

24 January 2020

Weekly Economic Update

Brake on economic growth

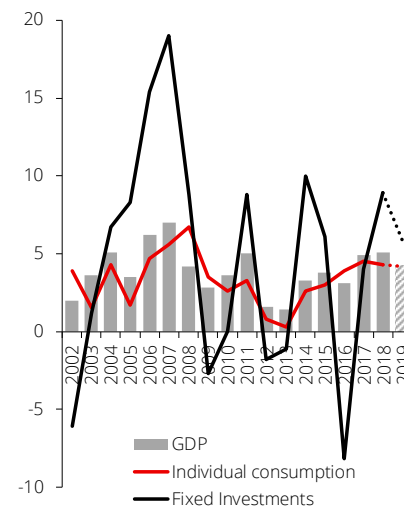
What's hot next week

- As we predicted, most of domestic data releases for December were below consensus and confirmed economic slowdown in 4Q19. Only wages surprised to the upside, but it is too early to say whether it was a sign of strengthening wage pressure or just a temporary volatility related with bonus payments. So far, the recent data releases supported the NBP president's claim that the higher inflation can be left without reaction due to the economic slowdown.
- After the weekend the scale of economic slowdown will be verified by the **flash GDP data for 2019**, to be released on Wednesday. In our view, the latest production and sales data implied a high risk that the GDP growth in 4Q19 did not exceed 3.5% y/y, which would imply average 2019 growth at 4.1%. Market consensus is at 3.8% and 4.2%, correspondingly, which means the potential for another negative surprise.
- During the week there will be few more publications, which will help to assess the state of Polish economy: GUS **Statistical Bulletin**, NBP Quick Monitoring, NBP credit survey. However, they are less important for investors.
- There will be quite a lot data releases abroad: GDP in USD and Europe, German Ifo, ESI business climate, US consumer data (sentiment, income, spending). After the last positive surprise from the European PMIs every positive news may reinforce upward pressure on core bond yields.
- On Wednesday evening the **FOMC announces its decision**. No change in monetary policy is expected, but markets will closely watch any hints regarding the outlook for the future.
- Friday, January 31st, is the constitutional deadline when the 2020 budget should be sent to the President for signature. If it does not happen (and there is no chance for it to happen, as the work in Sejm on the bill has just started), **the President will have the right to call snap elections**. However, we think that the risk if such scenario is very low, as we do not see strong arguments that would support and justify such decision.

Market implications

- As we expected, the zloty started trimming earlier gains and we expect this tendency to continue, as local data disappoint and dollar gets stronger. The nearest target for EURPLN is 4.27.
- Bond yields retraced after disappointing domestic data, which we see as a short-term correction in a medium-term upward trend. But the resuming of the trend may be delayed by the release of disappointing GDP data.

Growth of GDP and its components, %y/y



Source: GUS, Santander

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Last week in economy

The December set of data clearly confirmed that the Polish economy was slowing down at the end of 2019 and we see a growing risk that GDP growth did not exceed 3.5% y/y in 4Q19.

Industrial output expanded by 3.8% y/y in December 2019, slower than we expected (4.8% y/y) and below the market consensus (6.4% y/y). Seasonally-adjusted data showed a decline by 2.9% m/m (the worst since 2009) and a rise by 2.1% y/y. Most market analysts were assuming a strong rebound versus 1.4% y/y in November on the back of positive working day effect, but we estimated that this effect will not be so strong given the distribution of holidays in December, encouraging to take more days off. Still, Polish industry is suffering due to the euro zone slowdown, resulting in declining orders, especially in industrial supplies (+3.1% y/y output in December), while investment goods were doing quite well (6.1% y/y). We are expecting the Polish industry to stay rather sluggish in the nearest months, at least as long as the German industry remains in the doldrums. However, a gradual recovery is possible later in 2020.

Construction output fell in December by 3.3% y/y, while we expected a less pronounced decline by 1.6% y/y and the consensus forecasted a small rise by 1.0% y/y. The negative trends in construction (with exception of housing) are likely to hold for some time, even despite the very favourable weather conditions. Construction will be undermined by weak public sector activity and by worsening investment sentiment in the private sector.

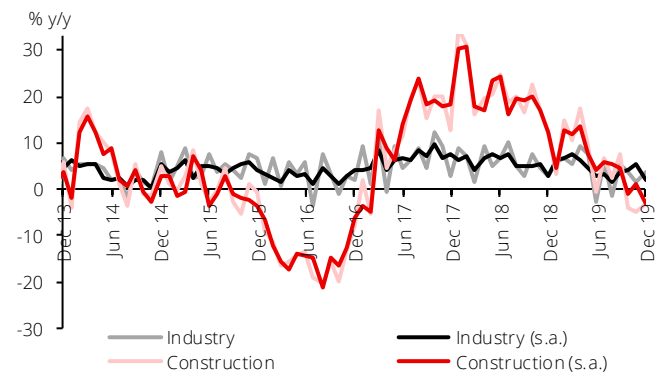
The first indicators of Polish **business sentiment** for January released by GUS showed a rebound in manufacturing to the highest level in a year in seasonally adjusted terms, thanks to 'current assessment' rather than 'outlook' components. Construction sentiment kept decreasing at a very mild pace. There was some improvement in wholesale trade, but retail trade was significantly more pessimistic than in December (due to worse prognostic components of the sentiment index). It is interesting to see industrial sentiment improve at a time when real data suggest a tough period for the sector.

Retail sales expanded by 5.7% y/y in December, in line with our expectations and slightly below the market consensus. We see some minor slowdown in retail sales and consumption to come, but private consumption will remain the main growth driver given rising social benefits. The implications from January **consumer confidence** survey data are similar - in general, the sentiment is going down gradually, but the indicators regarding openness to larger expenditures remain robust.

December **wage growth** was 6.2% y/y vs 6.1% market expectations and our 5.6% forecast. Note that the 3M moving average of wage growth kept going down, despite the rebound of the monthly reading vs November. We think wage growth will go up to almost 7% y/y in January, but the 2020 average could be close to 6%. December corporate **employment growth** remained at 2.6% y/y, in line with expectations.

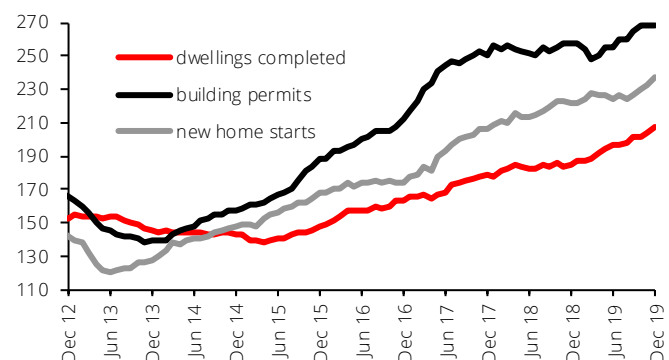
Minutes from the last MPC meeting showed that in January the Council voted on both a 25bp rate cut and a 15bp rate hike. The motion to cut rates has kept appearing since September, but at the previous meetings it had only one supporter, Eryk Łon. The last rate hike motion was filed in July 2019 and found support of two members, Eugeniusz Gatnar and Kamil Zubelewicz. The January motion might have had more supporters, but we still doubt - even with inflation going higher - that in this term the MPC could raise rates. The January minutes also include information that the members who fear inflation would stay permanently elevated after going above the tolerance band are convinced that the current economic slowdown will not be deep. We think this means that the voices that rates need to be higher will be getting quieter as GDP growth goes down.

Output in industry and construction, % y/y



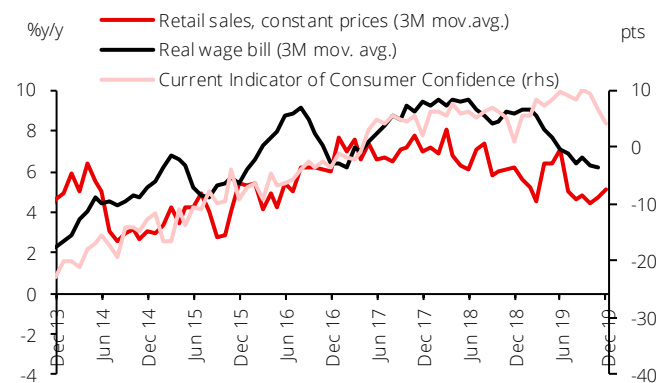
Source: GUS, NBP, Santander

Dwellings construction, 12-month moving sum, thousands



Source: NBP, Santander

Retail trade, consumer confidence and income



Source: GUS, Santander

Quote of the week:

Jerzy Kropiwnicki, MPC member, 20 Jan, PAP: So far the MPC has no reason to react. We were expecting CPI to go up and we are still assuming that CPI should return to the target at the end of 1Q20. The NBP aims at keeping the inflation at 2.5% +/- 1 percentage point. As long as the inflation is within this tolerance range, I see no grounds to worry about this gauge and call for interest rate changes.

FX and FI market

Last week on the market

FX The zloty and its CEE peers depreciated in the passing week amid a stronger dollar and a shaky global market sentiment. Sentiment indexes for Germany and whole euro zone beat expectations but these were accompanied by the below-consensus Polish economic activity data that could have also contributed to the zloty weakening. EURPLN rose to 4.25, USDPLN to 3.85, CHFPLN to nearly 3.97 and GBPPLN to 5.04.

The Hungarian forint underperformed its CEE peers as EURHUF rose to its fresh all-time-high at c337.5. EURCZK rebounded slightly from its multi-month low at c25.0 and ended the week close to 25.15. The ruble lost vs the dollar second week in a row. USDRUB failed to break the support at 61.0 and has temporarily risen above 62.0.

FI Polish bond yields and IRS rates fell amid below-consensus Polish data and strengthening on the core market driven by the unstable global mood and cautious ECB rhetoric. As a result, the 10Y bond yield pulled back below 2.30% and the respective IRS rate to c2%. The 10Y PL-DE bond yield spread has been holding in the upward trend so far this year and this has continued in the recent days – the spread rose to 258bp, its highest since September.

At the bond auction, the Ministry of Finance sold bonds for PLN6bn, the demand amounted to PLN10bn.

Key events

In the final week of January, the FOMC will announce its decision on the interest rates and we will see crucial data from the US and Poland. The market shall still follow the situation in China trying to contain the new virus spreading so the global market sentiment may remain unstable.

We and the consensus expect the Fed Fund rates to be left unchanged but the market is currently pricing more than 50% probability that the 25bp cut could take place in September at the earliest.

Market expectations regarding the next Fed move could be influenced by the upcoming US macro data, including the first estimate of 4Q19 GDP growth and consumer data (sentiment, earnings, spending).

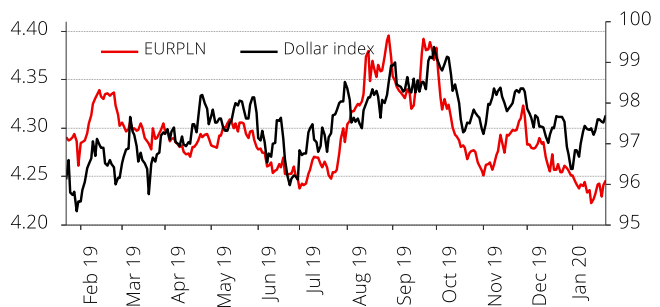
In Poland, 2019 GDP data will be released that could help to estimate the economic growth in 4Q19. After the recent monthly data, we see downside risk for the headline figure.

Market implications

FX So far, EURPLN is trading in line with our expectations. The zloty is under mild but a systematic pressure and we assume EURPLN to hold in its gradual upside trend. The first target is 4.27. EURUSD failed to rise even after some better-than-expected sentiment indexes (ZEW, PMI) which suggest the dollar could remain strong in the short-term. This, together with the likely still shaky global market mood should weigh on the zloty and its CEE peers.

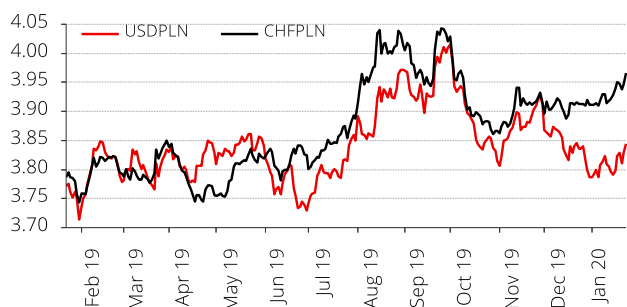
FI Polish bonds have recovered somewhat but yields are still holding near their local peaks. Recently, Polish macro data have had a meaningful impact on the domestic debt – high inflation pushed yields up, while output and retail sales data helped bonds to recover somewhat. We expect these two opposite forces could be in balance in the short-term and yields/IRS could remain in the range in which they have been holding since mid-January waiting for an another trigger. Any downward move could be in our view only a correction in the upward trend we expect in the medium-term.

EURPLN and dollar index



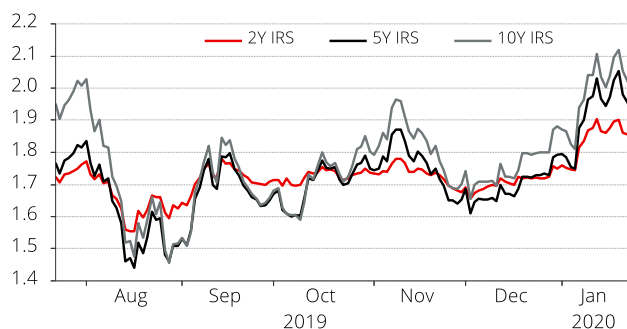
Source: Refinitiv Datastream, Santander Bank Polska

USDPLN and CHFPLN



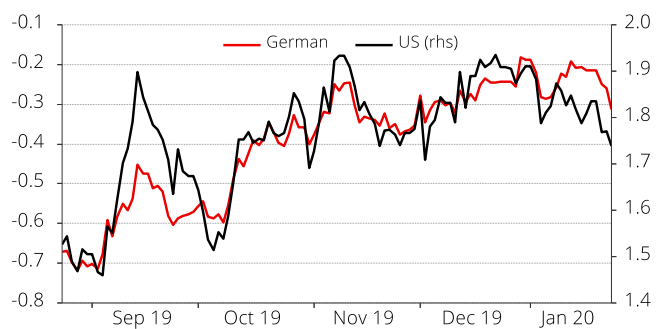
Source: Refinitiv Datastream, Santander Bank Polska

Poland IRS



Source: Refinitiv Datastream, Santander Bank Polska

10Y Bund and UST yields



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST
					MARKET	SANTANDER	VALUE
MONDAY (27 January)							
10:00	DE	IFO Business Climate	Jan	pts	97.0	-	96.3
10:00	PL	Unemployment Rate	Dec	%	5.2	5.2	5.1
16:00	US	New Home Sales	Dec	% m/m	1.5	-	1.3
TUESDAY (28 January)							
14:00	HU	Central Bank Rate Decision		%	0.9	-	0.9
14:30	US	Durable Goods Orders	Dec	% m/m	1.2	-	-2.1
16:00	US	Consumer Conference Board	Jan	pts	128.0	-	126.5
WEDNESDAY (29 January)							
10:00	PL	GDP	2019	% y/y	4.2	4.1	5.1
16:00	US	Pending Home Sales	Dec	% m/m	0.6	-	1.2
20:00	US	FOMC decision		%	1.75	-	1.75
THURSDAY (30 January)							
11:00	EZ	Unemployment Rate	Dec	%	7.5	-	7.5
11:00	EZ	ESI	Jan	pts	101.7	-	101.5
14:00	DE	HICP	Jan	% m/m	-0.7	-	0.6
14:30	US	GDP Annualized	4Q	% q/q	2.2	-	2.1
14:30	US	Initial Jobless Claims	week	k	214	-	211
FRIDAY (31 January)							
11:00	EZ	Flash HICP	Jan	% y/y	1.4	-	1.3
11:00	EZ	GDP SA	4Q	% y/y	1.0	-	1.2
14:30	US	Personal Spending	Dec	% m/m	0.3	-	0.4
14:30	US	Personal Income	Dec	% m/m	0.3	-	0.5
14:30	US	PCE Deflator SA	Dec	% m/m	0.2	-	0.2
16:00	US	Michigan index	Jan	pts	99.0	-	99.1

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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