03 April 2020

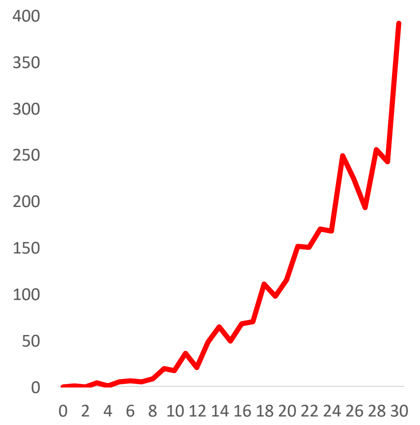
Weekly Economic Update

Election fever

What's hot in the next two weeks

- A few days ago we have published a new MACROscope with updated economic forecasts in a world affected by Covid-19. The report is available here – we encourage to read it.
- Another week has passed in which the markets have sought stabilization and this time without announcements of another biggest in history emergency packages by governments and central banks. The incoming data already cover periods of **significant disruptions in economic activity** created by the epidemic. US jobless claims showed 10mn new jobseekers in 2 weeks, march PMIs have just set new record lows – sharply falling below the levels seen even during the Global Financial Crisis. Markets tried to get some hope from the Russia-Saudi Arabia unconfirmed talks regarding curbing oil supply. Looking at the number of Covid-19 cases globally alone, it does not seem the mood should improve just now. Rather, more likely scenario is that of factories closed for longer and limited shopping and movement in many countries.
- In the next two weeks we will find out how the US real estate market has reacted to the pandemic, and also how the consumer prices have had: both in the US and in our region.
- At the **MPC meeting** on Wednesday we expect no signalling of further rate cuts and focus on the launched non-conventional instruments. Possibly some details of the Polish TLTRO will be given.
- Just after Easter, Polish **March inflation** data will be released. We expect CPI eased to 4.4% (consensus at 4.4%) and this trend should accelerate in the months to come. In March, there has probably been a strong negative effect of cheaper oil, core inflation has likely started to fade amid companies trying to seize at least some of the disappearing demand by price cuts and plenty of online discounts. In food prices, there might have been a positive effect of panic stock building by consumers.
- After Easter, the stat office is to release revised GDP data for the past years and February foreign trade volumes.
- Polish political affairs may also be an important driver of the market since there is a **disagreement among the coalition parties if to run a presidential elections** on May 10. If there is no solution the stability of the Polish government could be threatened which in turn could have an adverse impact on the market. Recently, investors have negatively received the strengthening of power by PM Orban (indefinite right to rule by decree) so weakening of the Polish government in time of pandemic could trigger nervous reaction among investors.
- Among the external events, it is worth to mention G20 and IMF meetings (April 16 and 17). Let's hope the message from these could improve the market mood dampened by the pandemic.

New Covid-19 cases in Poland, daily data, since the first infection



Source: Ministry of Health, Santander

Market implications

- We stick to our view that EURPLN down move to 4.50 from 4.63 is just a correction in the upside wave that might be resumed anytime in the nearest future. The zloty may suffer some negative pressure from the forint that might be under pressure given the recent change in law. Thus, we would rather expect EURPLN to rise above 4.63 rather than fall below 4.50 in the upcoming weeks.
- Outlook for a deep economic slowdown shall support market pricing of a loose monetary policy (keeping front end of the curve low) while the central bank's QE program should prevent mid- and long-end yields from a bigger rise.

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Last week in economy

In the passing week we saw the government fine-tuning its fiscal In the passing week we got more soft indicators for March, showing the reaction of business sentiment to the new conditions caused by the epidemic. We have also published our MACROscope titled: Coronavirus crisis: v-, V- or U-shaped GDP scenario? In which we show different scenarios of economic growth in Poland. The one that we think is currently the baseline, assumes that economic activity in Poland is severely supressed until early June and then revives quite vigorously (V-shaped rebound). In this scenario, GDP contracts almost 1% in 2020, to rebound almost 5% in 2021. However, if for any reasons (problems with supply-chains, very slow recovery in demand) the re-opening of the economy is delayed, we may move to the alternative scenario, assuming more lengthy recovery (U-shaped), with -2.5% GDP drop in 2020, followed by 2.2% rise in 2021. Both variants should be approached with caution, as the uncertainty regarding the evolution of the disease and its consequences remains unprecedented. As a result, the magnitude and the length of the shocks could in fact prove even stronger.

Polish **manufacturing PMI** fell in March to 42.4 (our forecast 44.5, market consensus 45.2), posting the most considerable monthly decline in the history of the survey (since 1998). Three sub-indicators: production, new orders and employment recorded highest-ever monthly collapse, reflecting a sudden stop in economic activity after the country lockdown in mid-March. Despite a sharp drop in new orders, companies were struggling with lengthening delivery times, which confirms that the sector was hit by both a demand-side and supply-side shock at the same time. The survey confirms that the economy is heading towards a recession, at least in 2Q20. The pace of revival will be conditioned on the evolution of the disease and the length of the resulting restrictions imposed on activity.

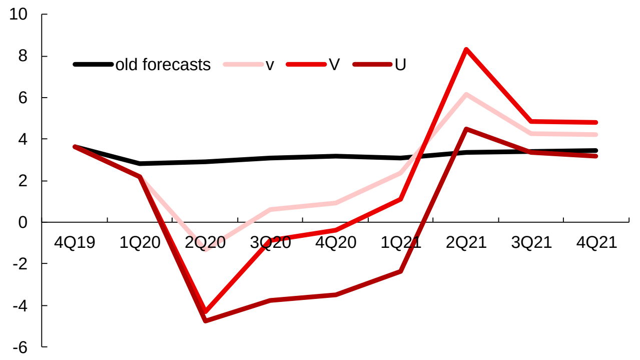
Main **ESI index** for the Polish economy dropped in March to 95.3 pts from 99.2 in February and reached the lowest level since late 2013. A significant drop was recorded in industry, services, retail trade and construction, while the consumer confidence index went up (survey fieldwork did not cover the lockdown period). Indicators regarding current situation did not change much, but expectations components collapsed (expected output, prices, orders, employment).

Fitch rating agency kept Polish credit score at A- with stable outlook. The agency's analysts think it is likely that the fiscal rule will be broken in 2020, but do not plan to change the rating because of this. Poland is considered as relatively resilient to the coronavirus shock due to being a diversified and relatively closed economy, moderate development of the tourism sector, the status of net exporter, flexible exchange rate, balanced C/A and room for fiscal stimulus. The forecast of 2020 general government deficit was shown at 5% and 2021 at 3.3% of GDP. A few days after the rating decision, Fitch agency lowered Polish GDP forecast for 2020 to -0.6% from 1.8%. The forecast for 2021 was raised to 3.8% from 3.2%.

According to GUS, in 2019 the **general government deficit** was 0.7% GDP, the second lowest reading in the last years. **Public debt** was 46% GDP, at the lowest level since 2007. This year we expect the deficit to grow to 6% GDP and debt to 52% GDP.

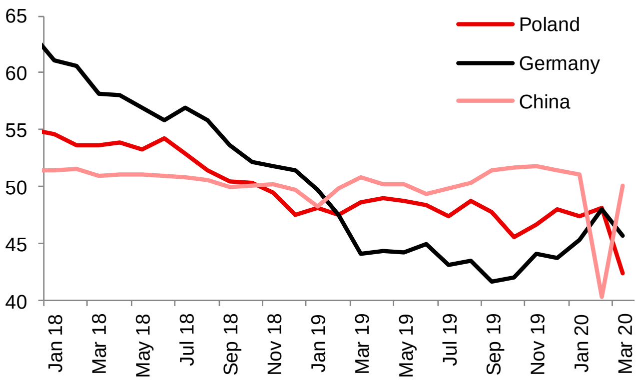
NBP **reviewed data on current account** for 2019. The surplus of €5.9bn was reduced to €2.5bn, or from 1.1% of GDP to 0.5% of GDP (which still is the best outcome since Poland joined the EU in 2004). The primary income balance saw the largest revision, worsening by €4.2bn. Other C/A items were little changed. The financial account was mostly revised in the foreign direct investments part (investments in shares raised by €3.9bn).

Santander scenarios for GDP, %y/y



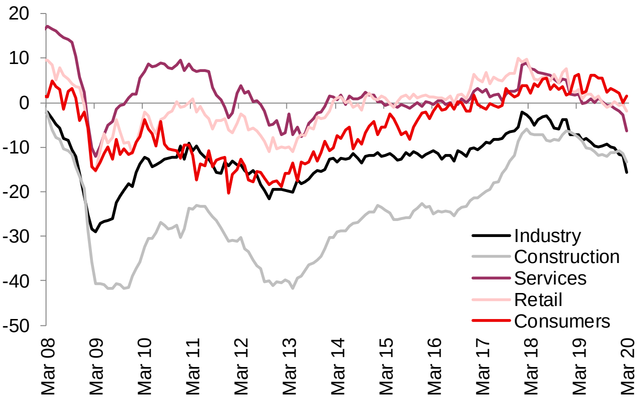
Source: GUS, Santander

Manufacturing PMIs



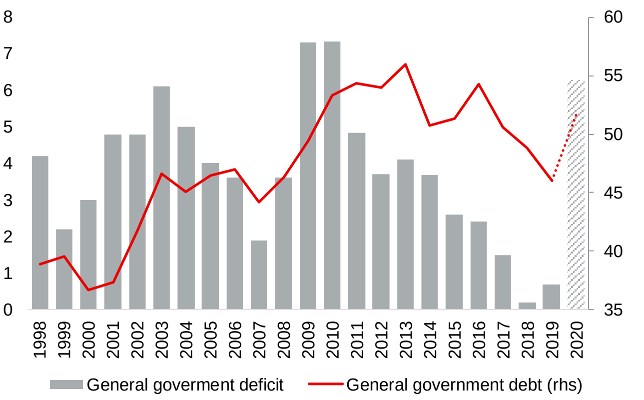
Source: Bloomberg, Santander

Sectoral ESI indicators



Source: European Commission, Santander

General government deficit and debt as % of GDP



Source: GUS, Santander

FX and FI market

Last week on the market

FX The global market mood remained much less volatile than during the first wave of a very high risk aversion. Global stock managed to keep most of their recent gains which prevented EURPLN from further rise. The exchange rate remained within 4.50-4.60 range, the narrowest for three weeks. USDPLN neutralized nearly the whole drop recorded in the previous week and the exchange rate rose to 4.20 from 4.07. GBPPLN rose for the third week in a row and reached 5.20, its highest since late 2016. CHFPLN rebounded back to 4.33 after it fell to 4.25 a week earlier.

The forint remained the underperformer with EURHUF hitting its new all-time-high at c370. It seems that the market negatively received the recent change in the Hungarian law that gave PM Orban the right to govern the country by decree. The Hungarian central bank tried to stop the forint depreciation by increasing the interest rate at the deposit tender, but that provided only a temporary relief. EURCZK and USDRUB remained in horizontal trends just below their multi-month peaks.

FI Polish IRS and bonds yields remained close to their all-time-lows. In the first part of the week, rates continued the down move but later a bonds gave up part of gains. This resulted in a widening of the asset swap spread. The 10Y PL-DE bond yield spread stayed close to 240bp.

According to the Ministry of Finance, in February nonresident bought Polish PLN-denominated marketable bonds for PLN3.4bn of nominal value. This was their first monthly purchase since June 2019. The biggest buyers were the mutual funds (PLN1.1bn). PLN2.1bn more than at the end of January was at the omnibus accounts. Polish banks sold debt for PLN4bn, individuals bought for PLN1.2bn.

Key events The upcoming two weeks are rather light in terms of macro data releases as the numbers published will refer to the pre-lockdown period. The reports related to the COVID-19 spread should be key again. As long as the situation looks to be stabilizing in Italy, the market may now focus on the US where the number of infected is already more than twice bigger than in China.

On Thursday, April 16, the G20 meeting will start while a day later the IMF will hold its summit. The market might be waiting for any common statement that would include a plan of a cooperation in fighting the coronavirus epidemic.

Polish MPC is likely to keep interest rates unchanged after an emergency cut in mid-March. The Council shall stress it is ready to act if needed but for now its members need to see how fast the economic growth is decelerating.

Another issue to watch is tensions within the ruling coalition regarding the possibility to hold presidential elections on May 10. According to media, this issue could even destabilise the government, in which case the reaction of the financial market could be negative.

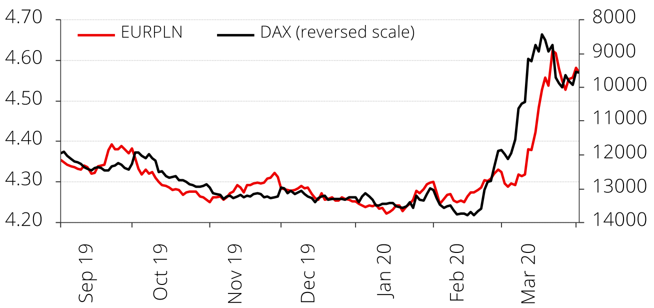
Market implications

The global market mood is still far from stabilization and the attention may switch from Italy to the US. The number of infections in the world's biggest economy is rising fast and the pace of increase would have to slow to allow for a firmer improvement of the global market mood to emerge. This looks rather unlikely to happen in the short term, in our view.

FX We stick to our view that EURPLN down move to 4.50 from 4.63 is just a correction in the upside wave that might be resumed anytime in the nearest future. The zloty may suffer some negative pressure from the forint that might be under pressure given the recent change in law. Developments on the Polish political scene could be unsupportive as well. Thus, we would rather expect EURPLN to rise above 4.63 rather than fall below 4.50 in the upcoming weeks.

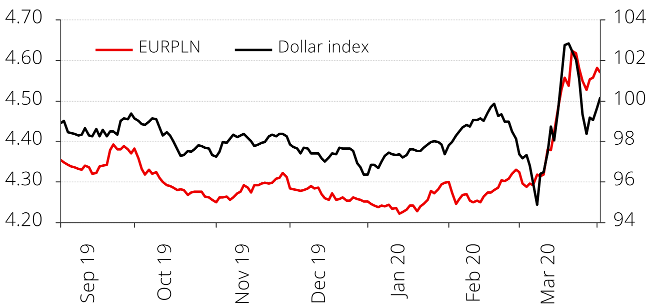
FI Outlook for a deep economic slowdown shall support market pricing of a loose monetary policy (keeping front end of the curve low) while the central bank's QE program should prevent mid- and long-end yields from a bigger rise.

EURPLN and German DAX index



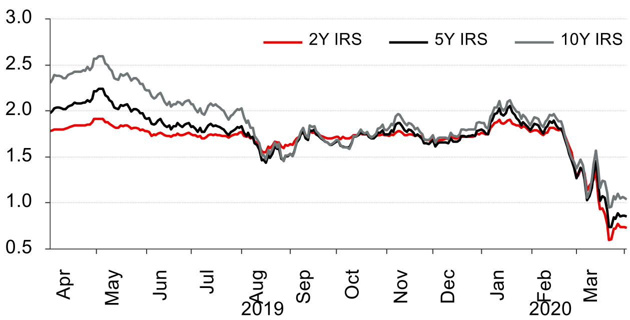
Source: Refinitiv Datastream, Santander Bank Polska

EURPLN and dollar index



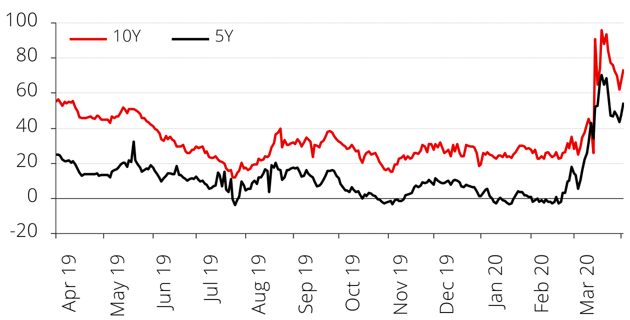
Source: Refinitiv Datastream, Santander Bank Polska

Poland IRS



Source: Refinitiv Datastream, Santander Bank Polska

Poland asset swap spreads



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
		MONDAY (6 April)					
08:00	DE	Factory Orders	Feb	% m/m	-0.3	-	5.5
09:00	CZ	Industrial Production	Feb	% y/y	-1.5	-	-1.4
		TUESDAY (7 April)					
08:00	DE	Industrial Production SA	Feb	% m/m	-0.8	-	3.0
09:00	HU	Industrial Production SA	Feb	% y/y	-	-	2.74
		WEDNESDAY (8 April)					
	PL	**MPC decision**		**%**	**1.00**	**1.00**	**1.00**
09:00	HU	CPI	Mar	% y/y	-	-	4.4
20:00	US	FOMC Meeting Minutes					
		THURSDAY (9 April)					
08:00	DE	Exports SA	Feb	% m/m	-	-	0.1
14:30	US	Initial Jobless Claims	week	k	5000	-	3283
16:00	US	Michigan index	Apr	pts	82.0	-	89.1
		FRIDAY (10 April)					
14:30	US	CPI	Mar	% m/m	-0.3	-	0.1
		TUESDAY (14 April)					
9:00	CZ	CPI	Mar	% y/y	-	-	3.7
14:00	**PL**	**Current account balance**	**Feb**	**€mn**	**-**	**902**	**2265**
14:00	**PL**	**Exports**	**Feb**	**€mn**	**-**	**19 800**	**19 167**
14:00	**PL**	**Imports**	**Feb**	**€mn**	**-**	**19 289**	**18 837**
		WEDNESDAY (15 April)					
10:00	**PL**	**CPI**	**Mar**	**% y/y**	**4.4**	**4.4**	**4.7**
14:30	US	Retail sales	Feb	% m/m	-	-	-0.5
15:15	US	Industrial production	Mar	% m/m	-	-	0.6
20:00	US	Fed Beige Book					
		THURSDAY (16 April)					
11:00	EZ	Industrial output	Feb	% m/m	-	-	2.3
14:00	**PL**	**Core CPI**	**Mar**	**% y/y**	**3.5**	**3.4**	**3.6**
14:30	US	Building permits	Mar	% m/m	-	-	-6.3
14:30	US	House starts	Mar	% m/m	-	-	-1.5
14:30	US	Initial jobless claims	week	k	-	-	-
		FRIDAY (17 April)					
11:00	EZ	HICP	Mar	% y/y	-	-	1.2

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

Additional information is available on request. Please contact Santander Bank Polska S.A. Financial Management Division. Economic Analysis Department. al. Jana Pawła II 17. 00-854 Warsaw. Poland. phone +48 22 534 18 87. email ekonomia@santander.pl. http://www.santander.pl.