

25 October 2019

# Weekly Economic Update

## Inflation down again

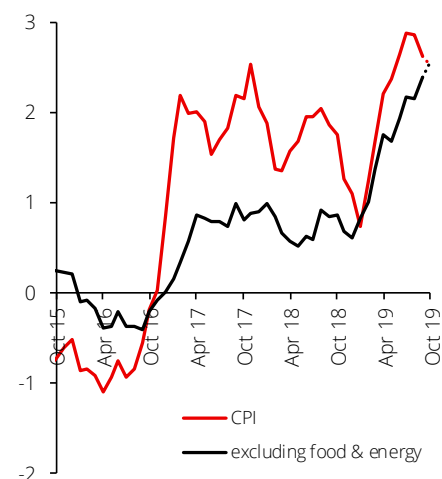
### What's hot next week

- The Brexit case will be alive for the yet another week. The UK PM Boris Johnson suggested snap election on 12 December and motion in this matter is to be voted in the House of Commons on Monday. It has to gather support of 2/3 of the house, and the opposition announced it will support the motion only provided that no-deal Brexit is ruled out. In the meantime, we are waiting for the EU to decide on the "final" Article 50 extension as the current Brexit data is pretty close (October 31).
- In mid-week, the market attention could turn to the US where the FOMC will decide about the interest rates. The market widely expects third cut to be delivered this year so the most interesting would be the accompanying statement. We think the October cut will conclude the FOMC "adjustment".
- In Poland we will see flash CPI for October. It seems that the monthly price growth was lower than average in the previous years and on top of that petrol prices went down for the fourth month in a row. As a result, the annual CPI growth could have slid to 2.5% from 2.6%, despite still rising core inflation (to 2.6% y/y from 2.4% y/y). If fuel and food prices continue to follow a downward path and energy prices for households continue to be frozen, then the probability of CPI hitting 4% at the start of 2020 will go down markedly. Given that Friday is holiday, PMI will be released in the following week.

### Market implications

- We think that EURPLN down impulse observed since early October may stop, at least in the short term. One of the factors recently boosting the zloty was hope for the soft Brexit to be arranged soon however it seems that we will finally end up with a yet another delay. Thus, an important supportive driver will disappear. Furthermore, Wednesday's Fed rate cut could be yet another "hawkish" one supporting the US currency, particularly after its recent weakening.
- We do not expect Polish bond yields to extend a decline in the coming week. The recent European and most of the US data did not provide more reason for the market to concern about the global growth. The Bund and UST yields stayed higher and this could be a factor that could pressure Polish bonds, particularly after the recent noticeable spread tightening. Locally, the ruling party officials have recently mentioned that there could be lower revenues and higher expenditures in 2020 compared to the initially presented budget plan that assumed zero budget deficit. As a result, the market may start to play the option of a higher bond issuance to cover higher deficit.

Inflation, % y/y



Source: GUS, Santander

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## Last week in economy

The data released last week confirmed that the GDP growth was slowing down in 3Q19. We are expecting 4.1% y/y vs 4.5% y/y in 2Q19 with risk skewed downwards. First data on leading indicators in 4Q19 suggested a further deterioration.

**Polish retail sales** decelerated to 4.3% y/y in September from 4.4% y/y in August, while an acceleration was broadly expected. Weak food sales was the main culprit, probably a one-off factor, as sales of durable goods were quite strong. Read more on retail sales [here](#). In general, the macro environment is favourable for consumption (low unemployment, high consumer confidence, new social benefits and tax cuts) and we see no reason for a major weakening in retail sales trend. There was, however, some deterioration in **October consumer sentiment**. Main indexes deteriorated, but they remained pretty close to their record high levels reached in the previous month. The current situation index fell to 9.3pt from 10.2pt and the leading index to 3.6pt from 7.0pt. The majority of the sub-indexes eased and the biggest drop was recorded for the change of unemployment (by 7.3pt to 2.5pt, its lowest since January 2017) and conditions for saving money (down 4.9pt m/m). Lower optimism regarding change of unemployment is coherent with our forecast of stabilisation of employment and unemployment in the months to come. We think that consumers' optimism might fall in the coming months but the cut in PIT tax rate (effective since October) might have some positive effect on that index.

**Construction output** added 7.6% y/y in September, a bit stronger than expected. We are expecting construction growth to remain in one-digit area in the months to come, given that the peak in EU funds utilisation is already behind us. Still, the housing sector is likely to continue to deliver high growth rates. Read more on construction [here](#).

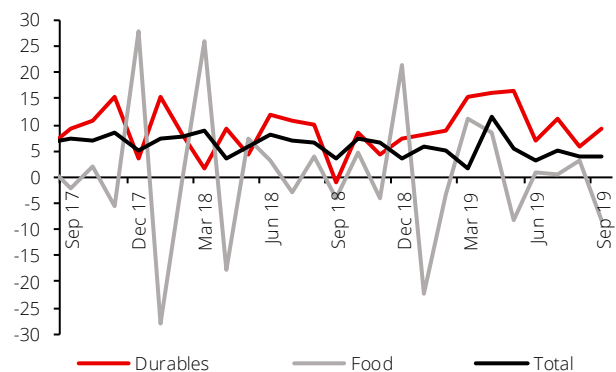
First **business sentiment indicators for October** showed a rebound in industry, but further deterioration in retail trade and services. Importantly, the rebound in industry came from the most severe depletion of stocks of finished products since 2008, while new orders and expected output gauges remained depressed. Retail trade and services sectors turned even more bearish on future demand (the lowest readings of these sub-indexes in c6 years). As a consequence, the current assessment part of the overall sentiment index rose to the highest level since March, while the prognostic part of the index kept declining and went below the long-term average for the first time since January 2017. The publication does not look like a positive turning point.

**M3 money supply** decelerated to 9.4% y/y in September from 9.9% y/y in August. Growth rate of cash in circulation and deposits remained roughly unchanged versus the previous month and the slowdown was due to lower value of buy-sell back transactions and outstanding bonds with maturity below 2 years.

**NBP released September voting records** when the motion for a 25bp rate cut was submitted. The only supporter of this idea was Eryk Łon, as we had expected. We think that the same might have happened in October when there was also a motion to cut rates.

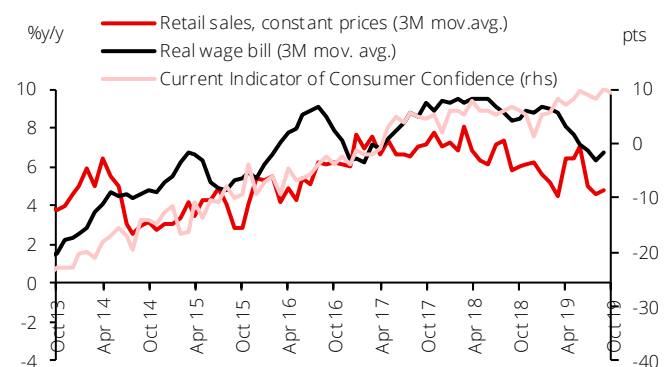
**MPC member** Kamil Zubelewicz said in the interview for Reuters that keeping interest rates too low artificially fuels demand on the real estate market, encourages households to take loans, leads to noticeable prices growth and it is a mistake for some members to keep looking abroad for the source of higher Polish inflation. He added, however, that given the current balance of votes, interest rates are likely to stay on hold until the end of MPC's term (early 2022) which we find a possible scenario, especially as **NBP Governor Adam Glapiński** is a strong advocate of keeping rates unchanged. In our view, there could be an (unsuccessful) attempt to hike rates at the next meeting.

## Retail sales, main categories, % y/y



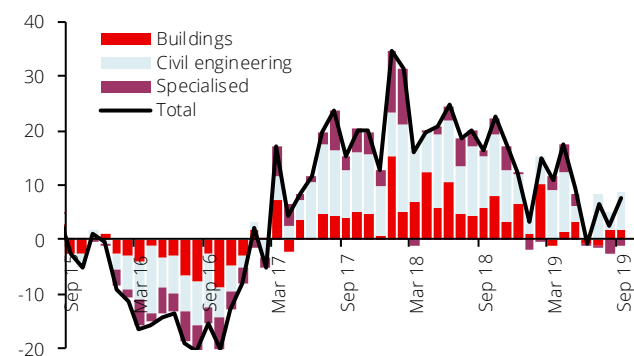
Source: GUS, Santander

## Consumer confidence indicators and retail sales



Source: GUS, Santander

## Construction output breakdown, % y/y



Source: GUS, Santander

## Quote of the week:

**Adam Glapiński, 25 Oct, PAP:** The upcoming NBP projections give no reasons to expect any changes in interest rates.

**Kamil Zubelewicz, 24 Oct, Reuters:** The policy of low interest rates boosted the housing market and encouraged economic agents to take more debt. (...) Interest rates proved to be too low and loans were demanded by entities that would not need credit in normal circumstances. (...) The current policy of the MPC is encouraging the Polish people to eat the fruit of economic growth. The low interest rate policy fuelled a major price growth. The current MPC outline suggests that rates will remain unchanged until the end of the current term. (...) Proponents of rate cuts are wrong when they say about choice between economic growth and price stability, because the choice is between economic growth today and tomorrow.

## FX and FI market

### Last week on the market

**FX** The zloty appreciation vs the euro, the dollar and the Swiss franc paused in the passing week since the pace of arranging the “soft Brexit” faded and no further progress has been made. EURPLN down trend halted at an important support (4.27). USDPLN was hovering around 3.84 for the whole week, CHFPLN traded near 3.88 while GBPPLN in a wide 4.80-4.98 range.

In the case of the other CEE currencies, the koruna held gains recorded in the previous week, the forint gained vs the euro for the fourth week in a row while the ruble gave up part of the recent gains vs the dollar.

**FI** Polish bond yields and the IRS rates fell by 2-4bp amid somewhat more cautious global market sentiment due to lack of Brexit progress. The 10Y asset swap spreads did not move much while the 10Y PL-DE bond yield spread fell temporarily to c235bp trading at its lowest since 2015/2016 turn. Bunds and Treasuries did not benefit much from the less positive global market mood and yields remained near their local peaks. This might have partly been due to the European data – flash PMIs and Ifo showed stabilization or even some minor rebound.

### Key events

Unsurprisingly, the Brexit is still lingering and it is likely that it would stay so until January 31. The UK PM Boris Johnson suggested snap election on 12 December and motion in this matter is to be voted in the House of Commons on Monday. It has to gather support of 2/3 of the House, and the opposition announced it will support the motion only provided that no-deal Brexit is ruled out. We expect the EU to agree to postpone Brexit and then the UK parliament will go for elections.

In that case, we think the market attention could turn to the US affairs. On Wednesday, the FOMC is expected to cut rates third time this year while on Friday monthly nonfarm payrolls and manufacturing ISM will be released.

### Market implications

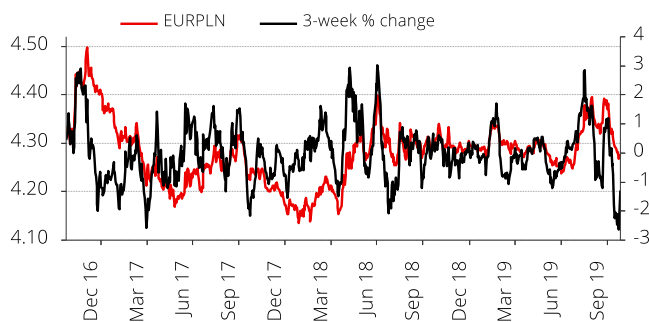
**FX** We think that EURPLN down impulse observed since early October may stop, at least in the short term. EURPLN moved lower noticeably in the previous three weeks and this move was the biggest since 1Q17 (in % terms). Note that EURUSD has been on the rise in the previous three weeks as well (weaker dollar also backed the zloty) and the respective percentage change reached its highest since early 2018. This suggests that both EURPLN down and EURUSD up trend might be overdone in the short-term perspective.

One of the factors recently boosting the zloty was hope for the soft Brexit to be arranged soon however it seems that we will finally end up with a yet another delay. Thus, an important supportive driver will disappear. Furthermore, Wednesday's Fed rate cut could be yet another “hawkish” one supporting the US currency, particularly after its recent weakening. The dollar index approached its c97 support.

**FI** We do not expect Polish bond yields to extend a decline in the coming week. The recent European and most of the US data did not provide more reason for the market to concern about the global growth. The Bund and UST yields stayed higher and this could be a factor that could pressure Polish bonds, particularly after the recent noticeable spread tightening. Continuing with the global factor, we think that the coming Fed rate cut could be followed by a rather reserved statement giving little reason for lower bond yields.

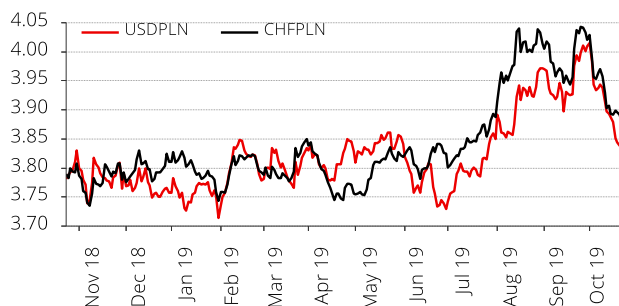
Locally, the ruling party officials have recently mentioned that there could be lower revenues and higher expenditures in 2020 compared to the initially presented budget plan that assumed zero budget deficit. As a result, the market may start to play the option of a higher bond issuance to cover higher deficit.

### EURPLN



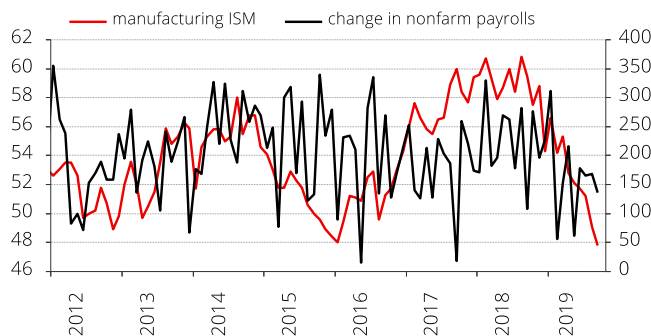
Source: Refinitiv Datastream, Santander Bank Polska

### USDPLN and CHFPLN



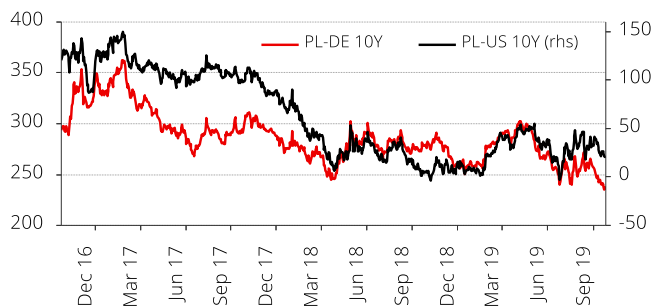
Source: Refinitiv Datastream, Santander Bank Polska

### US data



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
				MARKET	SANTANDER	VALUE	
<b>MONDAY (28 October)</b>							
No important data releases							
<b>TUESDAY (29 October)</b>							
15:00	US	Consumer Conference Board	Oct	pts	127.8	-	125.1
15:00	US	Pending Home Sales	Sep	% m/m	1.0	-	1.6
<b>WEDNESDAY (30 October)</b>							
11:00	EZ	ESI	Oct	pts	101.1	-	101.7
13:15	US	ADP report	Oct	k	132	-	134
13:30	US	GDP Annualized	3Q	% Q/Q	1.6	-	2.0
14:00	DE	HICP	Oct	% m/m	0.0	-	-0.1
19:00	US	FOMC decision		%	2.0	-	2.0
<b>THURSDAY (31 October)</b>							
08:00	DE	Retail Sales	Sep	% m/m	0.25	-	-0.1
<b>10:00</b>	<b>PL</b>	<b>Flash CPI</b>	<b>Oct</b>	<b>% y/y</b>	<b>2.5</b>	<b>2.5</b>	<b>2.6</b>
11:00	EZ	Flash HICP	Oct	% y/y	0.7	-	0.9
11:00	EZ	GDP SA	3Q	% y/y	1.1	-	1.2
11:00	EZ	Unemployment Rate	Sep	%	7.4	-	7.4
13:30	US	Initial Jobless Claims	week	k	215	-	212
13:30	US	Personal Spending	Sep	% m/m	0.3	-	0.1
13:30	US	Personal Income	Sep	% m/m	0.3	-	0.4
13:30	US	PCE Deflator SA	Sep	% m/m	0.0	-	0.0
<b>FRIDAY (1 November)</b>							
	<b>PL</b>	<b>Market holiday</b>					
13:30	US	Change in Nonfarm Payrolls	Oct	k	95	-	136
13:30	US	Unemployment Rate	Oct	%	3.6	-	3.5
15:00	US	ISM manufacturing	Oct	pts	49.0	-	47.8

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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