

04 October 2019

# Weekly Economic Update

## Time for consolidation

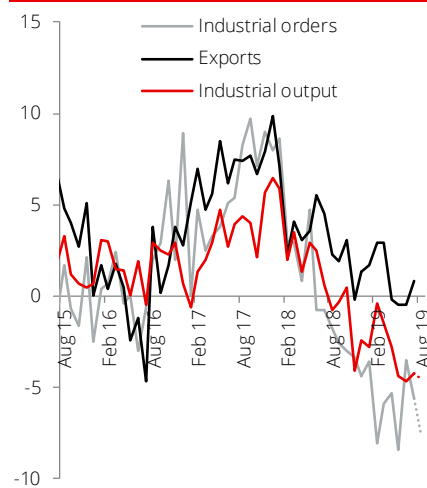
### What's hot next week

- In Poland, there will be no important macro data publications this week. On the domestic market, the dust is settling after the 3 October ECJ ruling and this should support consolidation of Polish asset prices. On Friday, after the session, **Moody's and S&P** rating agencies may present their reviews of Poland. We do not expect changes to the credit score. In our view, the agencies' expectations about 2020 fiscal deficit will be more interesting (Moody's analysts have already suggested that the zero deficit the government assumes for next year is too optimistic) as well as their views on the impact of the ECJ ruling on the Polish economy.
- Abroad, **important German data** will be released (new orders and output in industry, exports). Recent readings from Germany were weak and the market is expecting to see more of this weakness, which will strengthen the conviction about further easing of monetary policy and possibly also of fiscal policy in Europe. In the USA, we will get inflation and the publication of **minutes from the September FOMC meeting**, where rates were lowered and a rather hawkish communique was delivered. Apart from this, **Fed chairman Jerome Powell** will be speaking, so the market will have plenty of opportunities to think about the shape and outlook of US monetary policy.
- On Thursday and Friday **trade talks between the USA and China** are to be restarted. What is more, the Brexit issue will be back in the spotlight – Friday is the deadline the UK's PM Boris Johnson has set for the EU to answer to the **modification of the Brexit deal** he proposed (Northern Ireland would remain in the single market, but leave the customs union).

### Market implications

- After the ECJ ruling **the zloty** will be searching for a new equilibrium while investors will be looking into the ruling in detail and try to figure out the market implications. We think that the local currency can strengthen a bit but should not break 4.30 for too long.
- On the **fixed income market** we expect a consolidation around current levels at the beginning of next week and a rebound back to 2% in the second part of the week. The move should be driven by external factors of which US CPI and US-China trade talks in Washington might prove the most important. Bank of Japan's actions toward steepening its yield curve might have an indirect impact on yield curves globally, Poland included.

German economic activity, %y/y, with market expectations



Source: Bloomberg, Santander

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### Last week in economy

Growing weakness of business climate in the euro zone and Germany in particular is affecting Poland – PMI report for September was full of pessimism. The decline of inflation recorded in September is in our view temporary. NBP governor Adam Glapiński reminded at the MPC press conference that rates may stay unchanged until the end of his term.

Poland's **manufacturing PMI** fell in September to 47.8 pts from 48.8 pts. The lowest level of new orders index in over ten years was recorded, with poor readings of both domestic and foreign components (signals about weak demand from Western Europe, especially Germany and France). Current output index remained below the neutral level and output expectations turned record low (the series began in 2012). Purchasing activity was also reduced (the index is the lowest in six years). The recent readings of Polish industrial production were disappointing and the PMI report for September does not leave much hope for a rebound (not taking into account the positive working day effect). While Polish industry already feels the weaker demand from the EU, the labour market remains strong and the economy is supported by fiscal stimulus. Still, 3Q GDP growth was most likely visibly below 4.5% y/y for 2Q.

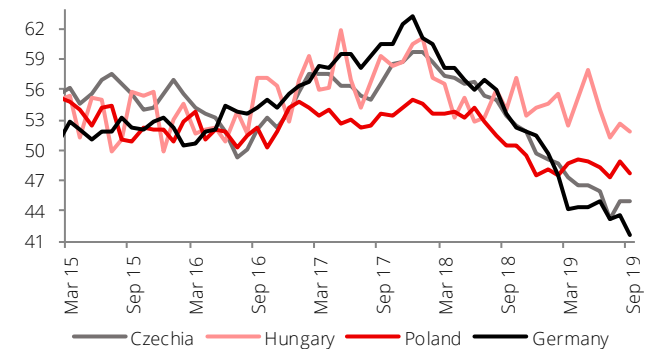
Polish **inflation** eased in September to 2.6% from 2.9% y/y, as we expected, due to non-core elements. At the same time our estimates show that core inflation resumed its uptrend in September, to 2.3-2.4%, after holding at 2.2% in July and August. There was a substantial decline of vegetable prices in September, which drove the whole food category to -0.2% m/m. Fuel prices kept going down for the third month, in September by 1.8% m/m. We continue to expect that headline CPI and core inflation will push higher in the coming months, both to above 3% y/y, and in early 2020 CPI inflation could go above 4% y/y.

Polish **MPC left rates unchanged**. At the press conference, governor Adam Glapiński said that arguments for tighter policy are quickly disappearing of late as the global outlook gets worse. He did not however say that the number of arguments for rate cuts is growing. In particular, if the slowdown in Poland continues in a gradual way, this will be no reason to ease policy. In his view it is highly probable rates will stay unchanged until the end of his term as all analyses point to such conclusion. If there are other views in the council, they are represented by small minorities and offset each other. We do not expect any changes to interest rates in Poland coming this year or next.

The **European Court of Justice** issued a verdict on Polish fx mortgage loans, which was received by the market as not as negative for Polish banks as it might have turned out. As a result, the zloty gained vs the euro, the dollar and the Swiss franc, while domestic bond yields fell (the poor data from abroad also supported such move). After the ECJ ruling two MPC members issued comments. Rafał Sura said the ruling removes uncertainty regarding the stability of the banking system, which is not threatened. Jerzy Kropiwnicki expressed an opinion, that Polish banks are well prepared for the outcomes of ongoing lawsuits. According to the Finance Ministry, Polish banking system is stable, well capitalised and prepared for a situation that results from the ruling. The Financial Supervision Authority responded in a similar tone: the sector has enough capacity to absorb potential losses which allows for maintenance of trust for the financial system (including the banking sector).

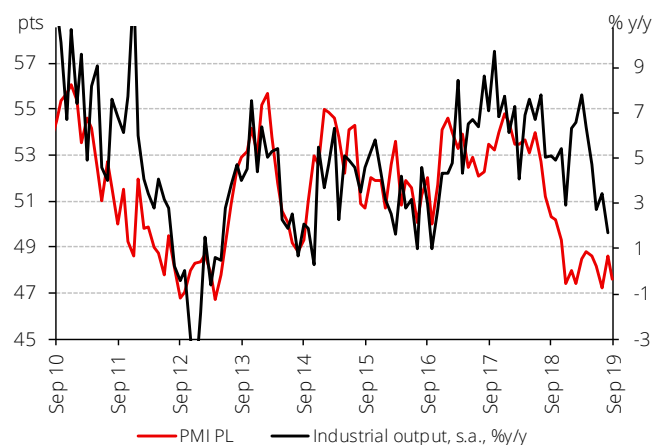
**Fitch Ratings** confirmed Poland's sovereign credit score at A-/stable outlook. The agency trimmed GDP growth forecasts for 2019-21 by 0.1-0.2pp, to respectively 4.1%, 3.3% and 2.9%. Rating could go up if strong GDP growth continues (pushing incomes up and net foreign debt-to-GDP down towards the median for A- countries) and there is a lasting decline of public debt to GDP. Worsening of debt-to-GDP and the business climate as well as weaker fiscal discipline would work towards lower grade.

### Manufacturing PMIs in CEE vs Germany



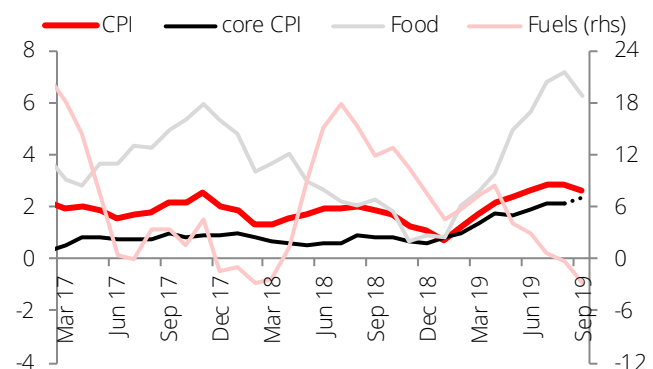
Source: Markit, Santander

### Polish manufacturing PMI vs industrial output



Source: GUS, Markit, Santander

### Inflation in selected categories, % y/y



Source: GUS, NBP, Santander

## FX and FI market

### Last week on the market

**FX** With dollar index flat on the week chart, the intraweek volatilities of EURPLN, USDPLN, CHFPLN and GBPPLN (lower by more than 1.0%) were a function of weaker US data and local factors. Past week was pretty busy from the local factors perspective just to mention September CPI, MPC meeting and ECJ ruling regarding CHF mortgages. The zloty gained after the ECJ ruling as markets probably got caught short and was the best performer in the CEEMEA region and the whole EM universe in that week. CHFPLN fell by most, around 2%, because of the EURCHF move higher post Tuesday's weak Swiss PMI data.

The Hungarian forint and the Czech koruna were the 2<sup>nd</sup> and 4<sup>th</sup> best performing EM currencies, just after the zloty, and closed, respectively, at 333.4 (-0.6%) and 25.75 (-0.4%). The Russian ruble lost 1.2% to 65.1 per USD as a function of falling oil prices (7%).

**FI** Polish bond yields and the IRS rates again fell a bit during the week (10Y bond by 10bp to 1.9%) but in the meantime 10Y bond traded as high as 2.04% after poor Japanese government bond auction sent core markets higher on Tuesday. Only after weak US ISM manufacturing data the next day did the core markets reverse and Polish 10Y traded below 1.9%. In Poland, the Tuesday's lower-than-expected September CPI was a non-event as was the fact that Thursday government bond auction was called off. Once ECJ ruling became known on Thursday did yields finally catch up. The 10Y PL-DE bond yield spread narrowed from 257bp to 250bp, or by 7bp. Polish asset swaps narrowed by 5bp as well - to 31bp.

### Key events

Local factors calendar is relatively scarce next week with two rating agencies, S&P and Moody's scheduled to review Poland's rating on Friday October 11<sup>th</sup>. We do not expect any change to rating nor outlook.

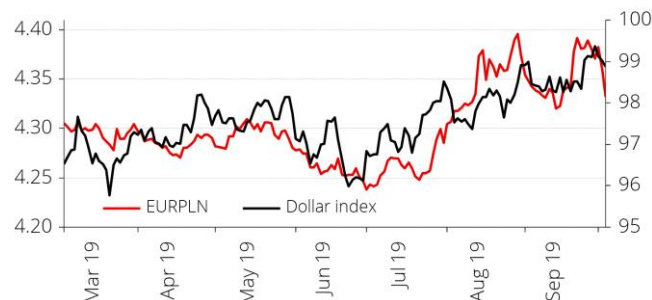
Hence in the coming days markets will probably focus more on the global factors. After it became obvious this week that the global manufacturing sector has taken a serious hit and does not seem to rebound, markets will surely be watching for any signs of spillover of the weakness into other sectors. Potentially market moving data starts with the US nonfarm payrolls release on Friday 4<sup>th</sup> October. There are factory orders and industrial production data from Germany, Fed minutes on Wednesday 9<sup>th</sup> Oct and US CPI on Thursday 10<sup>th</sup>. The US-Chinese talks restart in the second half of the week. Also Brexit should come back to focus again as the date of British ultimatum towards European Union (Friday 11<sup>th</sup> October) nears.

### Market implications

**FX** With ECJ ruling out of way EURPLN should try to find new equilibrium in the coming days as the markets tries to understand the detailed implications of the ruling. We expect the zloty to trade a bit stronger in the coming days, possibly testing 4.30, and then to resume a weakening trend whose pace will be determined by external factors of which US CPI and the Washington-based US-China talks are the most likely market movers next week.

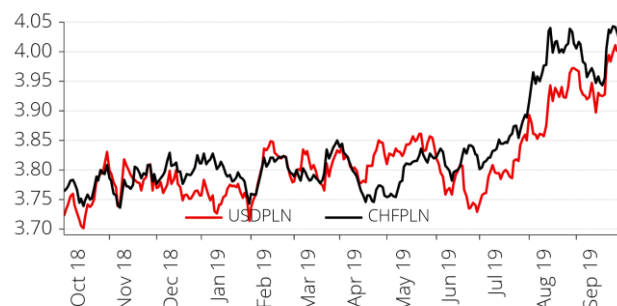
**FI** Polish 10Y bond yield broke the 2% support level and as in the FX case we expect some consolidation in the next few days (testing briefly below 1.9%) before rising back to 2%. The local calendar is relatively empty next week. In case of FI there is one additional important global factor one has to be aware of namely the BoJ's efforts to steepen its curve and bring the JGB10 bond back to presumably mid of its target range e.g. 0.0%. The process of pricing this possibility should, on the margin, put a steepening pressure on yield curves around the globe, Poland included.

### EURPLN and dollar index



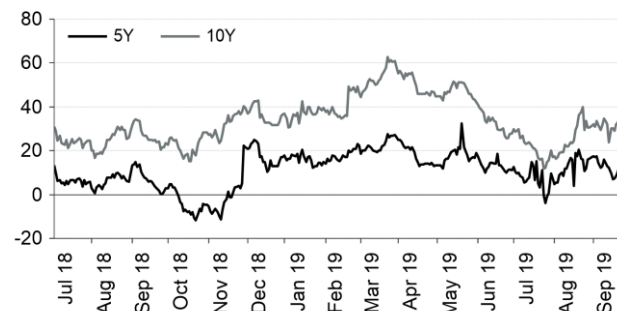
Source: Refinitiv Datastream, Santander Bank Polska

### USDPLN and CHFPLN



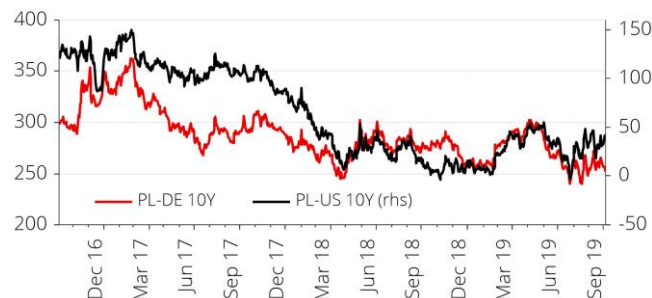
Source: Refinitiv Datastream, Santander Bank Polska

### Asset swap spreads (bp)



Source: Refinitiv Datastream, Santander Bank Polska

### 10Y bond yield spreads (bp)



Source: Refinitiv Datastream, Santander Bank Polska

## Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE
				MARKET	SANTANDER	
<b>MONDAY (7 October)</b>						
08:00	DE	Factory Orders	Aug	% m/m	-1.0	-2.7
09:00	CZ	Industrial Production	Aug	% y/y	-2.7	5.6
09:00	HU	Industrial Production SA	Aug	% y/y	4.9	8.72
<b>TUESDAY (8 October)</b>						
03:45	CN	Caixin China PMI Services	Sep	pts	52.0	52.1
08:00	DE	Industrial Production SA	Aug	% m/m	-0.3	-0.6
09:00	HU	CPI	Sep	% y/y	2.9	3.1
<b>WEDNESDAY (9 October)</b>						
20:00	US	FOMC Meeting Minutes	Sep.19		-	-
<b>THURSDAY (10 October)</b>						
08:00	DE	Exports SA	Aug	% m/m	0.0	0.8
09:00	CZ	CPI	Sep	% y/y	2.9	2.9
14:30	US	CPI	Sep	% m/m	0.1	0.1
14:30	US	Initial Jobless Claims		k	215.0	213.0
<b>FRIDAY (11 October)</b>						
08:00	DE	HICP	Sep	% m/m	-0.1	-0.1
16:00	US	Michigan index	Oct	pts	92.25	93.2
	PL	<b>Moody's, S&amp;P rating review</b>				

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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