Bank Zachodni WBK
Grupa Santander

WEEKLY ECONOMIC UPDATE

4 – 10 September 2017

Lack of any hawkish signals from the central bankers gathered in Jackson Hole and sound US macro data determined that the global market sentiment was positive in the last few days. Elevated risk aversion that emerged after the North Kore launched a missile in direction of Japan had only temporary negative impact on the risky assets. In Poland, 2Q GDP growth was confirmed at robust 3.9% but both the growth structure and another disappointing PMI reading call for caution regarding chances for faster economic growth in the coming quarters. Flash CPI did not surprise and 1.8% y/y figure was close to the market consensus.

This week the ECB holds a meeting and in our view this could be the main event for the market. We think that the tone of the statement and outcome of the press conference might sound rather dovish given the recent signals from the central bank and the euro's strength. Also, numerous FOMC members will speak in the coming days. Polish central bankers meet after August holiday break and we expect the dovish rhetoric to be maintained. At the end of the week Moody's may release its review of Poland's rating. In our opinion the agency will decide to affirm A2 rating with stable outlook so there should be hardly any market reaction to this event.

Until now, we have been expecting that EURPLN could stay high in the next two-three months and ease towards 4.20 at the end of the year but we are of the opinion that order of the events will be the opposite – we think the zloty may appreciate vs the euro and give up part of its gains at the end of the year. More details on the FX page of this report.

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	BZWBK	
		MONDAY (4 September)					
		No important data releases					
		TUESDAY (5 September)					
9:00	HU	GDP	Q2	% y/y	3.2	-	4.2
9:55	GE	PMI – services	Aug	pts	53.4	-	53.1
10:00	EZ	PMI – services	Aug	pts	54.9	-	55.4
11:00	EZ	GDP	Q2	% y/y	2.2	-	1.9
16:00	US	Industrial orders	Jul	% m/m	-3.2	-	3.0
		WEDNESDAY (6 September)					
	PL	**MPC decision**		**%**	**1,50**	**1,50**	**1,50**
8:00	GE	Industrial orders	Jul	% m/m	0.3	-	1.0
9:00	CZ	Industrial output	Jul	% y/y	6.7	-	2.2
16:00	US	ISM – services	Aug	pts	55.1	-	53.9
20:00	US	Fed Beige Book					
		THURSDAY (7 September)					
8:00	GE	Industrial output	Jul	% m/m	0.5	-	-1.1
13:45	EZ	ECB decision		%	0.0	-	0.0
14:30	US	Initial jobless claims	week	k	-	-	236
		FRIDAY (8 September)					
	PL	**Poland rating review by Moody's**					
8:00	GE	Exports	Jul	% m/m	1.3	-	-2.7
9:00	HU	CPI	Aug	% y/y	2.5	-	2.1

Source: BZ WBK, Reuters, Bloomberg

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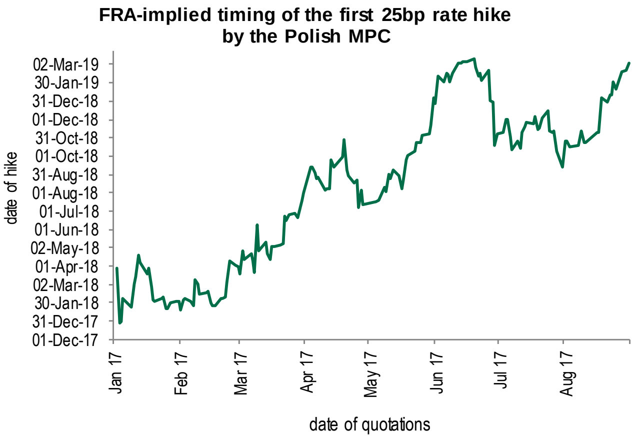
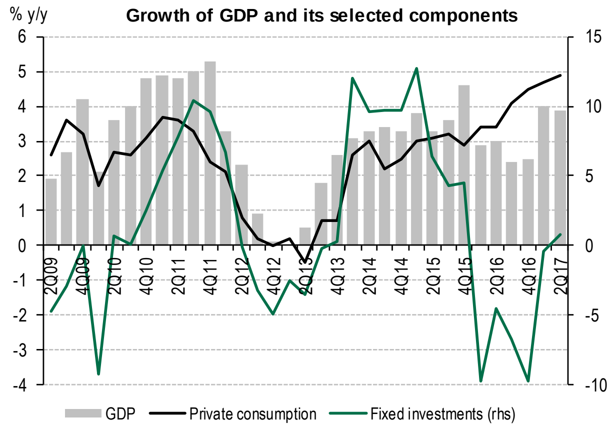
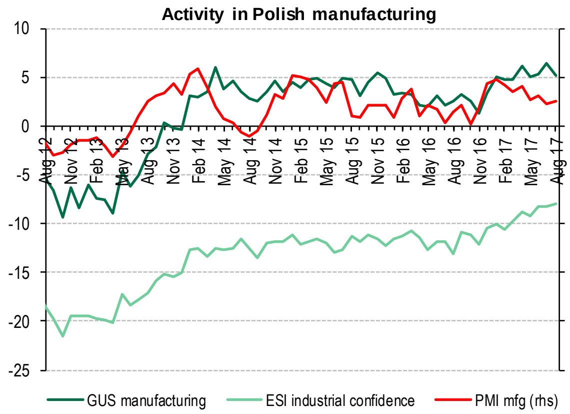
What's hot next week – MPC meeting and Moody's review



- Polish central bankers meet this week after August holiday break. Since the last meeting in July, annual inflation has not changed much while the economic activity data were quite good. Recent months showed that there is a group of hawks calling for a fast rate hikes, but we think the majority of MPC members still shares the view of governor Glapiński. Thus, we expect the Council's rhetoric to remain dovish.
- Moody's is planning to review Poland's rating on Friday. In our opinion the agency will decide to affirm A2 rating as well as stable outlook. The decision is likely to be based on positive economic and fiscal outlook for Poland (solid GDP growth, fiscal deficit well below 3% of GDP). The agency may point out the concerns regarding the planned judicial system changes or the conflict with the European Commission, but in our view it is unlikely to outweigh the positive assessment of the economic situation.

Last week in economy – GDP growth still decent, inflation picking up





- Polish 2Q17 GDP growth was confirmed at 3.9% y/y. Private consumption remained the main engine of growth, rising by nearly 5% y/y, while investments remained subdued (+0.8% y/y). Net exports' contribution to GDP growth was negative (-1.5pp), mainly due to significant slowdown of real export growth. The latter seems to be odd given the recovery in the euro zone, Poland's main trading partner, but deceleration in German exports could be an explanation. We think that economic growth in Poland should remain decent in the coming quarters, yet slightly below 4% y/y. For more details, please refer to our Instant comment.
- Polish PMI disappointed again, reaching 52.5 in August (vs 52.3 in July). The activity indicator for Polish manufacturing has clearly diverged from the corresponding index for the euro zone, which is quite surprising, as the euro area is Poland's biggest trading partner. The report confirmed that domestic orders rose faster than external ones, which is in contrast to the recent past. However, we also see the growing evidence of supply-side constraints affecting Polish firms due to the tightening labour market. PMI report says that Polish firms reported a rise in backlogs of work for the first time since February 2015, with the shortages of labour and supply constraints as potential causes. This suggests some caution regarding the GDP growth outlook for the coming quarters.
- Flash estimate of August CPI showed a rise to 1.8% y/y from 1.7% y/y in July, in line with our forecast. No details were released yet but we suspect that that CPI rise was driven mainly by prices of fuels and food, while core inflation remained subdued. The CPI growth is likely to continue climbing in the coming months, to 2% in November, before dropping to 1.5% in December due to base effect. This would allow the Polish central bank to maintain its dovish rhetoric, in our view.

Quote of the week – Polish rates should rise now

Kamil Zubelewicz, MPC member, Reuters, 29 August

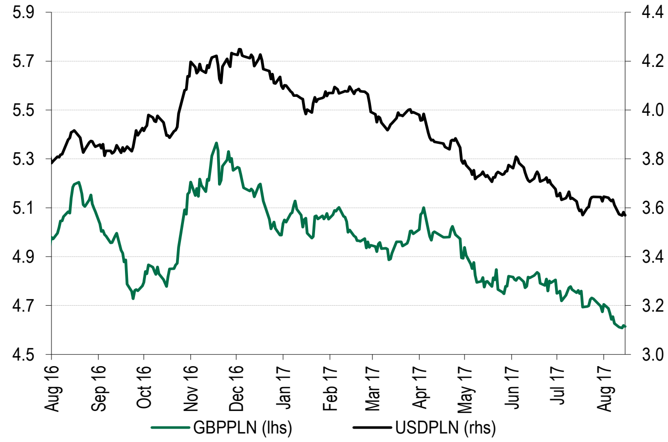
Rates should be increased gently now, as the economic situation is favourable. (…)This move would have a positive impact on the zloty's exchange rate, but it would have little [negative] effect on investment, which depends on the cost of lending only to a very small extent when rates are so low. (…) It would be worth taking the step to avoid risk factors related to rising commodity prices or exchange rate fluctuations, and it would also prevent higher interest rate hikes in the future. (…) At the moment, a wait-and-see approach is in place, which assumes that the current situation is rather good, while I think it is important to look ahead (...) and move away from policies that favour an unnatural weakening of the zloty's exchange rate.

Kamil Zubelewicz said that the economic situation already justifies a small interest rate hike. In his view, such move would have a limited negative impact on investment activity and it seems this remark was a reference to a sentence that appeared in the minutes from the July MPC meeting that said majority of the Council's members favour keeping interest rates unchanged in order not to hit investments. Nevertheless, Zubelewicz sees hardly any chances for rate hikes even until the end of 2019 (probably because he realizes the majority of the MPC members share views of the NBP governor Adam Glapiński).

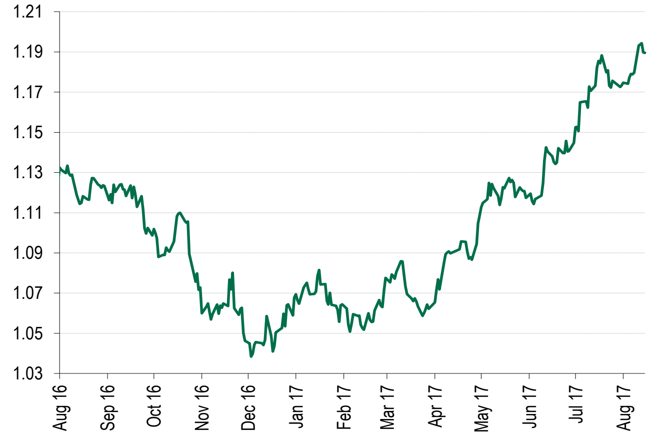
Foreign exchange market – ECB may boost zloty and hit euro

EUR/PLN

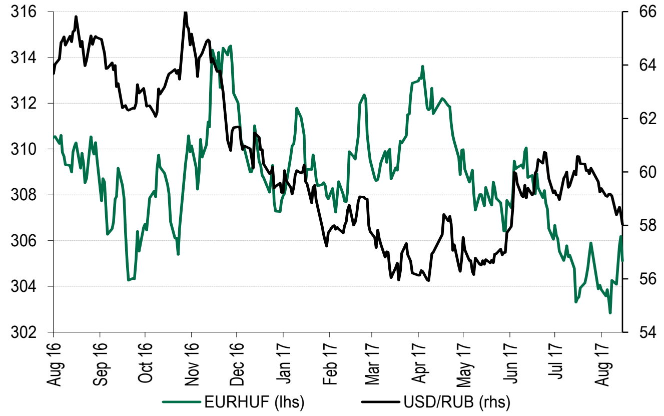
GBPPLN and USDPLN



EUR/USD



EURHUF and USDRUB



Balance turns to stronger zloty

- Last week, EURPLN fell for the third week in a row thanks to lack of any hawkish signals from the central bankers that gathered in Jackson Hole and anonymous sources saying that strong euro could prevent the ECB from fast withdrawal of its highly accommodative monetary policy. Elevated risk aversion that emerged during the week after the North Korea launched a missile in direction of Japan had only temporary negative impact on the Polish currency. As a result, EURPLN was testing the lower end of the 4.25-4.30 range. At the same time, CHFPLN stabilized just above 3.70, GBPPLN rose to 4.63 from 4.58 and USDPLN stayed in a 3.52-3.60 range.
- Until now, we have been expecting that EURPLN could stay high in the next two or three months and ease towards 4.20 at the end of the year but we are of the opinion that order of the events will be the opposite. In our view, global market sentiment could remain positive in the weeks to come amid robust economic data and no signals from the central banks of an acceleration of monetary policy normalization process. Also, the Polish government-European Commission conflict may not attract that much market attention as long as the risk of imminent financial consequences is low. At the same, time we still expect one more 25bp Fed rate hike to be delivered this year and the market is not pricing such scenario. Once this hike becomes more likely, we expect emerging currencies, including the zloty, to be under pressure in late 2017. This week the ECB holds a meeting and we think the outcome could be positive for the zloty.
- EURPLN is testing support at 4.25. Next important levels to watch are at 4.235 (August low) and 4.213.

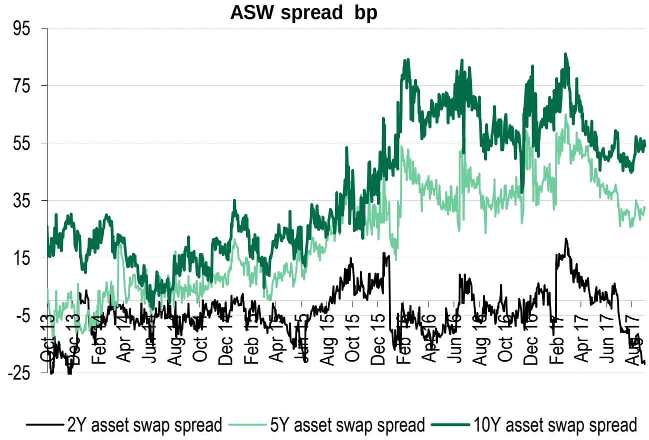
Dollar caught a breath

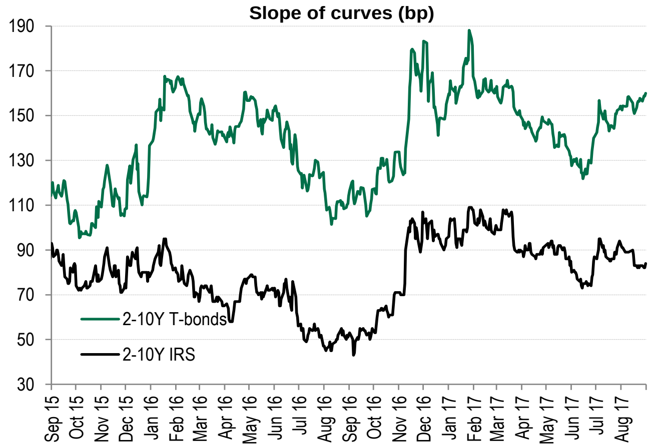
- Last week the EURUSD upside trend halted. The euro gained after the end of the Jackson Hole symposium with the exchange rate jumping above 1.20 but the sound US data released later in the week pulled EURUSD down to 1.18. At the end of the week the exchange rate was close to 1.19.
- This week the ECB holds a meeting. We think that the tone of the statement and outcome of the press conference might sound rather dovish given the recent signals from the central bank and the euro's strength.
- We think that it will be difficult for EURUSD to maintain such fast pace of rise without deeper correction. The exchange rate has been rising for 35 weeks already and the 35-week % change for EURUSD has recently reached its highest since mid-2011. Also, most of the recent US data was solid which should support the dollar.

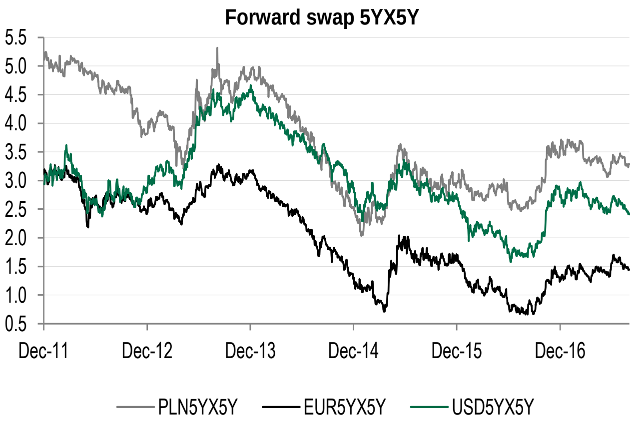
Ruble gains, forint under pressure, koruna stable

- Last week, the ruble gained vs the dollar and USDRUB fell to 57.9 (its lowest since June) on rising oil prices and positive data on Russian FX reserves. At the same time, EURHUF rose temporarily to 306.5 from 304 on profit taking after recent forint rally. EURCZK held above 26.0. Two Czech central bankers (Hampl and Mora) said that rates in Czechia could go up again before the year end while the final 2Q GDP data surprised to the upside (beating already surprisingly strong flash estimate) but this provided only temporary support for koruna.

Interest rate market – The central banks in focus







Yields stayed stable despite strong Eurozone PMI

- On the data front most of Eurozone data released positively surprised last week. Eurozone August inflation reading (CPI flash) rose to 1.5% y/y from 1.3% in July and exceeded estimates (1.4% y/y), ESI leading indicators beat the estimates, while core Eurozone PMI manufacturing rose to 57.4 from 56.6 recorded in July. US numbers were not as optimistic as European ones, however. Only non-farm payrolls data disappointed significantly, while PCE and personal income numbers were located close to market median forecast. Investors were keeping their minds focused on Jackson Hole statements as well as information how ECB policy makers would react to rapid gain of EURUSD. As a result the core markets debt yield were decreasing in the first part of week and recovering in the other one.
- Domestic bond market was supported by Ministry of Finance (MoF), which announced only one switch auction in September. Additionally Piotr Nowak, Deputy Minister of Finance, said that Poland already financed 72% of borrowing needs (or even 85% if we take into account the likely lower-than planned realization of budget deficit). Yields of domestic bonds followed the same pattern. In the first part of the week central bankers statements on the Jackson Hole conference pushed Polish sovereign yield curve down by 1-3bp. In the second part of the week we observed yields recovery. However, the scale of the upward shift was not significant and concentrated on the front end and the middle part of the curve. The long end of the curve rebounded only slightly owing to MoF information about cancellation of traditional auction in September. Investors did not react for the solid GDP data from Poland as well as flash CPI.

Waiting for the central banks

- We expect domestic bond yield stabilisation this week. ECB conference is not likely to change the positive mood on the bond market. However last ECB's rates setter E. Nowotny comment about rapid growth of EURUSD ("I would not over-interpret or dramatise this development"), was interpreted by bond investors as a signal of more hawkish ECB's sound on the September conference (10Y bund yield jumped to 0.39% from 0.36%). It suggests that bond market players will try to find hawkish remarks in the ECB conference. In our opinion Polish MPC conference as well as services Eurozone PMI data (which will be announced in this week) will be ignored by debt market players.

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