

11 January 2019

# Weekly Economic Update

## Brexit – take two

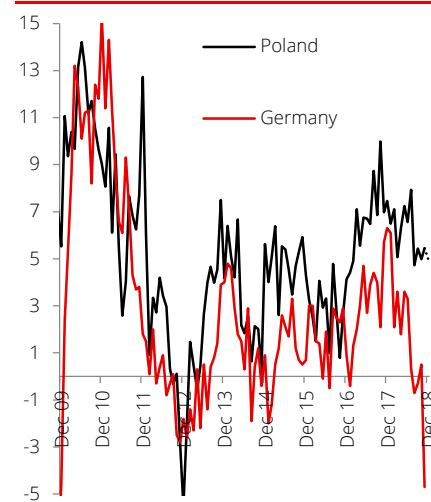
### What's hot next week

- The main event of the week would be the Tuesday's vote of the Withdrawal Agreement in the UK parliament. In December, PM May postponed the voting due to low chances of a success. Not much has changed since then, but recently a few lawmakers changed their mind which gives hope that support will rise further during the weekend. The voting result could set the market mood for the rest of the week. In the US, some agencies are closed amid the government shutdown and the most recent FOMC members' comments were reserved as regards the room for imminent rate hikes (the market stopped pricing hikes and started to discount cuts). The upshot is that the dollar lost versus main currencies over the passing week. In the upcoming week, we are going to see (probably, because there is the government shutdown) US data on retail sales and output as well as flash consumer confidence index – weak readings would be another heavy blow for the dollar.
- In the domestic calendar there are important readings for December (production, wages, employment, inflation) and for November (trade balance). Poor German data released recently raise the question whether (or rather: how much longer) the Polish economy can remain immune to the problems of its main trading partner. A trace of deteriorating real activity may already appear in the upcoming data, but market consensus and our forecasts are set at more or less neutral levels.

### Market implications

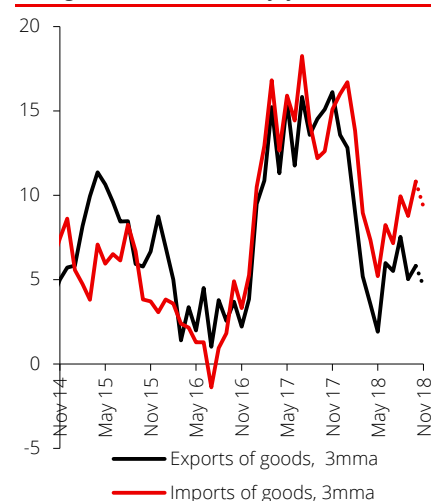
- We see limited room for the zloty to appreciate vs the euro in the short term amid uncertainty related to Brexit and low volatility persisting (not only) on the Polish market. EURPLN is holding in the middle of the 4.26-4.34 range in which it has been moving since August and we think there are higher chances the exchange rate will move towards the upper end.
- It seems to us that in the recent days, the environment for bonds has turned more positive and we expect this to hold in the coming week. The risk factor to this scenario is a rise of risk of a "hard Brexit" after the weekend.

### Production: Germany vs Poland, % y/y WDA



Source: GUS, Bloomberg, Santander

### Foreign trade turnover, % y/y



Source: NBP, Santander

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### What's hot next week

The gap between German and Polish industry sectors performance is historically wide to the benefit of Poland. Polish business sentiment indicators are still showing optimism, with the exception of PMI going deep below the neutral 50-pt mark in December.

With this background in mind we are keen to see this week's set of economic activity data – if the economy remains well insulated from the weakness that has stricken the main trade partner (28% of Polish goods exports in Jan-Oct 2018, 22.5% of imports). November exports have good reasons to both collapse (due to supply chains – German output sank -4.7% y/y) and to shoot up (very high path of new export orders index in ESI survey in 2018 with new record set in December). Our 3.6% y/y call would be a neutral result.

We expect December output growth in industry at 5% y/y, construction at 15.6%. Employment growth might have decelerated below 3% y/y for the first time in 2.5 years, while wage growth could have dropped back to 7% y/y due to mining bonuses being paid out in earlier months.

### Last week in economy

The December registered **unemployment rate** rose to 5.9% from 5.7% in November after adding 20.8k jobseekers in monthly terms, according to the Labour Ministry. Rise of unemployment rate in December is a seasonal pattern, but December 2018 saw the highest increase since 2013 and this is another sign that the positive labour market tendencies dry out. The Eurostat measure of Polish unemployment rate, based on LFS, remained at 3.8% in November (flat since April) in seasonally adjusted terms.

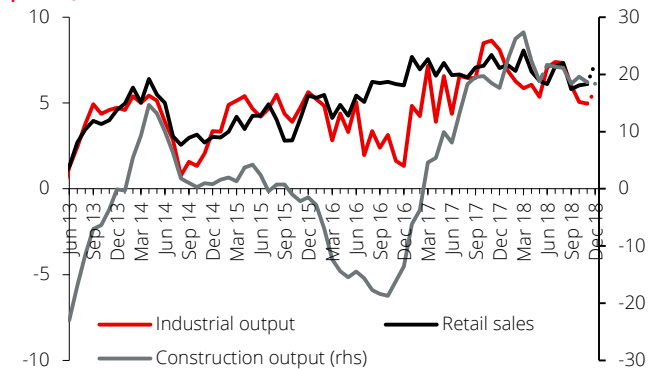
European Commission's **ESI business climate survey** only partly confirmed the positive picture shown earlier by GUS leading indicators. The main sentiment index fell in December from 109 to 107.8 (100 is a long-term average), and the average for 4Q18 was lower than in the previous quarters. Sentiment in manufacturing remained unchanged vs November and were was similar as in 1H18. Export orders recorded one of the higher highest readings in history. For services it was one of the worst months in 2018, while for construction one of the best (which confirmed our belief that the peak in EU-financed investments is yet to come). The retail trade recorded the highest level of optimism since February, even though consumer confidence deteriorated (to the lowest level since October 2017). Consumers have clearly got scared of looming inflation (probably due to a threat of energy costs spike in 2019).

Finance Minister Teresa Czerwińska said that at the end of 2018 the **central budget deficit** was markedly lower than PLN15bn. The Minister also repeated her claim that the deficit-to-GDP will be below 0.5%.

### Quote of the week

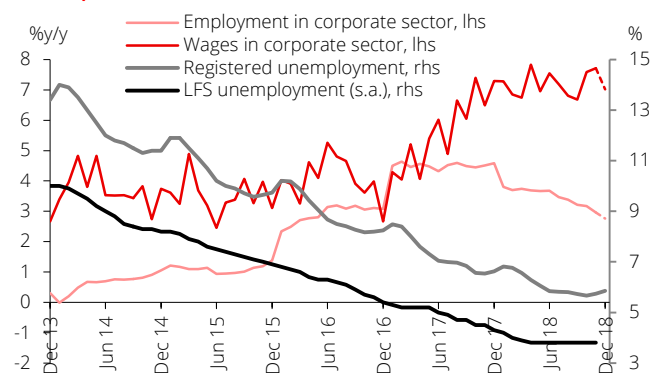
In line with expectations, the **MPC** left interest rates unchanged with the reference rate at 1.50%. Governor Adam Glapiński visibly changed his tone to even more dovish during the press conference and suggested that rates might even remain intact until the end of the MPC term (i.e., until 2022). In the previous months, Glapiński indicated 2019 or 2020 as the horizon of interest rate stability. Later on, monetary easing is possible with use of non-conventional tools, as further rate cuts would be risky. Glapiński explained that after oil prices fell and energy price hike was averted, inflation does not exceed the target in the whole forecasting horizon. Moreover, after 2022 the inflow of EU funds will fall markedly, contributing to slower GDP growth. We see the CPI inflation to be higher than the MPC expectations, but we believe that the inflation rebound will be too slow to change the MPC rhetoric in 2019, thus we think that rates will stay stable this year. Find more in our [Economic comment](#).

### Output and sales growth, %y/y (3M moving average, constant prices)



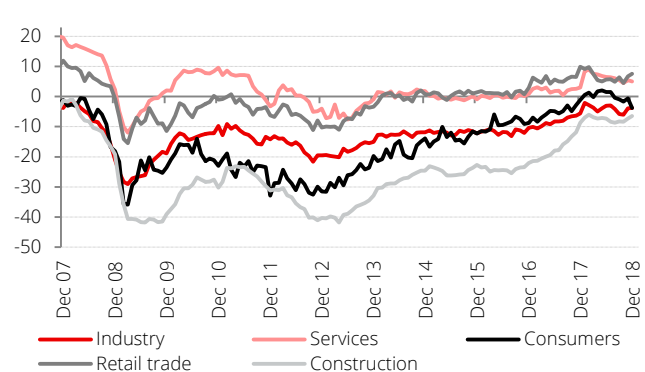
Source: GUS, Santander

### Developments in the labour market



Source: GUS, Eurostat, Santander

### ESI sentiment indicators for Poland



Source: European Commission, Santander

### Adam Glapiński, NBP head, MPC press conference 9 January

I would risk stating we cannot rule out stable rates until end of the current MPC term [2022] (...) The next step might not be a hike, but a discussion on cuts, or – and we are prepared for that – instead of cuts, which would be risky for some banks, some unconventional methods.

### MPC statement, NBP, 9 January

According to current forecasts, the annual price growth will increase in the coming months, yet – due to the decline in oil prices and the freeze on electricity prices – the scale of this increase will be smaller than anticipated in the November projection. In the medium term, the expected slowdown in economic growth will have a dampening effect on inflation. Consequently, in the monetary policy transmission horizon inflation will remain close to the target.

## FX and FI market

### Last week on the market

**FX** Last week, EURPLN remained stubbornly stable hovering close to 4.295, holding in the range it had been moving in since August. Polish currency ignored a jump in global stock indexes and a rise of EURUSD. At the same time, USDPLN fell to 3.72 from above 3.76 thanks to the euro appreciation vs the dollar.

**FI** Last week on the Polish interest rate market we observed a bullish steepener as the short-end of the bond and IRS curves fell in response to the dovish MPC rhetoric. The belly and long end moved up in the first part of the week and corrected later on also thanks to the reserved comments of the US central bankers. The 2Y asset swap spread fell a bit while the 5Y and 10Y spreads rose marginally.

The bond auction was pretty successful. The Ministry of Finance sold bonds for PLN6bn (upper limit of the planned supply), with a demand at PLN12.5bn. PS0424 and OK0521 attracted the biggest interest (PLN1.9bn and PLN1.1bn sold, respectively). The Ministry informed after the auction that this year's borrowing needs are covered in 38%.

### Key events

This week, we will see some of Poland's important data – December industrial output and inflation and November C/A.

Abroad, on Tuesday the UK Parliament is expected vote the Withdrawal Agreement and this could be the key event for the global investors. At the moment, it looks PM May is short of votes to support the Brexit conditions she negotiated with the EU. However, a few members of the parliament have recently changed their mind and turned positive giving hope this trend could continue over the weekend.

The calendar is also stuffed with important US data. The recent numbers have been mixed – strong nonfarm payrolls, weak ISM. The recent FOMC members comments, including those of Fed's governor Powell, were reserved as regards the room for further rate hikes. More FOMC members speeches are on the agenda in the coming days.

### Market implications

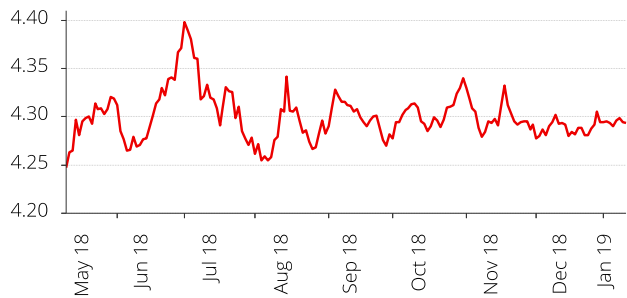
**FX** In [our 2019 Outlook](#) released this week, we mention the uncertainty related to Brexit as one of the factors that could weigh on the zloty at the beginning of the year as the Polish economy is among the most exposed to the no-deal Brexit. Furthermore, the volatility on the (not only) Polish market is very low and this also makes us cautious as regards the room for a stronger zloty in the short term. EURPLN is hovering in the middle of the 4.26-4.34 range and we see higher chances for the exchange rate to move towards the upper end.

We do not expect much impact from the Polish data on the zloty since our forecast of the industrial output and C/A deficit are at or very close to the market consensus.

**FI** It seems to us that in the recent days, the environment for bonds has turned more positive. The Polish MPC sounded even more dovish during the last press conference and the FOMC members suggested the Council could wait for more data before hiking interest rates. If the upcoming US data disappoint and another FOMC members also sound cautious, yields could head further south.

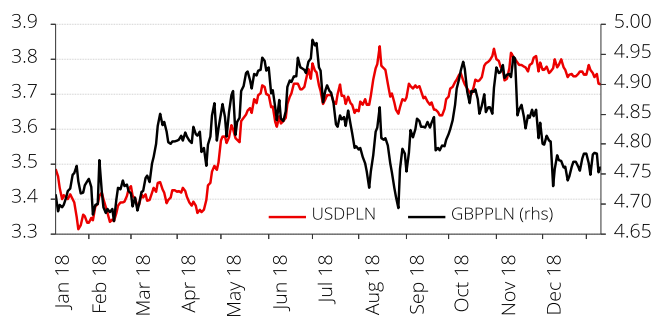
The risk factor to the scenario of stronger bonds is Brexit, in our view. Poland could be one of the countries to be most severely hit in case of "hard Brexit" and if the risk for this rises after the weekend, the market may start pricing deterioration of the state budget. Recall that an outstanding budget result in 2018 was one of the key factors pushing yields down.

### EURPLN



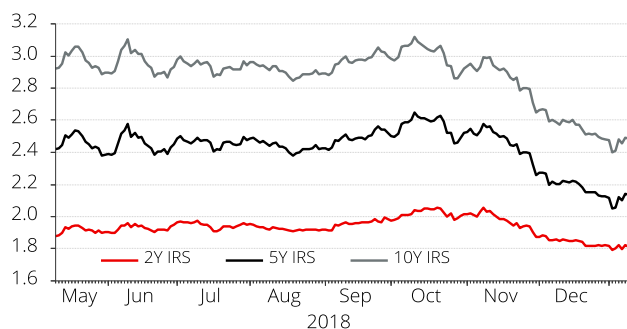
Source: Thomson Reuters Datastream, Santander Bank Polska

### GBPPLN and USDPLN



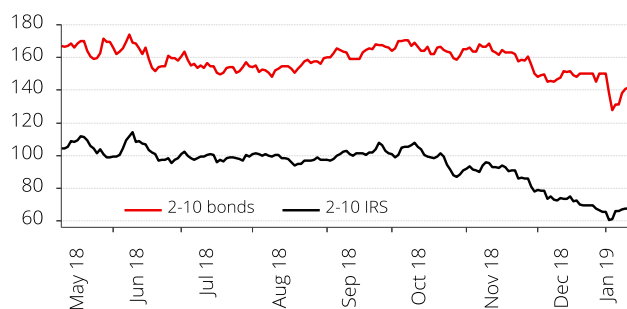
Source: Thomson Reuters Datastream, Santander Bank Polska

### IRS rates (%)



Source: Thomson Reuters Datastream, Santander Bank Polska

### 2-10 spreads



Source: Thomson Reuters Datastream, Santander Bank Polska

## Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	SANTANDER		
<b>MONDAY (14 January)</b>							
	US	Durable Goods Orders	Nov	% m/m	0.0	-	0.8
	US	New Home Sales	Nov	% m/m	4.0	-	-8.9
	US	Factory Orders	Nov	% m/m	0.3	-	-2.1
11:00	EZ	Industrial Production SA	Nov	% m/m	-1.2	-	0.2
<b>14:00</b>	<b>PL</b>	<b>Current Account Balance</b>	<b>Nov</b>	<b>€mn</b>	<b>-482</b>	<b>-474</b>	<b>-457</b>
<b>14:00</b>	<b>PL</b>	<b>Trade Balance</b>	<b>Nov</b>	<b>€mn</b>	<b>-405</b>	<b>-313</b>	<b>-588</b>
<b>14:00</b>	<b>PL</b>	<b>Exports</b>	<b>Nov</b>	<b>€mn</b>	<b>19 354</b>	<b>19 373</b>	<b>20 143</b>
<b>14:00</b>	<b>PL</b>	<b>Imports</b>	<b>Nov</b>	<b>€mn</b>	<b>19 643</b>	<b>19 686</b>	<b>20 731</b>
<b>TUESDAY (15 January)</b>							
9:00	HU	CPI	Dec	% y/y	2.8	-	3.1
<b>10:00</b>	<b>PL</b>	<b>CPI</b>	<b>Dec</b>	<b>% y/y</b>	<b>1.1</b>	<b>1.1</b>	<b>1.3</b>
<b>WEDNESDAY (16 January)</b>							
8:00	DE	HICP	Dec	% m/m	0.3		0.3
<b>14:00</b>	<b>PL</b>	<b>CPI Core</b>	<b>Dec</b>	<b>% y/y</b>	<b>0.7</b>	<b>0.7</b>	<b>0.7</b>
14:30	US	Retail Sales Advance	Dec	% m/m	0.3		0.2
<b>THURSDAY (17 January)</b>							
11:00	EZ	HICP	Dec	% y/y	1.6		1.6
14:30	US	Initial Jobless Claims	week	k	226		216
14:30	US	Housing Starts	Dec	% m/m	-0.2		3.2
14:30	US	Index Philly Fed	Jan	pt	10.0		9.1
<b>FRIDAY (18 January)</b>							
<b>10:00</b>	<b>PL</b>	<b>Employment in corporate sector</b>	<b>Dec</b>	<b>% y/y</b>	<b>2.8</b>	<b>2.8</b>	<b>3.0</b>
<b>10:00</b>	<b>PL</b>	<b>Average Gross Wages</b>	<b>Dec</b>	<b>% y/y</b>	<b>7.3</b>	<b>7.0</b>	<b>7.7</b>
<b>10:00</b>	<b>PL</b>	<b>Sold Industrial Output</b>	<b>Dec</b>	<b>% y/y</b>	<b>5.0</b>	<b>5.0</b>	<b>4.7</b>
<b>10:00</b>	<b>PL</b>	<b>Construction Output</b>	<b>Dec</b>	<b>% y/y</b>	<b>15.4</b>	<b>15.7</b>	<b>17.1</b>
<b>10:00</b>	<b>PL</b>	<b>PPI</b>	<b>Dec</b>	<b>% y/y</b>	<b>2.6</b>	<b>2.6</b>	<b>2.7</b>
15:15	US	Industrial Production	Dec	% m/m	0.3	-	0.6
16:00	US	Flash Michigan index	Jan	pts	96.4	-	98.3

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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