Bank Zachodni WBK
Grupa Santander

ECONOMIC COMMENT

31 August 2018

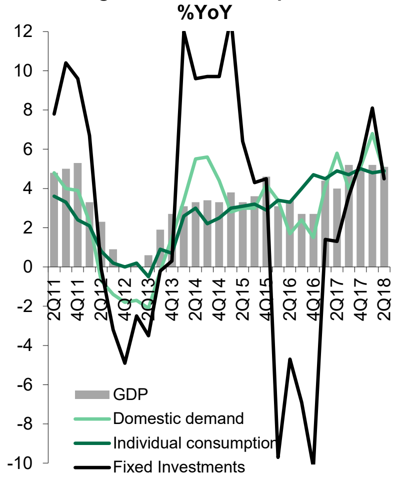
Strong growth, weak investment, inflation clinging to 2%

GDP growth in 2Q18 reached 5.1% y/y, confirming the flash estimate. The breakdown of growth surprisingly showed a significant slowdown in investments – to 4.5% y/y from 8.1% in 1Q, despite earlier signals from big companies and local governments about significant acceleration of investment spending. Stats office explained that the weakness came partly from changes in accounting of military spending and that other sectors saw improvement. Private consumption remained the main engine of growth rising almost 5% y/y. Net exports added 0.5pp to GDP growth. We still think that the peak of economic cycle is behind us and 2H18 will show a gradual slowdown of GDP growth.

Inflation remained in August at 2.0% y/y, in line with market expectations and above our 1.8% forecast. This was caused by a significant rebound of core CPI from 0.6% y/y to 0.8-0.9% - the first one so far this year. In our view this will not make the MPC more active. In the coming months CPI growth should gradually subside due to high base effects, towards 1.6% y/y in December. At the same time, core inflation should be going up to 1.2-1.3% y/y by year-end.

Piotr Bielski
tel. 22 534 18 87
piotr.bielski@bzwbk.pl

GDP growth and its components, %YoY



High GDP growth despite weaker investments

GDP growth in 2Q18 amounted to 5.1% y/y in line with flash estimate. Seasonally adjusted q/q growth reached 1% (vs flash estimate 0.9%).

The structure of economic growth in 2Q is surprising, especially the behavior of the investment component. Its growth rate shrank to 4.5% y/y from 8.1% y/y in 1Q (seasonally adjusted growth was just 0.4% q/q, the lowest in 1.5 years). Meanwhile, earlier information pointed to significant rebound of investments in big companies and in local governments in 2Q, which suggested that this category could come stronger, not weaker than expected. If total investments slowed down significantly despite higher activity of big enterprises and local governments, then probably the remaining part of the enterprise sector was still in investment stagnation or even saw investments falling y/y. We can suspect some link to difficult situation on labour market and rising cost pressure. It is likely that bigger companies are able to deal with these challenges more effectively. The data showing quickly growing number of firms' restructuring (mainly smaller companies) seem to support this theory. A milder interpretation could be offered, when taking into account the comment of Stats office director Maria Jeznach, that investment weakness was caused partly by accounting changes when it comes to military orders, while an improvement was seen after exclusion of the military sector. It does not remove our worries about SME investments, however.

The private consumption did not surprise, rising 4.9% y/y, in line with our estimates, and stayed the main engine of economic growth. In the next quarters we do not expect a change of its trend. We believe that the household income will continue to grow fast, thanks to rapid wage growth. It should help maintain elevated pace of consumer spending.

In 2Q18 the contribution of inventories to GDP growth decreased to nearly zero from almost 2pp in the 1Q18 (in line with our expectations). We still expect that in the next quarters, the impact of this category will be marginal.

Net export added to the 2Q18 GDP growth 0.5pp, which was a big improvement compared to the negative impact of this category in 1Q18 (-1.2pp). In our opinion, in the next quarters the influence of this category on GDP growth will return to the negative territory, due to the fact that export growth will be probably outpaced by imports.

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

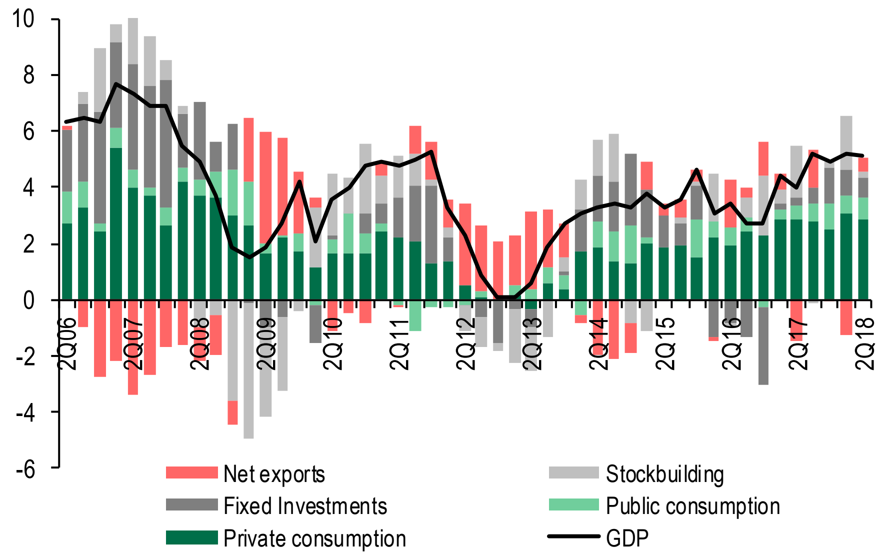
In our opinion GDP data support expectations that in coming quarters the gradual slow down of economic growth is probable. The strong disappointement with investments in 2Q18 (even though according to the Stats office it was caused probably by accounting changes) suggests that in the remaining part the year their pace of growth will not be very high. Without it, it will be difficult to maintain GDP growth above 5% y/y, even with solid consumption growth.

GDP growth and its components (% y/y)

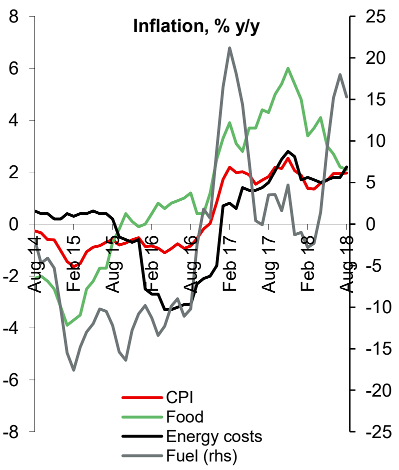
	2015	2016	2017	2Q17	3Q17	4Q17	1Q18	2Q18
GDP	3.8	3.0	4.6	4.0	5.2	4.9	5.2	5.1
Domestic demand	3.3	2.2	4.7	5.8	4.0	5.1	6.8	4.8
Total consumption	2.8	3.4	4.4	4.2	4.3	4.9	4.5	4.8
Private consumption	3.0	3.9	4.8	4.9	4.7	5.0	4.8	4.9
Public consumption	2.4	1.8	3.4	2.9	3.3	4.8	3.6	4.4
Gross accumulation	4.9	-2.4	6.2	11.9	2.8	5.5	21.0	4.9
Fixed investment	6.1	-8.2	3.4	1.3	3.6	5.4	8.1	4.5
Stockbuilding *	-0.2	1.2	0.6	1.9	-0.1	0.1	1.9	0.2
Net export *	0.6	0.8	0.1	-1.5	1.3	0.0	-1.2	0.5

* contribution to GDP growth (percentage points)

GDP growth breakdown, % y/y



Grzegorz Ogonek
tel. 22 534 19 23
grzegorz.ogonek@bzwbk.pl



Inflation stable in August despite high base effect

According to the flash estimate, CPI inflation stayed at the level 2% y/y in August, for the third month in a row. The result was in line with market consensus while we had expected a drop to 1.8% y/y. The August data were influenced by the high base effect in food prices and fuel prices. However, this base effect was offset by smaller than we had assumed decline of food prices in August this year and (mainly) by growth of core inflation components.

After the flash August release, we upgraded our core inflation forecasts for this month to 0.8-0.9% y/y from July's 0.7% y/y. It would be the first clear acceleration of core inflation this year. In our opinion, this data will not change the MPC stance, however. The gradual recovery of core inflation was widely anticipated. However until recently, we have been consistently surprised negatively by delaying core inflation rebound.

We predict that the next CPI y/y readings will be slightly lower as the high base effect will continue, and at the end of the year will see inflation at 1.6% y/y. At the same time, core inflation will gradually increase to 1.2-1.3% in December.

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