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Economic Comment

Strong wages amid drop in output and employment

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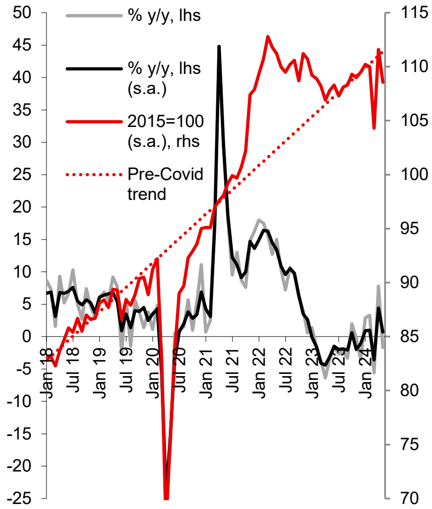
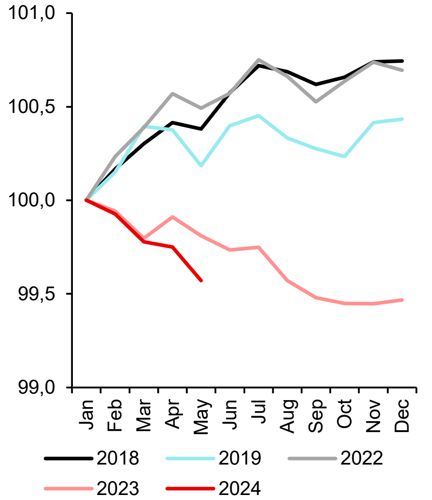
Industrial production unexpectedly fell by 1.7% y/y and 2.1% m/m on a seasonally adjusted basis in May. The market and we had hoped for positive y/y growth of around 1%. Also below consensus, but in line with our forecasts, was the employment data for the corporate sector (-0.5% y/y). May was another month in which activity was heavily distorted by calendar effects, making it difficult to interpret the data. Two long weekends apparently did their job. In these circumstances, the lack of deceleration and downward surprise from wages (they accelerated in May to 11.4% y/y from 11.3% y/y in April) may be indicative of persistent wage pressure. As wages are currently in the MPC's centre of attention, high wage growth may prove more important than doubts about industry. May PPI inflation rose to -7.0% y/y from -8.5% y/y in April, in line with expectations.

Industrial production in Poland



Source: GUS, Santander

Employment, January = 100



Source: GUS, Santander

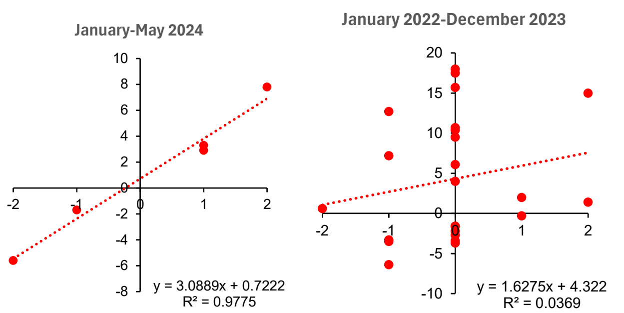
The industrial zigzag continued in May

Industrial production growth printed -1.7% y/y in May, way below market expectations at 0.9% y/y and our 1.2% y/y forecast. A substantial decline of the growth rate from April's 7.8% y/y (originally reported as 7.9% y/y) was widely expected due to working day differences but also due to the fact that unusually there were two long weekends in May. Seasonally adjusted production growth was 0.7% y/y in May, equal to the January-April average. In month-over-month terms this means -2.1% in May, which is quite a large decline, but markedly below March's -5.2% m/m.

The reduced level of activity was felt in all main components: out of the 9.5pp drop in the y/y production growth, manufacturing was responsible for 8.3pp, mining and utilities decreased their contribution by 0.3pp each and water and waste management by 0.1pp. Division by main groupings showed intermediate goods production falling by 4.9% y/y, investment goods down 2.7% y/y. Consumer goods, both durable and non-durable recorded marginal y/y declines and energy goods output was up 6.4% y/y.

Like in the previous two months (March's output collapse by 5.6% y/y and April's mighty 7.8% y/y rebound), the large May swing in the production data may be attributed to a large extent to calendar effects and it is hard to separate the impact of these from actual changes in the business environment. The fact that May weakness is really broad-based, as 27 out of 28 industries reported by the stats office recorded growth rates weaker than their historical medians for this month, suggests that the statistical effects played a major role this time. The difference in the number of working days is actually expelaining the growth rate of industrial output quite well this year (see charts below). We did not think this effect would be so strong, as this relationship was much weaker in the preceding two years.

Increase in industrial output versus calendar effect:



Vertical axis: industrial output growth in % y/y; horizontal axis: difference in working days y/y

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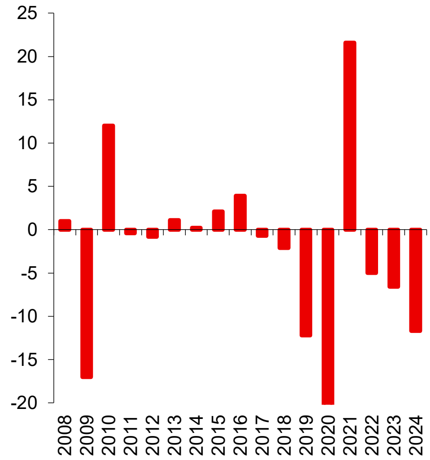
Rising business confidence indicators in the EU, if followed by a rebound in real economy, should provide Polish industry sector with the external demand it needs to return to moderate positive growth this year.

Further reductions of employment

The annual employment growth rate declined to -0.5% y/y in May from -0.4% y/y in April, in line with our forecast, but 0.1 percentage point below the market consensus. The decline of annual dynamics was caused by a decrease in the number of full-time equivalents by 0.2% m/m (-11.7k), mostly due to further reductions in the manufacturing sector (which shed 5.2k FTEs), but also due to job cuts in administration services (-1.8k), transport (-1.3k), and trade (-1.2k).

Although we do not predict major increases in employment, as the unemployment rate is already very low and the remaining free labour force is limited , we expect that the annual employment growth rate should improve in the following months and return slightly above zero near the end of the third quarter of the year.

Employment change in May, thousands



Source: GUS, Santander
Note: the Y axis was cut off at -20k, so it does not fully capture the decline in employment in 2020.

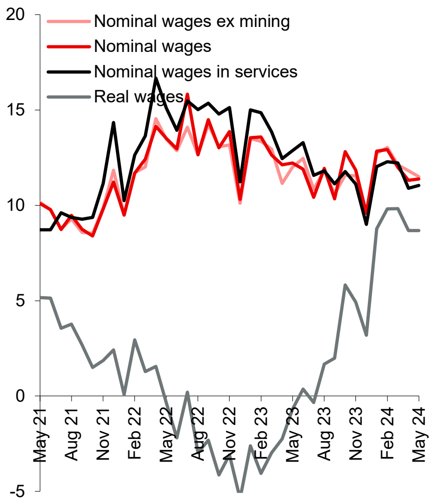
Wage growth remains stable

Wage growth accelerated in May to 11.4% from 11.3% in April, 0.1pp above our forecast and 0.1pp below the consensus. The acceleration of wage growth counterbalanced the increase in the inflation rate, allowing real wage growth to remain unchanged at 8.7% y/y. Wage growth outside of the mining sector declined from 11.8% y/y to 11.5% y/y and wage growth in the service sector rose from 10.9% y/y to 11.1% y/y. In monthly terms, wages declined by 3.3%, mostly due to lower payments of awards and bonuses.

Given the fact that industrial production in May was very weak (which we attribute to stronger than expected impact of calendar effects, i.e. two long weekends that shortened effective working hours), it seems that such wage growth should be interpreted as relatively strong.

According to our forecasts, wage growth should remain in double digits for the rest of the year, with real wage growth staying above 5% y/y.

Wage growth, % y/y



Source: GUS, Santander

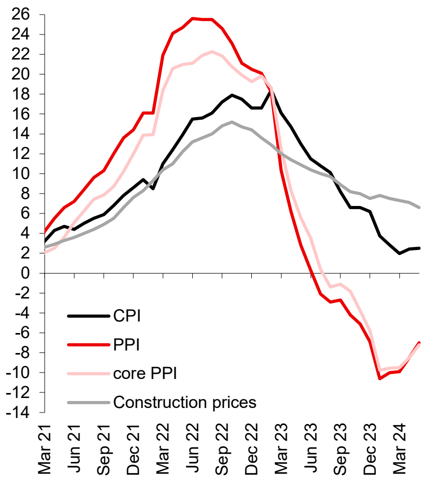
PPI rebounding slightly

May PPI inflation rose to -7.0% y/y from -8.5% y/y in April (revised data from -8.6% y/y), in line with forecasts. On a monthly basis, industrial prices fell by 0.3% m/m, largely driven by lower prices in manufacturing (-0.5% m/m), with upward trends in other sectors. In manufacturing, prices fell most sharply in the production of coke and refined petroleum products (-3.9% m/m), which was related to lower oil prices and the stronger zloty. However, other manufacturing sectors also recorded a slight decline in average prices (-0.2% m/m).

We estimate that the gradual economic recovery in Poland and the eurozone will translate into a gradual increase in prices in manufacturing, and by the end of the year, the annualised PPI may approach zero.

In the construction sector, price growth remains elevated and was 0.4% m/m in May, which translated into a decline in the annual price index to 6.6% y/y from 7.1% y/y in April.

Inflation, % y/y



Source: GUS, Santander

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