Bank Zachodni WBK
Grupa Santander

WEEKLY ECONOMIC UPDATE

21 – 27 August 2017

Last week, the market sentiment remained negative, with terrorist attacks in Spain supporting the general risk-off mood. Data from the global economy were rather mixed, while CEE readings surprised to the upside. Polish GDP for Q2 proved a bit better than expected, data on employment and construction output also beat expectations. However, these numbers failed to provide a strong support for PLN, which gained only temporarily. As regards monetary policy, dovish moods prevailed, with both FOMC and ECB minutes providing quite soft messages. This fueled a downward move of yields.

This week, we will get to see flash PMI indices from Europe as well as some important data from the USA amid no important releases of domestic statistics. Jackson Hole conference starts on Thursday and in our view this will be the key event of the week. In our view, the market is expecting the conference to prove boring. However, we would not rule out that the main central banks will send a coordinated message that the era of ultra-loose monetary policy is ending, like it happened in Sintra, as they seem to be increasingly worried about rising asset prices. This could weigh on the Polish zloty and send bond yields globally higher.

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		MONDAY (21 August)					
14:30	US	Chicago Fed index	Jul	pts	-	-	0.13
		TUESDAY (22 August)					
11:00	DE	ZEW indeks	Aug	pts	-	-	86.4
14:00	HU	Central bank rate decision	Aug	%	0.90	-	0.90
		WEDNESDAY (23 August)					
9:30	DE	Flash PMI - manufacturing	Aug	pts	-	-	58.1
9:30	DE	Flash PMI - services	Aug	pts	-	-	53.1
10:00	EC	Flash PMI - manufacturing	Aug	pts	-	-	56.6
10:00	EC	Flash PMI - services	Aug	pts	-	-	55.4
14:00	**PL**	**Money supply**	**Jul**	**% y/y**	**5.1**	**5.0**	**5.0**
15:45	US	Flash PMI - manufacturing	Aug	pts	-	-	53.3
15:45	US	Flash PMI - services	Aug	pts	-	-	1.9
16:00	US	New home sales	Jul	% m/m	0.4	-	0.8
		THURSDAY (24 August)					
10:00	**PL**	**Unemployment rate**	**Jul**	**%**	**7.0**	**7.1**	**7.1**
14:00	**PL**	**MPC minutes**					
14:30	US	Initial jobless claims	Aug	k	-	-	-
16:00	US	Existing home sales	Jul	% m/m	0.6	-	-1.8
		FRIDAY (25 August)					
8:00	DE	GDP SA	2Q	% q/q	-	-	0.6
10:00	DE	Ifo index	Aug	pts	-	-	1.3
10:00	**PL**	**LFS unemployment rate**	**2Q**	**%**	**4.8**	**4.8**	**5.4**
14:30	US	Durable goods orders	Jul	% m/m	-5.7	-	6.4

Source: BZ WBK, Reuters, Bloomberg

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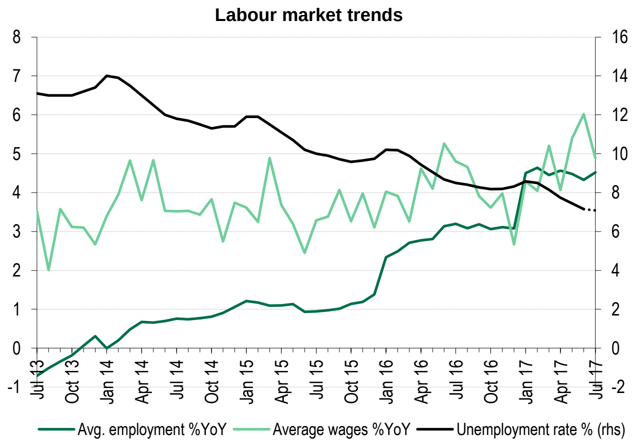
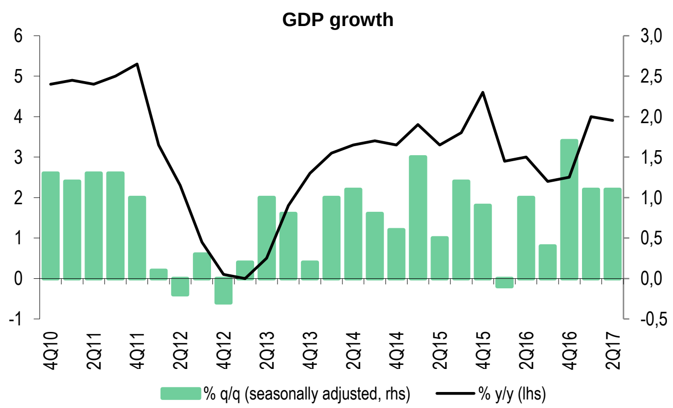
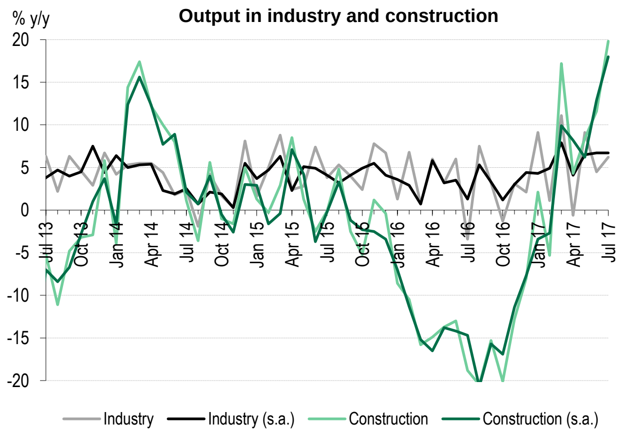
What's hot next week – Labour market riddle, MPC minutes



- The registered unemployment rate probably remained unchanged in July at 7.1%, which is already a record low level. In fact, the level was so low that we considered the labour market to be almost deprived of any slack. The June deceleration in employment growth seemed to strengthen this view. And yet the data on employment for July surprised with a massive monthly increase, suggesting it is still possible to get new employees on the market without a big swing in wages. More detailed data in the Statistical Bulletin due this week should help to solve this riddle.
- MPC minutes from the July meeting will be released, but there is little to expect from this document. We still assume that the view of governor Adam Glapiński is the prevailing one, meaning that rates should stay on hold for at least another year.

Last week in economy – Strong real momentum





- GDP growth in 2Q17 reached 3.9% y/y, and 1.1% q/q after seasonal adjustment, following the corresponding 4.0% y/y and 1.1% q/q in 1Q17. The result was slightly above market and our expectations of 3.8% and almost exactly in line with the latest NBP projection. The flash reading did not contain any details. We may suspect that the main engine was still the private consumption, possibly rising by nearly 5% y/y and buoyed by healthy income growth. In the coming quarters, consumption growth may decelerate slightly, but investments should continue recovering. We maintain the view that GDP growth should reach almost 4% on average this year.
- Employment in corporate sector showed the largest monthly rise since the economic downturn in 2009 (if we omit January readings, which are distorted by technical factors). Despite the very tight labour market. Employment growth is back at 4.5% y/y, beating consensus that was expecting it to stay at 4.3%. Wage growth in corporate sector decelerated to 4.9% y/y, while the market expected it to move from 6% to 5.4%. The July reading was exactly in line with our forecast and even though it came below market expectations it is in our view not a sign of diminishing wage pressures.
- Industrial production in July rose 6.2% y/y, less than expected (market consensus 8.4%) but seems to be a decent result, given that this was the first time the data have not been affected by calendar effects. The construction output soared 19.8% y/y, much more than predicted and at fastest growth rate since Jan'12, which seems to be finally a clear sign of recovery in investments (output in engineering surged 33.7% y/y). Retail sales growth was also decent, rising by 6.8% y/y in real terms and confirming that private consumption remains strong. On balance, the data show that Polish economic growth remains solid, still near 4% y/y, at the start of 3Q17.

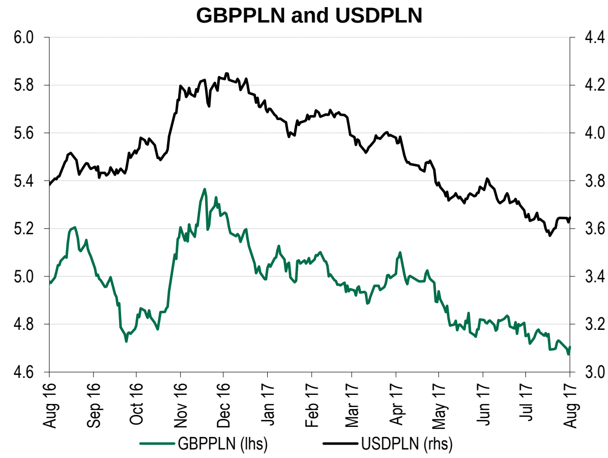
Quote of the week – Investments nearly neutral to GDP growth in 2Q

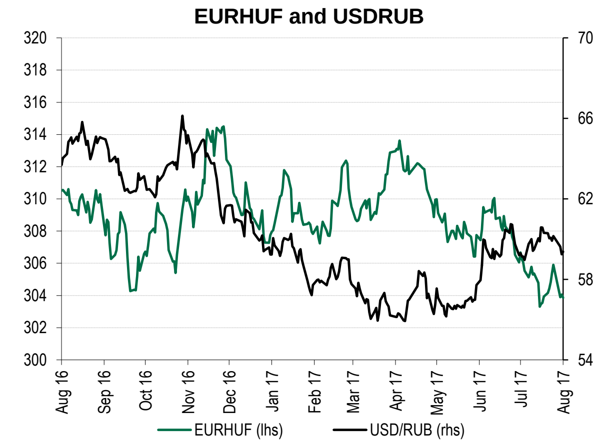
Maria Jeznach, head of National Accounts Dept., GUS, 16 August 2017, Bloomberg, PAP, ISBNews

All economic sectors except financial industry had positive impact on 2Q GDP. Construction industry recovery accelerated in 2Q. Investment demand was nearly neutral for GDP growth in quarter. Domestic demand had positive impact on GDP growth mainly thanks to consumer demand. Trade balance was "slightly positive" for 2Q GDP, but its impact was weaker than in 1Q.

The flash GDP reading of 2Q was not far from the consensus, but the comment added by the Statistical Office representative has given us food for thought. It seems that investment expenditures were still almost flat y/y in 2Q – it had to be not higher than 2% y/y to provide only what she called 'a nearly neutral' contribution, after the surprisingly poor print of -0.4% y/y in 1Q. So the investment rebound that was supposed to be the pillar of Polish growth this year is seeing more delay. What also struck us was her comment on net exports contribution being positive, yet smaller than previously. The problem is that in 1Q the category added only a marginal 0.1pp boost and that the monthly data on trade balance of goods and services for April-June showed a significant deterioration in y/y terms.

Foreign exchange market – PLN may be under pressure





EURPLN may be under pressure

- EURPLN started last week at 4.28 amid lower market liquidity due to bank holiday. Later, the positive data on Polish GDP as well as good macro releases from the CEE region supported the Polish currency, which gained to 4.25 per euro. However, this move was quickly corrected to 4.27 and rise in risk aversion after terrorist attacks in Spain helped the rate anchor around this level. Worse-than-expected data on Polish industrial output pushed the rate above 4.28 at the end of the week.
- Given lack of important domestic macro releases this week, foreign events will prove crucial for the exchange rate. In our view, flash PMI from Europe will be positive and likely to support risk appetite and Polish assets.
- Jackson Hole conference, starting on Thursday, 24 August, is another important event. In our view, given the relatively dovish minutes of FOMC and ECB released last week, the market is expecting the conference to prove rather boring. However, we would not rule out that the main central banks will send a coordinated message that the era of ultra-loose monetary policy is ending, like it happened in Sintra, as they seem to be increasingly worried about rising asset prices. This could weigh on the Polish zloty.
- Note also that moods towards EM and other risky assets turned less positive recently, which could limit the zloty's potential to gain.
- EURPLN is also close to an important technical level, 200-day moving average (4.29). Break through this level can trigger a more significant depreciation.
- To sum up, risks to EURPLN are skewed upwards, in our view, especially in the second half of the week. We see a move to 4.29 likely.

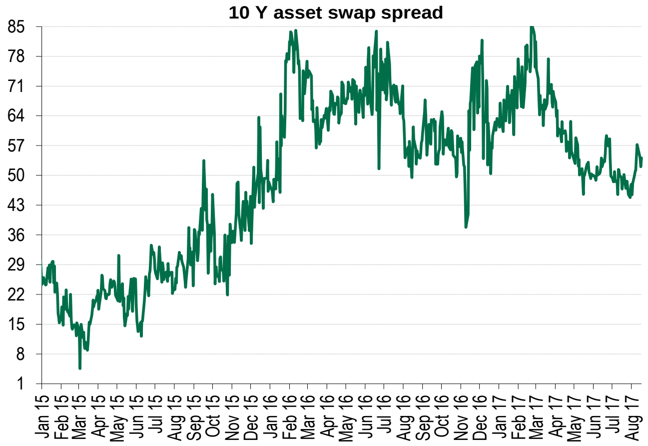
US dollar likely to appreciate

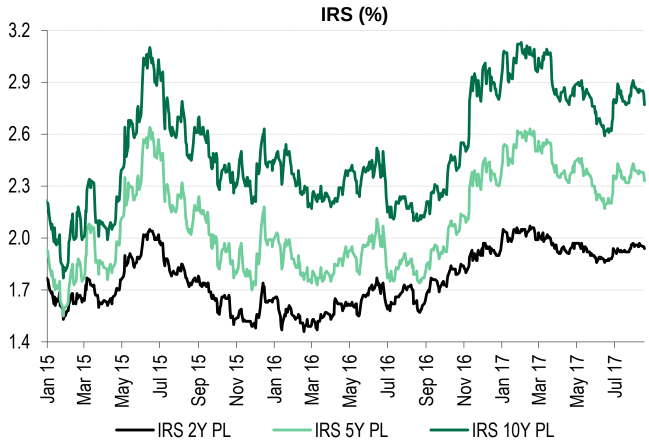
- Last week was quite interesting for EURUSD, which moved in 1.165-1.182 range. US data were mixed (positive on retail sales, negative on output), so their impact on EURUSD was twofold. Upward pressure on the rate was put by dovish FOMC minutes and turmoil in Donald Trump administration (e.g conflict with GOP deputies), while downward pressure by hawkish comment of William Dudley and dovish ECB minutes. Finally, dollar ended the week a bit stronger, at 1.173.
- This week, the risk-off mood is likely to support the US dollar. The possible hawkish message from Jackson Hole should also be positive for the US currency, given that ECB members were worried about excessive euro strengthening. Pressure stemming from GOP-Trump conflict should also mitigate.
- In general, the upcoming week will be supportive for the dollar, as we see EURUSD heading towards 1.16.

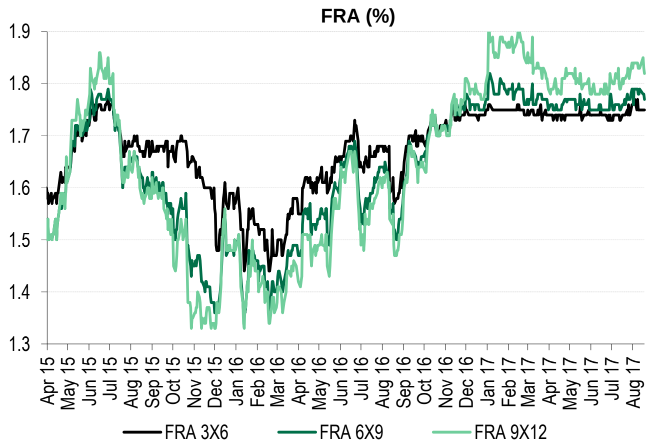
A mixed bag of CEE currencies

- The Czech koruna gained last week with EURCZK falling from 26.15 to almost 26.00 (the lowest level since 2013) thanks to a very positive surprise in GDP growth in 2Q (4.5% vs consensus at 3.0%). End of the week saw some weakening above 26.10. EURHUF was oscillating slightly above 304.00 for the better part of the week, but then gained on Friday to 303.50. USDRUB was the most volatile pair, inching to 60.0 amid cheaper oil and lower EURUSD. Later, as oil prices rebounded, Russian data on budget performance proved positive and the market was expecting a flow of dollar sales by Russian exports, the USDRUB slid to 59.0.
- This week is likely to be negative for CEE currencies, like for the zloty.

Interest rate market – Waiting for the central bankers







Yield curve drops on domestic GDP data

- Last week we observed decreasing of asset swap spread (ASW) of Polish debt, after the two weeks of spread widening. The ASW spread drop from 58bp to 54 for 10Y, from 36bp to 33 for 5Y and -8bp to -11 for 2Y mainly owing to solid domestic GDP data released in the middle of the week. The bond yield curve downfall (fueled by ASW spread compression) was supported by IRS rates decrease at the end of the week. The downshift of IRS curve was a reaction for the rise of political risk after the Thursday's Barcelona terror attack. As a result Polish T-bonds yield curve was pushed down by c10bp on the long end, c8bp in the middle and c3bp on the front end of the curve.
- The market players completely ignored solid domestic employment and wages dataset, as well as bunch of mainly solid industrial production, construction output and retail sales data for July.
- FRA and WIBOR rates remained unchanged.

Jackson Hole in the spotlight

- In our opinion the debt market the next week will be focused on the Jackson Hole annual symposium, which will start on Thursday. Investors will bet on Mario Draghi and Janet Yellen statements. Market participants are waiting for a signal to wind down ultra-easy monetary policy.
- We anticipate that the Polish T-bonds yield curve will be pulled up by hawkish central bankers' comments and as result will return to the levels seen at the beginning of last week. The main part of this move will probably be an effect of the ASW spread decompression.
- FRA and WIBOR rates will likely remain stable.

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