Bank Zachodni WBK
Grupa Santander

WEEKLY ECONOMIC UPDATE

3 – 9 August 2015

This week's macro calendar includes several important events. The U.S. will release key data – the ADP report and non-farm payrolls. The FOMC statement from its meeting in July read that "some" improvement in the labour market would trigger a rate hike, but the U.S. central bankers did not comment on when this could possibly happen. Last week's U.S. Q2 GDP data came out solid (yet below expectations) and showed an upward revision of the Q1 growth. This means that a good reading from the labour market could make the September hike more probable. PMI indices will also be important. Readings for the euro zone and Germany are not likely to be crucial since we have already seen the flash numbers. We expect a slight rise of Poland's PMI, but even a slight decline should not have a major market impact given the strong rise of the index in June and importance of the global events. Greece may attract attention again as negotiations on its third bailout are starting and there are many hurdles to overcome. Given that Syriza is divided on whether to support the bailout conditions and the IMF is threatening to withdraw from the bailout unless Greek debt is restructured and Greece introduces deeper reforms, talks may be prolonged and more bridge financing may be needed. China is another risk factor and further falls on the equity markets cannot be ruled out.

Negative news flow from Greece or China could hit risky assets. As regards the U.S. payrolls data, a positive reading may trigger higher volatility than a negative one as the market is not betting on a FOMC rate hike in September. Thus, in our view, the risk is skewed toward a weaker PLN and higher yields.

Economic calendar

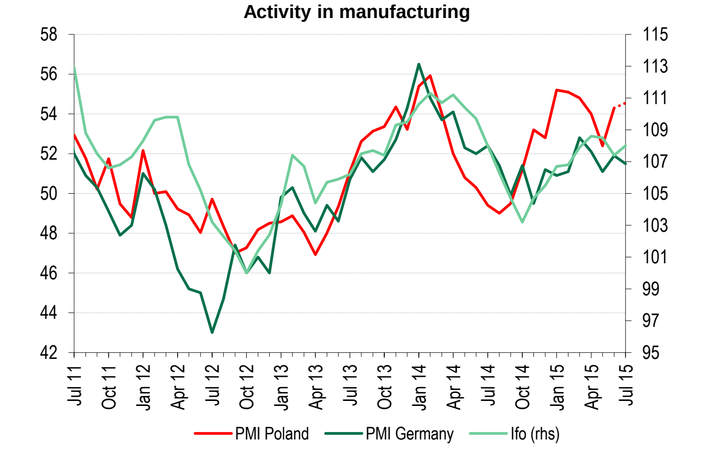
CZAS W-WA	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
		MONDAY (3 August)					
9:00	**PL**	**PMI – manufacturing**	**Jul**	**pts**	**54.3**	**54.5**	**54.3**
9:55	DE	PMI – manufacturing	Jul	pts	51.5	-	51.9
10:00	EZ	PMI – manufacturing	Jul	pts	52.2	-	52.5
14:30	US	Personal income	Jun	%MoM	0.3	-	0.5
14:30	US	Personal spending	Jun	%MoM	0.2	-	0.9
16:00	US	ISM – manufacturing	Jul	pts	53.5	-	53.5
		TUESDAY (4 August)					
16:00	US	Factory orders	Jun	%MoM	1.7	-	-1.0
		WEDNESDAY (5 August)					
9:55	DE	PMI – services	Jul	pts	53.8	-	54.4
10:00	EZ	PMI – services	Jul	pts	53.7	-	53.8
14:15	US	ADP report	Jul	k	210	-	237
16:00	US	ISM – non-manufacturing	Jul	pts	56.3	-	56.0
		THURSDAY (6 August)					
8:00	DE	Factory orders	Jun	%MoM	0.1	-	-0.2
11:30	**PL**	**Bond auction**					
14:30	US	Initial jobless claims	week	k		-	267
		FRIDAY (7 August)					
8:00	DE	Industrial output	Jun	%MoM	0.3	-	0.1
8:00	DE	Exports	Jun	%MoM	0.0	-	1.7
14:30	US	Non-farm payrolls	Jul	k	225	-	223
14:30	US	Unemployment rate	Jul	%	5.3	-	5.3

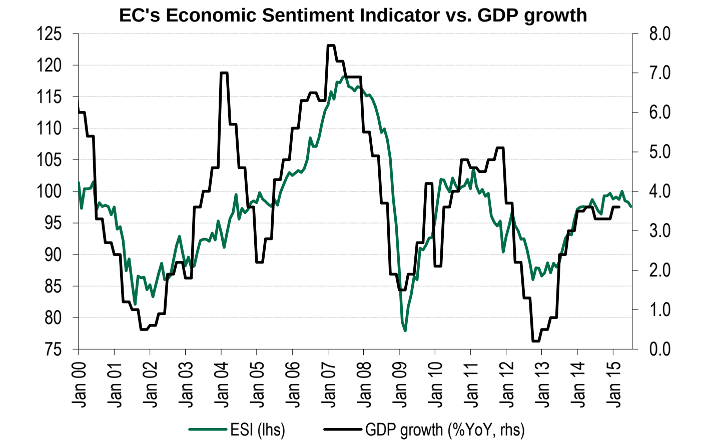
Source: BZ WBK, Reuters, Bloomberg

ECONOMIC ANALYSIS DEPARTMENT:
al. Jana Pawła II 17, 00-854 Warszawa fax +48 22 586 83 40
email: ekonomia@bzwbk.pl Web site: http://www.bzwbk.pl
Maciej Reluga (Chief Economist) +48 22 534 18 88
Piotr Bielski +48 22 534 18 87
Agnieszka Decewicz +48 22 534 18 86
Marcin Luziński +48 22 534 18 85
Marcin Sulewski +48 22 534 18 84

TREASURY SERVICES:
Poznań +48 61 856 5814/30
Warszawa +48 22 586 8320/38
Wrocław +48 71 369 9400

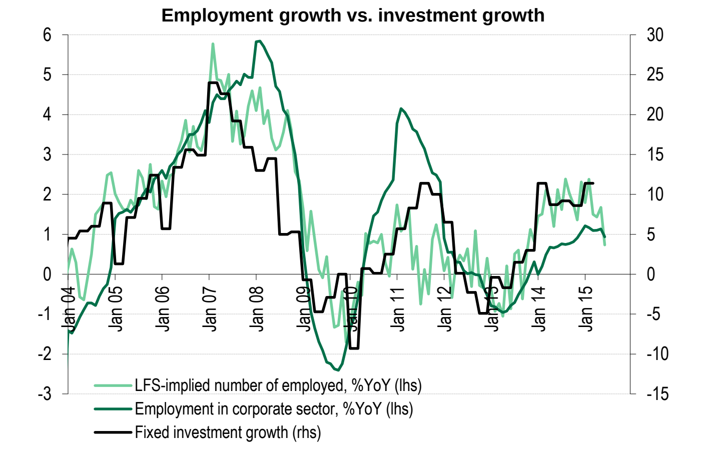
What's hot this week – Will PMI continue to recover?





- Following the significant rebound of the Polish manufacturing PMI in June, we expect the index to edge slightly higher in July now that the Grexit risk has fallen, at least for now. The corresponding flash indicators for Germany and the euro zone were slightly down, but remained at relatively healthy levels. The German Ifo index even rose in July. We believe this signals that economic growth in the euro zone remains decent and, thus, we expect Polish companies to continue benefiting from further growth in new export orders amid the competitive exchange rate.
- Other business climate surveys for July released so far offered a mixed picture. The stats office's indicator of economic climate in manufacturing rose to its second-highest level in the last four years. At the same time, its indicators for other sectors also improved. Meanwhile, BIEC's Leading Indicator and the European Commission's Economic Sentiment Index (ESI) inched down in July. The latter fell to 97.6, the lowest since September 2014, which – if sustained – may signal a slowdown of economic growth in Q3. Interestingly, the decrease was triggered mainly by weaker consumer confidence, while other components (including confidence indicators for the industrial, construction and retail trade sectors) improved in July. The stats office's indicator of consumer confidence also fell in July, but only slightly, and remained close to its seven-year high.

Last week in the economy – Fed keeps door open for September lift-off



- As expected, the FOMC kept interest rates unchanged in July. The Fed did not say when it was going to normalise its monetary policy, but stated it would raise interest rates if the labour market showed "some" further improvement. Even though the Fed's statement was not extremely hawkish, we believe the door to the Fed's lift-off remains wide open. Incoming U.S. data releases (especially from the labour market) may be key for global market sentiment, as they may determine whether the first rate hike will take place in September (our base-case scenario) or later.
- According to Eurostat's Labour Force Survey (LFS) the seasonally adjusted unemployment rate in Poland fell in July to 7.7%, its lowest since April 2009. However, the data signal that the pace of improvement in the labour market is waning – the implied growth of employed slowed below 1%YoY, which, if sustained, may herald a slowdown in investment growth.

Quote of the week – Enthusiasm for joining the euro is going to be even weaker

Marek Belka, NBP governor, 25.07, The Telegraph

The situation around Greece does not increase confidence in the euro, that's for sure, and if we have a political change more into the right, then the enthusiasm to join the euro is going to be even weaker.

You shouldn't rush when there is still smoke coming from a house that was burning. It is simply not safe to do so. As long as the eurozone has problems with some of its own members, don't expect us to be enthusiastic about joining.

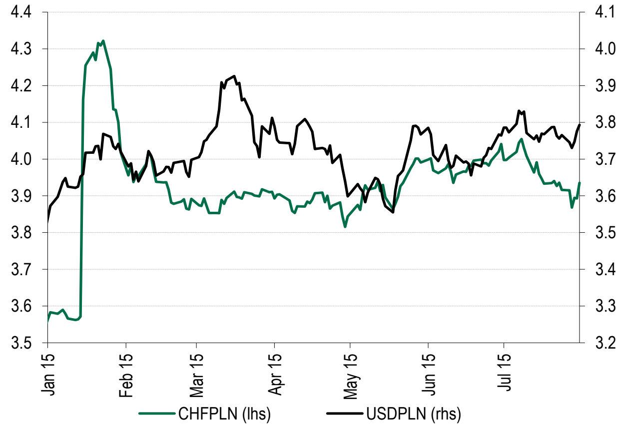
The eurozone needs to grow solidly and build up a solid foundation for its currency, including elements of fiscal union and common economic policy. This is something that we cannot say fully determine upfront. It's more of a moving target.

Some people predicted that euro adoption may be one of the main topics of the election campaign in Poland. The main opposition party Law and Justice (PiS) strongly declared at the start of July that if they win the election, scrapping plans of joining the euro zone will be one of its government's first decisions. However, it seems there is very little controversy in Poland right now about euro adoption as neither the ruling PO government nor the central bank want to hurry with adopting the euro since the euro zone is still in trouble. Even though we agree Poland should not hurry too much to join the euro area, we think it should not stop preparing the economy for a potential accession because the necessary steps (including further fiscal consolidation) would benefit the country anyway, even outside the euro zone.

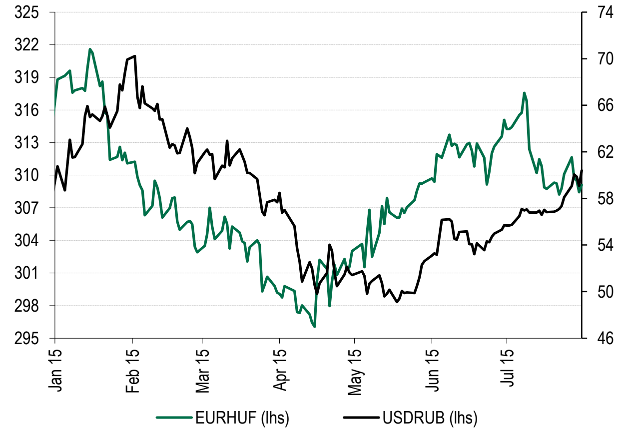
Foreign exchange market – Global factors still key for market direction

EURPLN

USDPLN and CHFPLN



EURHUF and USDRUB



EURUSD

Zloty weaker due to higher risk aversion …

- Poland's zloty, similarly to its emerging market peers, weakened over the past week. This was caused by the Fed's rate outlook (investors saw rising odds for a September rate hike in the U.S.) and negative news from Greece. As a consequence, EURPLN tested its strong resistance level at 4.15, but did not manage to break it permanently.
- The zloty lost significantly against the U.S. dollar due to the EURUSD decline. The rate temporarily rose towards 3.81, the highest level since the beginning of July. As regards the other main currencies, in weekly terms, the zloty lost 1.2% against the British pound and 0.5% against the Swiss franc.
- From the technical point of view, EURPLN did not change much over the past week. The rate kept fluctuating between 4.10 and 4.15. These levels are still effective and investors will mainly focus on the global factors, which should be decisive for markets in the upcoming days/weeks. The release of the U.S. non-farm payrolls will be the key event, especially since the FOMC, in its July statement, pointed out that it would be appropriate to hike rates in case of "some" further improvement in the labour market. On the domestic front, July's manufacturing PMI will be the only release. We expect it to rise slightly and have no significant impact on the market.

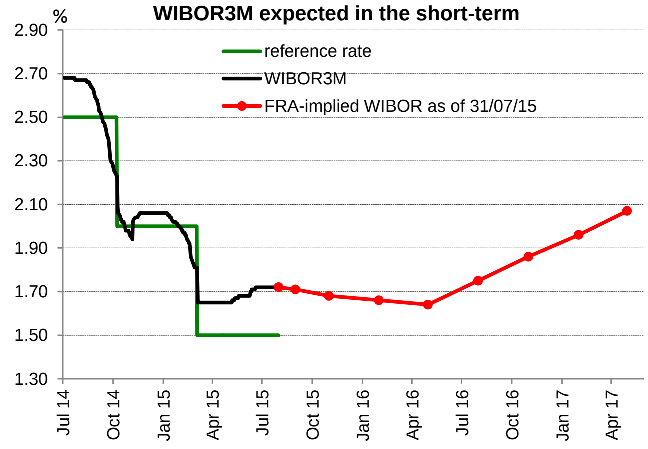
… as other CEE currencies

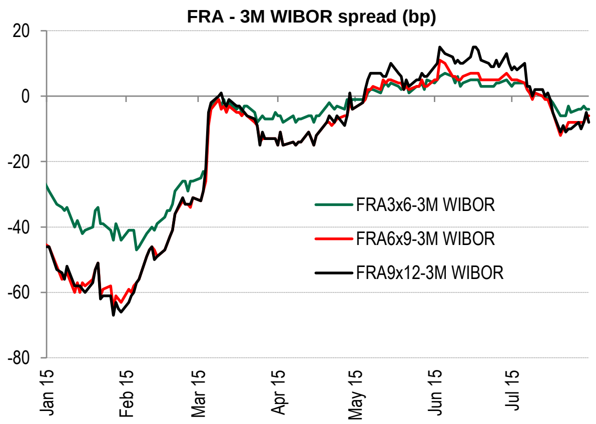
- After the relatively calm beginning of the week, the CEE region's currencies lost ground due to higher risk aversion. However, the Hungarian forint's and the Czech koruna's depreciation was rather limited. The Russian rouble was more volatile, losing the most among the emerging markets peers vs. the U.S. dollar (nearly 3% in weekly terms). USDRUB rose above 60 for the first time since mid-March due to a downward trend in crude oil, among others.
- This week, the region's currencies will be under the influence of global factors. The continuing risk aversion mode may weigh on their valuation. In the Czech Republic, investors will also focus on the central bank (CNB) meeting. The market expects the CNB to keep its monetary conditions unchanged, however, the meeting could provide some clues as to whether the 27.0 EURCZK floor will be maintained in the coming months or raised.

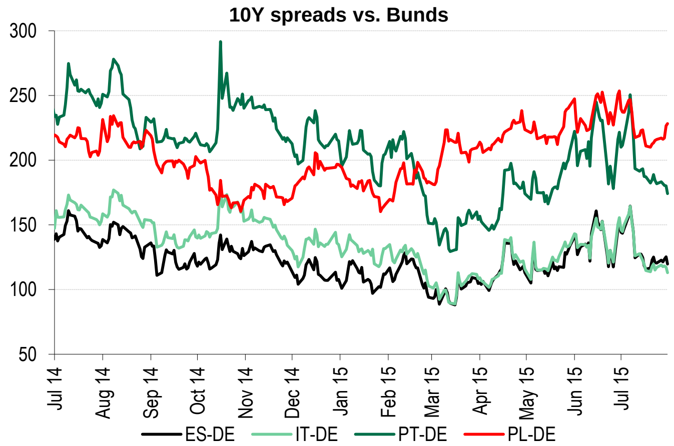
Dollar gains on FOMC

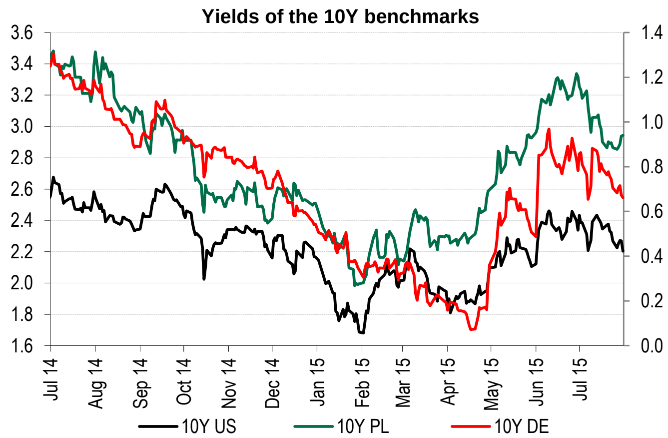
- The beginning of the week was relatively quiet ahead of the FOMC meeting. EURUSD was range-bound between 1.098 and 1.112. The euro lost ground against the main currencies after the Fed's statement fuelled expectations that it could start to tighten its monetary policy in September and on a negative news flow from Greece (which raised the risk of an earlier election, the possibility that the IMF would withdraw from the third bailout). Consequently, EURUSD temporarily fell to 1.089 after the FOMC meeting, and to rise towards 1.11 at the end of the week.
- This week investor focus should be split between U.S. and euro zone data, although these could potentially cancel each other out. In our view, July's PMI for the euro zone countries should be relatively supportive if the figures do not differ significantly from their flash readings. On the other hand, July's non-farm payrolls should be strong enough to support the start of monetary normalisation by Fed in September, which could push the rate down. All in all, we think that a break of the EURUSD support at 1.09-1.092 will open the door to another at 1.082.

Interest rate market – Profit-taking ends July, auction and U.S. data in the spotlight









Yields and IRS rates higher

- Money market rates were roughly stable (WIBOR 9M rose 1 bp in weekly terms) over the past week. The beginning of the week brought a gradual decline of FRAs, which trimmed all their earlier gains as investor sentiment deteriorated. The FRA curve shifted up in weekly terms, with the biggest rise seen on the long end of the curve (starting from FRA12x15). The spread between FRAs and WIBOR 3M narrowed visibly, but up to 9 months is still negative.
- Poland's bonds and IRS weakened more significantly due to a risk averse mode. Yields and IRS rates rose visibly already after the FOMC statement, which suggested that the Fed would start to hike rates later this year, with September the most probable timing of the first hike. Polish bonds weakened despite the gradual strengthening on the core markets, which could point to funds being shifted to safe heaven assets due to the situation in Greece. Consequently, the 10Y benchmark yields rose temporarily to 2.97%, its highest in two weeks. In our view, the low liquidity due to the holiday season deepened the bond market's weakening at the end of month.
- The higher risk aversion caused the spread over Bunds to widen. The spread for the 10Y sector widened towards 230 bp, the most since early July. What is more, the belly and the long-end of the curve underperformed the front end, which resulted in the curve's steepening in both the bond and IRS markets.

Domestic T-bond auction in the spotlight

- We think that WIBORs and the front-end of the bond and IRS curves should remain stable in the coming weeks, backed by expectations that the NBP rates will remain unchanged in the upcoming months. At the same time, the belly and the long-end of the curves will be more macro-data dependent. In the short term, we expect a horizontal trend in both yields and the IRS rates, but, in the medium term, an upward trend seems likely.
- Global factors will continue to play the main role this week. Investors will particularly focus on U.S. macro data, including the monthly labour market reading, looking out for some confirmation of the September rate hike by the Fed. In our view, data should remain relatively strong and, consequently, have a negative impact on Poland's T-bonds and IRS markets, especially the long-end of the curves. News from Greece could also affect the domestic bonds and IRS valuation. These factors imply that curve steepener trade might dominate the market this week.
- The Finance Ministry confirmed there will be only one bond auction and the offer will be equal to PLN1-4bn, in line with the plan. Bond offer will be released two days prior to the auction (i.e. on 4 August). Supply is moderate, so we expect no problems with sales.
- We currently see a growing holiday spirit on the market with liquidity remaining very low. This could cause higher market volatility in the upcoming weeks.

Additional information is available on request. Please contact Bank Zachodni WBK S.A. Rates Area, Economic Analysis Department, Al. Jana Pawła II 17, 00-854 Warsaw, Poland, phone +48 22 534 18 88, email ekonomia@bzwbk.pl, http://www.bzwbk.pl.