Weekly Economic Update

01 February 2019

Time to rest?

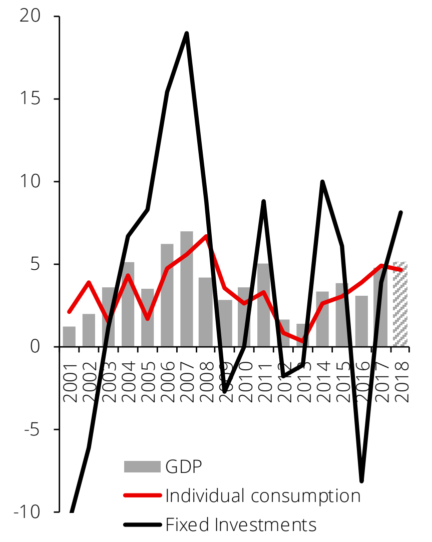
What's hot next week

- The data releases calendar for the coming week is not particularly rich. Several **activity indicators from Germany** (factory orders, production, export) are likely to follow the recent negative trends. In the US the President has signed the law allowing to reopen the government until 15 February, but the government's agencies are still struggling to make up for the lost time, so the releases of some key indicators (e.g. GDP) could be still delayed.
- On Tuesday Donald Trump will hold the State of the Union address. New information about **US-China trade negotiations** are also possible. Recently media informed about some progress in bilateral talks and suggested that a new presidential summit might be necessary to settle the economic conflict within the next month. **As regards Brexit**, we do not expect to see any real progress – PM May was sent back to Brussels to renegotiate terms of the deal, but EU leaders are refusing to open the talks. The next UK parliament's vote is planned for 14 February.
- In Poland there are **no major data releases** on the agenda. The only exception may be the flash results of the state budget for the full year 2018. According to recent FinMin's suggestions, the deficit reached PLN10-11bn, i.e. 4x lower than planned.
- On Wednesday the **MPC decision and press conference** are planned. No surprises from this side expected. The last President Glapiński's declaration about possible interest rates stabilisation until 2022 was probably a bit of overstatement (not the first time, to be honest), and his view is not shared unanimously in the Council. MPC's Gatnar and Osiatyński said recently that interest rate hike in 2019 cannot be ruled out completely. However, stable majority of Council members believes that current level of interest rates is good for the economy and given the recent information (slowing growth, low inflation) this consensus is unlikely to change anytime soon. It is quite possible that there will be more questions about salaries at the central bank than about the monetary policy outlook at the MPC press conference.

Market implications

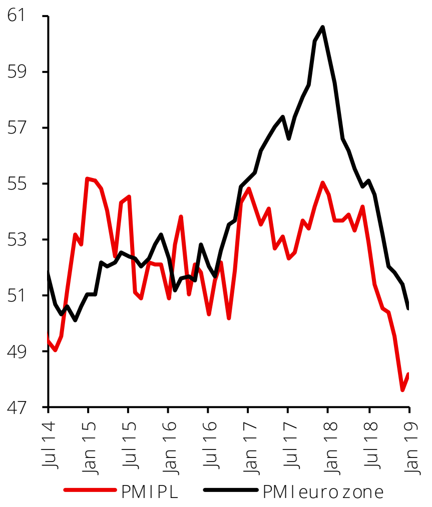
- It could be a relatively boring week for the financial market. Not many data releases in the agenda or events that could change investors' perception of the economic outlook. As a result, both bond yields and exchange rates should stabilise near current levels, waiting for new impulses. The latter may come in the following week, when new inflation data in Poland and USA will be released. The range of Polish inflation forecasts is unusually wide, due to uncertainty about impact of energy prices and scale of price hikes in core categories at the start of the year. While the headline CPI inflation is likely to fall below 1% y/y in January, there is a risk of upward surprise from core inflation.

GDP growth in Poland, % y/y



Source: GUS, Santander

PMI manufacturing, pts.



Source: Markit, Santander

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Last week in economy

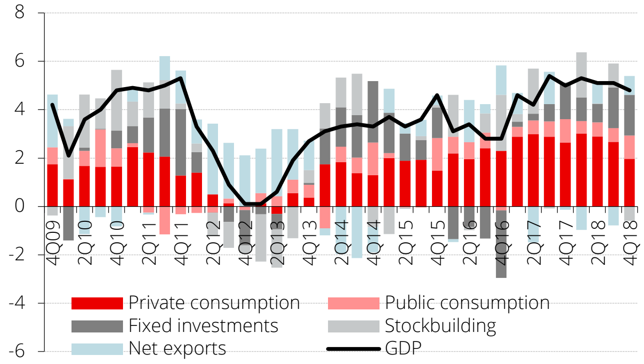
This week's data confirmed that the economy has already entered the slowdown phase of the cycle.

2018 GDP growth reached 5.1%, according to flash estimate, which confirmed this was an excellent year for Polish economy, despite growing evidence of deteriorating business climate across Europe. However, the implied 4Q result (official flash estimate due 14 February) most likely went below 5% y/y for the first time in six quarters, with a sub-4% private consumption growth and sub-7% fixed investments growth. We also have doubts about the strong contribution of net exports in 4Q implied from the 2018 GDP data, given the signals from business surveys about poor foreign demand and the hard data about foreign trade turnover. Still, we remain (moderately) optimistic for the near-term outlook. GDP growth is going to slow in every consecutive quarter of 2019, in our view, but the average growth should remain quite decent, around 3.8%.

NBP's quarterly Quick Monitoring report confirmed the peak is behind us, judging by companies' assessment of their own business situation, export and demand outlook. Manufacturing PMI rebounded slightly in January, but remained well below 50 pts, suggesting a decrease of industrial activity. Meanwhile, ESI indicators showed a broad-based collapse.

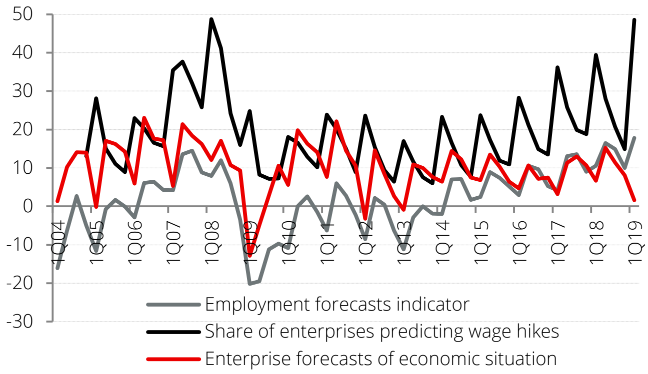
This week we also received some hints about the prospects of the Polish labour market. ZUS (Polish Social Insurance Institution) informed that **the number of registered Ukrainians fell** for the first time since at least 2012, suggesting that the vital stream of migrant labour supply is getting weaker, which could only lead to more tensions on the labour market. Consistently with this observation, the NBP's Quick Monitoring survey pointed to **significant rise of wage pressure** and growing labour shortage problem: in 1Q there was a jump in the share of enterprises that plan wage hikes and a rise of the share of employees to be covered by the hikes. At the same time, the indicator of employment forecasts reached the highest level in the history of this survey (i.e. since 2001) indicating high labour demand. This suggests that in 2019 we will see continued strong rise of wages, but diminishing growth of employment due to labour supply constraints. In total, this would mean a gradual slowdown of the growth of household income from labour, leading to somewhat lower private consumption growth.

GDP growth breakdown, with implied 4Q18 values, % y/y



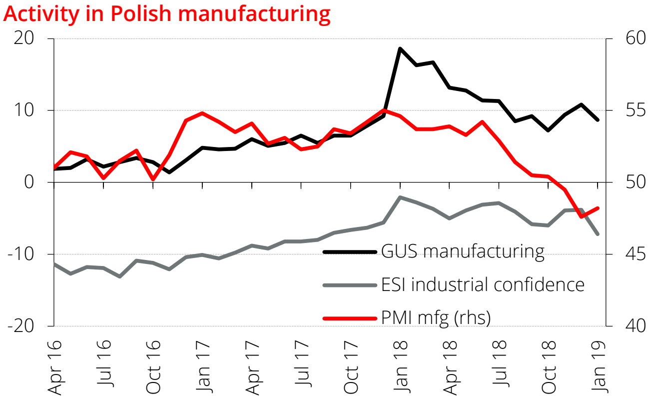
Source: GUS, Santander

Quick Monitoring, selected survey results



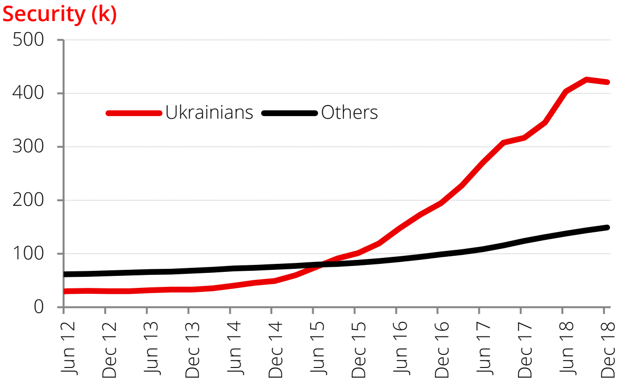
Source: NBP, Santander

Activity in Polish manufacturing



Source: GUS, European Commission, IHS Markit, Santander

Number of foreigners paying contributions to Polish Social Security (k)



Source: ZUS, Santander

FX and FI market

Last week on the market

FX CEE currencies and the zloty strengthened over the last week. The CEE currencies' gains were driven (mainly) by change in FOMC rhetoric and much more dovish views of the European central bankers. As a consequence, EURPLN went down to 4.2620 from 4.2930 (the biggest weekly change since August 2018), while USDPLN to 3.7250 from 3.7600.

FI Over the last week we observed significant falls of bond yields and IRS on the core and domestic markets. The downshifts were mainly a consequence of change of central banks rhetoric and poor European macro data releases (ESI, HICP and German retail sales). FOMC declaration that it would be cautious with further rate increases strengthened the downward trend of yields that has been observed since the beginning of the week. Over the week the domestic curve moved down by 8-12bp in the 5-10Y segment and by 2bp in 2Y. The IRS curve went down in the similar scale in the 5-10Y segment, while 2Y IRS moved down by 4bp.

Key events

This week numerous European data will be released (industrial orders, productions, export). We expect all of them to be below previous readings and below the market estimates, following the leading indicators. In our opinion the US data (industrial orders and ISM-services) are unlikely to surprise positively. We believe that MPC conference scheduled for Wednesday will have no impact on the markets.

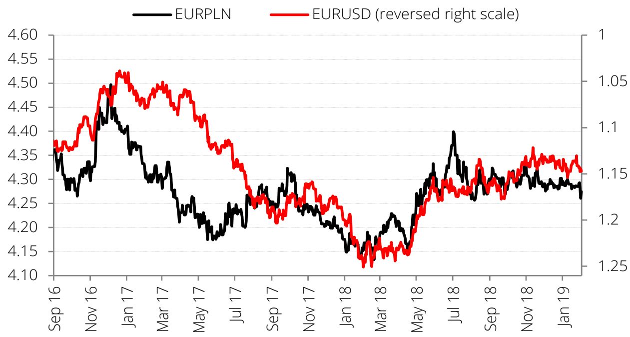
Market implications

FX In case of EURPLN, we expect the exchange rate to stabilise after a strong drop in the passing week. We think that poor European data would keep market expectations for softer ECB rhetoric which in turn could support the EM currencies, including the zloty. However, the room for the Polish currency appreciation is limited, in our view, due to the next sluggish European economic activity (German output, exports and orders). The US data (industrial orders and services ISM) shall not influence the outlook for the US economy and thus should be neutral for the zloty.

FI We believe that at the end of the week yields and IRS will stay close to the current level. We believe that German data will support lower yields and IRS. However, the jump of Italian yields in the last days suggests that the market seeks the trigger for the profit-taking. However, in our opinion it will be difficult to find a reason to sell bonds this week.

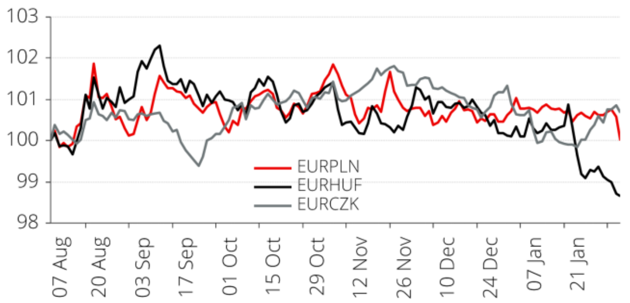
Any sell-off could only take place after the Polish inflation data (if the core CPI surprise to the upside) due for release at the end of the next week. This could be fueled also by the US inflation (if the agencies manage to return to the daily routine after the government shutdown). We think that whole IRS curve and 5-10Y bond yields could rise by 4-7bp. The MPC press conference should be market-neutral.

EURPLN and EURUSD



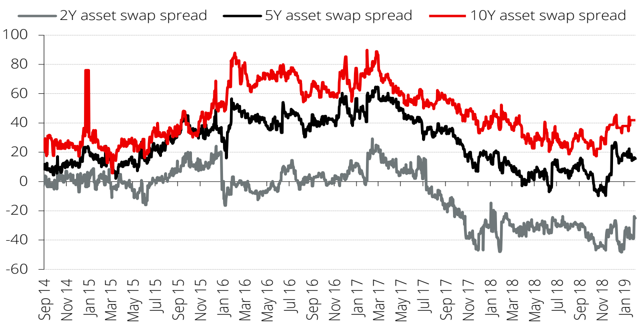
Source: ThomsonReuters, Santander Bank Polska

CEE currencies (August 1 = 100)



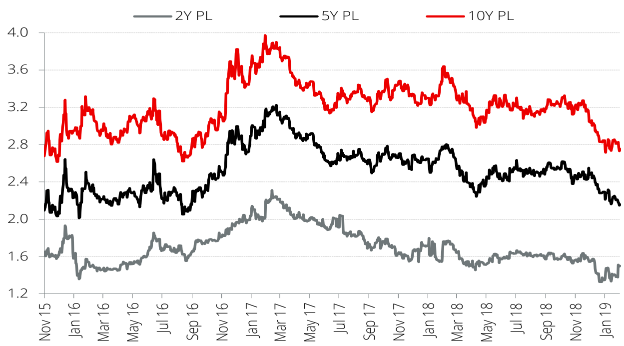
Source: Thomson Reuters Datastream, Santander Bank Polska

Asset swap spreads (bp)



Source: ThomsonReuters, Santander Bank Polska

Bond yields



Source: Thomson Reuters, Santander Bank Polska

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Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
			MONDAY (4 February)				
*	US	GDP Annualized	4Q	% Q/Q	2.6		3.4
*	US	Personal Spending	Dec	% m/m	0.3		0.4
*	US	Personal Income	Dec	% m/m	0.5		0.2
*	US	PCE Deflator SA	Dec	% m/m	0.0		0.1
16:00	US	Durable Goods Orders	Nov	% m/m	1.7		0.8
16:00	US	Factory Orders	Nov	% m/m	0.3		-2.1
			TUESDAY (5 February)				
*	US	Housing Starts	Dec	% m/m	-0.48		3.2
*	US	New Home Sales	Dec	% m/m	4.78		16.9
*	US	Retail Sales Advance	Dec	% m/m	0.1		0.2
09:55	DE	Markit Germany Services PMI	Jan	pts	53.1		53.1
10:00	EZ	Eurozone Services PMI	Jan	pts	50.8		50.8
11:00	EZ	Retail Sales	Dec	% m/m	-1.05		0.6
16:00	US	ISM services	Jan	pts	57.3		58.0
			WEDNESDAY (6 February)				
	PL	**MPC decision**		**%**	**1.5**	**1.5**	**1.5**
08:00	DE	Factory Orders	Dec	% m/m	0.3		-1.0
09:00	CZ	Industrial Production	Dec	% y/y	0.55		4.8
			THURSDAY (7 February)				
08:00	DE	Industrial Production SA	Dec	% m/m	0.85		-1.9
09:00	HU	Industrial Production SA	Dec	% y/y	0.0		3.5
13:00	CZ	Central Bank Rate Decision	Feb-19		1.75		1.75
14:30	US	Initial Jobless Claims	Feb-19	k	215.0		253.0
			FRIDAY (8 February)				
08:00	DE	Exports SA	Dec	% m/m	0.35		-0.3

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg
**The publication depends on US government agencies activity after the "government shutdown"*

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