Low-interest loan scheme is not enough

This week

- **The most important event this week will be the FOMC meeting scheduled for Wednesday.** We expect that after the rate hike in December 2018, the Federal Reserve will maintain status quo in monetary policy this week – the target range for the Federal Reserve funds equals to [2.25%; 2.50%]. The markets will focus on possible changes in the statement's tone and the FED chairman's bias, reflecting the slowdown in global trade and the government shutdown taking place in the last few weeks on the US macroeconomic outlook. We believe that they will not provide any new information altering our scenario assuming two interest rate hikes in the US by 50bp in total in 2019. In our view, the publication of the statement and the press conference after the FOMC meeting will be neutral for the financial markets.
- **The readings of US data are scheduled for this week but some of them may be postponed due to the government shutdown taking place in the last few weeks**. We expect the non-farm payrolls to have increased by 185k in January vs. 312k in December 2018, with unemployment rate up to 4.0% from 3.9% in December. In accordance with the survey methodology, the temporary suspension of the federal government will only be conducive to higher unemployment rate without impacting the estimate of the payrolls. Smaller increase in employment will mainly result from the high base effect from the month before (the increase in the number of jobs in December was the sharpest since February 2018). 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 178k in January vs. 271k in December). The flash estimate of GDP in Q4 is scheduled to be released on Wednesday. We expect that the annualized economic growth rate will decrease to 2.7% vs. 3.4% in Q3, due to lower contributions of investments and net exports. Higher contributions of change in inventories and consumption will have an opposite impact. We forecast that the ISM index for manufacturing dropped to 53.4 pts in January vs. 54.1 pts in December, running in line with the regional business surveys. We expect that the Conference Board Consumer Confidence Index (126.0 pts vs. 128.1 pts in December), like the final University of Michigan Index (90.0 pts vs. 98.3 percentage points), will signal deterioration of households' sentiment in January. We believe that the US readings should not be market moving.
- **Important data from the Eurozone will be released this week.** We expect that the quarterly GDP dynamics rose to 0.3% in Q4 from 0.2% in Q3. The results of business surveys (PMI) for October-December period pose a downside risk to our forecast. In addition, we forecast that HICP inflation decreased to 1.3% in January vs. 1.6% in December. Higher core inflation has only partially offset lower dynamics of energy prices. We believe that the materialization of our forecast of GDP in the Eurozone that is higher from the consensus (0.2%) will be conducive to the depreciation of PLN and higher yields on Polish bonds, while the inflation reading is not likely to be market moving.
- **The January PMIs for Chinese manufacturing (Caixin and CFLP) will be released this week**. The market expects that CFLP decreased to 49.3 pts vs. 49.4 pts in December. In accordance with the market consensus, the Caixin PMI is also expected to decrease to 49.5 pts in January vs. 49.7 pts in December. The readings will be relevant to assessing the impact of the slowdown in global trade on the economic situation in China. We believe that the January business survey results will not reflect yet the stimulus measures of the Chinese government and the People's Bank of China.
- **The estimate of GDP in Poland for 2018 will be released on Thursday.** We expect that the economic growth rate amounted to 5.0% YoY vs. 4.8% in Q4 2017. Data for 2018 will allow to estimate the growth rate of investments and GDP in Q4 2018. We expect that the data will point to a slower growth of these two indicators, which will be conducive to a slight depreciation of PLN and lower yields on Polish bonds.

- **Data on business sentiment in Polish manufacturing will be released on Friday.** We expect that PMI rose to 48.0 pts from 47.6 pts in December, mainly due to the low base effect from the month before. On the other hand, the scale of the recovery in Polish manufacturing was limited by the downturn in Germany (see below). Our forecast is close to the consensus; therefore, its materialization will be neutral for PLN and yield on Polish bonds.

Last week

- **The ECB meeting was held last week.** The statement after the meeting continued to include the provision that the ECB expected "interest rates to remain at their present levels at least through the summer of 2019, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to levels below, but close to, 2% over the medium term" (so called forward guidance). In the statement after the meeting, the ECB presented the view that the balance of risks currently surrounding the euro area growth outlook has moved to the downside. In the statement after the December meeting, the ECB had believed those risks to be roughly balanced. During the press conference, among downside risks to the Eurozone growth, M. Draghi indicated i.a. uncertainty around Brexit, protectionism in global trade, slowdown in China, and downturn in the German automotive industry. However, M. Draghi's remarks after the meeting suggest that the ECB sees the current slowdown as temporary. Consequently, the ECB view on economic outlook for the Eurozone remains relatively optimistic. In our view, crucial for the ECB bias will be the March macroeconomic projection, in which the ECB will have to confront the question whether the slowdown observed currently in the global economy is really temporary. We see a downside risk to our scenario, in which the ECB will hike the deposit rate in total by 40 bp in H2 2019 and the main rate by 25 bp in Q4 2019, the market is currently pricing in the first interest rate hike in Q2 2020.
- **In accordance with preliminary data, PMI Composite (for manufacturing and services) in the Eurozone dropped to 50.7 pts in January vs. 51.1 pts in December, running below the market expectations (51.4 pts) and our forecast (51.7 pts).** The index decline resulted from lower values of its sub-indices for output in manufacturing and business activity in services. Geographically, slower growth rate of economic activity was recorded both in Germany and in France. The deterioration of sentiment in Germany resulted from increase in the sub-index for business activity in services and decrease in the sub-index for output in manufacturing. Whereas in France, it resulted from decrease in the sub-index for business activity in services while increase in the sub-index for output in manufacturing had an opposite impact. In accordance with the press release, the source of lower activity in the French services sector was the strike of "yellow vests" in this country. Deterioration of sentiment was also recorded in other Eurozone countries covered by the survey. From the point of view of Polish exports especially noteworthy in the data is the decline in PMI for German manufacturing to 49.9 pts in January vs. 51.5 pts in December. It thus stood below the 50 pts threshold diving expansion from contraction of activity for the first time since November 2014. Conducive to the index decline were lower contributions of four of its five sub-indices (for output, new orders, suppliers' delivery times, and employment), while higher contribution of the inventories sub-index had an opposite impact. Worth noting is a sharper decrease in total orders from export orders. This shows that the main reason for lower orders in German manufacturing in January was weaker internal demand. Both Germany and the whole Eurozone have also recorded an increase in stocks of finished products. This signals that the slowdown of demand surprised the Eurozone manufacturing. We believe that the stagnation in the Eurozone economy may continue for several months before we will see the results of the stimulation of economic growth in China (see MACROmap of 7/1/2019). The business survey results pose a significant downside risk to our forecast, in which the quarterly GDP dynamics in the Eurozone will

increase to 0.5% in Q1 2019 vs. 0.3% in Q4.

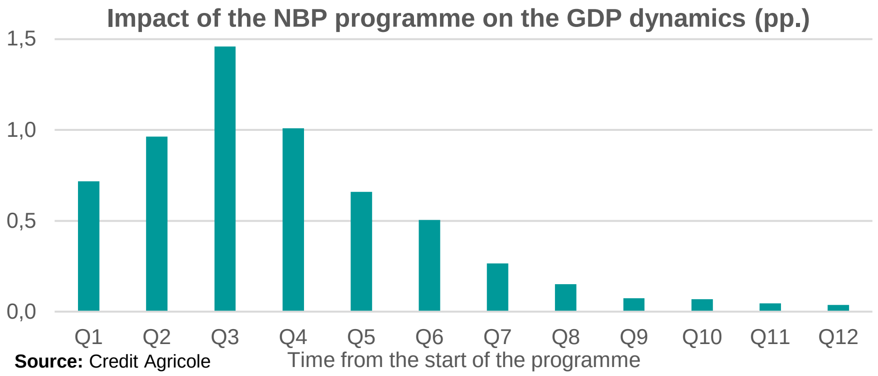
- **ZEW index reflecting the sentiment among analysts and institutional investors regarding the economic situation in Germany rose to -15.0 pts in January vs. -17.5 pts in December.** The index recorded slight improvement in January despite further deterioration of economic outlook for Germany, slower GDP growth in China, and rejection of draft Brexit deal by the British parliament. In accordance with the press release, these developments were expected by the survey participants, therefore their impact on sentiment was limited. Ifo Index reflecting the sentiment among German managers representing the manufacturing, construction, wholesale and retail trade sectors, was also released week and decreased to 99.1 pts in January vs. 101.0 pts in December. The index decrease resulted from lower sub-indices concerning both the assessment of the current situation and expectations. Sector-wise, deterioration of sentiment was recorded in all its four sectors (manufacturing, construction, trade, and services). The data pose a downside risk to our forecast, in which the quarterly GDP growth rate in Germany will increase to 0.5% in Q1 2019 vs. 0.1% in Q4 2018.
- **Retail sales dynamics in Poland decreased in current prices to 4.7% YoY in December vs. an 8.2% increase in November, running significantly below the market expectations (7.7%).** The sales growth rate in constant prices dropped to 3.9% YoY in December vs. 7.8% in November. The deceleration in retail sales growth in December was wide ranging – seven of the nine categories recorded a decrease in annual dynamics compared to December. The decrease in retail sales dynamics may result from the abatement of the effect of early Christmas shopping done in November (see MACROpulse of 22/1/2019). In the whole Q4 2018 retail sales in constant prices rose by 6.2% vs. a 5.6% increase in Q3, posing a slight upside risk to our forecast, in which private consumption growth rate dropped to 4.4% YoY in Q4 vs. 4.5% YoY in Q3. The slowdown in retail sales growth in December, combined with the deterioration in retail sales recorded in January 2019 (synthetic indicator has dropped to the lowest level since December 2016), is consistent with our scenario assuming a gradual decrease in the consumption dynamics in the coming quarters of 2019.
- **The publication of US data (existing home sales and preliminary durable goods orders) was scheduled for last week**. However, the data were not released due to the government shutdown in the US, namely the suspension of the functioning of the federal government, resulting from no adoption of the budget for 2019. The reason the budget was not adopted is the conflict between the US President and the politicians of the Democratic Party in the Congress regarding the financing of the wall along the US border with Mexico. Last week D. Trump and the Congress reached an agreement on a temporary reopening of the federal government until 15 February. An agreement on the financing of the wall is supposed to be reached in that time. The decision on the temporary opening of the federal government is positive for USD. We estimate that the government shutdown has so far decreased the US GDP growth rate in Q1 by ca, 0.6pp. Consequently, we expect that the annualized US GDP growth rate will decrease to 1.4% in Q1 2019 vs. 2.7% in 2018.

Low-interest loan scheme is not enough

Last week we presented a report on the possibility of the NBP launching a program of low-interest credits for the sector of small and medium size enterprises (SME) to stimulate the economy amid significant slowdown of GDP. Below we analyze what should be the scale of this program to effectively stimulate economic growth in Poland.

For the purpose of the analysis we assume an alternative scenario in which the expected by us recovery of global economic growth does not take place and consequently GDP dynamics in Poland significantly and sustainably decrease to 2.0% YoY. We assume that in such situation the NBP's objective would be to stimulate economic growth to its potential level estimated at ca. 3% YoY. That is why, in order to assess the necessary scale of the scheme, we are working on the assumption that during the first year of its life it is supposed to boost the economic growth rate by 1 percentage point on a yearly average.

Our simulation assumes that the funds offered by the NBP to commercial banks will be allocated in full for new investment loans for SME. Companies will not benefit under the scheme from working capital loans and will not use cheaper financing to repay existing obligations. This means that the amount of the NBP scheme can be considered equal to the value of new corporate investments. We also assume that the scheme will operate for a year and that the same value of new loans for SME will be granted in each of the four quarters.



Source: Credit Agricole

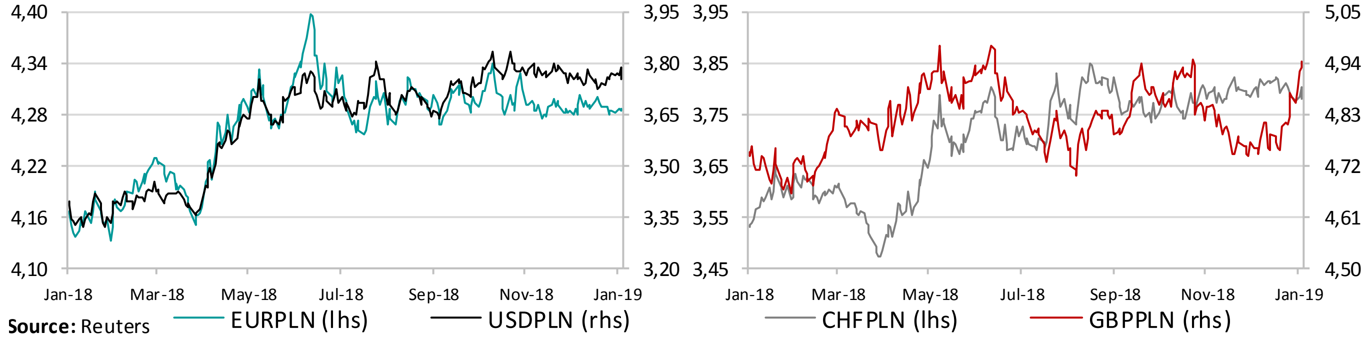
Considering the above simulation parameters and based on our quarterly forecasting model, we estimate that PLN 10bn of new loans would have to be granted in each quarter (in total PLN 40bn, 1.9% of GDP). Due to delays of economic processes, the transmission of such shock on GDP growth would not be constant over time. This impact would be increasing in the first three quarters of the scheme functioning (to 1.5 pp in Q3) and would then gradually decrease (see the chart). It should be pointed out that the scheme's positive impact on the rate of economic growth would not abate straight after its termination. The results of econometric modelling show that in the second year the GDP dynamics would be higher by 0.4 pp compared to a scenario whereby the NBP would not decide to ease the monetary policy and higher by 0.06 pp in the third year after the launch of the scheme.

However, we should bear in mind that the above-indicated scale of the program (PLN 40bn) would bring the expected results only if SME show such demand for bank loans. In the previous MACROmap we signaled that this would have been the main obstacle in the program implementation in Poland. In addition to the quoted structural characteristics of Polish companies (i.a. low propensity to finance investments with loans in favour of using own funds), the large scale of the scheme compared to the selected macroeconomic indicators would also be a problem. Full absorption of the NBP-offered funds would mean that total corporate investments would increase by 19.6% YoY in the first year of the scheme operation and SME gross capital formation by 42.7% YoY. The launch of the program would substantially increase the volume of loans for SME (by 19.3% YoY) and companies overall (by 10.7%). Such growth rates have been rare in Poland's modern economic history and were recorded in the conditions of very fast economic growth (2006-2007, 2011). In our view, the likelihood that SME will decide to implement new investments at such a scale amid strong global economic slowdown and low growth of domestic demand is limited. In addition, the companies would most probably first use the cheap financing to repay the existing obligations (to reduce their service costs), instead of launching new investment projects.

Considering the above constraints, we believe that the NBP would be unable to stimulate economic growth in Poland at the assumed scale (i.e. by 1 pp on a yearly average) only with the use of low-interest loan scheme. This means that the central bank would have to decide to simultaneously launch other unconventional tools of monetary policy. In the next MACROmap we will present an analysis of subsequent instruments in the potential arsenal of the NBP.

Data on GDP in the Eurozone may weaken PLN

FX rates



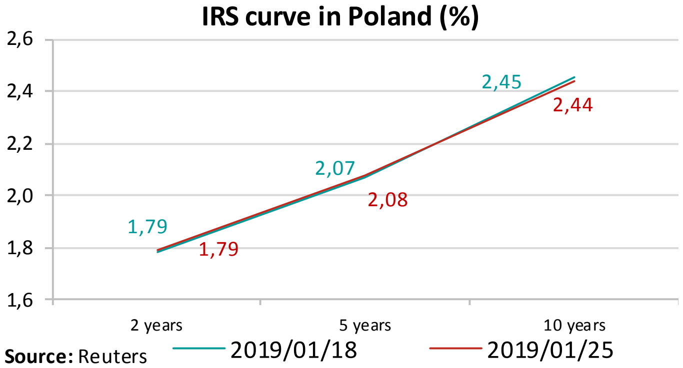
Source: Reuters

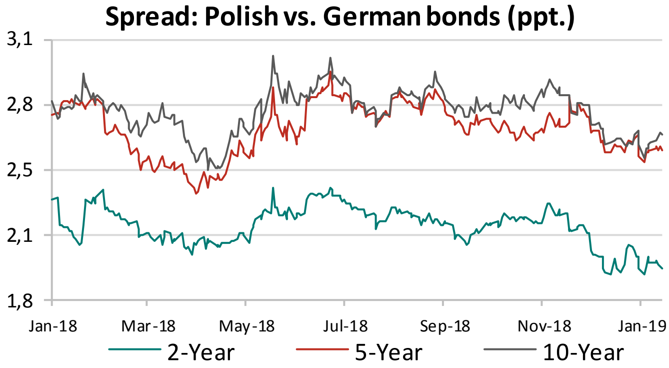
Last week, the EURPLN exchange rate amounted to 4.2863 (no change compared to the level from two weeks ago). Throughout last week EURPLN showed low volatility and ranged between 4.18 and 4.20. The publication of weaker-than-expected business survey results in the Eurozone as well as the conference after the ECB meeting had a limited impact on the market.

Especially noteworthy is the last week's decrease in EURGBP. The strengthening of GBP was supported by increased investors' expectations of the UK managing to avoid a hard Brexit scenario. The scale of last week's appreciation of PLN vs. EUR was smaller from EUR depreciation vs. GBP and consequently PLN depreciated vs. GBP by 1.6%. Friday also recorded USD weakening vs. EUR due to rumours that FED would soon stop decreasing its balance-sheet by gradually limiting the reinvesting of proceeds from maturing assets. However, USD depreciated after the closing of the Polish market.

This week the market will focus on data on GDP in the Eurozone. If our forecast that is higher from the market consensus materializes, the data may be slightly negative for PLN. Domestic data on GDP may also contribute to a slight weakening of PLN. On the other hand, Poland manufacturing PMI will not have any substantial impact on PLN, we believe. In our view, preliminary data on inflation in the Eurozone, US data (non-farm payrolls, Conference Board Index and final University of Michigan Index) as well as FED meeting will be neutral for PLN, we believe. The US GDP reading, if published, will also not be market moving. In addition, the beginning of this week may see USD strengthening vs. EUR, due to temporary reopening of the federal government in the US.

FED meeting neutral for IRS rates





Source: Reuters

Last week, 2-year IRS rates have not changed compared to the level from two weeks ago and amounted to 1.79, 5-year rates increased to 2.08 (up by 1bp), and 10-year rates decreased to 2.44 (down by 1bp). The whole of last week saw the stabilization of IRS rates across the curve. The publication of weaker-than-expected business survey results for the Eurozone and the conference after the ECB meeting had a limited impact on the curve. On Friday there were debt auctions (main and supplementary) at which the Finance Ministry sold PLN 8.5bn of 2-, 5-, 9-, and 28-year bonds with demand amounting to PLN 11.7bn. The auction had no impact on IRS rates.

Crucial for IRS rates this week will be data on GDP in the Eurozone which may be conducive to their increase. Domestic data on GDP may have an opposite impact. The publication of Poland manufacturing PMI is likely to be neutral for the market. We believe that FED meeting will not have any substantial impact on IRS rates. Preliminary data on inflation in the Eurozone and US data (non-farm payrolls, Conference Board Index and final University of Michigan Index) will also a limited impact on the curve. The US GDP reading, if published, will also not be market moving.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-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*	4,18	4,15	4,17	4,21	4,24	4,31	4,37	4,27	4,30	4,28	4,34	4,29	4,29	**4,29**
USDPLN*	3,48	3,34	3,42	3,42	3,51	3,69	3,74	3,66	3,71	3,69	3,84	3,79	3,74	**3,74**
CHFPLN*	3,57	3,59	3,62	3,58	3,54	3,74	3,78	3,69	3,83	3,75	3,80	3,79	3,81	**3,76**
CPI inflation (% YoY)	2,1	1,9	1,4	1,3	1,6	1,7	2,0	2,0	2,0	1,9	1,8	1,3	1,1	
Core inflation (% YoY)	0,9	1,0	0,8	0,7	0,6	0,5	0,6	0,6	0,9	0,8	0,9	0,7	0,6	
Industrial production (% YoY)	2,8	8,6	7,3	1,7	9,3	5,2	6,7	10,3	5,0	2,7	7,4	4,6	2,8	
PPI inflation (% YoY)	0,3	0,2	-0,1	0,5	1,0	3,0	3,7	3,4	3,0	3,0	3,2	2,7	2,2	
Retail sales (% YoY)	6,0	8,2	7,9	9,2	4,6	7,6	10,3	9,3	9,0	5,6	9,7	8,2	4,7	
Corporate sector wages (% YoY)	7,3	7,3	6,8	6,7	7,8	7,0	7,5	7,2	6,8	6,7	7,6	7,7	6,1	
Employment (% YoY)	4,6	3,8	3,7	3,7	3,7	3,7	3,7	3,5	3,4	3,2	3,2	3,0	2,8	
Unemployment rate* (%)	6,6	6,8	6,8	6,6	6,3	6,1	5,8	5,8	5,8	5,7	5,7	5,7	5,8	
Current account (M EUR)	-1354	2289	-792	-914	263	297	112	-994	-681	-858	-471	-221		
Exports (% YoY EUR)	4,8	15,5	6,6	-4,4	9,9	1,4	7,0	8,4	7,3	0,0	12,1	7,1		
Imports (% YoY EUR)	13,2	19,0	9,5	0,3	13,6	2,9	8,7	10,0	11,2	5,4	17,5	9,9		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

	Indicator	2018				2019				2018	2019	2020
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
	Gross Domestic Product (% YoY)	5,3	5,1	5,1	4,5	3,7	3,6	3,2	2,9	5,0	3,3	3,2
	Private consumption (% YoY)	4,7	4,9	4,5	4,4	4,2	3,5	3,4	3,3	4,6	3,6	3,0
	Gross fixed capital formation (% YoY)	8,2	4,7	9,9	9,3	8,1	6,7	4,4	3,6	8,3	5,2	4,2
	Export - constant prices (% YoY)	3,4	7,6	4,9	4,4	4,7	4,7	4,9	5,4	5,1	4,9	4,5
	Import - constant prices (% YoY)	5,5	6,5	6,9	6,5	5,7	5,6	6,3	5,8	6,4	5,9	6,0
GDP growth contributions	Private consumption (pp)	3,0	2,8	2,7	2,2	2,7	2,0	2,0	1,6	2,7	2,1	1,7
	Investments (pp)	1,0	0,8	1,7	2,3	1,0	1,1	0,8	0,9	1,5	1,0	0,8
	Net exports (pp)	-1,0	0,9	-0,9	-0,9	-0,4	-0,3	-0,6	-0,1	-0,5	-0,3	-0,6
	Current account (% of GDP)***	-0,2	0,0	-0,5	-0,7	-1,0	-1,0	-1,0	-0,9	-0,7	-0,9	-0,8
	Unemployment rate (%)**	6,6	5,8	5,7	5,8	6,1	5,6	5,7	5,8	5,8	5,8	5,8
	Non-agricultural employment (% YoY)	1,4	1,0	1,1	0,8	0,4	0,4	0,4	0,4	1,1	0,4	0,1
	Wages in national economy (% YoY)	6,2	7,1	7,6	7,3	7,5	7,2	6,9	6,2	7,1	7,0	5,5
	CPI Inflation (% YoY)*	1,5	1,7	2,0	1,4	1,6	1,6	1,2	1,4	1,6	1,5	2,0
	Wibor 3M (%)**	1,70	1,70	1,72	1,72	1,72	1,72	1,72	1,80	1,72	1,80	2,30
	NBP reference rate (%)**	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	2,00
	EURPLN**	4,21	4,37	4,28	4,29	4,30	4,33	4,29	4,25	4,29	4,25	4,15
	USDPLN**	3,42	3,74	3,69	3,74	3,74	3,64	3,52	3,43	3,74	3,43	3,22

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST*	
					CA	CONSENSUS**
		Monday 01/28/2019				
10:00	Eurozone	M3 money supply (% MoM)	Dec	3,7		3,8
		Tuesday 01/29/2019				
15:00	USA	Case-Shiller Index (% MoM)	Nov	0,4		
16:00	USA	Consumer Confidence Index	Jan	128,1	126,0	125,0
		Wednesday 01/30/2019				
11:00	Eurozone	Business Climate Indicator (pts)	Jan	0,82		0,73
14:00	Germany	Preliminary HICP (% YoY)	Jan	1,7	1,6	1,8
14:15	USA	ADP employment report (k)	Jan	271		178
14:30	USA	Preliminary estimate of GDP (% YoY)	Q4	3,4	2,7	2,5
20:00	USA	FOMC meeting (%)	Jan	2,50	2,50	2,50
		Thursday 01/31/2019				
2:00	China	Caixin Manufacturing PMI (pts)	Jan	49,4		49,3
10:00	**Poland**	**Annual GDP (% YoY)**	**2018**	**4,8**	**5,0**	**5,0**
11:00	Eurozone	Preliminary GDP (% QoQ)	Q4	0,2	0,3	0,2
11:00	Eurozone	Unemployment rate (%)	Dec	7,9		7,9
14:30	USA	Real private consumption (% MoM)	Dec	0,3		
15:45	USA	Chicago PMI (pts)	Jan	65,4		62,0
		Friday 02/01/2019				
2:45	China	Caixin Manufacturing PMI (pts)	Jan	50,2		49,5
7:00	Germany	Preliminary GDP (% QoQ)	Q4	-0,2	0,1	
9:00	**Poland**	**Manufacturing PMI (pts)**	**Jan**	**47,6**	**0,0**	
9:55	Germany	Final Manufacturing PMI (pts)	Jan	49,9	49,9	49,9
10:00	Eurozone	Final Manufacturing PMI (pts)	Jan	50,5	50,5	50,5
11:00	Eurozone	Preliminary HICP (% YoY)	Jan	1,6	1,3	1,4
14:30	USA	Unemployment rate (%)	Jan	3,9	4,0	3,9
14:30	USA	Non-farm payrolls (k MoM)	Jan	312	185	168
16:00	USA	Final U. of Michigan Sentiment Index (pts)	Jan	90,7	90,0	90,7
16:00	USA	ISM Manufacturing PMI (pts)	Jan	54,1	53,4	54,3

*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

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