INSTANT COMMENT

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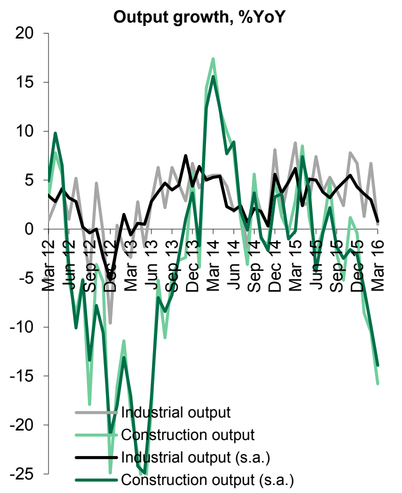
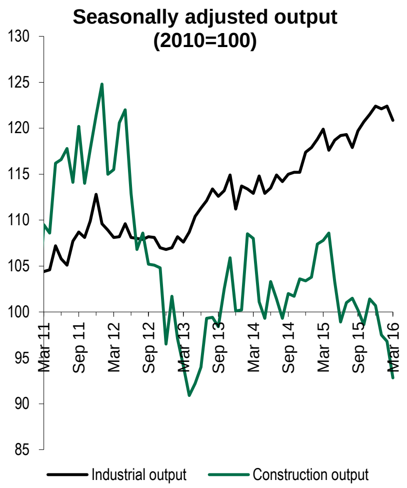
Surprisingly weak March

March increase in retail sales (by 3% y/y in constant prices), industrial production (by 0.5% y/y) and construction (-15.8% y/y) strongly disappointed. Currently, it is hard to identify the source of this slowdown, because both the situation in Poland's economy – the improvement on the labor market, decent income growth and improving consumer optimism – and abroad – improvement in the economic activity of our main trading partners, rising foreign orders – seem to support continuation of positive trends. Although it is hard to disregard the poor data for March, however, we assume that the growth in industrial output and retail sales should bounce up later this year, supported, among others, by revival of economic activity in Europe and an increase in consumer spending boosted by '500+' child benefit programme. Poland's Statistical Office revised up GDP growth in 4Q15 to 4.3%, mainly due to higher public consumption. In our opinion, in the first quarters of 2016 economic growth is unlikely to stay above 4% y/y, while starting form the third quarter of 2016 GDP growth will be supported by a significantly higher growth of private consumption.





Output clearly disappointed

Industrial output grew merely 0.5% y/y in March vs market consensus at 3.9% y/y and our forecast at 4.4% y/y. After the seasonal adjustment the output grew 0.8% y/y, at the slowest pace since August 2014. Even bigger disappointment was recorded in the construction sector where the output contracted 15.8% y/y (and 13.9% y/y after the seasonal adjustment, the weakest performance since June 2013) while the market expected -8.7% y/y and we forecasted -12.8% y/y. This time, in contrast to the two previous months, it is hard to blame the calendar effect for the annual deceleration of output growth, as the number of the working days was the same in March 2016 and in 2015. Very weak industrial output is particularly surprising given the fact that the most recent business climate surveys were showing quite high optimism among the companies, rising output and the new orders, mainly the foreign ones. At the same time, economic activity indicators for the euro zone – our biggest trading partner – have also improved recently and the zloty's exchange rate is making Polish exports competitive. This all should support exports and the industrial output. Although we are far from ignoring the weak March result, we still expect output to recover later in the year fueled by rising economic activity in Europe and rising domestic orders amid accelerating domestic demand. Our economic growth forecasts for the most of the euro zone countries are above the market consensus.

The situation looks different for the construction sector that is probably still burdened by the slowdown in public investments and infrastructure projects co-financed from the EU funds. For the companies specialized in civil engineering output contracted by nearly 22%. We do not expect any fast improvement in construction in the months to come.

Retail sales below expectations

Real retail sales rose in March by 3.0% y/y (vs 6.2% y/y in February) as compared to market expectations at 5.8% y/y and our at 6.8% y/y. In nominal terms sales rose by 0.8% y/y.

We were expecting that retail sales will be supported by the Easter effect – in 2016 it was scheduled for 27 March and in 2015 for 5 April, so some shopping, especially concerning food, was conducted earlier. And our expectations were right: food sales rose by 6.4% y/y (vs 5.8% y/y in February) and other sales in non-specialised stores by 9.7% y/y (vs 8.5% y/y in February). Our forecasts were accurate also as regards car sales (11.9% y/y), fuel sales (-3.5% y/y) and drug sales (10.6% y/y).

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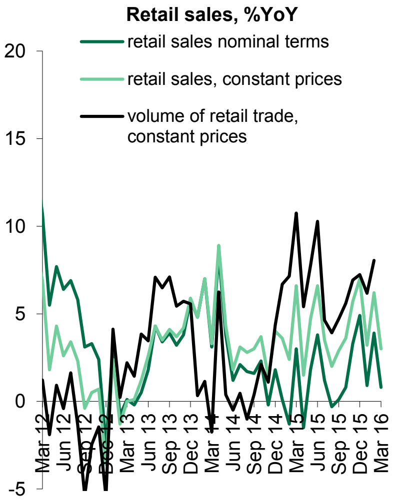

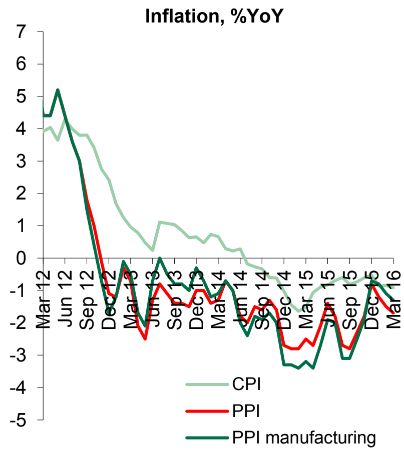

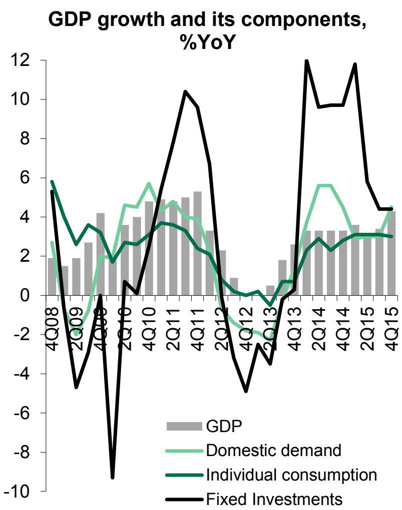

Meanwhile, our forecasts of growth in other categories were strongly missed – clothing sales rose by 4.2% y/y (vs 20.6% y/y in February and our forecast at 19.9% y/y), household appliances by 0.9% y/y (vs 15.1% y/y in February and our forecast at 14.1% y/y), press by 0.6% y/y (vs 7.0% y/y in February and our forecast at 5.9% y/y), other sales at -14.1% y/y (vs -7.4% y/y in February and our forecast at -7.9% y/y). We think that retail sales suffered from a break in seasonal pattern, so some shopping conducted usually in March was shifted, e.g. to February, which was much better than expected. Please note that a similar phenomenon was visible in February's data on balance of payments – imports surprised to the upside, mainly under impact of sales of electrical appliances. In our view, this development is a reason to cut March's import forecasts.

In whole Q1 retail sales climbed by 4.1% y/y and we are expecting it to oscillate slightly above this level, which will be connected to stronger private consumption.

Deeper deflation in producer prices

Producer prices declined in March by 1.7% y/y (after fall by 1.5% y/y in February – data after revision), more than our (-1.3% y/y) and market (-1.4% y/y) expectations. On monthly basis producer prices dropped by 0.1%. Interestingly, in previous months decline in PPI inflation mainly resulted from fall in prices of both oil and other commodities. This time in March prices in manufacture of coke and refined petroleum products increased by 6.6% m/m, while prices in mining of metal ores grew by 6.5% m/m. Despite the strong growth in these categories, prices in total decreased, which resulted from fall in prices of other categories, mainly in manufacture of chemical products (-1.3%), paper (-1.2%), computers (-0.9%) and cars (-0.8%). It seems that deflationary tendencies intensify in sectors which so far have remained weak or moderate.

March data on PPI confirmed earlier signals from data on leading indicators - according to PMI for the manufacturing sector in March was the seventh month in a row of falling purchase prices. We expect that annual PPI growth will remain negative until the end of this year, although the pace of decline should slow down from month to month.

Higher GDP growth in 4Q2015

The statistics office revised its quarterly GDP growth estimates for the past three years, so GDP growth for 4Q2015 went up from 3.9% to 4.3% y/y. At the same time, previous quarters were revised slightly downwards, so the annual growth rate for the entire 2016 stayed unchanged at 3.6%. The seasonally adjusted GDP growth for 4Q2015 was revised upwards to 1.5% q/q, the highest level in five years (previous estimate was at 1.1%). Interestingly, the upward revision of GPD growth in 4Q was primarily due to a strong rise in public consumption – to 8.7% y/y from 4.8% y/y, so contribution of this component to GDP growth rose to 1.7pp from 0.9pp. At the same time, investment growth went down to 4.4% y/y from 4.9% y/y, similarly as growth rates of export and import (yet net exports contribution to GDP growth remained unchanged).

In our view, maintaining a 4+ growth rate in the first two quarters of 2016 is unlikely. However, from 3Q on, the GDP growth will be supported by much higher private consumption growth after start of payments from the 500+ programme.