Bank Zachodni WBK
Grupa Santander

WEEKLY ECONOMIC UPDATE

23 – 29 April 2018

This week, we will see April economic activity indicators. Should they continue to decline, doubts over the pace of the economic growth in 2H18 would become more serious. Polish retail sales data should also be watched closely. Our forecast assumes strong growth that could neutralize the disappointing industrial output figure, at last partly. The stat office will release also revised quarterly GDP data for 2016-2017. General trends are rather unlikely to change but the updated numbers may influence forecasts for 2018. Money supply and unemployment data should be market-neutral. At the same time, the stat office statistical bulletin may shed some more light on the breakdown of wages growth in March and help assess chances for further acceleration in the months to come.

As regards the debt market, the Friday's bond auction will be an important event as it will be preceded by maturity of large amount of bonds and coupon payments (PLN15bn in total). Thus, the demand should be decent.

After a series of weaker European data, market will watch any changes in the ECB tone. Should there be any hints for delaying QE program and postponing rate hikes, this could fuel yields down trend.

Economic calendar

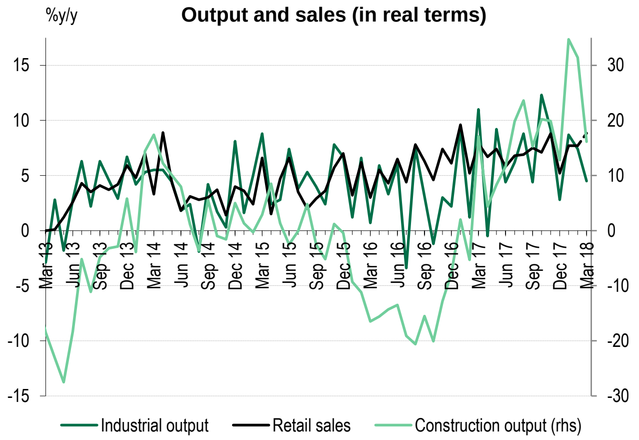
TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		MONDAY (23 April)					
09:30	DE	Germany Manufacturing PMI	Apr	pts	57.5	-	58.2
09:30	DE	Markit Germany Services PMI	Apr	pts	53.7	-	53.9
10:00	EZ	Eurozone Manufacturing PMI	Apr	pts	56.0	-	56.6
10:00	EZ	Eurozone Services PMI	Apr	pts	54.6	-	54.9
10:00	**PL**	**Retail Sales Real**	**Mar**	**% y/y**	**7.9**	**8.8**	**7.7**
16:00	US	Existing Home Sales	Mar	% m/m	0.18	-	2.97
		TUESDAY (24 April)					
10:00	DE	IFO Business Climate	Apr	pts	102.8	-	103.2
14:00	HU	Central Bank Rate Decision	Apr-18	%	0.9	-	0.9
14:00	**PL**	**Money Supply M3**	**Mar**	**% y/y**	**5.2**	**5.6**	**4.9**
16:00	US	Consumer Conference Board	Apr	pts	126.0	-	127.7
16:00	US	New Home Sales	Mar	% m/m	1.13	-	-0.6
		WEDNESDAY (25 April)					
	PL	**Buyback PS0418 (PLN11.5bn)**	**Apr**				
10:00	**PL**	**Unemployment Rate**	**Mar**	**%**	**6.5**	**6.6**	**6.8**
		THURSDAY (26 April)					
13:45	EZ	ECB Main Refinancing Rate	Apr-18	%	0.0	-	0.0
14:30	US	Durable Goods Orders	Mar	% m/m	1.05	-	3.0
14:30	US	Initial Jobless Claims	Apr-18	k	230	-	232
		FRIDAY (27 April)					
11:00	EZ	ESI	Apr	pct.	112.0	-	112.6
11:30	**PL**	**Bond Auction**					
14:30	US	GDP Annualized	1Q	% Q/Q	2.1	-	2.9
16:00	US	Michigan index	Apr	pts	98.0	-	97.8

Source: BZ WBK, Reuters, Bloomberg

ECONOMIC ANALYSIS DEPARTMENT:
al. Jana Pawła II 17, 00-854 Warszawa fax +48 22 586 83 40
email: ekonomia@bzwbk.pl Web site: http://www.bzwbk.pl
Piotr Bielski +48 22 534 18 87
Marcin Luziński +48 22 534 18 85
Grzegorz Ogonek +48 22 534 19 23
Konrad Soszyński +48 22 534 18 86
Marcin Sulewski +48 22 534 18 84

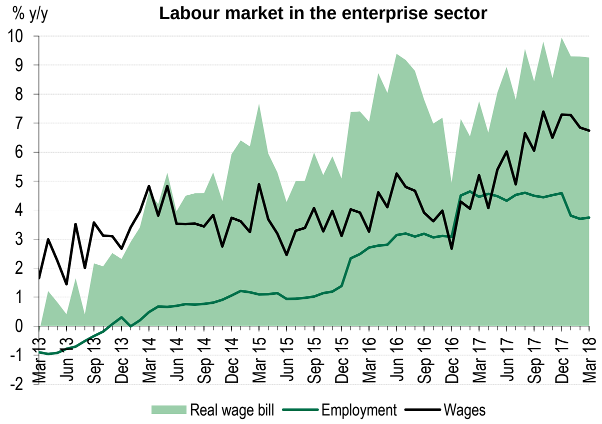
TREASURY SERVICES:
Poznań +48 61 856 5814/30
Warszawa +48 22 586 8320/38
Wrocław +48 71 369 9400

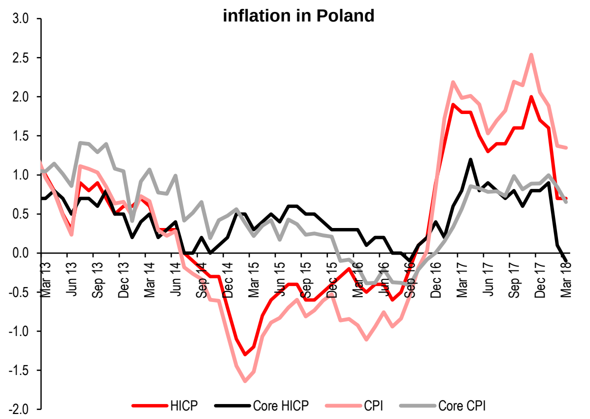
What's hot next week – Last hope for 1Q GDP



- A strong retail sales reading could offset the dismal March output figures, and prevent downgrades to 1Q GDP growth forecasts. Our real retail sales estimate (8.8% y/y), supported by unparalleled levels of consumer optimism and strong real wage bill growth, is above consensus. On the other hand, cold weather in March discouraged clothing sales. Additionally, Sunday trade ban was introduced in March, increasing uncertainty of the result.
- March Statistical Bulletin will help assess the breadth of the standstill in wage growth and the slowdown of industrial output.
- March MPC minutes come after Jerzy Kropiwnicki's remarks that the Council wants to discuss unconventional measures, just in case (given that many members reject further rate cuts), and that CPI escaped south from the path projected by the NBP staff.
- There have been press reports that Convergence Programme Update due this week will show 2019 (general elections year) fiscal deficit at just 1.5% GDP, vs 2.1% MinFin estimate for 2018 and a falling debt/GDP path.

Last week in economy – Rating outlook up, output growth down





- S&P improved outlook of Poland's BBB rating to positive from stable. The move was based on assumption that GDP growth in Poland will stay strong in 2018 thanks to solid external demand, large inflow of EU funds and strong fundamentals of the economy. A rating upgrade will be possible, if debt/GDP ratio continues falling. A downgrade would require a deterioration of economic and fiscal situation, as well as EU funds freeze. The agency sees 2018 GDP growth at 4.5% (vs its 3.8% forecast from December). A very positive assessment of current policies is important for odds of getting an upgrade. In S&P' view, tax administration reform 'have generated a secular increase in revenues' and the government 'was able to navigate risks associated with overheating as well as complex relations with the EU' (despite still unresolved rule-of-law spat). Frank Gill, S&P analyst, doubted it would be possible to achieve further improvement in VAT collection, but said that the newest government proposals were not worrying as regards fiscal impact.
- "Dziennik Gazeta Prawna" cited a draft of the Convergence Programme Update which assumes no cut in CIT rates, maintained cap on social security contributions for high-earners and 2.3% public sector wages growth in 2019.
- HICP inflation was 0.7% y/y in March, just like in February. Core HICP excl. food and energy fell to -0.1% y/y, equal to the all-time low set in Sep-16. Weakness of core inflation is putting the expected acceleration of this category this year in question.
- Industrial output in March was weak, 1.8% y/y vs 7.4% in Feb and 3% consensus. The disappointing industry print showed up after a series of weak data on German economic activity. Construction output rose 16.2% y/y. See our comment.

Wages grew 6.7% y/y in March vs 6.8% in Feb. Employment growth stabilized at 3.7% y/y. See this comment.

Quote of the week – Morawiecki's five-pack

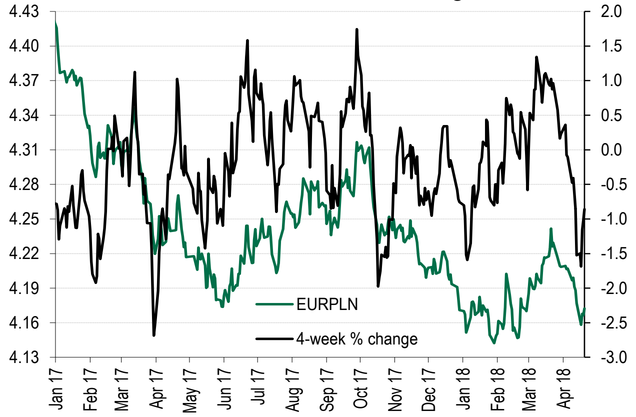
Mateusz Morawiecki, Prime Minister, PAP, April 15

We want every child in the school age, below 18, to be getting PLN300 as 'school kit' before every year of their education. There are no extra conditions, all parents will receive it. For the second time, we will decrease taxes for SMEs. In the coming years, the government will warrant PLN23bn for Accessibility+ programme: it is as much as we spend on 500+ (child benefit programme), to improve living standard of the elderly, the weak, the disabled. Soon the government will propose additional, minimal state pension for women who, having reached the retirement age, do not get such transfers, but had given birth to at least four children. Already this year we will assign an amount never assigned before to upgrade of the most needed local roads.

At the ruling Law and Justice (PiS) convention, Mateusz Morawiecki announced new plans of his government. In 2019, CIT rate for small companies will be cut to 9% from 15% and their social security contributions will be linked to sales revenues. The government intends to earmark more funds for roads and additional support for elderly people and families. We calculated that new measures might cost PLN4.5bn per year (c0.2% of GDP), which is fairly low. In our view, in 2019 the spending rule will allow public expenditures to rise by at least PLN30bn. Part of this will be consumed by programmes that have already been introduced (such as lower retirement age) but the cost of new ideas looks moderate so there should not be a problem finding fiscal space for them. More on the new proposals in this comment.

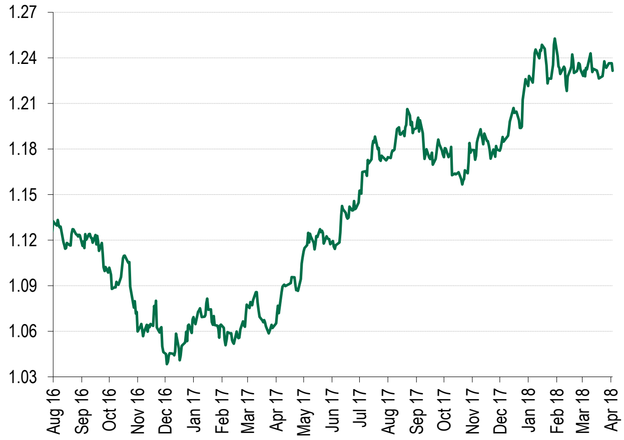
Foreign exchange market – Waiting for data and ECB

EURPLN and 4-week % change

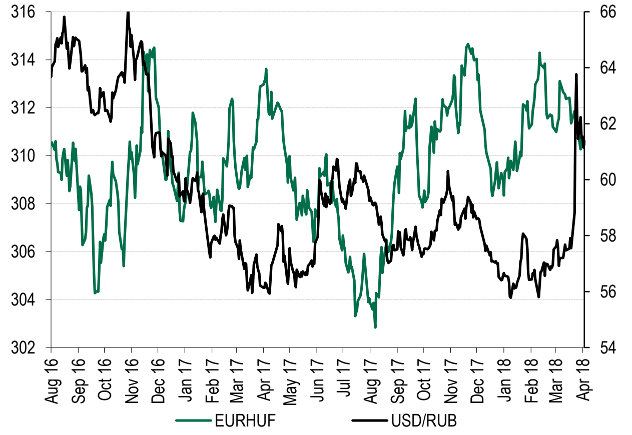


CHFPLN

EURUSD



EURHUF and USDRUB



Zloty appreciation stops

- EURPLN down-trend lasting for the previous three weeks stopped. The zloty gained to 4.15 per euro at the beginning of the week in reaction to the surprising Poland rating outlook upgrade by the S&P but in the next days the Polish currency gave up gains. USDPLN dropped to 3.345 from 3.38, GBPPLN moved down to 4.76 from 4.81.
- CHFPLN eased to 3.46 (its lowest since December 2014) from 3.51. This was possible not only thanks to lower EURPLN, but also higher EURCHF that reached 1.20 – last time seen in January 2015 when the SNB surprisingly stopped its policy of preventing the exchange rate from falling below this level.
- The zloty is moving pretty closely with stocks and Polish bonds. However, that although 10Y yields broke their local lows, EURPLN remains above its 2018 bottom. Bonds gains are driven by both low inflation numbers and weaker outlook for the global economy and the latter may be curbing zloty gains. The most recent global data have shown some moderation in pace of economic growth and the trade wars are rather unlikely to improve the market sentiment. This week, we will see flash April PMI's and German Ifo index that might give some clue if the sentiment cooling seen in the previous months continues.
- Looking at purely statistical measures, 4-week % change of EURPLN has reached its lowest since late 2017 suggesting that scale of the exchange rate recent short-term decline is starting to look too big, when compared to historical pattern.
- We think the zloty could give up part of recent gains and we do not expect EURPLN to resume the down-trend.

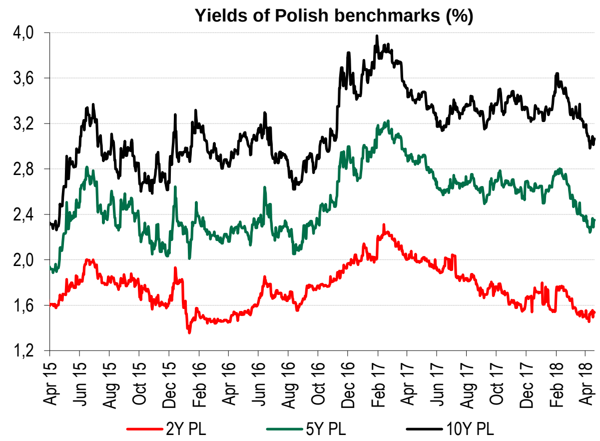
EURUSD still in a narrow range

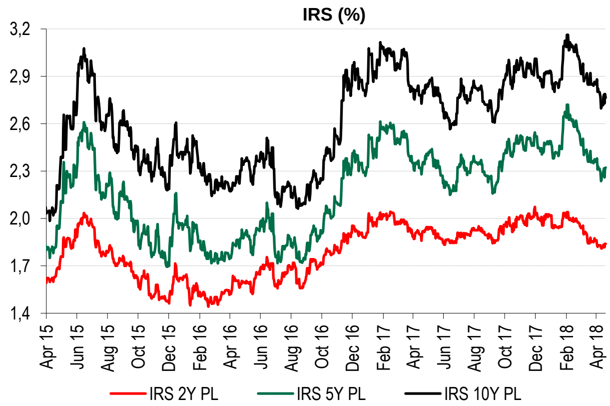
- EURUSD remained virtually unchanged oscillating in a narrow range around 1.235.
- Since the beginning of the year, EURUSD has been holding in a horizontal trend. Recently, the volatility has faded further.
- We are still waiting for a trigger that could at least push the exchange rate closer to either lower or upper end of the 1.22-1.255 range. This week, the ECB holds a meeting and looking into the calendar, this even seems to be first candidate to spur volatility in the coming days. At the same time, the geopolitical issues should not be ignored despite they receded into the background in the last few days.

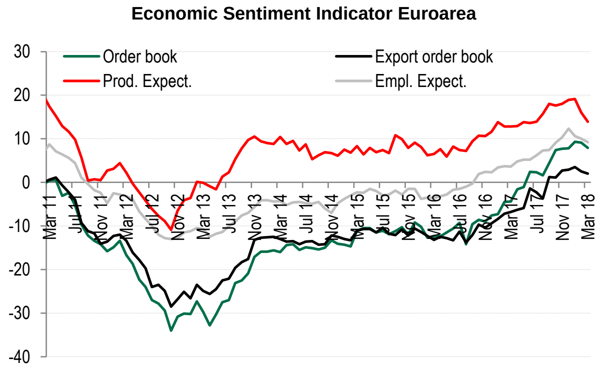
No big change in the region

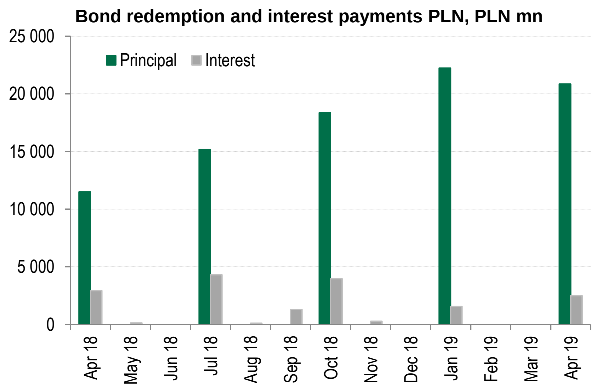
- In the case of the other CEE currencies, the koruna and forint did not move much and the ruble continued to recover vs the dollar after severe losses suffered in the previous week.
- This week, Hungarian central bank holds a meeting. We do not expect any meaningful changes in bank's rhetoric and so there should be no big impact on the forint.
- As regards the ruble, the currency recovered slightly as the geopolitical issues receded somewhat into the background. However, the US-Russia tensions are not over yet and we do not expect the ruble to start its sustainable recovery from the current levels already.

Interest rate market – PMI in the spotlight









Oil prices and profit-taking push yields up

- Over the last week, the yields have been rising following the core bond market. The yields in the 5-10Y segment increased stronger (the rates elevated by 4-6pb) than in the 1-2Y segment (where rates up by 1-2bp). At the beginning of the week, the domestic bonds sell-off was triggered by an information that S&P decided to revise outlook to positive. In the following days, the yields were decreasing. At the end of the week, the domestic yields returned to upward trend. The yields upward move was fueled by the core markets sell-off, where the investors were affected by oil and certain metals prices hike (as a reaction to the sanctions imposed on Russian companies).

Short end will benefit from bonds redemptions

- This week, we expect the domestic yield curve to decrease slightly (in a 1-4Y segment), due to the redemption of the PS0418 bonds (PLN11.5bn) and coupon payment (cPLN2.8bn). This means that up to the first auction in May, scheduled for 10 May, the outstanding volume of Polish debt will be substantially lower.

Long end under pressure

- We anticipate a slight upward move on the long end of the yield curve, due to the global market mood, where the slight upward pressures will be visible as a reaction to higher prices of oil and certain metals. Moreover, the expected higher supply of debt in the US will likely be an additional negative factor for the long end of the domestic curve. In our opinion, the European leading indicators release (PMI, Ifo) will negatively affect the bonds market only to marginal extent, due to the weakening of downward PMI trend or small rebound of Ifo. We believe that the upward pressures on yields will be weakening before the ECB conference (scheduled for Thursday). We think that president of ECB Mario Draghi will not be ready to change the rhetoric to more hawkish due to the negative impact of strong EUR on the Eurozone economy manifested in constantly decreasing reading of leading indicators. The aforesaid negative factors for the domestic bonds will likely be neutralized by a limited supply of domestic debt and still high demand for bonds from Polish financial institutions. The bigger pressure on the bond prices will still be limited by perspectives of low inflation.

Bonds auction

- At the next auction (scheduled for the 27 April), we expect PLN8bn supply (the upper range of PLN4-8bn planned by Ministry of Finance to sell). We think that the demand for both OK0720 (new 2L benchmark) and WS0428 bonds will be levelled (among the offered OK0720, PS0123, WZ0524, WS0428, WZ0528). We expect lower demand for floating-coupon bonds of the WZ series.

Additional information is available on request. Please contact Bank Zachodni WBK S.A., Economic Analysis Department, al. Jana Pawła II 17, 00-854 Warsaw, Poland, phone +48 22 534 18 87, email ekonomia@bzwbk.pl