# There will be no negative interest rates in Poland

## This week

- **Significant hard data on US economy and business survey results will be released this week.** We expect industrial production growth rate to have decreased to 0.1% MoM in January vs. 0.3% in December, due to lower production growth in manufacturing and mining. We forecast that nominal retail sales increased by 0.1% MoM in December vs. a 0.2% increase in November, due to falling fuel prices. Business survey results will also be released in the US. In our view the NY Empire State Index rose to 6.0 pts in February from 3.9 pts in January due to low base effects. We forecast that the preliminary University of Michigan Index (93.0 vs. 91.2 pts in January) will signal slight improvement of households' sentiment in February, mainly due to the end of the government shutdown. We believe that the aggregate impact of data on the US economy on the financial markets will be limited.
- **Data on the Polish balance of payments in December 2018 will be released on Wednesday**. We expect the current account deficit to increase to EUR 929M vs. EUR 221M in November 2018, mainly due to lower balance on trade. We forecast that export dynamics decreased from 7.1% YoY in November to 4.2% in December, while import growth rate decreased from 9.9% YoY to 3.4%. The decrease in both dynamics resulted from sharp slowdown of growth recorded in Polish manufacturing in December. In our view, the balance of payments data will be neutral for PLN and yields on Polish bonds.
- **Data on the Chinese trade balance will be released on Thursday.** The market expects it to have dropped to USD 33.5bn in January vs. USD 57.1bn in December, with a simultaneous decrease in exports and imports dynamics. The data will be relevant in assessment of the sustainability and scale of the slowdown in global trade.
- **The flash estimate of GDP in Poland in Q4 2018 will be released on Thursday.** Based on the GDP data for the whole 2018 published by GUS two weeks ago (see MACROpulse of 31/1/2019), we estimate that the GDP growth rate dropped to 4.9% YoY from 5.1% in Q3 2018. Slower GDP growth resulted from lower contributions of private investments, investments, and change in inventories as well as higher contributions of net exports and public consumption. The GDP reading should not be market moving.
- **On Friday we will see the data on the January inflation in Poland which, in our view, rose to 1.2% YoY vs. 1.1% in December.** The increase in inflation rate resulted from higher dynamics of food and energy prices and higher core inflation. Our forecast is above the market consensus (1.0%), therefore its materialization will be conducive to PLN appreciation and higher yields on Polish bonds.

## Last week

- **As we expected, the Monetary Policy Council left interest rates unchanged at its meeting last week (the reference rate amounts to 1.50%).** In the statement after the meeting, the Council repeated the view that the current level of interest rates was conducive to keeping the Polish economy on a sustainable growth path and maintaining macroeconomic stability. Like the month before, the Council emphasized that the outlook for economic conditions in Poland remained favourable, however, in the quarters to come, there would probably be a gradual slowdown in GDP growth. The Council repeated the view that in the monetary policy transmission horizon inflation would remain close to the target. At the conference after the MPC meeting, A. Glapiński, asked if he maintained his view voiced a month ago that interest rates might remain stable until the end of MPC term (the beginning of 2022), answered that "the rates may remain unchanged this year and probably also next year" (see MACROpulse of 6/2/2019). Thus, A. Glapiński has returned with his position concerning stable interest rates horizon to the view expressed before the January MPC meeting. A. Glapiński's more dovish tone than the month before supports our scenario, in which NBP interest rates will remain unchanged until the end of 2019 and the first hike (by 25 bp) will take place in March 2020.

- **Significant data from the German economy were released last week**. The dynamics of German industrial production rose to -0.4% MoM in December vs. -1.3% in November, running clearly below the market expectations (+0.7%). Slower pace of the deceleration in German industrial production resulted from higher dynamics of output in manufacturing, while their decrease in construction and energy had an opposite impact. Industrial production in Germany has showed a pronounced downward trend since May 2018 and in December reached the lowest level since March 2017. Data on orders in German manufacturing point to a high likelihood of further decline in industrial production in the coming months, as their dynamics decreased to -1.6% MoM in December vs. -0.2% in November, running way below the market expectations. The faster pace of the decline in new orders resulted from lower dynamics of both domestic and foreign orders. Data on German foreign trade were also released last week and showed that exports growth rose to 1.5% MoM in December vs. -0.3% in November while imports growth rose to 1.2% MoM vs. -1.3%. Though proving to be better from the consensus (the market expected that both imports and exports growth would amount to 0.2% MoM), the data should be viewed with great caution because they are highly volatile. We believe that the slowdown in German manufacturing will continue for several months before the effects of the stimulation of economic growth in China will start being conducive to the acceleration in global trade (see MACROmap of 7/1/2019). The last week's data from the German economy pose a downside risk to our forecast, in which the growth rate of the German GDP will decrease to 1.3% in 2019 vs. 1.5% in 2018.
- **Non-manufacturing ISM index in the US decreased to 56.7 pts in January vs. 58.0 pts in December, running slightly below the market expectations (57.0 pts**). The index decline resulted from lower contributions of its sub-indices for new orders and business activity. Higher contribution of the employment sub-index had an opposite impact while the contribution of the sub-index for suppliers' delivery times has not changed compared to December. We expect that the annualized US GDP growth rate will decrease to 1.4% in Q1 2019 vs. 2.7% in Q4 2018. Possible lack of agreement between D. Trump and the Congress on financing the wall along the US border with Mexico which may result in another government shutdown from 15 February poses a downside risk to this scenario

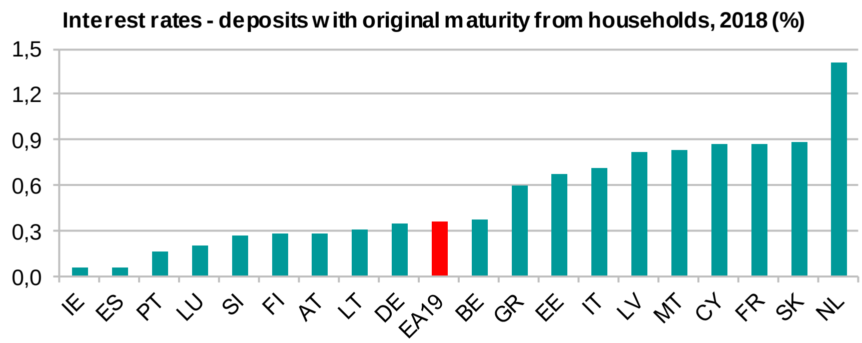
## There will be no negative interest rates in Poland

**In the previous MACROmap we pointed out that in the situation of a sharp slowdown of economic growth in Poland, the depreciation of PLN (resulting from interest rates cuts by the MPC and increase in global risk aversion) would be insufficient to markedly stimulate economic growth and inflation. In our previous analysis we focused on examining the impact of the currency channel while implicitly assuming a significant scale of interest rates cuts and disregarding the impact of the interest rate channel. Below we extend this analysis and ask to what extent the MPC (under certain assumptions) will be able to cut interest rates and what the aggregate impact of such measures will be on the economic conditions in Poland.**

Studies on the monetary policy transmission mechanism in Poland have shown that changes in rates in the interbank market (e.g. WIBOR) are practically fully reflected by the average interest on corporate and households' deposits and loans. However, such analyses were carried out in the context of markedly positive interest rates. The so-far experience of foreign central banks suggests that in the context of very low/negative interest rates, the reaction of the interest on deposits to central bank's rate cuts may be markedly weaker from that of the interest on loans (the reaction of interest on credits and deposits is strongly asymmetrical). This phenomenon, known as "the stickiness of deposit rates" results from commercial banks' concerns about the outflow of deposits in reaction to their interest rates decreasing to a level close to zero.

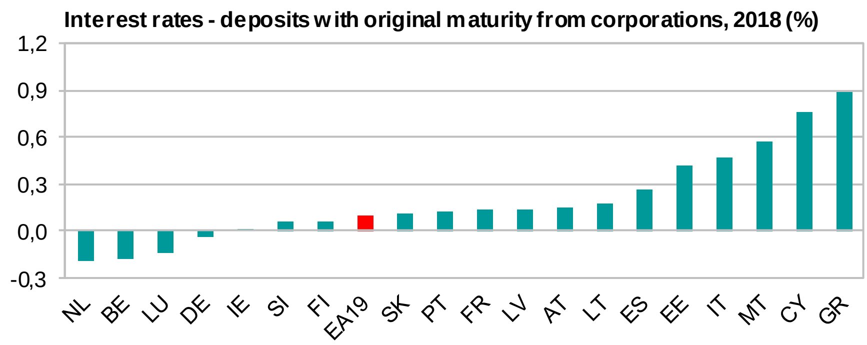
In assessing a maximum possible scale of interest rates cuts by the MPC, we noted two factors. Firstly, the MPC will not want to contribute towards the outflow of deposits from the banking sector resulting from an excessive decrease in their interest rates. Secondly, the MPC will want to avoid a situation whereby the banking sector's result would deteriorate due to interest rates cuts, as such a decline in profits would contribute to slower increase in capital in the banking sector and to lower lending. Our view is supported by MPC members' remarks and the MPC mandate, according to which the monetary policy should be conducted so as to support the stability of the financial system.

We have estimated the maximum scale of the reference rate cuts in the following way – we have analyzed how much commercial banks can reduce interest on corporate and households' deposits so as not to provoke their outflow. As long as commercial banks can reduce interest on deposits (and to the same extent the interest on credits), the cuts of the reference rate by the MPC will not be conducive to the deterioration of their result.




**Source:** ECB, Credit Agricole

To estimate the minimum level of interest on deposits with original maturity that would be acceptable to households, we studied the experience of the Eurozone countries. The ECB has carried out the policy of negative interest rates since 2014 (currently the deposit rate amounts to -0.4%), therefore the current interest on deposits in the banking sector can be treated as the state of equilibrium. In individual Eurozone member-countries in ranged, on the average, from 0.05% (in Ireland) to 1.4% (in the Netherlands) in 2018. In the whole Eurozone it amounted, on average, to 0.35%. That is why, for the purpose of our analysis, we assume that in the conditions of further interest rate cuts by the MPC, the average interest on households' deposits with original maturity in Poland should not fall below 0.4%. Currently interest on households' deposits amounts to 1.8%. In accordance with the transmission mechanism studies, changes in the reference rate are in the long term fully reflected by interest on deposits. This means that the MPC will be able to reduce the reference rate by 140bp to avoid the interest on households' deposit falling below 0.4%.



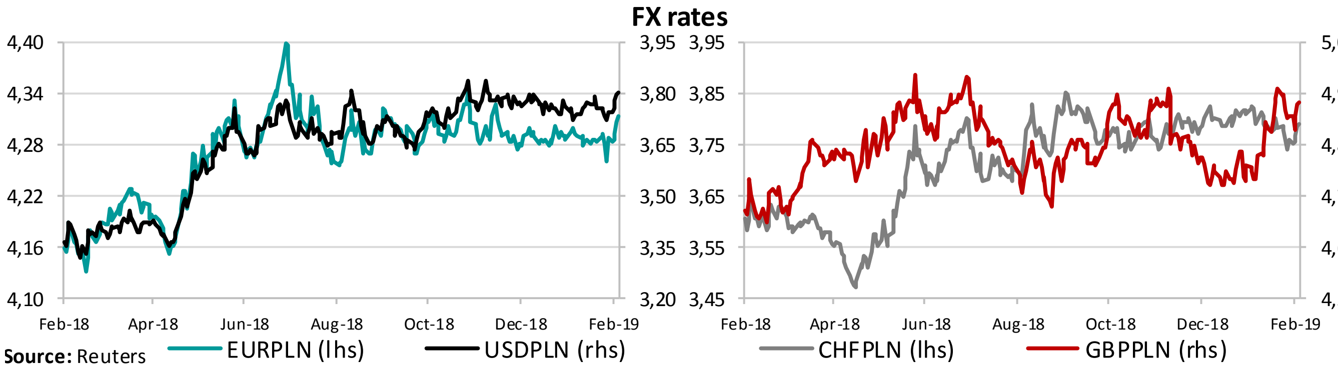

**Source:** ECB, Credit Agricole

We have applied a similar reasoning to corporate deposits. Based on the experience of the Eurozone countries (see the chart), we believe that in the situation of the monetary policy easing by the NBP, interest on deposits could be reduced by commercial banks to minimum ca. 0.1% (the current level of average interest on corporate deposits within the single currency area). The transmission of changes in the reference rate to changes of interest rates in the segment of corporate deposits is almost complete. Currently, the average interest on corporate deposits with original maturity amounts in Poland to 1.1%. This would mean that the MPC could reduce the reference rate by 100bp so as not to contribute to the outflow of corporate deposits from the banking sector.

The admissible scale of conventional monetary policy easing in Poland depends on the above two factors which determine the maximum scale of reference rate cuts from the point of view of interest on households' deposits (140bp) and corporate deposits (100bp) as well as the structure of financing (corporate deposits vs. households' deposits) of lending by commercial banks. Assuming that the future financing structure is consistent with the current relation of the volume of households' deposits and corporate deposits (3:1), the MPC could reduce the reference rate by maximum 130bp down to 0.2%.We believe that if our scenario materializes, the MPC would narrow the interest rate corridor and the deposit rate would remain at a non-negative level. Thus, the interest rates in Poland, unlike in the Eurozone, would not fall below zero.

According to the NBP surveys, the reduction of the reference rate by 130bp would be conducive to increase in the GDP growth rate by 0.1-0.4pp, increase in inflation by 0.3pp, and PLN weakening by 1.2-1.7%. The above estimates take into account the impact of both the currency channel and the interest rate channel due to interest rate cuts. On the other hand, they disregard the effects relating to PLN weakening resulting from higher risk aversion amid sharp slowdown of economic growth described by us in the previous MACROmap. The small scale of the impact of monetary policy carried out in a conventional way on the macroeconomic conditions in Poland supports our view that to significantly stimulate economic growth and inflation in Poland the use of unconventional tools would also be necessary. In the coming MACROmaps we will present subsequent methods of unconventional monetary policy easing (we have discussed the program of low-interest loans for small and medium-size businesses in the MACROmap of 28/1/2019).

## Increase in global risk aversion has weakened PLN



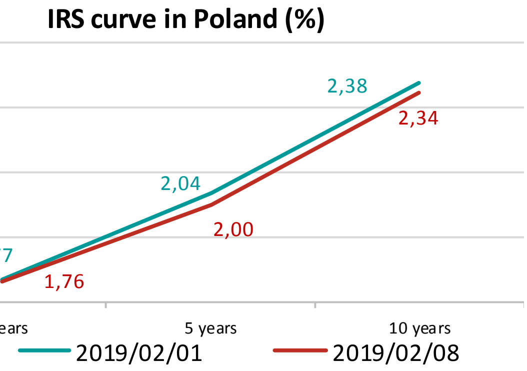

**Source:** Reuters

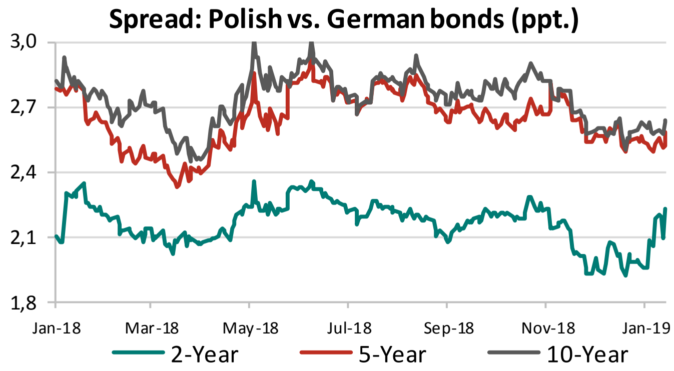
**Last week, the EURPLN exchange rate rose to 4.3131 (depreciation of PLN by 0.5%).** On Monday and Tuesday, EURPLN was relatively stable and stood between 4.28 and 4.29. From Wednesday, PLN was weakening like other currencies of the region, due to increase in global risk aversion, reflected by higher VIX index. It resulted from investors' concerns about the outlook for economic growth in the Eurozone, growing probability of hard Brexit, and no substantial progress in US-China talks on the de-escalation of trade war.

The increase in global risk aversion was supporting the appreciation of the currencies of the economies believed to be safe havens. Consequently, last week saw a decrease in EURUSD and EURCHF. Taking into account the increase in EURPLN, PLN depreciated vs. USD by 1.7% and vs. CHF by 0.8%. Despite the growing likelihood of Great Britain's uncontrolled exit from the EU, GBP has not weakened vs. EUR over the week. That is because GBP was supported by the announcement of the Bank of England that it planned to hike interest rates after Brexit. Consequently, PLN depreciated vs. GBP last week (by 0.6%).

Crucial for PLN this week will be domestic data on inflation. If our higher-from-the-market-consensus forecast materializes, the data may contribute to PLN appreciation. Other domestic data (flash GDP for Q4 and balance of payments) as well as numerous data from the US (CPI inflation, retail sales, industrial production, preliminary University of Michigan Index, NY Empire State Index) will not have any substantial impact on PLN, we believe.

## Market focuses on domestic inflation data




**Source:** Reuters

**Last week, 2-year IRS rates decreased to 1.76 (down by 1bp), 5-year rates to 2.00 (down by 4bp), and 10-year rates to 2.34 (down by 4bp).** The increase in IRS rates from two weeks ago, resulting from the publication of better-than-expected data from US labour market (see MACROmap of 4/2/2019), was continued on Monday. On Tuesday, IRS rates decreased, following the German market. Lower yields on German bonds were supported by the publication of subsequent weaker data on the German economy (industrial production and new orders in manufacturing –see above). Due to higher risk aversion, the spread between Polish and German bonds has increased. Last week the Ministry of Finance sold PLN 5.0bn of 2-, 5-, 9-, and 10-year bonds with demand amounting to PLN 10.2bn. However, the debt auction had a limited impact on the curve.

This week the market will focus on domestic data on inflation, which may contribute to increase in IRS rates. Other data from Poland (flash GDP for Q4 and the balance of payments) are likely to be neutral for the curve. Data from the US (CPI inflation, retail sales, industrial production, preliminary University of Michigan Index, NY Empire State Index) will not have any substantial impact on IRS rates, we believe.

# Forecasts of the monthly macroeconomic indicators

**Main monthly macroeconomic indicators in Poland**

| Indicator | 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 | Feb-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* | 4,15 | 4,17 | 4,21 | 4,24 | 4,31 | 4,37 | 4,27 | 4,30 | 4,28 | 4,34 | 4,29 | 4,29 | 4,26 | **4,28** |
| USDPLN* | 3,34 | 3,42 | 3,42 | 3,51 | 3,69 | 3,74 | 3,66 | 3,71 | 3,69 | 3,84 | 3,79 | 3,74 | 3,72 | **3,73** |
| CHFPLN* | 3,59 | 3,62 | 3,58 | 3,54 | 3,74 | 3,78 | 3,69 | 3,83 | 3,75 | 3,80 | 3,79 | 3,81 | 3,74 | **3,71** |
| CPI inflation (% YoY) | 1,9 | 1,4 | 1,3 | 1,6 | 1,7 | 2,0 | 2,0 | 2,0 | 1,9 | 1,8 | 1,3 | 1,1 | **1,2** | |
| Core inflation (% YoY) | 1,0 | 0,8 | 0,7 | 0,6 | 0,5 | 0,6 | 0,6 | 0,9 | 0,8 | 0,9 | 0,7 | 0,6 | **0,6** | |
| Industrial production (% YoY) | 8,6 | 7,3 | 1,7 | 9,3 | 5,2 | 6,7 | 10,3 | 5,0 | 2,7 | 7,4 | 4,6 | 2,7 | **3,7** | |
| PPI inflation (% YoY) | 0,2 | -0,1 | 0,5 | 1,0 | 3,0 | 3,7 | 3,4 | 3,0 | 3,0 | 3,2 | 2,8 | 2,2 | **2,7** | |
| Retail sales (% YoY) | 8,2 | 7,9 | 9,2 | 4,6 | 7,6 | 10,3 | 9,3 | 9,0 | 5,6 | 9,7 | 8,2 | 4,7 | **5,3** | |
| Corporate sector wages (% YoY) | 7,3 | 6,8 | 6,7 | 7,8 | 7,0 | 7,5 | 7,2 | 6,8 | 6,7 | 7,6 | 7,7 | 6,1 | **6,5** | |
| Employment (% YoY) | 3,8 | 3,7 | 3,7 | 3,7 | 3,7 | 3,7 | 3,5 | 3,4 | 3,2 | 3,2 | 3,0 | 2,8 | **1,8** | |
| Unemployment rate* (%) | 6,8 | 6,8 | 6,6 | 6,3 | 6,1 | 5,8 | 5,8 | 5,8 | 5,7 | 5,7 | 5,7 | 5,8 | **6,1** | |
| Current account (M EUR) | 2289 | -792 | -914 | 263 | 297 | 112 | -994 | -681 | -858 | -471 | -221 | **-929** | | |
| Exports (% YoY EUR) | 15,5 | 6,6 | -4,4 | 9,9 | 1,4 | 7,0 | 8,4 | 7,3 | 0,0 | 12,1 | 7,1 | **4,2** | | |
| Imports (% YoY EUR) | 19,0 | 9,5 | 0,3 | 13,6 | 2,9 | 8,7 | 10,0 | 11,2 | 5,4 | 17,5 | 9,9 | **3,4** | | |

*end of period

# Forecasts of the quarterly macroeconomic indicators

**Main macroeconomic indicators in Poland**

| Indicator | | 2018 Q1 | 2018 Q2 | 2018 Q3 | 2018 Q4 | 2019 Q1 | 2019 Q2 | 2019 Q3 | 2019 Q4 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Gross Domestic Product (% YoY) | | 5,3 | 5,1 | 5,1 | 4,9 | 3,7 | 3,6 | 3,2 | 2,9 | 5,1 | 3,3 | 3,2 |
| Private consumption (% YoY) | | 4,7 | 4,9 | 4,5 | 3,9 | 4,2 | 3,5 | 3,4 | 3,3 | 4,5 | 3,6 | 3,0 |
| Gross fixed capital formation (% YoY) | | 8,2 | 4,7 | 9,9 | 6,8 | 8,1 | 6,7 | 4,4 | 3,6 | 7,3 | 5,2 | 4,2 |
| Export - constant prices (% YoY) | | 3,4 | 7,6 | 4,9 | 4,4 | 4,7 | 4,7 | 4,9 | 5,4 | 5,0 | 4,9 | 4,5 |
| Import - constant prices (% YoY) | | 5,5 | 6,5 | 6,9 | 3,0 | 5,7 | 5,6 | 6,3 | 5,8 | 5,4 | 5,9 | 6,0 |
| GDP growth contributions | Private consumption (pp) | 3,0 | 2,8 | 2,7 | 2,0 | 2,7 | 2,0 | 2,0 | 1,6 | 2,6 | 2,1 | 1,7 |
| | Investments (pp) | 1,0 | 0,8 | 1,7 | 1,7 | 1,0 | 1,1 | 0,8 | 0,9 | 1,3 | 1,0 | 0,8 |
| | Net exports (pp) | -1,0 | 0,9 | -0,9 | 0,8 | -0,4 | -0,3 | -0,6 | -0,1 | 0,0 | -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** |
| | | **Wednesday 02/13/2019** | | | | |
| 11:00 | Eurozone | Industrial production (% MoM) | Dec | -1,7 | | -0,3 |
| **14:00** | **Poland** | **Current account (M EUR)** | **Dec** | **-221** | **-929** | **-945** |
| 14:30 | USA | CPI (% MoM) | Jan | -0,1 | 0,1 | 0,1 |
| 14:30 | USA | Core CPI (% MoM) | Jan | 0,2 | 0,2 | 0,2 |
| | | **Thursday 02/14/2019** | | | | |
| | China | Trade balance (bn USD) | Jan | 57,1 | | 33,5 |
| 8:00 | Germany | Preliminary GDP (% QoQ) | Q4 | -0,2 | | 0,1 |
| **10:00** | **Poland** | **Flash GDP (% YoY)** | **Q4** | **5,1** | **4,9** | **4,9** |
| 11:00 | Eurozone | Preliminary GDP (% QoQ) | Q4 | 0,2 | 0,2 | 0,2 |
| 14:30 | USA | Retail sales (% MoM) | Dec | 0,2 | | 0,1 |
| 16:00 | USA | Business inventories (% MoM) | Nov | 0,6 | | 0,3 |
| | | **Friday 02/15/2019** | | | | |
| 2:30 | China | PPI (% YoY) | Jan | 0,9 | | 0,4 |
| 2:30 | China | CPI (% YoY) | Jan | 1,9 | | 2,0 |
| **10:00** | **Poland** | **CPI (% YoY)** | **Jan** | **1,1** | **1,2** | **1,0** |
| 14:30 | USA | NY Fed Manufacturing Index (pts) | Feb | 3,9 | 0,1 | 6,5 |
| 15:15 | USA | Industrial production (% MoM) | Jan | 0,3 | 0,1 | 0,2 |
| 15:15 | USA | Capacity utilization (%) | Jan | 78,7 | 78,7 | 78,8 |
| 16:00 | USA | Initial U. of Michigan Sentiment Index (pts) | Feb | 91,2 | 93,0 | 94,0 |

*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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