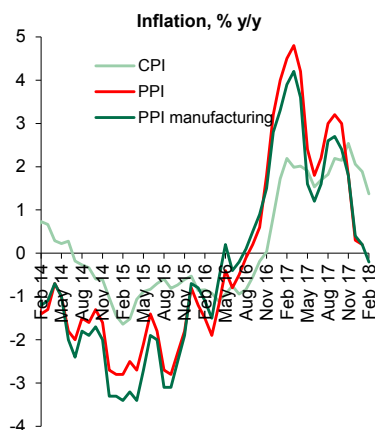
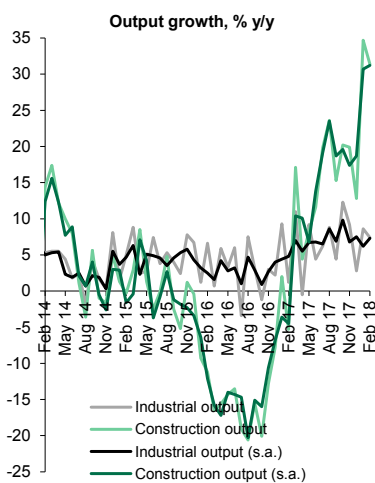


# ECONOMIC COMMENT

19 March 2018

## Demand boom in construction sector continues

Construction output rose in February by 31.4% y/y vs. 29.8% expectations, while industrial production at 7.4% y/y failed to reach the consensus of 8.1% y/y, but came above our 6.7% call. We are not expecting the construction output growth to remain as strong as in January and February. In the upcoming months the construction output will be under pressure of capacity constraints. The seasonally adjusted industrial output growth of 7.3% is quite close to an average calculated since mid-2017, and significantly better than 6.2% for January. We maintain our view that the GDP growth in 1Q18 will be comparable or only slightly lower than the result for 4Q17 of 5.1% y/y.



### Industrial output still in good shape, construction sector again above 30% y/y

Construction output rose in February by 31.4% y/y vs. 29.8% expectations. Industrial production (7.4% y/y) was below market expectations (8.1% y/y), while we forecasted a slowdown to 6.7% y/y. Civil engineering output rose by 65% y/y, despite the extremely low temperatures in the lasting for a half of the month. It shows the strength of demand, before the local government elections (planned for autumn) and the stronger utilisation of EU funds vs. year ago. However, we still do not expect that the pace of growth above 30% recorded in the first two months of the year could be maintained. In January and February, the level of activity is relatively low comparing to the rest of the year which makes it easier for the sector to achieve a high rate of growth. In the next months, the construction output will likely be limited by the supply side. Going forward, the construction sector should be facing further capacity constraints.

After seasonal adjustment, February's industrial output growth recorded 7.3% y/y, roughly equal to 2H17 average and well above January's 6.2%. Detailed data showed that production of energy had a big positive contribution which might have been due to the cold weather. "Other transportation" fell 7.2% y/y and this was the biggest factor pulling the headline down. However, this category is very volatile and does not reflect the overall economic situation well. Production of machinery and equipment, that is largely exports-oriented, was very strong growing 20.5% y/y. This, however, may not only mean that external demand is strong, but also that investments are reviving in Poland.

We keep our view that pace of the GDP growth in 1Q18 will be comparable or slightly below 5.1% y/y recorded in 4Q17.

### PPI deflation

PPI declined to -0.2% y/y in February from +0.2% y/y in January. Thus, PPI returned to the deflationary territory, left in August 2016. In monthly terms, producer prices fell by 0.3% mostly due to a fall in oil prices and stronger zloty versus the dollar (oil price in PLN fell by 7.5% m/m). In our view, in the upcoming months the PPI will return to positive growth rates under impact of weaker zloty and stop in downward tendency of commodity prices. In the preceding quarters, PPI was quite a good forecast of trends in CPI. Low PPI readings suggest no major growth in CPI inflation in the upcoming quarters.

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