

WEEKLY ECONOMIC UPDATE

25 June – 1 July 2018

The escalation in the trade war between the USA and China and the resulting concerns of central bankers voiced at the Sitra summit led to the strengthening of the US dollar and bonds on the core markets. The zloty and other CEE currencies reacted negatively to the information about the risk of global growth deterioration as a result of changes in the global trade regime. On the domestic front, the May's industrial production exceeded expectations, but 3M averages of real economic activity suggested a deceleration of GDP growth in 2Q18. The retail sales data met expectations while wages y/y was a little lower than in April.

This week, the markets will be still under the influence of the global trade war, but the players will be counting losses and testing their strength rather than continuing the fight. The leading indicators for June can only fuel the fears over global growth. In Poland, the rule of law story will also be back with the government called by EU Council for a formal hearing. Though the geopolitical situation remains unclear, we expect some corrections: a zloty rebound and the worsening of the domestic debt pricing. The Polish data (money supply and unemployment rate) will not generate much interest. On the core markets, we expect a subdued reaction to EZ flash HICP and US personal incomes and spending, which are usually closely monitored.

Economic calendar

TIME CET	COUNTRY	INDICATOR	PERIOD	FORECAST			LAST VALUE
				MARKET	BZWBK		
MONDAY (25 June)							
10:00	DE	IFO Business Climate	Jun	pts	-		102.2
10:00	PL	Unemployment Rate	May	%	6.1	6.1	6.3
16:00	US	New Home Sales	May	% m/m	1.2		-1.5
TUESDAY (26 June)							
16:00	US	Consumer Conference Board	Jun	pts	127.2		128.0
WEDNESDAY (27 June)							
	DE	Retail Sales	May	% m/m	-		1.6
13:00	CZ	Central Bank Rate Decision	Jun-18		-		0.75
14:30	US	Durable Goods Orders	May	% m/m	-0.7		-1.6
16:00	US	Pending Home Sales	May	% m/m	1.0		-1.3
THURSDAY (28 June)							
11:00	EZ	ESI	Jun	pct.	-		112.5
11:30	PL	Bond Auction			-		
14:00	DE	HICP	Jun	% m/m	-		0.6
14:30	US	GDP Annualized	1Q	% Q/Q	2.2		2.2
14:30	US	Initial Jobless Claims		k	220.0		218.0
FRIDAY (29 June)							
	PL	Central Budget Cumul.	May	bn PLN	-		9325.2
09:00	CZ	GDP SA	1Q	% y/y	-		4.4
11:00	EZ	Flash HICP	Jun	% y/y	-		1.9
14:00	PL	Current Account Balance Q	1Q1	€mn			
14:30	US	Personal Spending	May	% m/m	0.4		0.6
14:30	US	Personal Income	May	% m/m	0.4		0.3
14:30	US	PCE Deflator SA	May	% m/m	-		0.2
16:00	US	Michigan index	Jun	pts	-		99.3

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>

Piotr Bielski +48 22 534 18 87

Marcin Luziński +48 22 534 18 85

Grzegorz Ogonek +48 22 534 19 23

Konrad Soszyński +48 22 534 18 86

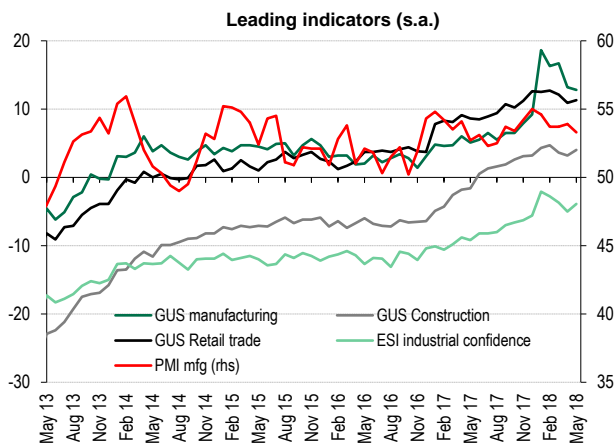
Marcin Sulewski +48 22 534 18 84

TREASURY SERVICES:

Poznań +48 61 856 5814/30

Warszawa +48 22 586 8320/38

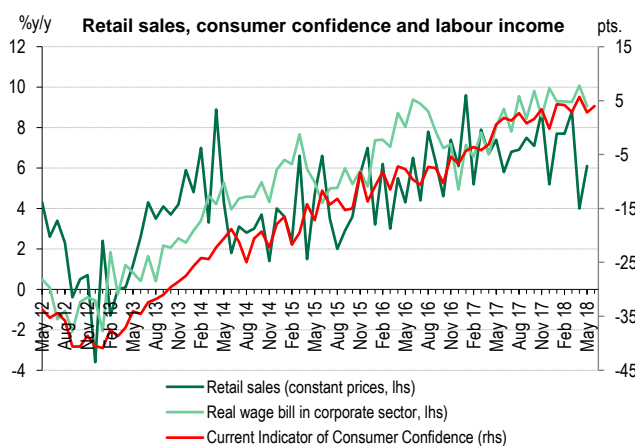
Wrocław +48 71 369 9400

What's hot next week – What business sentiment in June?

■ We already know May was quite decent when it comes to economic activity (retail sales) or even stronger than expected (output figures). It is time to have a look on what is to come in June by checking survey-based leading indicators from Statistics Poland and the European Commission.

■ We will also receive important information for monitoring the wage pressure: detailed data on May corporate wages and statistics on border crossings in 1Q, showing the evolution of immigration flows from our Eastern neighbours (a mitigating factor for wage pressure in the light of labour shortages).

■ The rule of law story will also be back with Poland called by EU Council for a formal hearing to explain its stance, as required by Article 7 procedure. The European Commission considers Polish concessions in the rule-of-law spat as not enough to drop charges.

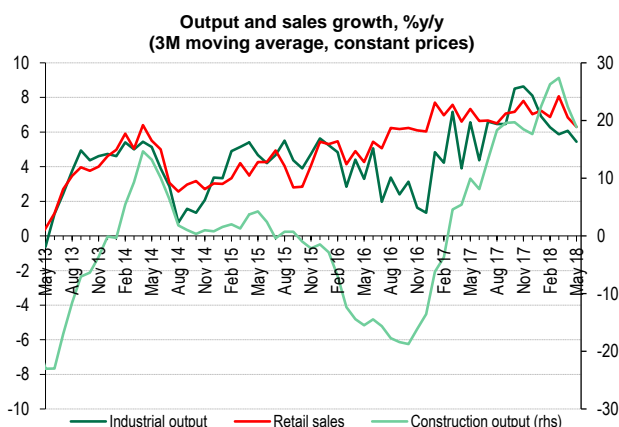
Last week in economy – Decent retail sales, strong output

■ Retail sales advanced in May by 6.1% y/y vs 4% in April, in line with the market consensus (6.0% y/y) and below our expectations (7.6% y/y). May saw a normalisation of sales of food (2.8% y/y) and in non-specialised stores (7.8% y/y), after two months of distortions caused by the timing of Easter and introduction of Sunday trade ban. Sales of durable goods were relatively weak, especially as regards cars and clothing due to a negative working day effect and combination of holidays. We expect the retail sales to accelerate in the next months and private consumption to remain the main driver of GDP growth this year rising by c5% y/y.

■ Industrial output rose in May by 5.4% y/y, above the market consensus (3.6% and our forecast, 3.9%). Industry was driven down from 9.3% y/y for April by the negative working day effect, but it seems that May results were boosted by foreign demand (export-oriented sectors recorded quite high growth rates). Still, we expect the gradual slowdown in the euro zone to undermine Polish exports and industry in the months to come. Construction rose by 20.8% y/y, in line with our expectations. We are expecting construction to slow down in the months to come due to capacity constraints.

■ May output figures exceeded forecasts, but 3M averages of real economic activity indicators suggest a slowdown of GDP growth in 2Q.

■ Wages in May decelerated from 7.8% y/y to just 7% while we expected the growth rate to ease only slightly from the previous reading. The market consensus was 7.1% y/y. The slowdown was due to calendar effects. The current state of the labour market, with severe labour shortages, continues to generate a pressure on wage hikes, but the process is gradual. Employment growth stayed at 3.7% while we and the market thought a rise to 3.8% was possible. In m/m terms, this was the weakest May for employment growth since 2009.

**Quote of the week** – Postponed investment, postponed hiring**Jerome Powell, Fed chairman, Bloomberg, June 21**

Changes in trade policy could cause us to have to question the outlook. For the first time, we are hearing about decisions to postpone investment, postpone hiring.

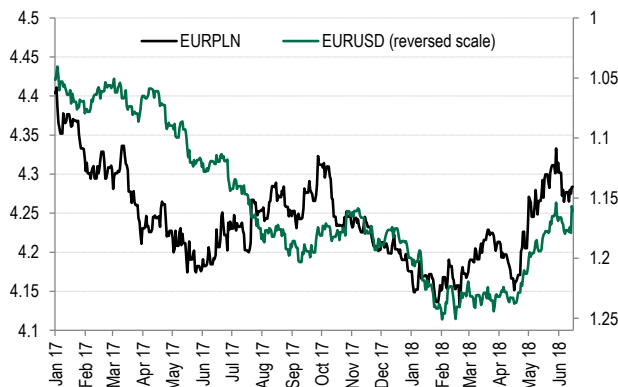
Mario Draghi, ECB president, Bloomberg, June 21

We will remain patient in determining the timing of the first rate rise and will take a gradual approach to adjusting policy thereafter.

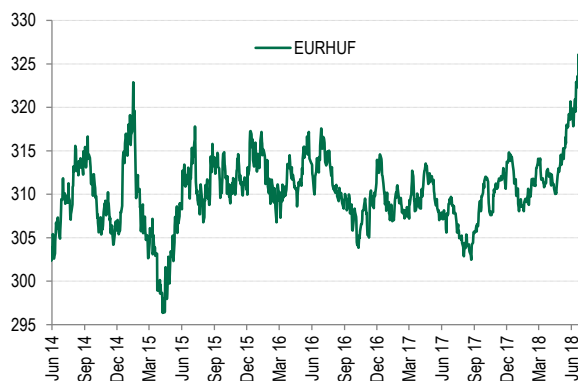
The central bankers who gathered at the conference in Sintra were preoccupied by the development of trade wars. They all tried to sound cautious when it comes to their plans for monetary policy normalisation. This is also the case for the Polish MPC as most members agree that monetary conditions and prospects in the nearest neighbourhood of Poland (read: euro zone) and prospects are an argument for keeping interest rates stable in the coming quarters.

FX and FI market – Counting losses after a "trade battle"

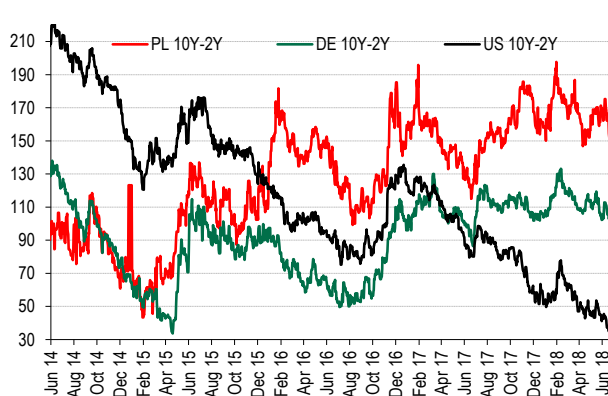
EURPLN and EURUSD



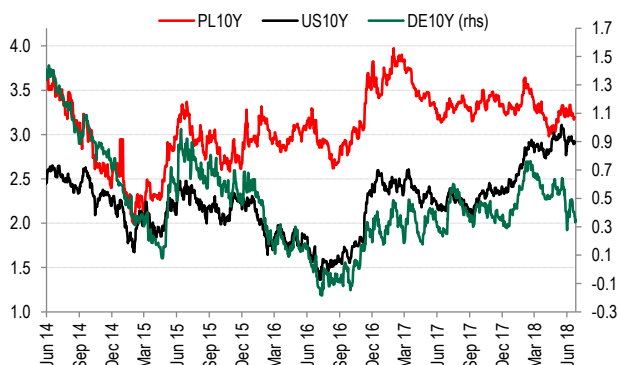
EURHUF



Bond curves slope



Yield of the Polish, German and US 10Y bonds



US dollar strengthens, zloty weakens, debt increases

▪ **FX** Last week, the USD strengthened while investors were selling the zloty and other CEE currencies. EURPLN climbed to 4.3300 on Thursday from 4.2850 on Monday, nervously reacting to a EURUSD drop to 1.1510 from 1.1590, which was due to information about introducing new trade tariffs. USDPLN rose above 3.7610 from 3.6790 as a result of higher EURUSD.

▪ **EURHUF** increased to the record high level as a reaction to the market fears of the negative influence of changes in the global trade on the Hungarian economy. The upward move of EURHUF did not stop despite the Hungarian central bank's attempt to support the currency by suggesting that its monetary policy will remain loose for a shorter –period than previously stated.

▪ **FI** The yields of Polish t-bonds and IRS rates have fallen, reacting to the news from the "trade battlefield" and following the yields of Bunds and US-treasuries. As a result, the IRS curve slipped by 15, 10 and 4bp respectively for the 10Y, 5Y, and 2Y tenors, while the bonds yield curve has shifted down by 12, 10 and 2bp.

What to watch for next week

▪ This week we will get to see the money supply and the unemployment rate for May. In both cases, our forecasts are close to the consensus. Neither of the above-mentioned data is usually closely monitored by investors.

▪ We believe, like last week, that the market players will be focused on the geopolitical tension, with new global trade regime negotiations still pending. In the core market, economic releases of important data are scheduled (flash Eurozone CPI, US personal spending and income). However, we feel that in the light of expected important changes in the global trade regime, investors will not be willing to deal with macro data given that the central bankers gathered at the Sintra conference underlined potential threats to the decisions and confidence of entrepreneurs and consumers, resulting from uncertainty about the future outlook for the global trade.

Market implications

▪ **FX** We expect some correction moves on the FX market after the marked strengthening of USD and sell-off of CEE currencies last week. This scenario is also to be supported by the EURUSD rebound from the support level at 1.15 (this year low) at the end of the week. This move should be accompanied by a slight appreciation of the zloty. EURUSD stayed slightly above the important support, while EURPLN is near the significant resistance at 4.34 (this year peak). It seems that the EURUSD rate will be crucial for the domestic currency in the coming days.

▪ **FI** This week, we expect profit taking and a rise in IRS rates and yields after the last week rally. However, the existing concerns about the global economic growth and the prospects of cancelling the regular bond auction will limit the upward-move of IRS rates and bond yields.

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Additional information is available on request. Please contact Bank Zachodni WBK S.A., Economic Analysis Department, al. Jana Pawła II 17, 00-854 Warsaw, Poland, phone +48 22 534 18 87, email ekonomia@bzwbk.pl