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Economic Comment

Data show weakness in September

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Most of today's data from the Polish economy for September surprised negatively. Industrial output was -0.3% y/y (-0.2% m/m sa), surprising to the downside for the third consecutive month, with weakness particularly evident in intermediate goods and export-oriented production. Improving soft leading indicators suggest some recovery, but this may be hampered by prolonged weakness in European manufacturing. Construction output narrowed the magnitude of the decline to -9% y/y (+0.9% m/m sa) from -9.6%, slightly above consensus. We think that over the next few months, positive momentum from the use of EU funds should start to show up in the construction production data, which should favour investments, although we also see a deceleration in the number of building permits and construction starts of dwellings. Employment growth remained at -0.5% y/y. Wage growth, on the other hand, unexpectedly slowed to 10.3% y/y from 11.1% y/y in August, with deceleration in services and manufacturing, but with strong wage growth in mining driven by bonuses. Real wage growth slowed to 5.2% y/y from 6.6% y/y. Although wage dynamics could reach single-digit levels in the coming months, this would be still strong wage growth supportive for private consumption. A deeper decline in September's PPI (to -6.3% y/y) with continued price declines in manufacturing suggests potentially lower pressure on core goods in the CPI. Tomorrow's retail sales data will give a better picture of 3Q activity, but at this point we maintain our forecast for GDP growth this year at 3% (above 3% y/y in 3Q) with the MPC's first rate cut in July 2025. Weakening in the labour market, lower inflation pressures, and a delayed recovery in the euro area as well as strong zloty could potentially increase risks to the baseline scenario towards a slightly faster rate cut.

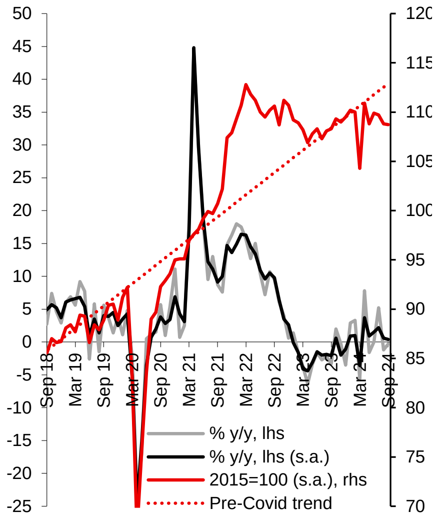
Industry – poor results despite improving sentiment

In September, the volume of Polish industrial output fell by 0.3% y/y, while the market was hoping to see +0.3% y/y and with our forecast at +1.1% y/y. This has already been the third negative surprise in a row, albeit the smallest of the three. In seasonally adjusted terms the annual growth rate of industrial output stayed positive at 0.4%, but fell by 0.2% m/m. There was also an upside revision of the previous, August print from -1.5% y/y to -1.2% y/y.

Positive annual growth was seen in consumer goods, durable and non-durable (2.3% y/y and 2.7% y/y, respectively) while intermediate goods output was down 2.6% y/y and investment goods dropped by 1.2% y/y (which still makes it the best print since April). According to our calculations, the aggregate result of industries focused on the domestic market (+2.0% y/y) remained well above the output performance of export-oriented industries (-2.3% y/y). Production of electrical appliances - the industry putting the most negative pressure on headline result - keeps showing gradual improvement (-15.7% y/y in September vs. -21.4% y/y in August), but not enough to make a material difference in total output. At the same time car production remains weak at -2.0% y/y (-1.9% y/y in August), despite the fact that the working day difference allowed for some rebound. A deterioration in y/y growth was also recorded, among others, in the production of tobacco products, rubber and plastic products, as well as the production of basic metals and electronic equipment. A fairly good result was achieved in the production of medicines, textiles, in products made of metal, wood and paper. In the production of other transport equipment, the annual growth rate returned above 18% y/y after a decline to 0.9% y/y in August.

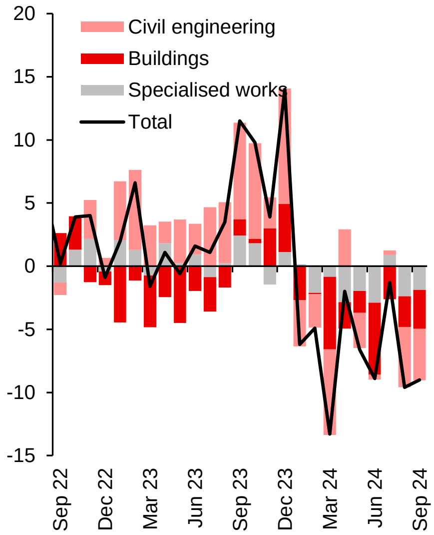
The worrying continued weakness of real industrial data remains in contrast with the swift rebound in business sentiment indicators covering the sector observed in recent months. The manufacturing PMI index for Poland rose between June and September from 45.0 pts to 48.6 pts, and the industrial ESI index has already recorded two increases in a row. The EU

Industrial production in Poland



Source: GUS, NBP, Santander

Breakdown of construction output, % y/y



Source: GUS, Santander

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funds-related projects may improve the situation of the sector in the coming quarters, but the rise of production volumes may come gradually.

Construction awaiting an impulse

Construction output declined in September by 9.0% y/y, roughly in line with expectations (us: -8.7% y/y, market: -9.8% y/y) and following a decline by 9.6% y/y in August. In monthly terms, output advanced by 12% m/m, which is pretty solid, yet coming in after a weak August (seasonally adjusted numbers point to an increase by 0.9% m/m in September after -0.5% m/m in August).

Quite strong performances were visible in civil engineering (-8.9% y/y vs -10.6% y/y in August) and specialised works (-7.9% y/y vs -9.8% y/y in August), while construction of buildings lagged at -10.1% y/y as compared to -7.9% y/y in August. Still, the general breakdown of construction in September remained fairly stable.

In general the data show that construction activity remains low, but is not deteriorating further. We think that the EU-funds impulse will become visible in the data in a couple of months' time.

Signs of slowdown in the housing market

In September, 16.6k dwellings were completed, i.e. 1.9% more than a year earlier, after an 18% drop recorded in August. However, a slowdown in market activity is visible in the data on the number of building permits and construction starts.

In September, building permits were issued for 23.0k constructions, i.e. 0.5% less than a year earlier, and the number of house starts amounted to 19.3 thousand, 0.8% more than a year ago. In August and in the previous months, both of these measures showed a double-digit growth rate. Our estimate of the number of projects in progress decreased in September for the first time since August 2023.

We assume that the market is starting to react to the deterioration of the outlook due to the decreasing chances for another program to support borrowers. However, a large increase in the number of building permits and construction starts in recent months should affect the increase in the number of dwellings completed in the coming quarters, which may have a negative impact on prices on the housing market.

Unexpected decline in wage dynamics

The pace of wage growth dropped from 11.1% y/y in August to 10.3% y/y in September, 0.8 percentage points below our forecast and 0.7 pp below the market consensus. As a result, real wage growth decelerated from 6.6% y/y to 5.2% y/y.

The main source of the decline in the general growth rate was the service sector, where, in line with our calculations, wage dynamics declined from 11.2% y/y to 10.0% y/y, over a percentage point below our expectations. The pace of wage growth declined also in the industrial sector, from 10.8% y/y to 10.4% y/y, mainly in manufacturing and in energy supply. The only sector which clearly surprised to the upside was mining, where wage dynamics rose from 4.9% y/y to 17.5% y/y, likely due to the payment of rewards in one of the companies from the copper industry. In effect, according to our estimates, wage dynamics outside of the mining sector dropped from 11.3% y/y to 10.1% y/y.

Overall, although wage growth managed to remain in double-digits in September, it is possible that in October it may decline slightly below 10% y/y. However, such a pace of growth will still be solid and should offer further support to consumption and the economic rebound.

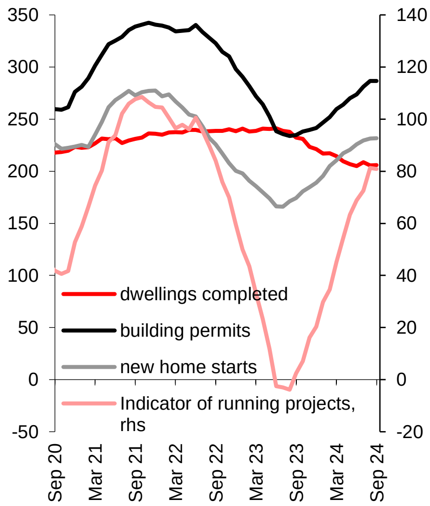
Employment growth remains stable slightly below zero

Employment growth remained at -0.5% y/y in September, unchanged from August. Month-on-month, the number of full-time equivalents dropped by c. 8k, almost exactly in line with our forecast.

As was also the case in August, the decline in the overall number of FTEs was caused mainly by manufacturing, which shed 4.5k FTEs. The next biggest reductions were registered in transport (-1.5k FTEs), and in trade and vehicle repair (-1k).

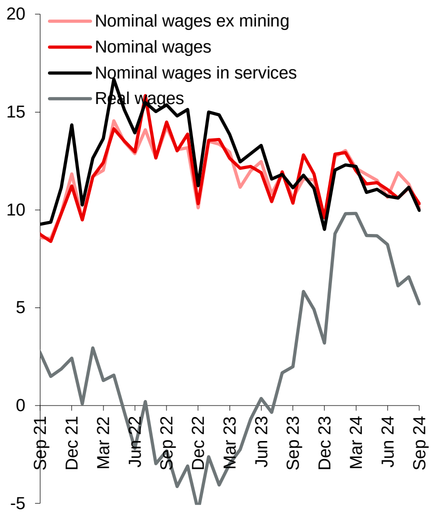
Employment dynamics will likely remain near their current level until the end of the year, but from the beginning of 2025, they should return to positive values. Later, as the economy further rebounds, and especially as investments begin to properly increase, employment should gradually improve.

Housing market statistics, 12m sums



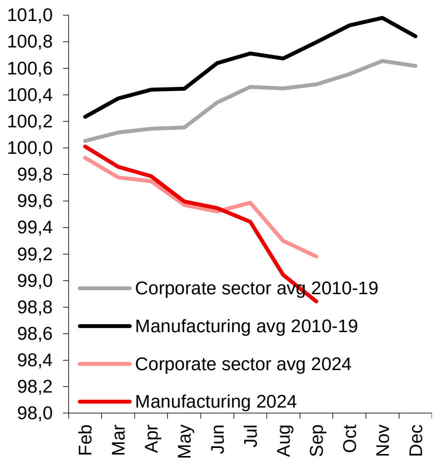
Source: GUS, Santander

Wage growth, % y/y



Source: GUS, Santander

Employment, January = 100



Source: GUS, Santander

Deeper decline in September PPI signals slow recovery ahead

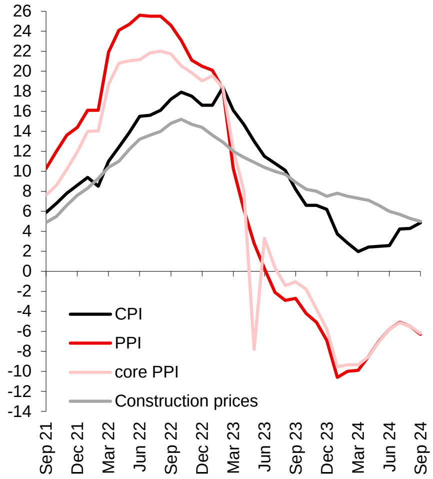
PPI annual price decline deepened in September to -6.3% y/y from -5.5% y/y in August vs. expected -5,7% y/y.

The downward surprise to a large extent resulted from a downward revision of price dynamics in most of categories for August, with the largest contribution coming from a drop in manufacturing (by -0.5% m/m vs. previous estimate at -0.1%). Effectively annual PPI growth was revised to -5.5% y/y from -5.1%. Moreover, price data surprised to the downside also for September with second consecutive month of 0.5% m/m producer prices decline with weaker than we presumed price dynamics in most of categories. Consequently the year-to-date PPI decline deepened to -3.2%. Meanwhile, core PPI inflation declined in September to -6.2% y/y from -5.5% y/y.

All in all, PPI data signal that amid continued weakness in European manufacturing the price pressures among producers are muted, which could ease inflation in CPI core goods.

We still expect that the annual PPI growth will gradually accelerate in the coming months amid low base from previous year though PPI inflation will likely reach positive territory only next year. This assumption is backed among others by presumed stability in the zloty exchange rate and mild increase in major commodities prices with only gradual pickup in demand in the euro area and stronger rebound in Poland.

PPI and other inflation measures, % y/y



Source: GUS, Santander