

# WEEKLY ECONOMIC UPDATE

## 31 August – 6 September 2015

Holidays are getting to an end and so the central bankers are also going back to job. However, we reckon that neither Polish MPC nor the ECB will be very busy in September. Rates in Poland are very likely to be left unchanged this week and the statement's rhetoric should not be modified noticeably so we do not expect this event to have a big impact on the zloty or bonds. As regards the ECB, the issue of the recent turmoil in China and drop in commodity prices may be commented by the central bank. Last week the ECB's chief economist said that the QE could be extended should reaching the inflation target be less likely due to the recent global developments. If Mario Draghi also sounds dovish, then the risky assets in Europe, including the zloty, could gain. The second, next to the ECB meeting, event that the market will be waiting for this week is the US nonfarm payrolls data. After the recent turmoil in the global market, investors have postponed their expectations for the first Fed rate hike and even the Fed's Dudley, who used to be a declared supporter for the September's hike said that now it "seems less compelling". However, this did not support the zloty and Polish bonds as the market has become more concerned about the global economic activity. As regards this week's US data, we think that both strong disappointment and number significantly above the consensus could weigh on the Polish assets – in the first case amid likely sharp deterioration of the global market mood amid worries about the next global crisis and investors' retreat from the risky assets; in the second – due to weaker mood in the EM as the September's Fed rate hike will become more likely.

### Economic calendar

CZAS W-WA	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	BZWBK		
<b>MONDAY (31 August)</b>							
11:00	EZ	Flash HICP	Aug	%YoY	0.1	-	0.2
14:00	PL	Inflation expectations	Aug	%YoY	0.2	-	0.2
<b>TUESDAY (1 September)</b>							
3:45	CN	PMI – manufacturing	Aug	pts	47.2	-	47.8
9:00	PL	PMI – manufacturing	Aug	pts	54.4	54.7	54.5
9:55	DE	PMI – manufacturing	Aug	pts	53.2	-	51.8
10:00	EZ	PMI – manufacturing	Aug	pts	52.4	-	52.4
16:00	US	ISM – manufacturing	Aug	pts	52.8	-	52.7
<b>WEDNESDAY (2 September)</b>							
	PL	MPC decision		%	1.50	1.50	1.50
14:15	US	ADP report	Aug	k	200	-	185
16:00	US	Industrial orders	Jul	%MoM	0.7	-	1.8
20:00	US	Fed Beige Book					
<b>THURSDAY (3 September)</b>							
9:55	DE	PMI – services	Aug	pts	53.6	-	53.8
10:00	EZ	PMI – services	Aug	pts	54.3	-	54.0
13:45	EZ	ECB decision		%	0.05	-	0.05
14:30	US	Initial jobless claims	week	k	-	-	271
16:00	US	ISM – services	Aug	pts	58.3	-	60.3
<b>FRIDAY (4 September)</b>							
8:00	DE	Industrial orders	Jul	%MoM	-0.8	-	2.0
9:00	HU	GDP	Q2	%YoY	2.7	-	3.5
14:30	US	Non-farm payrolls	Aug	k	218	-	215
14:30	US	Unemployment rate	Aug	%	5.3	-	5.3

Source: BZ WBK, Reuters, Bloomberg

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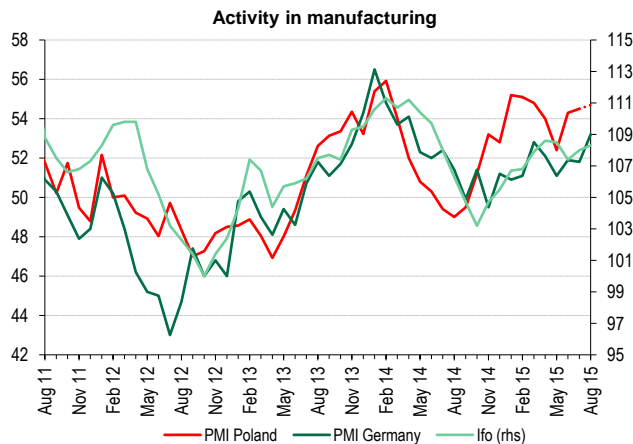
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## What's hot this week – Focus on ECB and FOMC

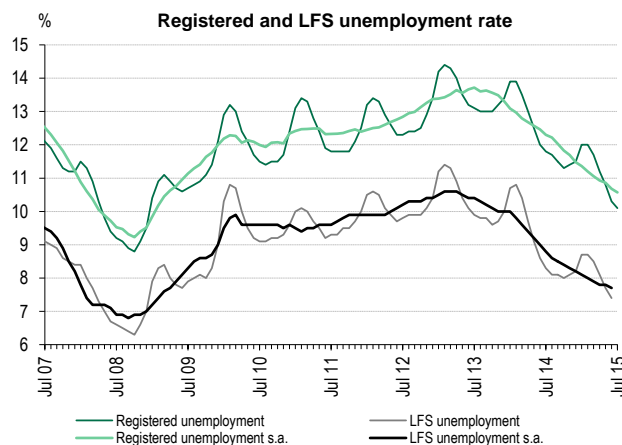


- Most activity indicators for Germany improved in August, suggesting that impact from the Chinese turmoil has (so far) been limited. This makes us believe that the Polish manufacturing PMI may also inch up, or at least stabilise at a high level, especially that other business climate surveys for Poland have so far also been relatively optimistic, reflecting a continued modest economic recovery.

- The first MPC meeting after the summer is unlikely to bring about any major surprise, with stable rates and the statement likely to point to no reasons to change the policy stance.

- ECB's press conference and Mario Draghi's comments on the recent turmoil in China, following the bank's chief economist's statement that the QE programme may be extended if needed, will be more interesting. Towards the end of the week, investors will focus on the U.S. labour market data, which should be key for expectations of the FOMC's next policy move.

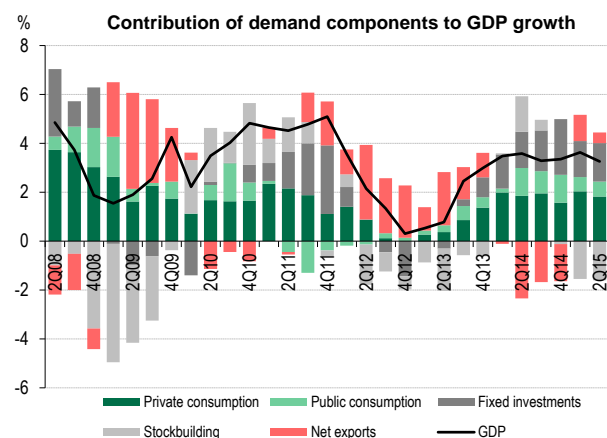
## Last week in the economy – Lower investment growth weighs on GDP



- The registered unemployment rate fell to 10.1% in July, its lowest since 2008. On a monthly basis, the number of the unemployed fell by 37k, more than a year ago (34k). A similar phenomenon was recorded in June and this means that the pace of the unemployment rate's decline has accelerated, while we had expected some slowdown due to a lower stock of labour force. However, the bigger fall of the jobless rate is partly due to a stronger intervention of the Labour Ministry – 9k more unemployed than a year ago got a subsidised job or were sent to training. According to LFS methodology, the unemployment rate fell to 7.4% in 2Q, its lowest since 2008.

- GDP growth slowed to 3.3%YoY in 2Q15 from 3.6%YoY in 1Q and was in line with the flash estimate. Domestic demand growth accelerated to 3.3%YoY, despite the slower investment growth (to 6.4%YoY, lowest since 4Q13) and stable consumption growth (3%YoY), with inventories surprising to the upside. The net exports' contribution to GDP growth decreased amid weaker exports and imports. The seasonally adjusted GDP growth remained quite robust, at 0.9%QoQ.

- The structure of GDP growth in 2Q15 (in particular the notable investment slowdown) has raised our doubts about the pace of expansion in the second half of the year. Private consumption growth should remain robust, supported by the falling unemployment and rising labour income. Export growth may even accelerate, fuelled by the economic revival in the euro zone. However, investment growth is not likely to re-accelerate significantly. We still think that GDP growth may accelerate in 2H15, but probably not as much as we had previously anticipated. Growth in all of 2015 should be closer to 3.5% than 4.0% and the 3.5% forecast for 2016 is still realistic. Our revised forecasts will be presented in detail in the upcoming monthly report.



## Quote of the week – Conversion can trigger negative effects

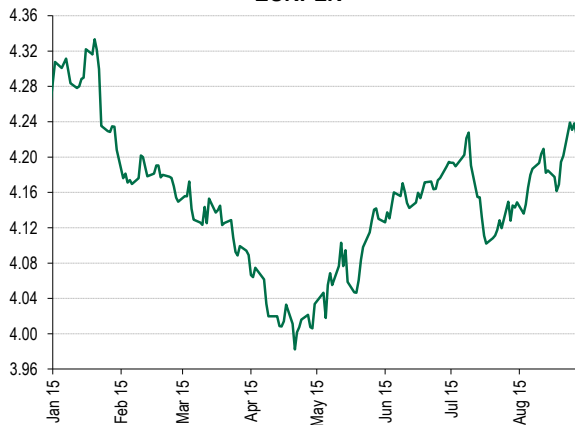
**Andrzej Raczek, NBP deputy president, 27.08.2015, PAP**

Mass conversion of FX mortgages (...) can cause a considerable depreciation of PLN versus CHF and other currencies. The central bank might intervene in such a situation. However, we have limited power in this matter, which means that a mass conversion could trigger very negative macroeconomic effects.

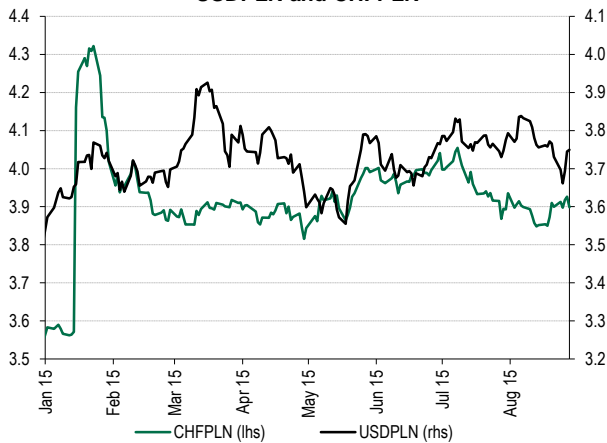
The Senate's public finance commission recommended to restore the original terms of the FX loan-restructuring bill, i.e. the 50/50 split of the conversion costs between clients and banks, the conversion's timing based on LTV. The size limits of apartments and houses that could qualify for the conversion were kept at 100 and 150 sqm, respectively. The Senate will debate on the bill this week and further modifications cannot be excluded. Then the bill will return to the Sejm, which can still reject the Senate's amendments. PO needs the support of its junior coalition partner in the Sejm to maintain the Senate's version of the bill. According to the NBP, the value of the loans eligible for the conversion stands at PLN68bn. In our view, the risk of introduction of bill weighing strongly on banks decreased recently, but this factor can still undermine market moods.

## Foreign exchange market – Volatility may remain high

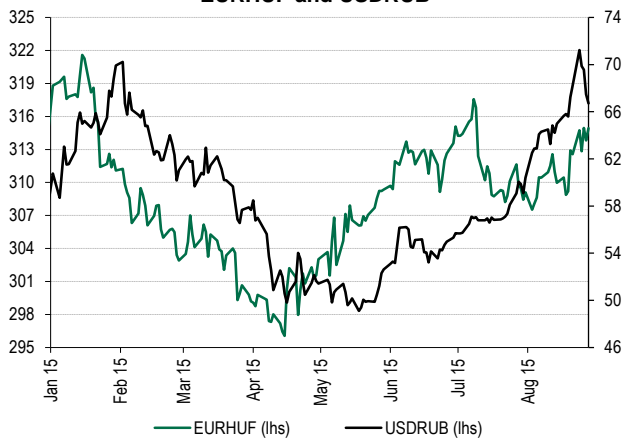
### EURPLN



### USDPLN and CHFPLN



### EURHUF and USDRUB



### EURUSD



### High zloty volatility could continue

▪ The zloty's exchange rate was pretty volatile in the past week amid sharp swings in market sentiment. Initially, EURPLN rose to 4.26, its highest since late January, exceeding the peak from early July at 4.24 on the back of global concerns about the world's economic growth. Later in the week some recovery was recorded and the exchange rate pulled back to 4.23. USDPLN was also moving a lot. It first dropped to 3.62 and then rebounded to 3.77.

▪ Holidays are almost over, which means that central bankers are also returning to their jobs. However, we reckon that neither the Polish MPC nor the ECB will be very busy in September. Rates in Poland are very likely to be left unchanged this week and the statement's rhetoric should not be modified noticeably so we do not expect this event to have a big impact on the zloty. As regards the ECB, the recent turmoil in China and falling commodity prices may be commented on by the central bank. Last week, ECB's chief economist said that the QE programme could be extended should reaching the inflation target prove to be less likely due to the recent global developments. If Mario Draghi also sounds dovish, Europe's risky assets, including the zloty, could gain.

▪ U.S. nonfarm payrolls data will be the second, next to the ECB meeting, event that the market will be waiting for this week. After the recent turmoil in the global markets, investors have postponed their expectations for the first Fed rate hike. Even the Fed's Dudley, a declared supporter of the September hike, said that it now "seems less compelling". However, this did not support the zloty as the market has become more concerned about the global economic activity. We think that both a strong disappointment and a number significantly above the consensus could weigh on the Polish currency. In case of the former - amid a likely sharp deterioration of the global market sentiment on worries about the next global crisis and investors' retreat from risky assets; in case of the latter - due to weaker sentiment in the EM as the Fed's September rate hike would become more likely.

▪ The last few weeks have been pretty volatile for EURPLN and given the importance of the this week's events we expect volatility to remain high in the coming days. In our view, the crucial EURPLN levels to watch for are at 4.15 and 4.265 (next resistance at c4.30).

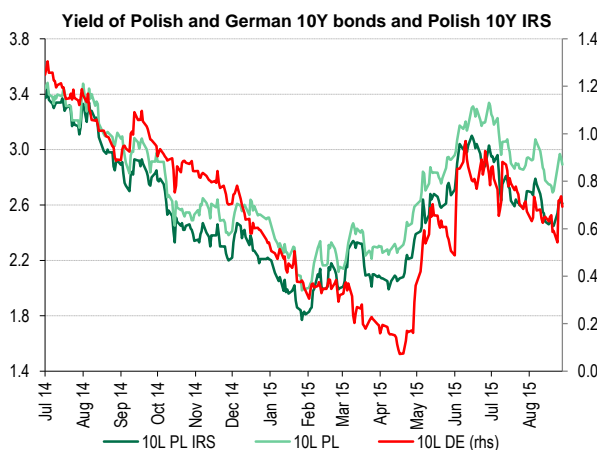
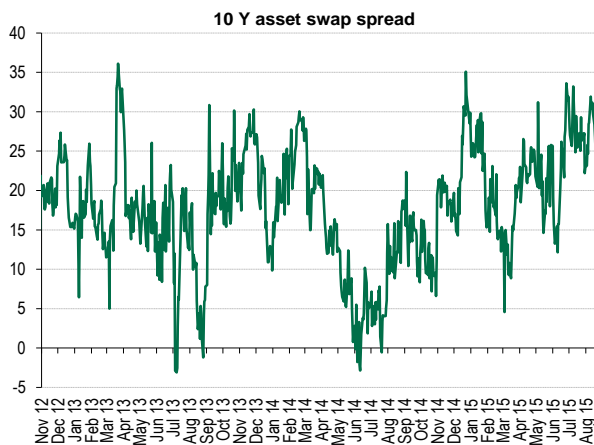
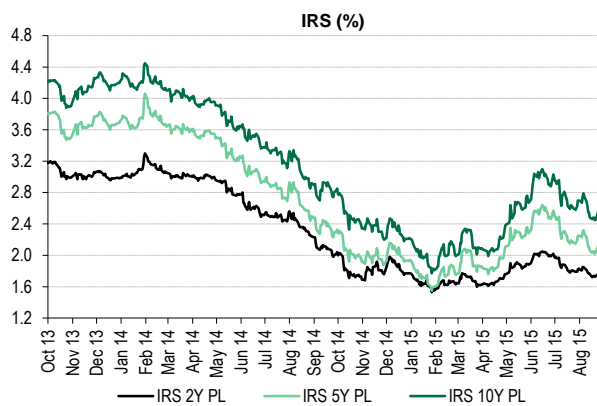
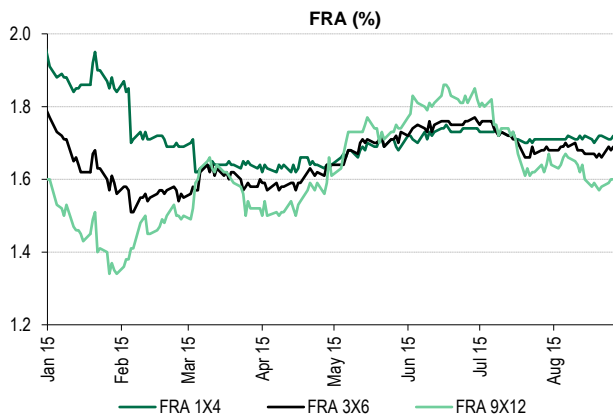
### China and U.S. data fuel volatility

▪ The falling odds for a Fed rate hike in September amid worries about China have pushed EURUSD sharply up to just above 1.17, its highest since mid-January. However, the decent U.S. data released later in the week supported the dollar and EURUSD ended the week close to 1.13.

▪ The recent market turmoil, concerns about China and the fairly strong U.S. macro data have caused a great deal of uncertainty regarding the timing of the first rate hike by the Fed and this was reflected in the strong volatility of EURUSD. Plenty of U.S. data are due this week, with the August nonfarm payrolls probably the most awaited. It seems that the market will continue to favour the dollar on strong U.S. figures and push EURUSD higher on disappointing releases.

▪ We think 1.12 and 1.17 are the important levels to watch this week.

## Interest rate market – Global sentiment still crucial



## Rates volatile due to external factors

Poland's IRS and bond curves moved noticeably up last week. Initially, the market was hit by capital outflows to safe assets. The negative impact of higher risk aversion amid the market turmoil in China proved to be more important for the market than the potentially positive impact from worries about the global economic slowdown and lower odds for a Fed rate hike in September. Consequently, the IRS curve rose 5-15bp and the bond curve 5-20bp on a weekly basis. The scale of the weakening was even bigger but the market recovered slightly at the end of the week. The 10Y benchmark yield rebounded from the 2.70% support. There was also a noticeable correction in the curve's slope – with the 2-10 and 2-5 spreads rising 10-20bp during the week to their highest level since early August. The 10Y asset swap spread broke temporarily the 33bp resistance and rose to nearly 40bp, its highest since September 2012.

When it comes to FRAs, rates up to 9 months stayed roughly stable and the market still sees some 50% chances for a rate cut in this horizon. The longer FRAs rose 5-9bp following the upward IRS move.

## Global sentiment still crucial

Swings in the global market sentiment have again been the main drivers of the Polish IRS/bonds last week. Recent days confirmed that once global risk aversion exceeds a critical level, Polish debt suffers even if the odds for worldwide monetary policy tightening are falling.

We think that the Polish MPC meeting is unlikely to offer any breaking news or trigger any long-lasting market reaction. External issues are likely to remain the key drivers for the Polish FI market. Plenty of U.S. macro data are due for release and could have a noticeable impact on the investors' assessment of the Fed's monetary policy outlook. They may trigger significant swings in the global FI market. The 10-session correlation between the Polish and German 10Y bonds is at 70% and the 1M correlation is slightly above 60% implying that global trends are currently key for the domestic FI market. We think that just like for the zloty, strong surprises from U.S. data in either direction (up or down) could weigh on the Polish bonds – due to higher odds for a September rate hike by the Fed in the first case, in the latter - due to the likely sharp deterioration of the global market sentiment amid worries about the next global crisis and investors' retreat from risky assets.

Liquidity has been extremely low during the holidays and we now hope that investors will become more active.

On Monday, the Finance Ministry will present details about its bond auctions in September. The ministry had initially scheduled two auctions for the final month of 3Q. Also, July's data on investor holdings of the Polish debt will be released at the beginning of the week.

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