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Economic Comment

Fourth quarter will be worse?

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Industrial production rose 3.5% y/y in October, exceeding expectations, but staying below 1H19 average. Construction output was a major disappointment, falling 4% y/y. The data suggest a collapse in infrastructural investments. We see growing risk that the investment and GDP slowdown in the coming quarters may be more pronounced than earlier expected. November business climate survey showed deepening worries of Polish manufacturers about production outlook and decreasing confidence in retail trade.

Downturn in construction, not so bad in manufacturing

Industrial production growth rose in October by 3.5% y/y, exceeding expectations (our forecast 2.0% y/y, market consensus 2.5% y/y). Seasonally adjusted growth reached 3.7% y/y. This is quite solid result, suggesting that Polish manufacturing copes surprisingly well with the global slowdown and stagnation in Germany. A number of export-oriented industrial branches recorded a decent production rise. At the same time, the production growth was clearly below the average growth recorded in 1H19 (5.8% y/y after seasonal adjustment), which shows that the external slowdown is triggering some deceleration in Polish manufacturing anyway. This trend may even deepen in future, if we believe in local business climate surveys (see below).

The construction output in October was a major disappointment as it contracted by 4% y/y (-1.1% after seasonal adjustment), versus market consensus +5/6% y/y and our forecast 8.8% y/y. The biggest downturn was recorded in civil engineering (-8.6% y/y), which confirms a 'sudden stop' in infrastructure investments across the country, that we've been signaling earlier. This seems to be consistent with signals we observed coming from heavy industries and anecdotal evidence about stalemate in public tenders for infrastructural projects.

Overall, the data suggest that we should be cautious with forecasts of GDP growth in 4Q19. Unless the downturn in construction is a result of some one-off factor (that we cannot identify at the moment), the investment and GDP slowdown may be more pronounced than earlier expected. A first hint about the situation in investments may be detailed GDP data for 3Q19 to be released on November 28.

Industrial prices in decline

In October PPI growth dropped from 0.8% y/y to -0.1%, below market expectations. The drop was mainly due to manufacturing prices inflation going negative in y/y terms for the first time in 3.5 years.

New record in the number of completed flats

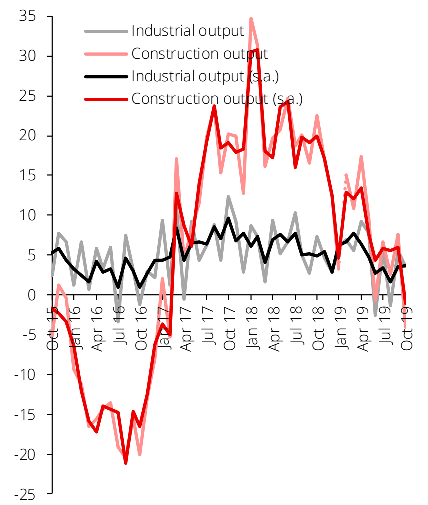
Significant slowdown was seen in real estate market, where the number of completed flats rose by 1.1% in October vs 27.4% in September. It is worth noting, that this time the one-off factors might be the reason because the monthly change of the variable has had high volatility recently. On a 12-month change basis the number of completed flats rose to 201.1k and was the highest since the data has been recorded (1991).

Simultaneously the number of building permits rose by 12.3% y/y while the number of house starts rose by 20.1% y/y. We think that dynamics on the flats market will be the bright spot in the construction sector in the nearest quarters.

Industry and retail trade concerned about future

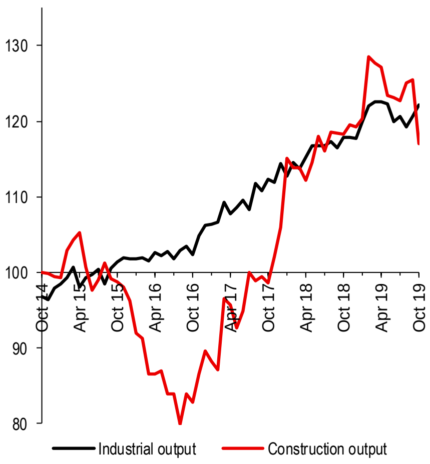
In November, GUS synthetic indicator of business climate declined from 100.9 pts to 100.2 pts, the second lowest reading in the last 2.5 years, with 100 being the long-term average. The sectors that contributed to the decline were industry and retail trade, while construction index went up and services index barely moved m/m (but is still far below the long-term average).

Production in industry and construction, % y/y



Source: GUS, Santander

Production in industry and construction, 2015=100



Source: GUS, Santander

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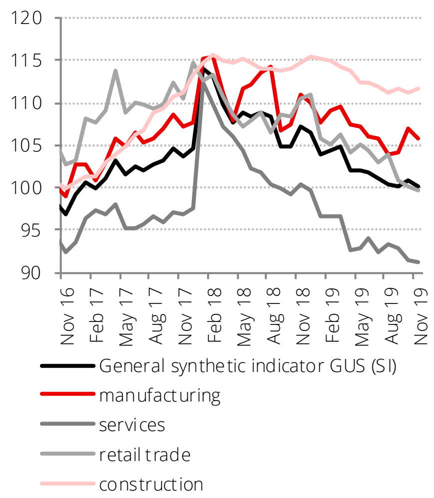
Industry index declined, but is now equal to the average of the past 6 months (so it seems the downward trend from 2H18-1H19 does not continue). A further deterioration in industry was entirely caused by further erosion of output expectations, to the lowest level in more than 6 years, while at the same time there was tiny improvement in new orders.

Retail trade index once again expressed worries about demand and signaled poor sales in recent months (the sales sub-index recorded one of the lowest values in the last 4 years) – for some time hard data on retail sales went against the signals from the business climate survey, but their October print was a negative surprise and there are signs that consumer confidence may start to worsen in the coming months.

Overall, the sentiment data confirm that the economy is in a slowdown phase.

Business sentiment indicators



Source: GUS, Santander

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