A Nike-shaped recovery of GDP growth in Poland

This week

- **The second round of presidential election in Poland will take place on Sunday**. The polls carried out in recent days point to a growing support for R. Trzaskowski. Due to similar support showed by the polls for A. Duda and R. Trzaskowski, the result of the coming election is now difficult to foresee. If R. Trzaskowski wins, we will see a slight increase in the uncertainty about the shape of the fiscal policy in the medium term. However, the materialization of such scenario will not have any significant impact on PLN.
- **Non-manufacturing ISM will be released in the US on Monday and in accordance with our forecast will increase to 48.5 pts in June vs. 45.4 pts in May.** A slower decrease in non-manufacturing activity has already been signaled earlier by regional business surveys for services. The improvement was supported by the lifting of the restrictions aimed at containing the COVID-19 epidemic in some states. We expect that the publication will not be market moving.
- **Data on orders in German manufacturing will be released today.** They increased by 10.4% MoM in May vs. a 26.2% decrease in April, running below the market expectations (+15.0%). The increase in total orders resulted from an increase in both domestic and foreign orders. We forecast that the German GDP will decrease by 6.1% in 2020 vs. a 0.5% increase in 2019 and will increase by 5.0% in 2021.

Last week

- **In accordance with the flash estimate, CPI inflation in Poland rose to 3.3% YoY in June vs. 2.9% in May, running clearly above the market expectations equal to our forecast (2.8%)**. GUS 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". On this basis we believe that the main source of the surprise was a marked increase in core inflation which in accordance with our expectations rose to 4.1% YoY vs. 3.8% in May. Most likely its increase resulted from the fact that some companies were transferring the costs of meeting the increased security requirements caused by the pandemic to consumers. In May such phenomenon was already signaled by a sharp increase in the dynamics of the prices of hairdressing, beauty treatment, personal care, medical and dental services (see MACROpulse of 15/6/2020).The increase in inflation resulted also from higher dynamics of fuel prices (-19.3% YoY in June vs. -23.4% in May), due to the recently observed increase in global oil prices. Lower dynamics of the prices of food and non-alcoholic beverages (5.8% YoY in June vs. 6.2% in May – mainly due to last year's high base effects for the prices of meat and vegetables) and of energy (5.1% YoY in June vs. 5.2% in May). We expect that subsequent months will bring a decrease in inflation. It will result from lower dynamics of food prices and lower core inflation. Nonetheless, the last week's data pose an upside risk to our forecast, in which inflation in the whole 2020 will rise to 3.6% YoY vs. 2.3% in 2019.
- **Polish manufacturing PMI rose to 47.2 pts in June vs. 40.6 pts in May**. The index increase resulted from higher contributions of 4 of its 5 sub-indices (for new orders, output, employment, and inventories), while lower contribution of suppliers' delivery times had opposite impact. However, it is worth noting that lower contribution of suppliers' delivery times means shorter delivery times, which in the present situation points to a gradual restoration of the supply chains that have been broken by the pandemic. Noteworthy in the data structure is further decrease in new orders, including new export orders, which, in our view, indicates that capacity utilization in Polish manufacturing will not return to pre-pandemic levels yet for a long time. In turn, low capacity utilization will limit the room for investment growth in subsequent quarters (see MACROpulse of 1/7/2020). The last week's data point to continuing negative

impact of the COVID-19 epidemic on Polish manufacturing activity, although some effects of its gradual unfreezing can already be seen. The average PMI value amounted to 39.9 pts in Q2 vs. 46.0 pts in Q1. The business survey results support our forecast of GDP dynamics in Q2 (-10.5% YoY vs. 2.0% in Q1). At the same time, the data structure pointing to further decrease in new orders is consistent with our forecast in which the Polish GDP will reach the pre-pandemic level no sooner than in H1 2022.

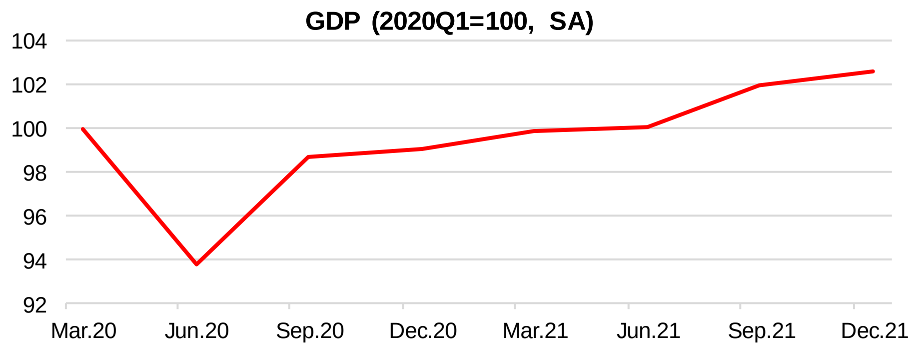
- **China Caixin manufacturing PMI rose to 51.2 pts in June vs. 50.7 pts in May, running above the market expectations (50.5 pts).** Further recovery in Chinese manufacturing was also pointed by CFLP PMI which stood at 50.9 pts in June vs. 50.6 pts. The increase in Caixin PMI resulted from higher contributions of three of its five sub-indices (for new orders, inventories, and suppliers' delivery times) while lower contributions of the sub-indices for output and employment had opposite impact. Especially noteworthy in the data structure is a sharp increase in the sub-index concerning new orders, which returned above the 50 pts threshold dividing expansion from contraction of activity, while the sub-index for new export orders continues to stand below the level of 50 pts. This shows that the source of the recovery currently observed in Chinese manufacturing is internal demand. Such data structure is consistent with our scenario, in which in the coming quarters the recovery in global trade will be slow.
- **China Caixin PMI for services rose to 58.4 pts in June vs. 55.0 pts in May, running clearly above the market expectations (50.5 pts)**. At the same time it reached the highest value in 10 years. The fast rate of increase in services was also indicated by CLFP PMI which rose to 54.4 pts in June vs. 53.6 pts. Coupled with the business survey results for Chinese manufacturing, the data indicate that the economic recovery in China is stronger than we had expected. Thus the data pose an upside risk to our forecast in which the Chinese GDP will increase by 3.0% in 2020. Possible imposition of subsequent US economic sanctions on China continues to be the source of uncertainty for the outlook for the recovery of economic growth in this country. However, we believe that even if such scenario materializes, the economic recovery in China will be continued.
- **According to the flash estimate, inflation in the Eurozone rose to 0.3% YoY in June vs. 0.1% in May, running above the market consensus (0.1%) and our forecast (0.2%).** The increase in inflation resulted from higher dynamics of energy prices, while lower dynamics of food prices had opposite impact. We maintain our scenario, in which from July the Eurozone will see deflation which will continue until Q1 2021. In our view, the main source of the deflation in the Eurozone will be a decrease in core inflation resulting from the deflationary tendencies amid the economic crisis within the single currency area. Consequently, we forecast that in the whole 2020 inflation in the Eurozone will decrease to 0.1% YoY vs. 1.1% in 2019.
- **Last week we saw important data from the US economy.** The number of initial jobless claims decreased last week to 1427k vs 1482k two weeks ago and thus continues to show a downward trend. However it is worth pointing out that it has visibly flattened in June. In other words, redundancies continue and their scale is considerable despite the reopening of the economy and increase in total employment. Last week we also saw data on non-farm payrolls, which rose by 4.8M in June vs. a 2.7M increase in May (revised upwards from 2.5M), running significantly above the market expectations (3.0M). In reaction to the reading, USD temporarily appreciated vs. EUR and yields on US bonds went up (see below). The highest increase in employment was recorded in leisure and hospitality (+2.1M), namely in the sector that was affected the most by the wave of redundancies due to the pandemic (cumulated decline in employment in March and April in this sector exceeded 8M). It is worth noting that increase in employment was recorded in as many as 12 of the 14 sectors. Employment decrease only in mining and logging (-10.0k) and utilities (-3.2k). However, we believe that the employment increase recorded in June resulted mainly from the resumption of activity by the companies whose operations were suspended in previous months due to administrative restrictions and that the situation in the

US labour market continues to be difficult. Hence we expect that the increase in non-farm payrolls will markedly slow down in the coming months. We therefore believe that the Federal Reserve will treat these data with great caution when assessing the economic recovery in the US. Unemployment rate dropped to 11.1% in June vs. 13.3% in May and decreased despite a higher participation rate (up to 61.5% in June from 60.8% in May). June saw further decrease in the dynamics of average hourly earnings to 5.0% vs. 6.6% in May. This is in line with our view presented in recent months that due to COVID-19 jobs were lost by people who were paid relatively low wages sharply boosting the average level of earnings in April and the wage dynamics will be gradually decreasing as these people find employment (see MACROmap of 11/5/2020). The results of business surveys were also released last week. The ISM index for manufacturing rose to 52.6 pts in June vs. 43.1 pts in May. The index increase resulted from higher contributions of 4 of its 5 sub-indices (for output, new orders, employment, and inventories), while lower sub-index for suppliers' delivery times had opposite impact. However, it is worth pointing out that lower contribution of suppliers' delivery times means shorter delivery times, which in the present conditions points to a gradual restoration of supply chains that were broken by the pandemic. The sub-indices for both output and new orders stand way above the 50 pts threshold dividing expansion from contraction of activity which points to a fast pace of the recovery in the US manufacturing. Last week we also saw the Conference Board Index which rose to 98.1 pts in June vs. 85.9 pts in May, running markedly above the market expectations. The significant improvement in the sentiment of US consumers results from a better assessment of both the current and future situation. The last week's data from the US labour market pose an upside risk to our scenario in which the US GDP decreased by -30% in Q2 (in annualized terms) and will decrease by 5.5% in the whole 2020 (see MACROmap of 1/6/2020). However the observed second wave of the COVID-19 pandemic in the US poses a risk to the sustainability of the recovery of US economic growth.

The Minutes of the June FED meeting were released last week. In accordance with the Minutes, the idea of communicating the FED's monetary policy outlook to market participants in a clearer manner (so-called forward guidance) is gaining increasing support among FOMC members. FOMC members were debating on the form of such communication. Many are in favour of directly linking the monetary policy decisions to the incoming data on inflation. Others believe that better solution would be to link the communication to the unemployment level while some members support the communication of a specific date from which market participants could expect the tightening of the FED monetary policy. The issue of possible communication of FED monetary policy outlook through yield curve control was also raised in the discussions. However talks on this issue are still at an initial stage and some FED members are voicing concerns about its applicability, especially in the context of central bank's independence (the central bank's demand for securities with certain maturities can differ from the government's debt management policy). We maintain our FED monetary policy scenario assuming that FED interest rates will stay close to zero at least until the end of 2021. However, the text of the Minutes poses a risk to our scenario in which FED will start controlling yield curve at its short end treating it is as a form of communicating its monetary policy outlook. It is worth noting that the discussion at the June meeting was held amid a dying out coronavirus epidemic in the United State while now there is a second wave of infections.

A Nike-shaped recovery of GDP growth in Poland

The issue of Polish economy recovering from the COVID-19 shock has often been raised in the economic discourse in recent months. The biggest attention was paid to the shape of this recovery – will it be V-shaped (sharp decline in GDP followed by rebound of activity), W-shaped (a sequence of several increases and decreases in GDP), L-shaped (activity staying at a visibly lower level for several quarters after the shock), or U-shaped (a visible rebound of GDP after a prolonged period of low economic activity). Below we present our expectations in this respect.



Source: Credit Agricole

To determine the shape of the economic recovery in Poland, one must calculate a seasonally-adjusted level of GDP. To this end we have used our quarterly forecast (see the table below). We should bear in mind that the seasonal adjustment algorithm is built in such a way that the addition to the sample of new observations (for the period from Q2 2020 to Q4 2021) affects also the past GDP values. In effect, the GDP decline in Q1 2020 currently reported by GUS at 0.4% QoQ, after the addition of new observations has risen – in accordance with our estimations – to 1.8%. We forecast that in Q2 2020 GDP decreased by additional 6.2% QoQ. Then, until the end of 2021 the seasonally adjusted GDP level will be gradually increasing. Consequently, the shape of the economic recovery in Poland after the shock caused by the COVID-19 epidemic will take on a shape resembling the Nike logo (see the chart).

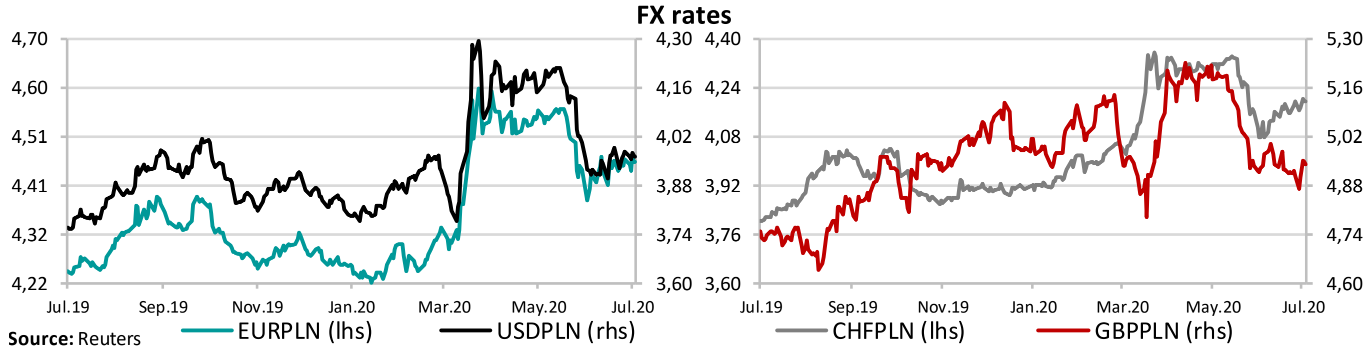
Such shape of recovery is close to the letter "V" but only at its first phase – a sharp increase in activity in Q3 due to the lifting of the government-imposed restrictions aimed at containing the spread of the epidemic. The feature by which a V-shaped recovery differs from a Nike-shaped one are changes in the economic activity in the subsequent quarters. If in the former the pre-shock level of activity is restored fast, in the latter it takes more time. In our scenario we expect that the pre-shock level of GDP (i.e. the one observed in Q4 2019) will be obtained no sooner than in Q3 2021.

In H2 2020 households concerns about the second wave of the epidemic will slow down the recovery in consumption. If private consumption should be restored soon in subsequent quarters, the economic growth in subsequent quarters will be limited by the pessimistic outlook for investments due to increased uncertainty about the further spread of the epidemic (see MACROmap of 8/6/2020). An additional factor slowing down the recovery will be the expected by us fiscal tightening in 2021. We forecast that the public finance deficit will decrease from 10% of GDP in 2020 to 4% in 2021.According to the forecasts of the European Commission, the structural deficit (in simple terms a variable reflecting the impact of fiscal policy on economic growth) will decrease from 8.5% of GDP in 2020 to 3.1% in 2021, which is consistent with our view. The main factors conducive to tighter fiscal policy will be the abatement of the impact of the government programs aimed at counteracting the negative consequences of the epidemic on the economy (so-called anti-crisis and financial shield) and the highly likely savings in the public sector in 2021.

It should be pointed out that the first investment projects under the EU recovery fund are most likely to be implemented in H2 2021. This will contribute to a fast increase in gross fixed capital formation and economic growth not only in 2021 but also in subsequent years (see MACROmap of 15/6/2020).

The expected by us relatively slow recovery of the Polish economic activity to pre-shock levels, slowed down at the same time by fiscal tightening, supports our scenario in which the accommodative monetary policy will be maintained for an extended period of time. We maintain our forecast in which interest rates will be increased no sooner than in H2 2022.

Information on the second wave of the pandemic in the US is significant for PLN



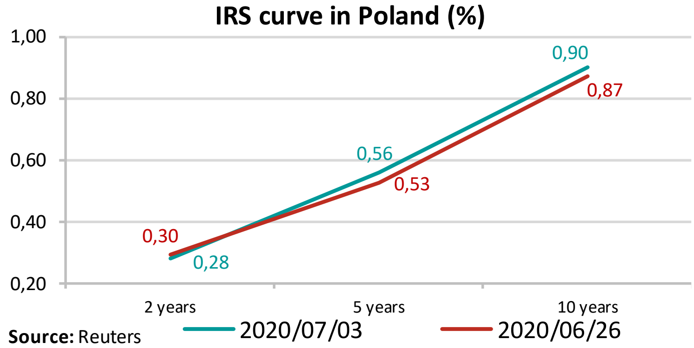
Source: Reuters

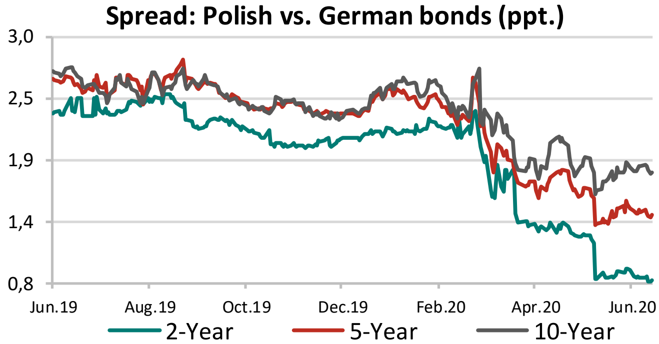
Last week, the EURPLN exchange rate dropped to 4.4578 (strengthening of PLN by 0.2%). Last week, the EURPLN exchange rate was showing low volatility and oscillated around 4.45. Thus, PLN was stable despite a visible decrease observed last week in risk aversion and supported by the publications of solid data from the global economy (USA, China). Data from the domestic economy (manufacturing PMI and flash inflation) were also insignificant for PLN.

The EURUSD was also stable. Although Thursday saw a slight strengthening of USD vs. EUR, it was temporary. At the same time the in-line-with-the-expectations decision of the German parliament to support the ECB asset purchase program was neutral for the market. Low volatility was also supported by the absence of the US investors on Friday due to the Independence Day in the US.

This week, like in the previous weeks, PLN will remain impacted by global sentiment related to the coronavirus pandemic. Crucial for the investors will be the information on the second wave of infections and new outbreaks in the US. It is worth noting that there was still no visible reaction of financial markets to a spike in infections in the US which, in our view, points to a high likelihood of a correction and USD depreciation vs. EUR. We believe that the publication of non-manufacturing ISM in the US scheduled for this week will be neutral for the market.

The situation in core markets is crucial for IRS rates





Source: Reuters

Last week, 2-year IRS rates decreased to 0.28 (down by 2bps), 5-year rates rose to 0.56 (up by 3bps), and 10-year rates to 0.90 (up by 3bps). The first part of the week saw an increase in IRS rates, following the core markets (Germany, USA). It was supported by the incoming data from the global economy (USA, China), pointing to a fast pace of the economic recovery in those countries. Media reports on growing numbers of coronavirus infections in the US and decisions of the German parliament to support the ECB quantitative easing program were not market moving. Domestic data (manufacturing PMI and flash inflation) were also neutral for the curve. Friday saw a correction, likely due to lower market liquidity in the absence of the US investors because of the holiday in the US. Last week BGK issued PLN 11.9bn of bonds providing financing for expenditures from the COVID-19 fund. The issue had a limited impact on the curve.

This week, the market will focus on information about the second wave of infections and new outbreaks in the US. It is worth noting that there was still no visible reaction of financial markets to a spike in infections in the US which, in our view, points to a high likelihood of a correction and decrease in yields in the core markets and consequently a decrease in IRS rates in Poland. We believe that the publication of non-manufacturing ISM in the US scheduled for this week will be neutral for the market.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Jun.19	Jul.19	Aug.19	Sep.19	Oct.19	Nov.19	Dec.19	Jan.20	Feb.20	Mar.20	Apr.20	May.20	Jun.20	Jul.20
NBP reference rate (%)	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,00	0,50	0,10	0,10	**0,10**
EURPLN*	4,24	4,29	4,38	4,37	4,26	4,31	4,26	4,30	4,33	4,55	4,54	4,44	4,44	**4,46**
USDPLN*	3,73	3,87	3,98	4,01	3,82	3,91	3,79	3,87	3,92	4,13	4,15	4,00	3,95	**3,98**
CHFPLN*	3,82	3,90	4,02	4,02	3,87	3,91	3,92	4,02	4,06	4,29	4,30	4,16	4,17	**4,18**
CPI inflation (% YoY)	2,6	2,9	2,9	2,6	2,5	2,6	3,4	4,3	4,7	4,6	3,4	2,9	**2,9**	
Core inflation (% YoY)	1,9	2,2	2,2	2,4	2,4	2,6	3,1	3,1	3,6	3,6	3,6	3,8	**3,5**	
Industrial production (% YoY)	-2,6	5,8	-1,5	5,5	3,7	1,5	3,8	1,1	4,8	-2,4	-24,6	-16,9	**-7,5**	
PPI inflation (% YoY)	0,5	0,5	0,9	0,8	-0,3	-0,1	1,0	0,9	0,2	-0,3	-1,4	-1,5	**-1,0**	
Retail sales (% YoY)	5,3	7,4	6,0	5,3	5,4	5,9	7,5	5,7	9,6	-7,0	-22,6	-8,6	**-2,5**	
Corporate sector wages (% YoY)	5,3	7,4	6,8	6,6	5,9	5,3	6,2	7,1	7,7	6,3	1,9	1,2	**1,6**	
Employment (% YoY)	2,8	2,7	2,6	2,6	2,5	2,6	2,6	1,1	1,1	0,3	-2,1	-3,2	**-4,0**	
Unemployment rate* (%)	5,3	5,2	5,2	5,1	5,0	5,1	5,2	5,5	5,5	5,4	5,8	6,0	**6,3**	
Current account (M EUR)	10	-824	-820	846	442	1412	366	2348	878	2438	1163	**1243**		
Exports (% YoY EUR)	-2,4	6,4	-1,2	13,0	4,0	0,8	9,0	3,6	7,5	-7,5	-29,2	**-22,9**		
Imports (% YoY EUR)	-5,3	6,7	-3,0	6,2	0,3	-3,5	-0,7	2,4	0,6	-4,5	-28,2	**-22,9**		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

Indicator		2020				2021				2019	2020	2021
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)		2,0	-10,5	-4,0	-2,5	-0,2	6,2	3,7	3,5	4,1	-3,8	3,2
Private consumption (% YoY)		1,2	-15,0	-3,1	0,0	2,1	8,1	4,3	3,7	3,9	-4,2	4,4
Gross fixed capital formation (% YoY)		0,9	-7,0	-12,2	-14,0	-5,4	5,1	5,4	5,9	7,2	-9,6	3,5
Export - constant prices (% YoY)		0,6	-11,0	-5,1	-3,1	2,0	5,1	4,2	4,1	4,7	-4,6	3,8
Import - constant prices (% YoY)		-0,2	-8,0	-7,4	-2,8	4,5	5,0	3,4	3,5	2,7	-4,6	4,1
GDP growth contributions	Private consumption (pp)	0,7	-8,7	-1,8	0,0	1,3	4,4	2,5	1,9	2,2	-2,4	2,5
	Investments (pp)	0,1	-1,2	-2,2	-3,5	-0,7	0,9	0,9	1,3	1,3	-1,8	0,6
	Net exports (pp)	0,4	-2,1	0,9	-0,3	-1,2	0,2	0,7	0,5	1,2	-0,3	0,1
Current account (% of GDP)***		1,3	1,2	0,8	0,5	0,2	0,1	0,2	0,2	0,5	0,5	0,2
Unemployment rate (%)**		5,4	6,3	6,5	7,5	7,3	6,1	5,5	6,1	5,2	7,5	6,1
Non-agricultural employment (% YoY)		0,7	-2,5	-3,1	-2,0	-0,9	3,2	2,9	2,2	0,3	-1,7	1,8
Wages in national economy (% YoY)		7,7	2,3	3,2	3,4	2,7	3,2	2,9	3,0	7,2	4,1	3,0
CPI Inflation (% YoY)*		4,5	3,2	3,0	3,5	2,2	2,9	2,2	1,5	2,3	3,6	2,2
Wibor 3M (%)**		1,17	0,26	0,30	0,30	0,30	0,30	0,30	0,30	1,71	0,30	0,30
NBP reference rate (%)**		1,00	0,10	0,10	0,10	0,10	0,10	0,10	0,10	1,50	0,10	0,10
EURPLN**		4,55	4,44	4,40	4,37	4,36	4,35	4,34	4,33	4,26	4,37	4,33
USDPLN**		4,13	3,95	3,86	3,80	3,79	3,82	3,84	3,83	3,79	3,80	3,83

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST*	
					CA	CONSENSUS**
		Monday 07/06/2020				
8:00	Germany	New industrial orders (% MoM)	May	-25,8		15,0
10:30	Eurozone	Sentix Index (pts)	Jul	-24,8		-11,0
11:00	Eurozone	Retail sales (% MoM)	May	-11,7		15,0
16:00	USA	ISM Non-Manufacturing Index (pts)	Jun	45,4	48,5	49,5
		Tuesday 07/07/2020				
8:00	Germany	Industrial production (% MoM)	May	-17,9		10,0
		Thursday 07/09/2020				
3:30	China	PPI (% YoY)	Jun	-3,7		-3,2
3:30	China	CPI (% YoY)	Jun	2,4		2,5
8:00	Germany	Trade balance (bn EUR)	May	3,2		
14:30	USA	Initial jobless claims (k)	w/e	1480		1375
16:00	USA	Wholesale inventories (% MoM)	May	-1,2		-1,2
16:00	USA	Wholesale sales (% MoM)	May	-16,9		

*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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