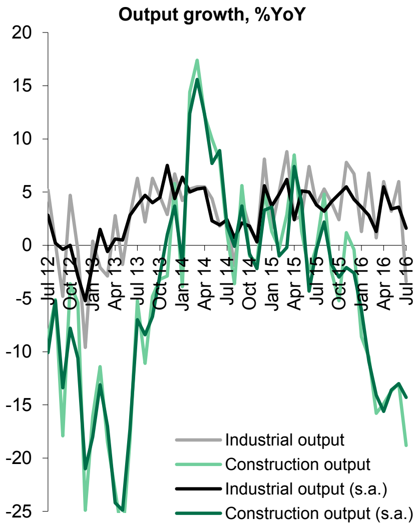
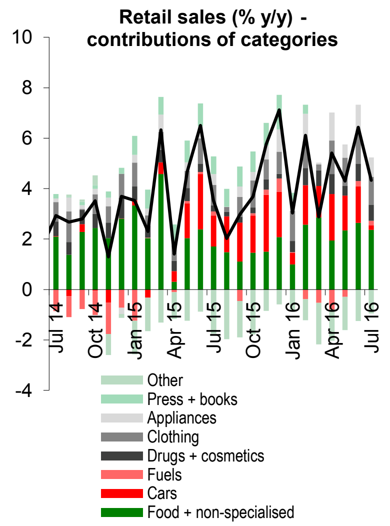
INSTANT COMMENT

18 August 2016

Weak data on activity at the start of Q3

Data on economic activity at the start of 3Q were below our expectations (not to mention market consensus). Industrial production was particularly disappointing, showing the decrease in annual terms (including the manufacturing sector), below all market forecasts. Although the figure was affected by a number of working days (minus two as compared with July 2015), the seasonally adjusted annual growth of industrial production was at a mere 1.6% (a half of average growth in 1H16). Construction output was also below forecasts (sharp fall by close to 20% y/y) and retail sales growth in real terms was at 4.4% (5.4% consensus, 5.0% our forecast). We expect the improvement in the data for August, but todays' release support our story of no GDP growth acceleration in 2H16. Recently we revised our forecast for GDP (c3% y/y in 2016 and below 3% in 2017). The data should be regarded as positive for the rates market, supporting the market to price-in monetary easing (although we do not think it will materialise) and are negative for the zloty (we see EURPLN back to above 4.30).





Industrial production down, construction sharply down

Industrial production for July disappointed, showing a fall by 3.4% y/y against our forecast of 0.5% growth and market consensus at 0.9%. The release was below all market forecasts. Although in July we had a negative effect of working days (two less as compared with July 2015), the seasonally adjusted figure showed a very low growth of only 1.6% y/y (as compared to the average of 3.4% in Jan-Jun period). The manufacturing sector's output also declined (by 2.8% y/y), but overall output growth was negatively affected to a larger extent by mining (down 8.7% y/y) and utilities sectors (down 9.1%Y/y).

Construction output for July was also below expectations, going down by 18.8% y/y (our forecast -17.2%, median forecast -15%). The fall in annual terms was widely expected, but this was the eight consecutive negative surprise in this release. The seasonally adjusted output growth in construction sector amounted to -14.3%, which was slightly below the average from the first half of the year.

Retail sales robust, but below consensus

Retail sales rose 4.4% y/y in real terms in July, below our forecast (5.0% y/y) and market consensus (5.4% y/y). Retail sales grew slower than in June when it advanced by 6.5% y/y. Detailed data showed that results in particular categories were near our expectations and a significant deceleration was recorded only in sales of autos that rose only by 1.9% y/y in real terms, the slowest growth since February 2015 (and vs 13% on average in 1H16). Pace of growth in all categories but "others" was slower vs June and this seems to confirm our thesis that robust growth in June was boosted by the positive effect of working days and holidays.

Retail sales growth remains solid, as the only negative surprise responsible for slowdown as compared to June was connected with car sales. We expect retail sales growth of 4-5% to be maintained in the following months, which would support our forecast of private consumption growth acceleration in the second half of the year. However, notice that data on retail sales do not show an impact of the so-called 500+ program (children benefit) despite the fact that until July a large part of money was already distributed (for period April-July i.e. 4 months!).

All in all, we maintain our view that private consumption acceleration in the second half of the year (strong labour market, social transfers) will not be enough to offset a weakness in exports (manufacturing production) and investments (construction). We maintain our recently-changed GDP growth forecasts of around 3% for the remainder of the year (and a year as a whole) and below 3% for 2017.

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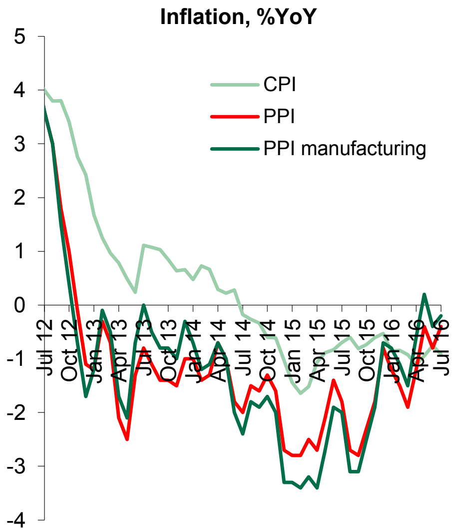

Producer prices gradually up

In July inflation PPI fell by 0.4% y/y (after decline by 0.8% y/y in June after revision) and by 0.1% m/m. On monthly basis this resulted from a decline in electricity, gas, steam and air conditioning supply(-0,4%) and in manufacturing (-0.2%). July was a second month in a row of decreasing prices in manufacture of coke and refined petroleum products (-5.1%), mainly due to fall in crude oil prices on international market (in July Brent prices fell by c7% m/m). On annual basis prices fall in nearly all categories, while in water supply; sewerage, waste management and remediation activities prices grew by 1.2%.

All in all, we expect gradual upward trend in inflation PPI, which should be on the positive territory in September. Our baseline scenario assume PPI at c1% y/y in December.

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