This week

- **The most important event this week will be the FOMC meeting scheduled for Wednesday.** We expect that FED will leave the target range for the Federal Reserve funds rate unchanged at [1.50%; 1.75%] this week. In our view, J. Powell will say during the conference after the meeting that, after the monetary easing in 2019, FED will now continue the wait-and-see policy. The markets will focus on information about the US monetary policy in the horizon of several months. We believe that the FED chairman will maintain his view that subsequent rate hikes would be possible in the event of a marked change of FOMC expectations concerning the macroeconomic outlook. He is likely to indicate the signing of the US-China deal as a factor justifying leaving interest rates at an unchanged level in the nearest future. The stabilization of interest rates by FOMC this week is in line with the market consensus and has been fully priced in by forward contracts. Thus, the conference after the meeting should not have any substantial impact on PLN and yields on Polish bonds. Our baseline scenario assumes that FED will cut interest rates by 25bp in Q2 2020 in reaction to the expected economic slowdown. The market is now pricing in one rate cut in 2020.
- **Important data from the US will be released this week**. The publication of the flash estimate of GDP in Q4 is scheduled for Thursday. We expect that the annualized economic growth rate rose to 2.2% vs. 2.1% in Q3, due to higher contributions of investments and net exports. A lower contribution of consumption will have opposite impact. We forecast that preliminary durable goods orders decreased by 0.1% MoM in December vs. a 2.1% decrease in November, due to low orders in the transport sector. We expect that the Conference Board Consumer Confidence Index (128.5 pts vs. 126.5 pts in December), like the final University of Michigan Index (99.1 pts vs. 91.3 pts), will indicate good households' sentiment in January. We believe that the publication of US data should not be market moving.
- **This week we will see important data from the Eurozone.** We expect that the quarterly GDP growth rate rose to 0.3% in Q4 from 0.2% in Q3. The results of business surveys (PMI) for October-December pose a downside risk to our forecast. In addition, we forecast that HICP inflation rose to 1.4% in January vs. 1.3% in December. Higher dynamics of energy prices were only partly offset by lower core inflation. We believe that the materialization of our forecast of GDP in the Eurozone, being higher from the consensus (0.2%), will be conducive to PLN weakening and higher yields on Polish bonds, while the publication of data on inflation is not likely to meet with a significant reaction of the market.
- **Ifo Index reflecting the sentiment among German managers representing the manufacturing, construction, wholesale and retail trade sectors was released today.** The index value will increase to 95.9 pts in January vs. 96.3 pts in December.
- **The January CLFP PMI for Chinese manufacturing will be released on Friday.** The market expects that the index has dropped to 50.0 pts vs. 50.2 pts in December. The index will reflect investors' concerns about the spreading of 2019-nCov virus in China on the economic activity in this country. However the scale of the index decline will be small due to the data of the survey (before the number of the infected persons has visibly increased). We believe that the publication will be neutral for the financial markets.
- **The estimate of GDP in Poland for 2019 will be released on Wednesday.** We expect that the GDP growth rate amounted to 4.2% YoY vs. 5.1% in 2018. Due to markedly lower-than-expected December data on construction-assembly production and industrial production, we see a slight downside risk to our forecast. The materialization of such risk would be negative for PLN and yields on Polish bonds.

Last week

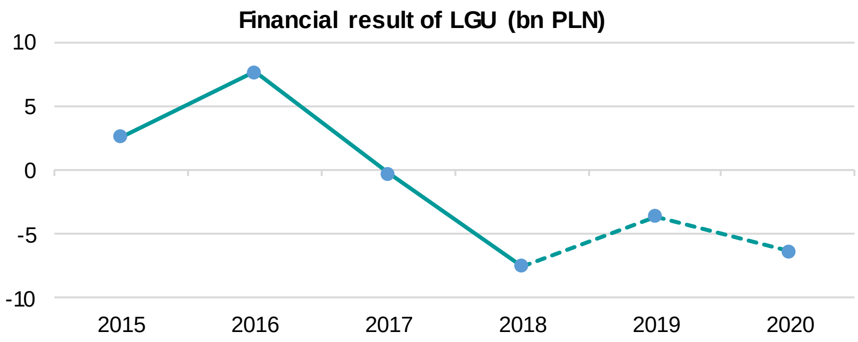
- **In accordance with flash data, the Composite PMI (for manufacturing and the service sector) in the Eurozone has not changed in January compared to December and amounted to 50.9 pts, running below the market expectations equal to our forecast (51.2 pts).** The stabilization of the Composite PMI resulted from higher sub-index for manufacturing output and lower sub-index for business activity in services. This is consistent with our assessment formulated in recent months, that the historically important differences between these sectors were short-lived and subsequent months might see deterioration in services in the wake of weaker sentiment in manufacturing (see MACROmap of 28/10/2019). Noteworthy in the data structure is an increase in the sub-index for the expected economic activity in a year's time which has reached the highest value in 16 months. According to the statement, this increase resulted mainly from better sentiment among the manufacturers who believe that the worst phase of the ongoing slowdown is already over. Geographically, a slight improvement was recorded in Germany, while the situation in France and in other economies covered by the survey has deteriorated. From the perspective of Polish exports, of particular importance is the sentiment in German manufacturing. German manufacturing PMI rose to 45.2 pts in January vs. 43.7 pts in December, hitting the highest level since February 2019. Nonetheless, the index has for 13 months now stayed below the 50 pts threshold, diving expansion from contraction of activity. Conducive to the index increase were higher contributions of four of its five sub-indices (for new orders, output, employment, and suppliers' delivery times), while lower contribution of the inventories sub-index had opposite impact. It is worth noting that the pace of the decrease in total orders and export orders in German manufacturing was at the lowest in more than a year. This is consistent with the view of the surveyed companies, which believe that the worst phase of the slowdown is over now and they expect an increase of activity in a year's horizon. The results of the business surveys in the Eurozone pose a downside risk to our forecast in which the quarterly GDP growth rate in the single currency area will not change in Q1 compared to Q4 and will amount to 0.3%.
- **The ECB meeting was held last week**. As we expected, the monetary policy parameters in the Eurozone have been left unchanged. The text of the statement repeated the provision from the month before saying that the ECB expected the key ECB interest rates to remain at their present or lower levels until it has seen the inflation outlook robustly converge to a level sufficiently close to, but below, 2% within its projection horizon, and such convergence has been consistently reflected in underlying inflation dynamics. Like the month before, the Council expects that the purchase of assets at the scale of EUR 20bn a month will be continued for as long "necessary to reinforce the accommodative impact of its policy rates, and to end shortly before it starts raising the key ECB interest rates". During the conference after the meeting, the Governor of the ECB, Ch. Lagarde, said that there were some signs of a moderate increase in inflationary pressure, which was in line with the ECB expectations. She pointed out at the same time that the risk to the outlook for economic growth in the Eurozone resulting from the situation in global trade had recently diminished. The ECB also announced the launch of a review of its monetary policy strategy. According to the statement the review covers: quantitative formulation of price stability, monetary policy toolkit, economic and monetary analyses and communication practices. The scope of the review will also encompass other considerations, such as financial stability, employment and environmental sustainability. In accordance with the statement, the review is expected to be concluded by end of 2020. Therefore, we do not expect it to have any impact whatsoever on the ECB monetary policy. Our baseline scenario assumes that the ECB will continue the quantitative easing program (QE2) until March 2002 and will cut the deposit rate by 10bp in June 2020. The slightly dovish tone of the conference after the ECB meeting has led to a slight depreciation of EUR vs. USD.

- **The dynamics of industrial production in Poland increased to 3.8% YoY in December vs. 1.4% in November**. Seasonally adjusted industrial production decreased by 2.9% MoM vs. a 1.5% increase in November, marking the sharpest monthly decline since December 2013. The main source of the increase of annual production growth between November and December was the statistical effect in the form of a favourable difference in the number of working days. Conducive to higher industrial production dynamics in December compared to November was also a sharp production increase in the category “other transport equipment” (see MACROpulse of 22/1/2020). Noteworthy in the data structure is a decrease in the production dynamics in some segments responsible for the supply of raw and other materials used in construction projects. In our view, this points to an increasing negative impact of the slowdown in domestic construction on Polish manufacturing activity. This view is supported by the last week’s data on construction-assembly production, which dropped by 3.3% YoY in December vs. a 4.7% decrease in November. Seasonally-adjusted construction-assembly production decreased by 3.5% MoM in December. The structure of data on construction-assembly production suggests that the main source of the decline in the construction activity is the end of cycle in public investments (see MACROpulse of 21/1/2020). We maintain our economic growth scenario which assumes that GDP dynamics will decrease to 3.3% YoY in Q1 vs. 3.5% in Q4.
- **Retail sales in the Polish sector of enterprises increased in current prices by 7.5% YoY in December vs. a 5.9% increase in November**. The sales dynamics in constant prices increased to 5.7% in December vs. 5.2% in November. The acceleration in retail sales growth in December was wide ranging and was recorded in eight out of nine categories, most likely due to the statistical effect in the form of a favourable difference in the number of working days (see MACROpulse of 23/1/2020). The core sales measures we use, i.a. retail sales excluding cars, food and fuels, point to further recovery in consumer demand. We estimate that in the whole Q4 2019 retail sales in constant prices increased by 5.2% vs. a 4.8% increase in Q3, not altering our forecast in which the growth rate of private consumption dropped to 3.8% YoY in Q4 2019 vs. 3.9% YoY in Q3.
- **Nominal wage dynamics in the sector of enterprises employing above 9 people increased to 6.2% YoY in December vs. 5.3% in November**. In December, the three-month rolling average for the annual nominal wage dynamics in enterprises amounted to 5.8%, hitting the lowest level since July 2017. This strongly supports our view that the decreasing capacity utilization and increasingly conservative wage policy of companies responding to unfavourable regulatory changes in the Polish labour market have had a growing negative influence on nominal wage dynamics in recent months (see MACROpulse of 21/1/2020). The results of an annual survey of the wage and employment plans of companies in 2020, published yesterday by Grant Thornton, also point to a sustained downward trend in annual wage growth. They indicate a sharp decline (to 5-year low) of the percentage of small and medium-size companies planning real pay increase in 2020. This is in line with our scenario of stable wage dynamics in the whole economy in 2020 despite the sharp increase in the minimum wage (see MCROmap of 20/1/2020). The employment dynamics in December have not changed compared to November and amounted to 2.6% YoY. Consequently, the real wage fund growth rate (the employment times the average salary) in enterprises increased to 5.4% YoY in December vs. 5.3% in November. In Q4 2019 the real wage fund rose by 5.5% YoY, showing the lowest dynamics since Q4 2015. The last week’s data strongly support our forecast assuming that in 2020 the sector of enterprises will see stabilization of wages, given a simultaneous stagnation of employment.
- **ZEW index reflecting the sentiment among analysts and institutional investors regarding the economic situation in Germany rose to 26.7 pts in January vs. 10.7 pts in December 2014, running significantly above the market expectations (15.0 pts)**. Thus, the index has reached the highest level since July 2015. According to the statement, the main factor behind the index sharp growth was improved sentiment of survey participants resulting from partial de-escalation of the US-China trade war. We forecast that the quarterly German GDP growth rate

will rise to 0.1% in Q1 vs. 0.1% in Q4.

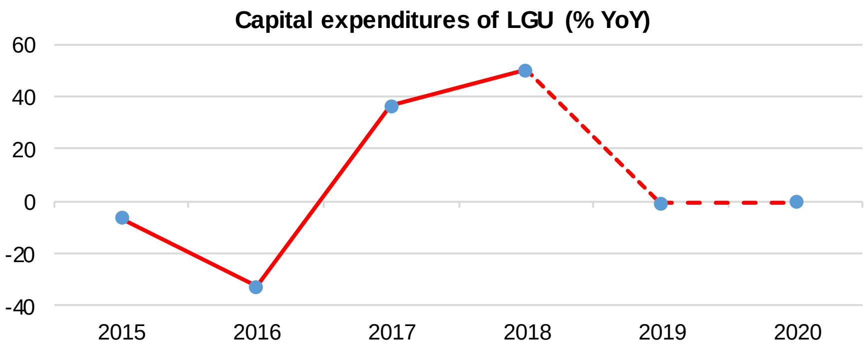
No slump in sight for investments of LGU?

In accordance with a statement of the Ministry of Finance, total income of the local government units (LGU) for the January-November 2019 period amounted to PLN 252.8bn while total expenditure equaled PLN 241.5bn. This means that after 11 months of 2019, LGU budgets recorded a surplus of PLN 11.4bn. Assuming that LGU incomes and expenditures were growing at the same pace in December as in the January-November period, i.e. by 9.9% and 8.0% YoY, respectively, LGU will record a deficit of PLN 3.7bn at the end of 2019. Below we are presenting our expectations concerning LGU incomes and expenditure in 2020 and estimate the impact of these values, for investment expenditure in particular, on the economic growth rate in 2020.



Source: Ministry of Finance, Credit Agricole

This year is especially difficult from the point of view of balancing LGU budgets due to changes in the economic policy. On the one hand, their incomes will be limited i.a. by lower PIT rates (including total exemption of young people from income tax). On the other hand, LGU expenditures will increase i.a. due to the sharp increase in the minimum wage. The second factor is reflected by the LGU-forecast increase in current expenditure (ca. 15% YoY) in 2019. In accordance with the available forecasts of total expenditure and income of individual LGU, the balance of LGU budgets can be expected to visibly deteriorate – forecast is a total deficit amounting to ca. PLN 18bn. However, looking at the last few years, we can see that the aforementioned LGU forecasts were usually overly pessimistic – overestimating the deficit in local governments compared to later execution. Allowing for this error, we estimate that the balance of LGU budgets will amount to ca. PLN -6bn in 2019. Taking such result into account, we forecast that the deficit of the public finance sector will amount to 1.4% of GDP in 2020.



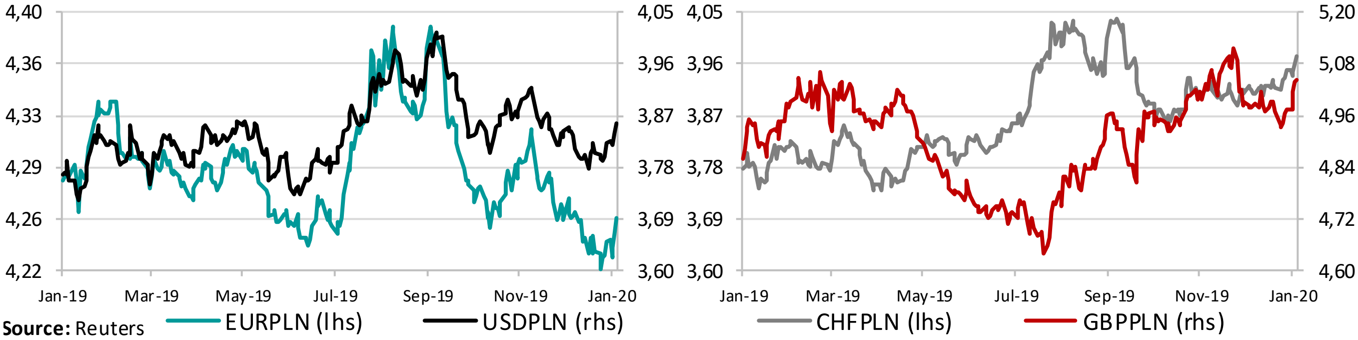
Source: Ministry of Finance, Credit Agricole

From the point of view of LGU functioning on the GDP growth rate, much more important from the budget balance is the profile of capital expenditures, i.e. mainly investments. Due to a high volatility between respective years, they may have a substantial impact on the trajectory of economic growth. Based on the available data on LGU fixed capital formation for the three quarters of 2019 and construction-assembly production for Q4, we estimate that LGU capital investments decreased by 1.0% YoY in 2019 vs. a 50.2% increase in 2018. This is the effect of the end of the investment peak resulting from municipal elections. In accordance with the latest forecasts of individual LGUs, it can be estimated that 2020 will record a stable level of capital expenditures in YoY terms.

When formulating our last quarterly macroeconomic forecast (see MACROmap of 9/12/2019), we were assuming that 2020 would see a marked decline in LGU investments. The since published LGU budget plans referred to above signal a marked upside risk to such scenario. This would mean that LGU fixed capital formation will be conducive to a faster economic growth (compared to our earlier expectations). However, it should be pointed out that the December data on constriction-assembly production and industrial production stood markedly below our expectations, thus suggesting a marked slowdown of growth in Q4 2019 as well as most likely a lower economic growth path in the whole 2020. We estimate that the influence of the aforementioned two opposite factors (the stabilization of LGU investments and the slowdown signaled in monthly data) on GDP dynamics will eliminate each other in 2020. Therefore, we maintain our forecast of the economic growth rate in 2020 at a level of 3.0% YoY.

Data on GDP in Poland and the Eurozone negative for PLN

FX rates



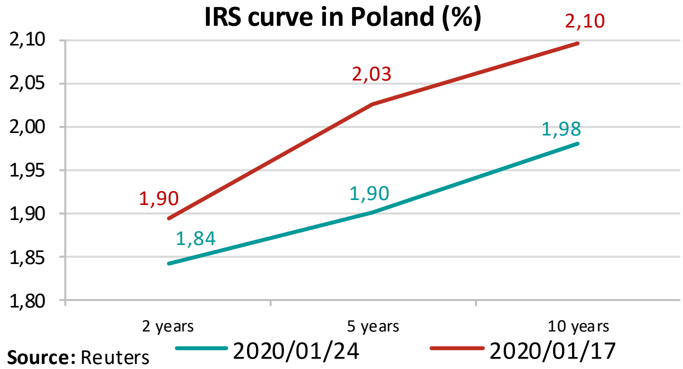
Source: Reuters

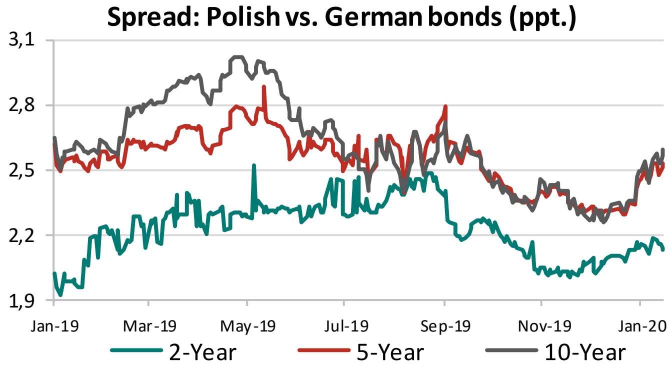
Last week, the EURPLN exchange rate rose to 4.2571 (PLN weakening by 0.4%). The beginning of last week saw a slight appreciation of PLN vs. EUR. It was a correction after the weakening of PLN observed two weeks ago (see MACROpulse of 20/1/2020). In the following days EURPLN resumed the upward trend, supported by increased global risk aversion reflected by higher VIX index. Numerous domestic readings had no substantial impact on PLN. On Friday PLN was highly volatile following the publication of flash PMIs for the Eurozone.

Last week, like two weeks ago, EURUSD was showing a downward trend. On Thursday an additional factor supporting EUR depreciation vs. USD was a slightly dovish – in the investors' view – tone of the conference after the ECB meeting. Last week saw further appreciation of CHF. EUR depreciation vs. CHF is supported by the prospect of further monetary policy easing by the ECB. Recently, conducive to CHF appreciation has also been the decision of the US Treasury Department from two weeks ago to add Switzerland to its watch list of countries manipulating the exchange rate. Some investors may see it as an increased likelihood of the SNB limiting currency interventions in the future. Consequently they may play for further CHF appreciation. Last week we saw data indicating that despite being added to the watch list, the SNB has increased the scale of the intervention in the foreign exchange market. Although the publication resulted in a slight depreciation of CHF, it has not succeeded in sustainably reversing the downward trend observed for EURCHF in recent weeks.

Crucial for PLN this week will be the data on GDP in Poland and in the Eurozone. We believe that they may lead to PLN depreciation. US data (first estimate of GDP in Q4, Conference Board Index and final University of Michigan Index), preliminary inflation in the Eurozone, CLFP PMI for Chinese manufacturing and Ifo index for Germany will not be market moving. The FOMC meeting will also be neutral for PLN. On the other hand, investors will focus on the meeting of the Bank of England. If our scenario assuming interest rates cut in the United Kingdom materializes, we may see GBP depreciation vs. EUR. This week, an increased risk aversion in the foreign exchange market may be supported by concerns about the spread of 2019-nCov virus on the economic activity in China. Higher uncertainty in the markets may be conducive to PLN depreciation.

Domestic data on GDP may lead to lower IRS rates





Source: Reuters

Last week, 2-year IRS rates decreased to 1.84 (down by 6bp), 5-year rates to 1.90 (down by 13bp), and 10-year rates to 1.98 (down by 12bp). Throughout the previous week, a drop in IRS rates was observed across the curve following the core markets. This was a correction after their marked increase two weeks ago in reaction to the partial de-escalation of the US-China trade war. Numerous domestic readings and publication of flash PMIs for major European economies had no substantial impact on the curve. On the other hand, conducive to lower IRS rates was a successful debt auction, at which the Ministry of Finance sold PLN 6.0bn of 2-, 4-, 5-, 9-, and 27-year bonds with demand amounting to PLN 10.2bn.

This week the market will focus on the publication of data on the Polish GDP. We believe that it may contribute towards a fall of IRS rates. In turn, the publication of data on GDP in the Eurozone may have opposite impact. In our view, the FOMC meeting as well as the publication of data from the US (first estimate of GDP in Q4, Conference Board Index, and final University of Michigan Index), preliminary inflation in the Eurozone and Ifo Index for Germany will not have any substantial impact on IRS rates.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland														
Indicator	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	Jan-20
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*	4,29	4,26	4,30	4,30	4,28	4,28	4,24	4,29	4,38	4,37	4,26	4,31	4,26	4,27
USDPLN*	3,74	3,72	3,79	3,84	3,82	3,83	3,73	3,87	3,98	4,01	3,82	3,91	3,79	3,81
CHFPLN*	3,81	3,74	3,79	3,85	3,75	3,83	3,82	3,90	4,02	4,02	3,87	3,91	3,92	3,90
CPI inflation (% YoY)	1,1	0,7	1,2	1,7	2,2	2,4	2,6	2,9	2,9	2,6	2,5	2,6	3,4	
Core inflation (% YoY)	0,6	0,8	1,0	1,4	1,7	1,7	1,9	2,2	2,2	2,4	2,4	2,6	3,1	
Industrial production (% YoY)	2,8	6,0	6,9	5,5	9,2	7,6	-2,6	5,8	-1,5	5,5	3,7	1,5	3,8	
PPI inflation (% YoY)	2,1	2,2	2,9	2,5	2,6	1,4	0,5	0,5	0,9	0,8	-0,3	-0,1	1,0	
Retail sales (% YoY)	4,7	6,6	6,5	3,1	13,6	7,3	5,3	7,4	6,0	5,3	5,4	5,9	7,5	
Corporate sector wages (% YoY)	6,1	7,5	7,6	5,7	7,1	7,7	5,3	7,4	6,8	6,6	5,9	5,3	6,2	
Employment (% YoY)	2,8	2,9	2,9	3,0	2,9	2,7	2,8	2,7	2,6	2,6	2,5	2,6	2,6	
Unemployment rate* (%)	5,8	6,1	6,1	5,9	5,6	5,4	5,3	5,2	5,2	5,1	5,0	5,1	5,2	
Current account (M EUR)	-1528	2529	-630	217	542	430	-114	-915	-246	962	573	1457		
Exports (% YoY EUR)	-0,5	5,9	10,5	7,8	9,6	11,5	-2,6	5,9	-1,8	13,5	3,8	-1,0		
Imports (% YoY EUR)	0,2	2,1	8,4	2,8	8,0	11,1	-5,4	6,9	-3,4	6,4	-0,2	-4,6		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland												
Indicator	2019				2020				2019	2020	2021
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)	4,8	4,6	3,9	3,5	3,3	3,2	2,7	2,7	4,2	3,0	3,3
Private consumption (% YoY)	3,9	4,4	3,9	3,8	3,4	3,6	3,4	3,0	4,0	3,3	3,0
Gross fixed capital formation (% YoY)	12,2	9,1	4,7	2,7	3,1	1,9	1,5	1,7	6,0	1,9	5,0
Export - constant prices (% YoY)	7,3	3,2	5,0	4,9	4,2	4,1	4,2	4,4	5,1	4,2	5,3
Import - constant prices (% YoY)	6,0	3,1	3,9	3,9	3,6	3,5	3,3	3,0	4,2	3,4	4,0
GDP growth contributions: Private consumption (pp)	2,5	2,5	2,2	1,9	2,1	2,1	2,0	1,5	2,3	1,9	1,7
GDP growth contributions: Investments (pp)	1,5	1,5	0,8	0,7	0,4	0,3	0,3	0,4	1,1	0,3	0,9
GDP growth contributions: Net exports (pp)	1,0	0,2	0,8	0,7	0,5	0,5	0,6	0,8	0,6	0,6	0,6
Current account (% of GDP)***	-0,6	-0,4	0,2	0,6	0,4	0,3	0,2	0,1	0,6	0,1	-0,2
Unemployment rate (%)**	5,9	5,3	5,1	5,2	5,5	5,0	5,0	5,3	5,2	5,3	5,5
Non-agricultural employment (% YoY)	0,0	0,2	0,5	0,1	-0,1	-0,1	-0,2	-0,3	0,2	-0,2	-0,5
Wages in national economy (% YoY)	7,1	7,0	7,7	7,0	7,5	7,6	7,4	7,0	7,2	7,4	6,0
CPI Inflation (% YoY)*	1,2	2,4	2,8	2,8	4,2	3,1	2,4	2,1	2,3	2,9	2,0
Wibor 3M (%)**	1,72	1,72	1,72	1,71	1,71	1,71	1,71	1,71	1,71	1,71	1,71
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	4,26	4,29	4,29	4,29	4,29	4,26	4,29	4,25
USDPLN**	3,84	3,73	4,01	3,79	3,83	3,73	3,64	3,70	3,79	3,70	3,76

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST* CA	FORECAST* CONSENSUS**
		Monday 01/27/2020				
10:00	Germany	Ifo busienss climate (pts)	Jan	96,3	96,4	97,0
16:00	USA	New home sales (k)	Dec	719	726	728
		Tuesday 01/28/2020				
14:30	USA	Durable goods orders (% MoM)	Dec	-2,1	-0,1	0,8
15:00	USA	Case-Shiller Index (% MoM)	Nov	0,4		0,4
16:00	USA	Richmond Fed Index	Jan	-5,0		
16:00	USA	Consumer Confidence Index	Jan	126,5	128,5	128,0
		Wednesday 01/29/2020				
10:00	**Poland**	**Annual GDP (% YoY)**	**2019**	**5,1**	**4,2**	**4,2**
10:00	Eurozone	M3 money supply (% MoM)	Dec	5,6		5,5
20:00	USA	FOMC meeting (%)	Jan	1,75	1,75	1,75
		Thursday 01/30/2020				
11:00	Eurozone	Business Climate Indicator (pts)	Jan	-0,25		-0,20
11:00	Eurozone	Unemployment rate (%)	Dec	7,5		7,5
13:00	UK	BOE rate decision (%)	Jan	0,75	0,50	0,75
14:00	Germany	Preliminary HICP (% YoY)	Jan	1,5	1,8	1,7
14:30	USA	Preliminary estimate of GDP (% YoY)	Q4	2,1	2,2	2,1
14:30	USA	Initial jobless claims (k)	w/e	211		211
		Friday 01/31/2020				
2:00	China	Caixin Manufacturing PMI (pts)	Jan	50,2		50,0
11:00	Eurozone	Preliminary GDP (% QoQ)	Q4	0,2	0,3	0,2
11:00	Eurozone	Preliminary HICP (% YoY)	Jan	1,3	1,4	1,4
14:30	USA	Real private consumption (% MoM)	Dec	0,3		
15:45	USA	Chicago PMI (pts)	Jan	48,9		48,8
16:00	USA	Final U. of Michigan Sentiment Index (pts)	Jan	99,1	99,1	99,3

*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

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