Sentiment in Polish manufacturing the weakest since 2009

This week

- **The most important event this week will be the meeting of the Monetary Policy Council scheduled for Wednesday**. We expect that the MPC will leave interest rates unchanged. In our view, during the conference, A. Glapiński will repeat his opinion that NBP interest rates are highly likely to stay at the present level until the end of the MPC term (the beginning of 2022). His view will be supported by the results of the latest NBP projection, presented during the conference this week. We believe that both the inflation and the GDP growth rate profiles will not change significantly compared to the July projection. Crucial for the projection results will be the NBP assumptions concerning the development of electricity prices in 2020. We believe that the tone of the press conference and the results of the November macroeconomic projection will be neutral for PLN and yields on Polish bonds.
- **Data on the Chinese balance on trade will be released on Friday.** The market expects it to have increased to USD 41.2bn in October vs. USD 39.65bn in September. According to the consensus, the export growth rate dropped to -3.5% YoY in October from -3.2% in September, while import dynamics decreased to -8.9% from -8.5% in September. We believe that the publication of data on the Chinese balance on trade will be overshadowed by the current US-China negotiations, and thus will be neutral for the financial markets.
- **The results of US business surveys will be released this week.** We expect that the non-manufacturing ISM rose to 53.6 pts in October vs. 52.6 pts in September. In turn, we forecast that the preliminary University of Michigan Index has not changed in November compared to October and amounted to 95.5 pts. In our view, the publication of the US data will not have any substantial impact on the financial markets.
- **We have downwardly revised our forecast of inflation in Poland in Q4 2019 and in the whole 2020**. Taking into account the latest remarks of government officials (J. Emilewicz, Minister for Business and Technology, and M. Dworczyk, Head of the Chancellery of the Prime Minister) and the approaching presidential campaign, our forecast assumes that the prices of electricity for individuals will not increase in 2020. Our previous forecast assumed a slight increase in electricity prices in January 2020. The change of assumptions in this regard is the main factor which justifies the lowering of the profile of total inflation. In addition, in our view, the dynamics of food prices will run below our earlier expectations, as was the case in the last few months. On the other hand, inflation will be boosted by the sharp increase of the minimum wage at the beginning of next year, which will be mostly responsible for an increase of core inflation (mainly of the prices of services). Considering the tendencies outlined above, we expect that CPI inflation will, on a yearly average, amount to 2.3% YoY in 2019 and to 2.0% in 2020 (see the quarterly table).
- **The results of business surveys for Polish manufacturing have been released today.** PMI dropped to 45.6 pts in October vs. 47.8 pts in September, running significantly below our forecast (48.3 pts) and the market consensus (48.1 pts). Thus, the index has for twelve months in a row stayed below the 50 pts threshold dividing expansion from contraction of activity (see below). We believe that today's reading is negative for PLN and yields on Polish bonds.

Last week

- **The most important event last week was FOMC meeting.** In accordance with our expectations and the market consensus, FED lowered the target range for federal funds by 25bp to [1.50%; 1.75%]. In justifying its decision to ease the monetary policy, FED pointed to the high uncertainty about global economic outlook and to limited inflationary pressure in the US. There have been some slight changes in the text of the statement after the meeting, which suggest that FED will for the time being refrain from further rate cuts while monitoring the incoming information. Nonetheless, during the conference after the meeting, J. Powell indicated that FED will take adequate measures should the US economic outlook significantly deteriorate. The tone of the FED meeting brought about a temporary appreciation of USD vs. EUR and increase of yields on US bonds. Our baseline scenario assumes that subsequent interest rate cuts in the US (totaling 50bp) will take place in H1 2020. They will be the reaction to the expected by us marked slowdown of US GDP growth resulting from further global downturn and the escalation of the US-China trade war.

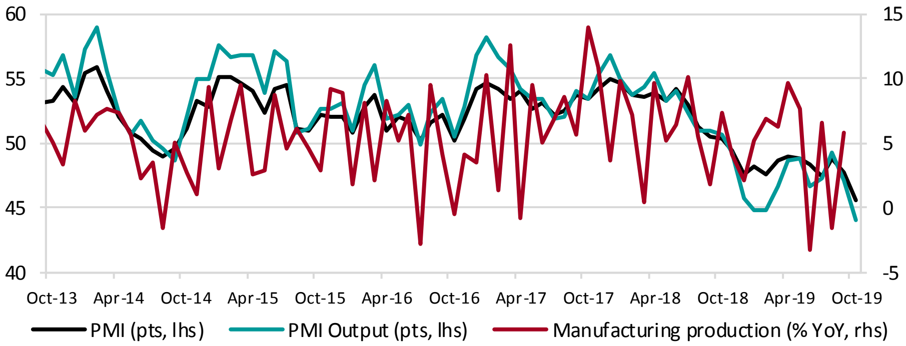
- **Significant data from the US economy were released last week.** In accordance with the flash estimate, the annualized US GDP growth rate decreased to 1.9% in Q3 vs. 2.0% in Q2, running above the market expectations (1.7%) and our forecast (1.5%). Lower economic growth rate resulted from lower contributions of private consumption (1.93 pp in Q3 vs. 3.03 in Q2) and government expenditure (0.35pp vs. 0.82pp), while higher contributions of inventories (-0.05pp vs. -0.91pp), net exports (-0.08pp vs. -0.68pp), and investments (-0.22pp vs. -0.25pp) had an opposite impact. Thus, like in Q2, private consumption was the main source of economic growth in Q3. Last week we also saw data on non-farm payrolls which rose by 128k in October vs. a 180k increase in September (revised upwards from 136k), running significantly above the market expectations (+85k) and our forecast (+75k). Employment has sharply increased despite the strike in General Motors and the cessation of work of persons engaged in the preparation of the Census (according to our estimates, these two factors reduced employment by 70k). The highest increase of employment in October was recorded in leisure and hospitality (+61.0k), education and health service (+39.0k), and business services (+22.0k). On the other hand, the sharpest decrease in employment was recorded in manufacturing (-36.0k), supply of information (-4.0k), the public sector (-3.0k), and other services (-3.0k). Unemployment rate rose to 3.6% in October vs. 3.5% in September, running in line with the market expectations and our forecast. It is worth noting that it remains significantly below the natural unemployment rate indicated by FOMC (4.2%, see MACROmap of 23/9/2019). Its increase resulted from the fact that labour resources rose more than employment. This shows that some previously inactive persons have decided to enter the labour market. Thus the participation rate rose to 3.6% in October vs. 3.5% in September. The annual dynamics of average hourly earnings have not changed in September compared to October and amounted to 3.0%. This points to continuing low wage pressure in the US economy. The results of business surveys in the US were also released last week. The ISM index for manufacturing increased to 48.3 pts in October vs. 47.8 pts in September, running below the market expectations (48.9 pts) and our forecast (49.0 pts). Thus the index has for third month running stayed below the 50 pts threshold dividing expansion from contraction of activity. The index slight increase resulted from higher contributions of three of its five sub-indices (for inventories, new orders, and employment) while lower contributions of the sub-indices for suppliers' delivery times and output had an opposite impact. At the same time it is worth noting that for the first time since April 2009 all the sub-indices stood below the 50 pts threshold. The results of consumer sentiment surveys were also released last week. The Conference Board Index dropped to 125.9 pts in October vs. 126.3 pts in September. Its decrease resulted from lower sub-index for expectations while higher sub-index for the assessment of the current situation had an opposite impact. We forecast that the annualized US GDP growth rate will decrease to 1.7% in Q4.
- **In accordance with the flash estimate, CPI inflation in Poland dropped to 2.5% YoY in October vs. 2.6% in September**. GUS has published partial data on the inflation structure, including information on the rate of inflation in the categories "food and non-alcoholic beverages", "energy", and "fuels". The decrease in inflation resulted from lower dynamics of the prices of fuels (-4.7% YoY in October vs. -2.7% in September), food and non-alcoholic beverages (6.1% YoY vs. 6.3%), and energy (-1.7% YoY vs. -1.6%), while core inflation, according to our estimates, has not changed in October compared to September and amounted to 2.4%. Final data on inflation will be released on 14 November. We believe that in the whole 2019 inflation in Poland

will amount to 2.3% YoY vs. 1.6% in 2018.

- **According to the flash estimate, inflation in the Eurozone dropped to 0.7% YoY in October vs. 0.8% in September, running below the market expectations equal to our forecast (0.8%).** The decrease in inflation resulted from lower dynamics of energy prices. We believe that inflation in the Eurozone has reached its local minimum in October. In subsequent months it will slightly increase but will not exceed 1.3% before the end of 2020. Moreover, we forecast that in the same period core inflation will not exceed 1.4%YoY.
- **The Caixin PMI for Chinese manufacturing rose to 51.7 pts in October vs. 51.4 pts in September, running clearly above the market expectations (51.0 pts) and our forecast (51.5 pts)**. Thus, it has been third consecutive month when the index stood above the 50 pts threshold dividing expansion from contraction of activity. The index increase resulted from higher contributions of three of its five sub-indices (for new orders, output and suppliers' delivery times), while lower contributions of the sub-indices for employment and inventories had an opposite impact. Especially noteworthy in the data structure is the continuing for three months now increase in total orders with a simultaneous increase in output. In our view it is the effect of the measures taken by the Chinese government to stimulate domestic demand. It is worth noting here that in October the sub-index for new export orders has, for the first time since May 2019, risen above the 50pts threshold, suggesting a slight improvement in the external environment of the Chinese economy. Last week we also saw the CFLP PMI for Chinese manufacturing which decreased to 49.3 pts in October vs. 49.8 pts in September, running below the market expectations (49.8 pts). In addition, it has reached the lowest value since February 2019. Noteworthy in the data structure is a sharp decrease in the sub-indices for output and new orders. The mixed business survey results for Chinese manufacturing indicate that it is highly likely that the business cycle has not reached the bottom yet and subsequent quarters may bring further slowdown of activity. Nonetheless, we maintain our forecast for economic growth in China (6.2% in 2019 and 6.0% in 2020). In our view, 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. The 4th Plenary Session of the 19th Central Committee of the Communist Party of China which ended last week has not brought any new significant information about the prospects for the economic policy in China in the coming quarters.
- **According to the flash estimate, the quarterly GDP dynamics in the Eurozone have not changed in Q3 compared to Q2 and amounted to 0.2% (1.1% YoY in Q3 vs. 1.2% in Q2), running in line with our forecast and above the market expectations (0.1% QoQ).** Last week we also saw flash GDP estimates for several Eurozone economies, i.a. in France (0.3% QoQ both in Q2 and in Q3), in Spain (0.4% QoQ both in Q2 and in Q3), and in Italy (0.1% in Q3 vs. 0.0% in Q2). Today's GDP reading is a flash estimate and does not include its structure. Subsequent GDP estimate for the Eurozone in Q3, reflecting the growth rate in all the countries of the single currency area, will be released on 14 November and full data on GDP structure will be released on 5 December. Particularly important will be the data from Germany which, in our view, will point to technical recession in that country (GDP down by 0.1% QoQ in both Q2 and Q3).
- **Last week the EU ambassadors decided to postpone Brexit until 31 January.** The postponement of Brexit is flexible (so called flextension). Thus, if the UK accepts the deal negotiated earlier by B. Johnson, it will be able to leave the EU on 1 December 2019 or on 1 January 2020. Last week, there was also a voting in the British Parliament which approved B. Johnson's motion for snap election, which was scheduled for 12 December 2019. Thus the vote on the B. Johnson's deal will take place during the new parliamentary term. Currently, the polls do not give B. Johnson's party an absolute majority, which points to the risk of the Brexit deadlock continuing into the next term. Consequently, subsequent weeks may see increased

volatility of GBP in reaction to the publications of subsequent poll results.

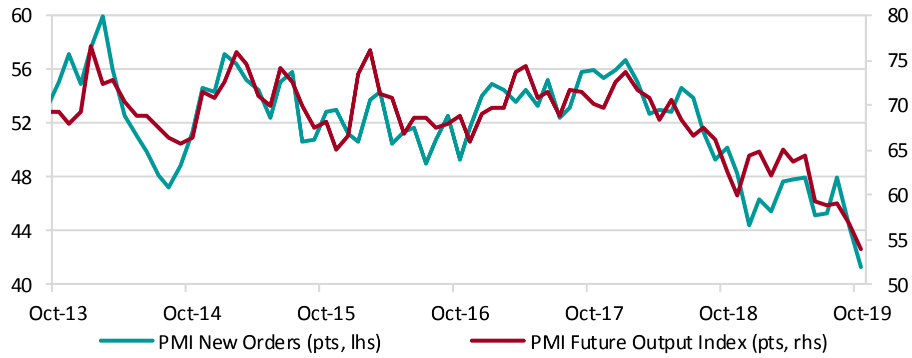
Sentiment in Polish manufacturing the weakest since 2009



Source: Markit. GUS

Polish manufacturing PMI dropped to 45.6 pts in October vs. 47.8 pts in September, running significantly below our forecast (48.3 pts) and the market consensus (48.1 pts). Thus, the index has now for twelve 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 all its sub-indices (concerning employment, output, total new orders, suppliers' delivery times, and stocks of goods purchased). In effect, PMI has reached the lowest level since June 2009.

The structure of the October PMI presented a more pessimistic picture of the Polish manufacturing than in the last few months. Especially noteworthy is an accelerating decrease in total new orders, including new export orders. It is surprising in the context of the stabilization recorded in October in the Eurozone manufacturing, including in Germany (see MACROmap of 28/10/2019). According to Markit report, the surveyed companies attributed the deterioration of sentiment to weaker demand in Europe and the competition from China. The business climate in Polish manufacturing looks especially bad against the backdrop of other countries of the region (the Czech Republic and Hungary) which recorded a slight increase in PMIs in October. Amid a decreasing inflow of foreign orders, the companies were clearing outstanding orders but it was not sufficient to stop a decline in production. The output sub-index decreased to 44.0 pts in October from 47.1 pts in September.



Source: Markit

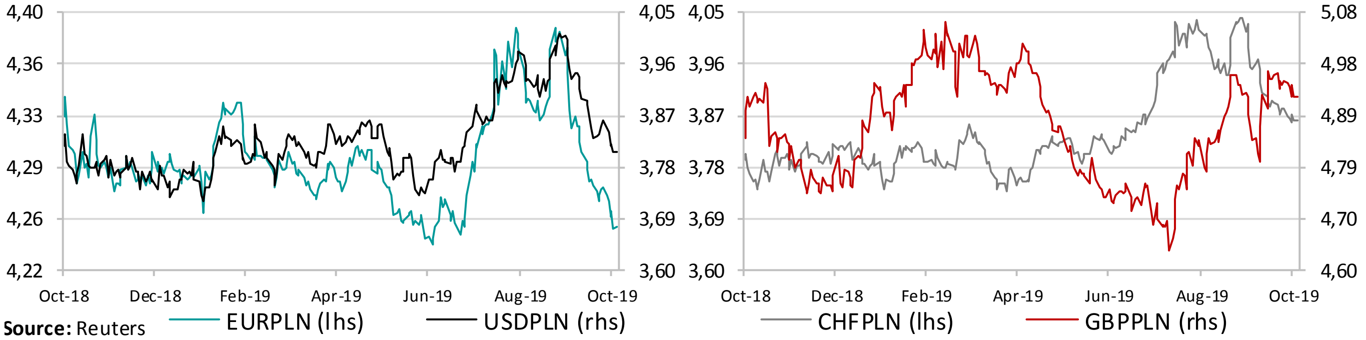
In October a decrease in the inventories of stocks purchased was recorded for fourth month in a row. Companies' limited tendencies to increase stocks might signalize their pessimistic expectations concerning demand in coming months. These expectations were also reflected by the Indicator of Future Output Index which stood in October at the record low level (the lowest since October 2012). At the same time the stocks of finished (i.e. unsold) products are increasing, which is yet another sign of weaker demand.

We believe that the marked deterioration recorded in October in Polish amid stabilization of sentiment in the Eurozone, including in Germany and in other countries of the region, is an outlier and November will probably see a slight increase in PMI for Poland. Nonetheless, today's business survey results pose a downside risk to our forecast of industrial production growth rate in Poland to 2.2% YoY in October from 5.6% in September.

It is worth emphasizing that the slowdown of industrial production growth in H2 2019 has been taken into account in our forecast of GDP growth in 2019. Thus, today's reading does not alter our forecast of economic growth in whole 2019 (4.4% YoY vs 5.1% in 2018). Today's worse-than-expected PMI reading is slightly negative for PLN and yields on Polish bonds.

Business survey results for Polish manufacturing negative for PLN

FX rates



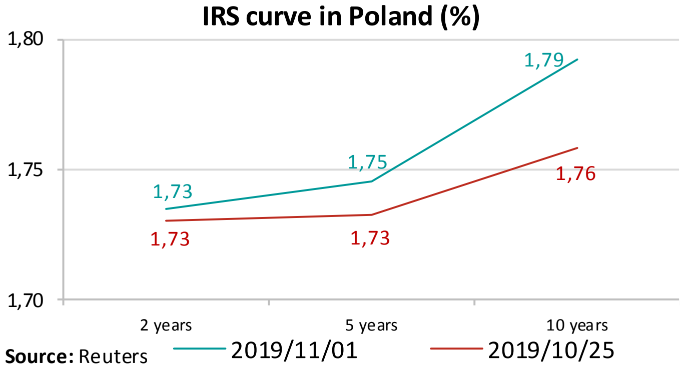
Source: Reuters

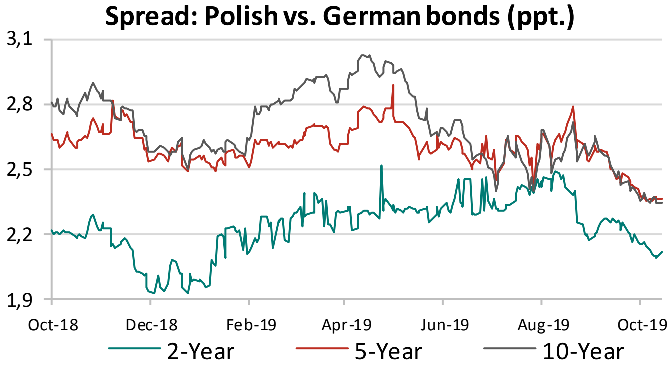
Last week, the EURPLN dropped to 4.2495 (PLN strengthening by 0.7%). Monday through Friday, EURPLN showed a relatively weak downward trend, with PLN slightly making up for the losses from previous weeks, due to higher investors' demand for risk assets. The publication of domestic inflation data that were in line with the expectations was not market moving. The better-from-the-consensus data from the US labour market were also neutral for PLN.

Last week also saw EUR strengthening vs. USD. The hawkish tone of the conference after the FOMC meeting led to only a temporary decrease in EURUSD. Consequently, last week also saw PLN strengthening vs. USD. Due to higher demand for risk assets, PLN was also appreciating vs CHF. PLN also slightly appreciated vs. GBP, due to a slight decrease in EURGBP (related to some investors' expectations of a final settlement of the Brexit issue after the British Parliament decided to hold snap election) and the aforementioned decrease in EURPLN.

The Polish manufacturing PMI released this morning is slightly negative for PLN. Crucial for PLN this week will be the MPC meeting. However, we believe that its impact on PLN will be limited. Data from the US (non-manufacturing ISM, preliminary University of Michigan Index) and on the Chinese balance on trade will also be neutral for PLN.

Market focused on MPC meeting





Source: Reuters

Last week, 2-year IRS rates have not changed compared to the level from two weeks ago and amounted to 1.73, 5-year rates rose to 1.75 (up by 2 bp), and 10-year rates to 1.79 (up by 3 bp). The first part of the week saw an increase in IRS rates, following the core markets. Some investors assumed in their strategies that contrary to market expectations FED would not cut interest rates. Consequently, FOMC meeting brought a correction and lower yields on the core markets across the curve, reflected also by a decrease in domestic IRS rates. On Friday the trading in the Polish debt market was suspended due to holiday.

The PMI released this morning for Polish manufacturing may support a slight decrease in IRS rates. This week the market will focus on the MPC meeting. We expect its impact on the curve to be limited. Also the US data (non-manufacturing ISM, preliminary University of Michigan Index) are not likely to have any significant impact on IRS rates.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland														
Indicator	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-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*	4,34	4,29	4,29	4,26	4,30	4,30	4,28	4,28	4,24	4,29	4,38	4,37	4,26	**4,28**
USDPLN*	3,84	3,79	3,74	3,72	3,79	3,84	3,82	3,83	3,73	3,87	3,98	4,01	3,82	**3,82**
CHFPLN*	3,80	3,79	3,81	3,74	3,79	3,85	3,75	3,83	3,82	3,90	4,02	4,02	3,87	**3,89**
CPI inflation (%YoY)	1,8	1,3	1,1	0,7	1,2	1,7	2,2	2,4	2,6	2,9	2,9	2,6	**2,6**	
Core inflation (%YoY)	0,9	0,7	0,6	0,8	1,0	1,4	1,7	1,7	1,9	2,2	2,2	2,4	**2,5**	
Industrial production (%YoY)	7,4	4,6	2,8	6,0	6,9	5,5	9,2	7,6	-2,6	5,8	-1,5	5,5	**2,2**	
PPI inflation (%YoY)	3,2	2,8	2,1	2,2	2,9	2,5	2,6	1,4	0,5	0,5	0,9	0,9	**0,7**	
Retail sales (%YoY)	9,7	8,2	4,7	6,6	6,5	3,1	13,6	7,3	5,3	7,4	6,0	5,3	**4,0**	
Corporate sector wages (%YoY)	7,6	7,7	6,1	7,5	7,6	5,7	7,1	7,7	5,3	7,4	6,8	6,6	**6,3**	
Employment (%YoY)	3,2	3,0	2,8	2,9	2,9	3,0	2,9	2,7	2,8	2,7	2,6	2,6	**2,6**	
Unemployment rate* (%)	5,7	5,7	5,8	6,1	6,1	5,9	5,6	5,4	5,3	5,2	5,2	5,1	**5,1**	
Current account (M EUR)	-447	113	-1528	2529	-630	217	357	379	-310	-797	-606	**-615**		
Exports (%YoY EUR)	14,7	9,3	-0,5	5,9	10,5	7,8	9,4	11,6	-3,1	7,7	0,2	**9,0**		
Imports (%YoY EUR)	19,3	10,3	0,2	2,1	8,4	2,8	7,7	10,1	-4,7	8,4	-2,5	**7,7**		

*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	4,3	4,0	3,8	3,7	3,2	3,2	5,1	4,4	3,5
Private consumption (%YoY)	3,9	4,4	4,6	4,4	4,5	4,3	3,9	3,5	4,3	4,3	4,1
Gross fixed capital formation (%YoY)	12,6	9,0	8,1	6,8	5,2	5,7	4,1	4,3	8,9	8,5	4,7
Export - constant prices (%YoY)	5,9	3,9	5,5	4,9	4,2	4,1	4,2	4,4	7,0	5,0	4,2
Import - constant prices (%YoY)	5,0	4,3	5,9	5,0	7,2	6,3	5,5	5,0	7,6	5,1	6,0
GDP growth contributions: Private consumption (pp)	2,4	2,5	2,7	2,2	2,8	2,5	2,3	1,8	2,5	2,5	2,3
GDP growth contributions: Investments (pp)	1,6	1,5	1,5	1,7	0,7	1,0	0,8	1,1	1,6	1,5	0,9
GDP growth contributions: Net exports (pp)	0,7	0,0	0,0	0,1	-1,4	-1,0	-0,6	-0,2	0,0	0,2	-0,8
Current account (% of GDP)***	-0,3	-0,1	0,0	-0,1	-0,8	-1,1	-1,2	-1,3	-0,6	-0,1	-1,3
Unemployment rate (%)**	5,9	5,3	5,1	5,6	5,8	5,2	5,1	5,5	5,8	5,6	5,5
Non-agricultural employment (%YoY)	0,0	0,2	0,1	0,1	-0,1	-0,1	-0,2	-0,3	0,9	0,1	-0,2
Wages in national economy (%YoY)	7,1	7,0	7,3	7,5	8,4	8,1	7,7	8,0	7,2	7,2	8,1
CPI Inflation (%YoY)*	1,2	2,4	2,8	2,7	3,3	2,1	1,5	1,3	1,6	2,3	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	4,37	4,32	4,32	4,32	4,29	4,27	4,29	4,32	4,27
USDPLN**	3,84	3,73	4,01	3,86	3,86	3,79	3,67	3,56	3,74	3,86	3,56

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST* CA	FORECAST* CONSENSUS**
		Monday 11/04/2019				
9:00	**Poland**	**Manufacturing PMI (pts)**	**Oct**	**47,8**	**48,3**	**48,1**
9:55	Germany	Final Manufacturing PMI (pts)	Oct	41,9	41,9	41,9
10:00	Eurozone	Final Manufacturing PMI (pts)	Oct	45,7	45,7	45,7
10:30	Eurozone	Sentix Index (pts)	Nov	-16,8		-13,8
16:00	USA	Factory orders (% MoM)	Sep	-0,1	-0,2	-0,5
		Tuesday 11/05/2019				
11:00	Eurozone	PPI (% YoY)	Sep	-0,8		-1,2
16:00	USA	ISM Non-Manufacturing Index (pts)	Oct	52,6	53,6	53,4
		Wednesday 11/06/2019				
8:00	Germany	New industrial orders (% MoM)	Sep	-0,6		0,1
10:00	Eurozone	Services PMI (pts)	Oct	51,8	51,8	51,8
10:00	Eurozone	Final Composite PMI (pts)	Oct	50,2	50,2	50,2
11:00	Eurozone	Retail sales (% MoM)	Sep	0,3		0,1
	Poland	**NBP rate decision (%)**	**Nov**	**1,50**	**1,50**	**1,50**
		Thursday 11/07/2019				
8:00	Germany	Industrial production (% MoM)	Sep	0,3		-0,4
13:00	UK	BOE rate decision (%)	Nov	0,75	0,75	0,75
		Friday 11/08/2019				
8:00	Germany	Trade balance (bn EUR)	Sep	18,1		18,1
16:00	USA	Wholesale inventories (% MoM)	Sep	-0,3		-0,3
16:00	USA	Wholesale sales (% MoM)	Sep	0,0		
16:00	USA	Initial U. of Michigan Sentiment Index (pts)	Nov	95,5	95,5	96,0
	China	Trade balance (bn USD)	Oct	39,7		40,8

*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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