimism of US consumers and rose to 98.4 pts in July vs. 98.2 pts in June (no change vs. the flash estimate). Its increase resulted from higher sub-index for the expectations and lower sub-index for the assessment of the current situation. The last week's readings from the US economy do not alter our forecast, in which the annualized US GDP growth rate will decrease to 2.0% in Q3 vs. 2.1% in Q2.

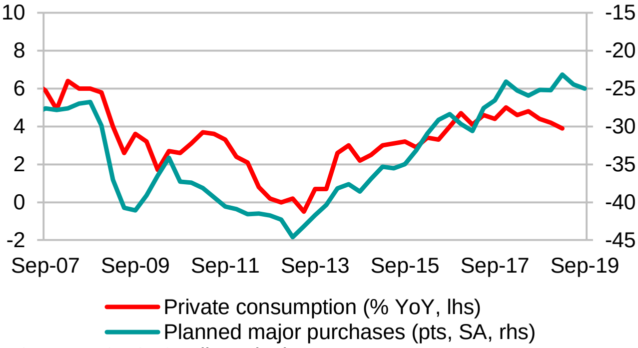
- **In accordance with the flash estimate, CPI inflation in Poland increased to 2.9% YoY in July vs. 2.6% in June, running above the market expectations (2.6%) and our forecast (2.5%).** Thus, inflation has for second month running stayed above the NBP inflation target (2.5% ± 1 percentage point). At the same time, it has reached the highest level since October 2012. GUS published partial data on the inflation structure with information on the rate of inflation in the categories "food and non-alcoholic beverages", "energy", and "fuels". The increase in inflation resulted from higher dynamics of the prices of food and non-alcoholic beverages (6.8% YoY in July vs. 5.7% in June – most likely due to higher dynamic of the prices of fruit and vegetables) and core inflation, which, according to our estimates, rose to 2.1% YoY in July vs. 1.9% in June. Lower dynamics of the prices of fuels (0.7% YoY in July vs. 3.0% in June) and energy (-1.0% YoY in July vs. -0.9% in June) had an opposite impact. The flash data on inflation pose a substantial upside risk to our forecast, in which inflation will not change in Q3 compared to Q2 and will amount to 2.4% YoY and in the whole 2019 it will increase to 2.1% YoY vs. 1.6% in 2018. The final data on inflation will be released on 14th August.
- **PMI index for Polish manufacturing dropped to 47.4 pts in July vs 48.4 pts in June, running below our forecast equal to the market consensus (48.0 pts) and hitting the lowest level since April 2013.** Thus, the index has now for nine months in a row been running below the 50 pts threshold dividing expansion from contraction of activity. The index decrease resulted from lower contributions of three of its five sub-indices (employment, stocks of goods purchases and suppliers' delivery times). Higher contribution of the sub-indices for output and for new orders had an opposite impact. In recent months we have observed continuing resilience of Polish manufacturing to the slowdown of manufacturing activity in the Eurozone. However, we believe that July may have been a breakthrough month in this respect and the weakening of external demand will be more pronounced in the July data than in previous months (see MACROpulse of 1/8/2019). The reading does not alter our forecast of GDP increase in the whole 2019 (4.4% YoY vs 5.1% in 2018.).
- **According to the flash estimate, the quarterly GDP dynamics in the Eurozone decreased to 0.2% in Q2 vs. 0.4% in Q1 (1.1% YoY in Q2 vs. 1.2% in Q1), running in line with the market expectations and below our forecast (0.3%).** Last week we also saw flash GDP estimates for several Eurozone economies, i.a. in France (0.2% QoQ in Q2 vs. 0.3% in Q1), Spain (0.6% in Q2 vs. 0.7% in Q1), and Italy (0.0% in Q2 vs. 0.1% in Q1). The GDP reading is a flash estimate and does not include its structure. Subsequent GDP estimate for the Eurozone in Q2, including the growth rate for all the countries of the single currency area, will be released on 14th August and full data on its structure on 6th September.
- **According to the flash estimate, inflation in the Eurozone dropped to 1.1% YoY in July vs. 1.3% in June, running in line with the market expectations and above our forecast (1.0%).** The decrease in inflation resulted from lower dynamics of prices of energy (0.6% YoY in July vs. 1.7% in June) and services (1.1% in July vs. 1.6% in June), while higher dynamics of food prices (2.0% YoY in July vs. 1.6% in June) had an opposite impact. We expect that in subsequent quarters inflation will be showing a downward trend and will reach its local minimum of 0.7% YoY in October. It will then slightly increase but will not exceed a level of 1.3% YoY in the entire horizon of our forecast (i.e. until the end of 2020). We expect that core inflation will also not

exceed the level of 1.3% YoY in the entire forecast horizon. This supports our scenario, in which the ECB will cut the deposit rate by 10bp to -0.50% in September, while introducing a tiered rate for commercial banks deposits at the central bank. In addition, the ECB will then decide to launch a subsequent round of quantitative easing (QE2) with the monthly purchase scale amounting to EUR 50bn. In our view, the program will be launched at the beginning of 2020 and will last 18 months.

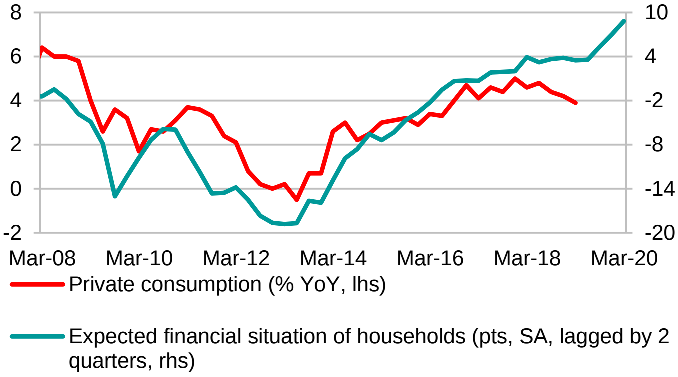
- **Caixin PMI index for Chinese manufacturing rose to 49.9 pts in July vs. 49.4 pts in June, running above the market expectations (49.6 pts) and our forecast (49.8 pts).** Nevertheless, it has been the second month in a row when the index is below the 50 pts threshold dividing expansion from contraction of activity. The index increase resulted from higher contributions of two of its five sub-indices (for new orders and output) while lower contributions of the sub-indices for employment, inventories, and suppliers' delivery times had an opposite impact. Especially noteworthy in the data structure is the increase in the sub-index for total new orders, including export orders. The sub-index for total new orders rose much sharper than the sub-index for export orders, suggesting that the source for its increase was mainly the improvement of internal demand. This may signal the first effects of the measures taken by the Chinese government to stimulate internal demand. The CFLP PMI index for manufacturing also recorded an increase and rose to 49.7 pts in July vs. 49.4 pts in June. The last week's data support our forecast of economic growth in China (6.4% in 2019 and 6.0% in 2020). However, to achieve such GDP dynamics, the scale of the growth stimulus implemented by the Chinese government will have to increase. We believe that to this end measures will be taken to increase lending (stopping the process of deleveraging banks, reduction of interest rates) and depreciate CNY in line with the deterioration of the Chinese trade balance. The fiscal policy will also have to be more expansionary. Our forecast is also not altered by the latest remark of the US President D. Trump who expressing his dissatisfaction with the progress of US-China negotiations announced the introduction of increased tariffs of 10% on the remaining goods imported from China (worth USD 300bn) from September 2019. In reaction to D. Trump's decision, the Chinese government called on the state-owned enterprises to suspend the imports of agricultural and food products from the US and allowed the USDCNY exchange rate to hit the highest level since March 2008. In our baseline scenario we were assuming further escalation of the trade war between those countries (MACROmap of 1/7/2019).

The "Family 500+" scheme has sustainably improved consumer sentiment

A gradual improvement of households' sentiment can be observed since 2013. In June 2019, the Current Consumer Confidence Index (BWUK) and the Leading Consumer Sentiment Index (WWUK) reached the highest levels in the survey history. In July 2019 consumer sentiment slightly deteriorated but the WWUK and BWUK readings remained at high levels. The profile of sentiment indicators is relevant to the assessment of consumption trends as they show high correlation with the annual real dynamics of private consumption. An even greater dependence of consumption growth on sentiment is observed for two of the WWUK sub-indices: "change in households' financial standing – 12-month forecast" and "major purchases – 12-month forecast" (see the chart). One of the factors frequently quoted as the reason for the marked improvement of households' sentiment in recent years is the payment of social transfers by the government ("Family 500+" and "Good Start" schemes and so-called 13th pension). Below we are trying to answer the question whether the government schemes have really improved the sentiment and sped up consumption.

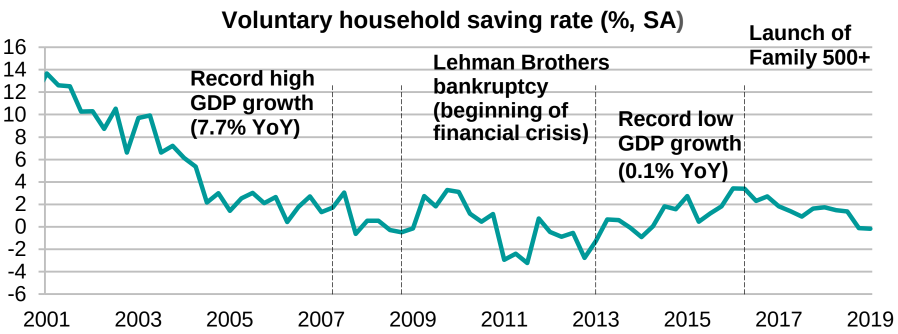


Source: GUS, Credit Agricole



To this end we have built two econometric models. Each explains the changes in one of the consumer sentiment indicators presented in the chart. The explanatory variables in both models are the unemployment rate and real wage fund growth rate (employment multiplied by wages) in the corporate sector. In addition, we have used two binary variables to test the impact of social schemes on household sentiment. One of them takes on the value “1” in every month since the launch of the “Family 500+” scheme in 2016. The second variable takes on the value “1” in the months in which the government was announcing the launch of the “Family 500+” scheme in 2015, the launch of the “Good Start” scheme in 2018, and announced the fiscal package this year.

In accordance with the results of the econometric modelling, the improvement of household sentiment is positively impacted by lower unemployment rate and faster wage fund growth. It should be emphasized that the marked decrease in unemployment rate was the factor which has contributed the most to the improvement of sentiment since 2013. In addition, the parameter next to the binary variable, which represents the period of the “Family 500+” scheme’s functioning, was also positive and statistically relevant. In turn, the announcements of the schemes’ launch have a positive but statistically irrelevant impact on the household sentiment. Considering the correlation between the aforementioned sentiment indicators and real consumption dynamics, the results of modelling indicate that the launch of the “Family 500+” in 2016 has sustainably boosted the growth rate of private consumption by ca. 1.1-1.2 percentage points. It should be noted that this estimate is sensitive to assumptions relating to the horizon of the scheme’s impact on the dynamics of consumption after its launch. Under the assumption of a shorter impact period the estimated impact would be bigger.



Source:Eurostat, Credit Agricole

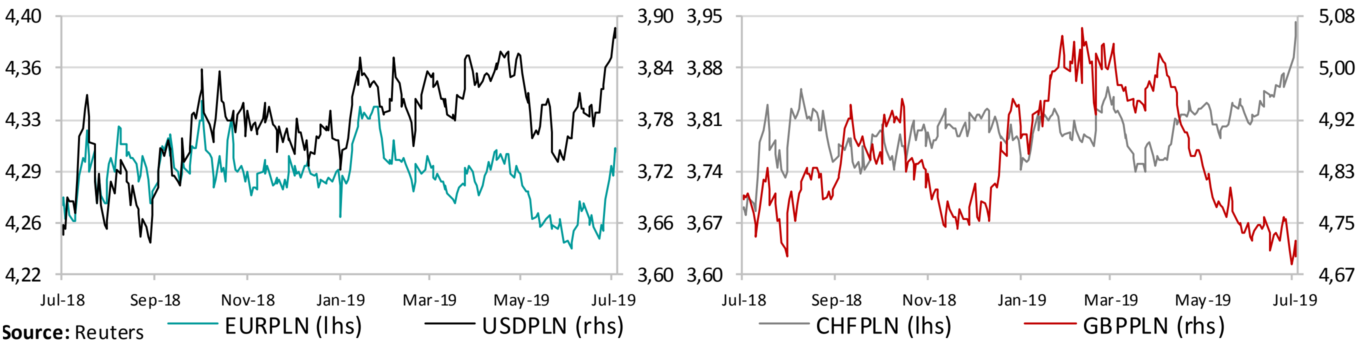
The functioning of social schemes is also important from the point of view of their impact on household savings. In accordance with the national accounts statistics, gross household savings constitute an excess of disposable income over consumer spending. The savings rate is savings divided by disposable income. The 2013-2015 period recorded an increase in the voluntary savings rate. In our view, the marked improvement in the labour market in that period was inclining consumers to rebuild the savings buffer, which had diminished in the downturn period. In accordance with the permanent income theory, a sustainable increase in household income (e.g. due to permanent monthly social transfers) will be conducive to an increase in current consumption and lower savings rate. With the launch of the “Family 500+” scheme, a decrease in the voluntary savings rate has been visible, which would be consistent with the permanent income theory.

However, we have not succeeded in building an econometric model that would clearly confirm a statistically relevant negative impact of the scheme's launch on the savings rate. In accordance with the results of econometric modelling this effect was negligible. Such result can be explained as follows. Probably a sizeable part of the scheme beneficiaries (namely poorer families), despite an increase in disposable income, continued to consume its dominant part (nearly 100%), which enabled them to improve the standard of living. Consequently, their savings rate has not visibly changed. Of much bigger significance for lower propensity to save was the decrease in real interest rates recorded in that period.

Strong labour market, payment of social transfers positively impacting household sentiment support our scenario assuming a sustainable fast increase in consumption in the coming quarters (4.3% in 2019 vs. 4.5% in 2018).

USD appreciation after FOMC meeting

FX rates



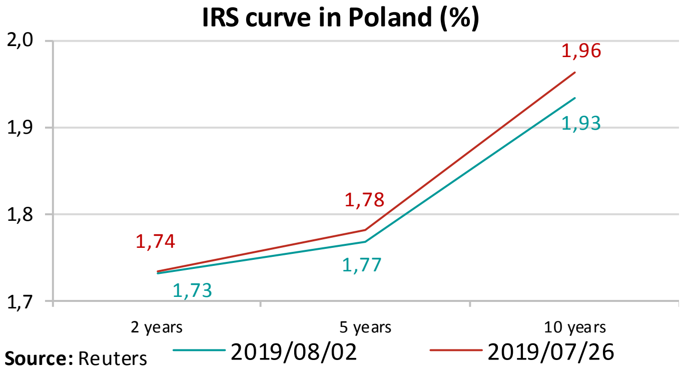
Source: Reuters

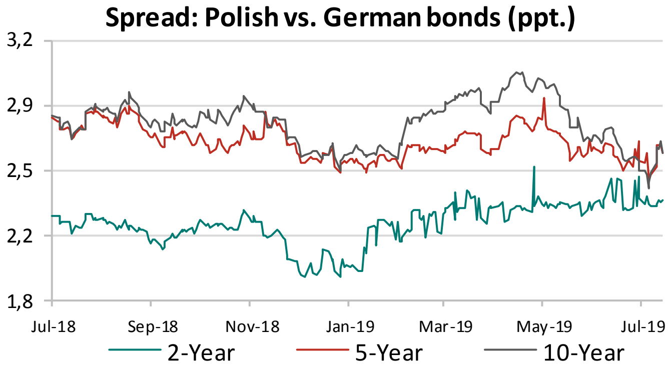
Last week, the EURPLN exchange rate rose to 4.3052 (PLN weakening by 0.8%). At the beginning of the week, PLN and other currencies of the region were slightly depreciating. This was the continuation of the trend from two weeks ago, related to the publication of better-than-expected data from the US economy (see MACROmap of 28/7/2019). Wednesday saw PLN strengthening supported by the publication of flash estimate of domestic inflation that was higher from the consensus. The tone of the conference after the FOMC meeting proved to be less dovish than expected, which was conducive to smaller demand for the Polish debt and PLN weakening. Friday saw a slight correction and PLN strengthening. The Friday's data from the US labour market had a limited impact on PLN.

Last week also saw USD appreciation vs. EUR in reaction to the aforementioned less dovish that expected tone of the conference after the FOMC meeting. D. Trump's announcement of the imposition of increased tariffs on the remaining goods imported from China resulted in EUR partly making up for the losses. Noteworthy is also the EUR depreciation vs. CHF continuing in recent weeks due to the investors' expectations of monetary easing by the ECB. Consequently, last week, CHFPLN exceeded 3.94, reaching the highest value since April 2017.

The data on the Chinese trade balance may be important for PLN this week. In our view, they will not have a significant impact on PLN. The publication of non-manufacturing ISM in the US is also likely to be neutral for PLN. We believe that due to the scarce macroeconomic calendar, PLN this week will be mostly impacted by global market sentiment determined by investors' expectations concerning the development of the trade conflict between the US and China.

Domestic data on inflation boosted IRS rates





Source: Reuters

Last week, 2-year IRS rates decreased to 1.73 (down by 1bp), 5-year rates to 1.77 (down by 1bp), and 10-year rates to 1.93 (down by 3bp). Monday through Friday saw an increase in IRS rates across the curve, supported by the publication of higher-than-the-consensus domestic data on inflation as well as the less-dovish-than-expected tone of the press conference after the FOMC meeting. On Friday there was a correction due to D. Trump's announcement of the imposition of increased tariffs on the remaining goods imported from China. In reaction to further escalation of the US-China trade war, yields on German bonds also decreased across the curve. Simultaneously, for the first time in history, the curve in the section of up to 30 years inclusive was below zero. The Friday's data from the US labour market has a limited impact on the curve.

We expect that due to the scarce macroeconomic calendar, IRS rates will be impacted this week by global market sentiment determined by investors' expectations concerning the development of the trade conflict between the US and China. The publication of non-manufacturing ISM in the US scheduled for today will be neutral for the curve, we believe.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19
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*	4,27	4,30	4,28	4,34	4,29	4,29	4,26	4,30	4,30	4,28	4,28	4,24	4,29	**4,28**
USDPLN*	3,66	3,71	3,69	3,84	3,79	3,74	3,72	3,79	3,84	3,82	3,83	3,73	3,87	**3,85**
CHFPLN*	3,69	3,83	3,75	3,80	3,79	3,81	3,74	3,79	3,85	3,75	3,83	3,82	3,90	**3,82**
CPI inflation (% YoY)	2,0	2,0	1,9	1,8	1,3	1,1	0,7	1,2	1,7	2,2	2,4	2,6	**2,5**	
Core inflation (% YoY)	0,6	0,9	0,8	0,9	0,7	0,6	0,8	1,0	1,4	1,7	1,7	1,9	**2,1**	
Industrial production (% YoY)	10,3	5,0	2,7	7,4	4,6	2,8	6,0	6,9	5,5	9,2	7,6	-2,7	**7,5**	
PPI inflation (% YoY)	3,4	3,0	3,0	3,2	2,8	2,1	2,2	2,9	2,5	2,6	1,4	0,6	**0,4**	
Retail sales (% YoY)	9,3	9,0	5,6	9,7	8,2	4,7	6,6	6,5	3,1	13,6	7,3	5,3	**8,0**	
Corporate sector wages (% YoY)	7,2	6,8	6,7	7,6	7,7	6,1	7,5	7,6	5,7	7,1	7,7	5,3	**7,1**	
Employment (% YoY)	3,5	3,4	3,2	3,2	3,0	2,8	2,9	2,9	3,0	2,9	2,7	2,8	**2,7**	
Unemployment rate* (%)	5,8	5,8	5,7	5,7	5,7	5,8	6,1	6,1	5,9	5,6	5,4	5,3	**5,3**	
Current account (M EUR)	-754	-1005	-876	-405	343	-1126	2438	-718	116	720	1006	**-197**		
Exports (% YoY EUR)	12,0	8,9	-1,5	13,2	8,1	1,7	5,4	9,9	7,8	10,1	13,3	**-1,1**		
Imports (% YoY EUR)	12,4	14,0	4,2	18,1	9,2	2,2	1,6	7,8	2,6	8,5	11,2	**-0,5**		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

Indicator		2019				2020				2018	2019	2020
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)		4,7	4,5	4,4	4,2	4,2	3,9	3,7	3,5	5,1	4,4	3,8
Private consumption (% YoY)		3,9	5,0	4,5	4,0	3,7	3,6	3,5	3,4	4,5	4,3	3,6
Gross fixed capital formation (% YoY)		12,6	8,9	8,1	6,9	4,8	4,9	5,2	4,8	8,7	8,5	4,9
Export - constant prices (% YoY)		5,9	6,0	5,0	4,9	5,0	5,2	5,2	5,0	6,3	5,4	5,1
Import - constant prices (% YoY)		5,0	6,2	7,5	7,2	6,9	6,7	6,2	6,3	7,1	6,5	6,5
GDP growth contributions	Private consumption (pp)	2,4	2,9	2,7	2,0	2,3	2,1	2,1	1,7	2,6	2,5	2,1
	Investments (pp)	1,6	1,4	1,4	1,7	0,6	0,8	1,0	1,2	1,5	1,5	0,9
	Net exports (pp)	0,7	0,2	-1,1	-1,0	-0,8	-0,6	-0,4	-0,6	-0,2	-0,4	-0,6
Current account (% of GDP)***		-0,4	-0,1	-0,3	-0,4	-0,5	-0,6	-0,8	-0,8	-0,7	-0,4	-0,8
Unemployment rate (%)**		5,9	5,3	5,4	5,7	5,8	5,1	5,3	5,6	5,8	5,7	5,6
Non-agricultural employment (% YoY)		0,0	0,2	0,2	0,1	0,1	0,1	0,1	0,1	0,9	0,1	0,1
Wages in national economy (% YoY)		7,1	7,6	7,8	7,7	7,7	7,7	7,3	7,1	7,2	7,6	7,5
CPI Inflation (% YoY)*		1,2	2,4	2,4	2,4	2,9	1,9	1,8	1,6	1,6	2,1	2,0
Wibor 3M (%)**		1,72	1,72	1,72	1,72	1,72	1,72	1,72	1,72	1,72	1,72	1,72
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**		4,30	4,24	4,28	4,28	4,28	4,28	4,25	4,23	4,29	4,28	4,23
USDPLN**		3,84	3,73	3,82	3,75	3,69	3,63	3,54	3,50	3,74	3,75	3,50

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST*	
					CA	CONSENSUS**
		Monday 08/05/2019				
10:00	Eurozone	Services PMI (pts)	Jul	53,3	53,3	53,3
10:00	Eurozone	Final Composite PMI (pts)	Jul	51,5	51,5	51,5
10:30	Eurozone	Sentix Index (pts)	Aug	-5,8		-7,7
16:00	USA	ISM Non-Manufacturing Index (pts)	Jul	55,1	55,3	55,5
		Tuesday 08/06/2019				
8:00	Germany	New industrial orders (% MoM)	Jun	-2,2		0,4
		Wednesday 08/07/2019				
8:00	Germany	Industrial production (% MoM)	Jun	0,3		-0,6
		Thursday 08/08/2019				
14:30	USA	Initial jobless claims (k)	w/e	215		215
16:00	USA	Wholesale inventories (% MoM)	Jun	0,2		0,2
16:00	USA	Wholesale sales (% MoM)	Jun	0,1		0,2
	China	Trade balance (bn USD)	Jul	51,0		37,5
		Friday 08/09/2019				
3:30	China	PPI (% YoY)	Jul	0,0		-0,1
3:30	China	CPI (% YoY)	Jul	2,7		2,7
8:00	Germany	Trade balance (bn EUR)	Jun	18,7		18,4

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

MACRO MAP

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