11 December 2020

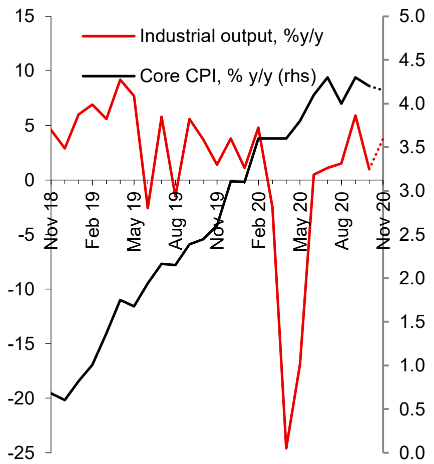
Weekly Economic Update

EU budget agreed, now Brexit

What's hot next week

- What a relief, the common sense won and there was no veto to the EU budget at the summit. As we wrote last week, for Poland this would have been too costly to become true. As a result, we may expect that **the new EU budget together with the Recovery Plan will provide a robust cash inflow** to Poland that could lift country's GDP by 4-5% in total until 2025.
- This is a very positive news for the economy while in politics it could spur more debate whether the ruling coalition will survive (junior coalition partner Solidarna Polska has warned it may leave if there is budget agreement). We do not know how the situation will evolve but one is sure: snap elections are not in the interest of the government and if we stick to the common sense once again, this scenario should be considered as rather unlikely. All in all, any political tensions after the summit should not have much impact on the Polish assets.
- In the coming week we will get back to economic news. There is **plenty of local data in the calendar**: C/A (Monday), CPI (Tuesday), core CPI (Wednesday), wages and employment (Thursday), industrial output and PPI (Friday). Abroad, key events will be flash PMIs from Europe, German Ifo and central bank meetings in the USA, Czechia and Hungary.
- We expect the data to confirm the broadly assumed scenario that the 4Q trough will be visibly shallower than the spring one, and in particular the industrial sector is this time definitely less affected, response of the labour market remains moderate and inflation is in a mild downward trend.
- We do not expect any changes in the monetary policy from the central banks, the Fed will present its new forecasts.
- In the background, the **Brexit talks** are in progress but the agreement does not seem to be any closer. However, it is worth to remind that the same could have been said last week regarding the Poland/Hungary veto and maybe in case of Brexit we will also have a happy end.

Industrial output and core inflation, % y/y



Source: GUS, NBP, Santander

Market implications

- The zloty gained in reaction to the EU budget deal after being stable in the previous days suggesting that such a scenario has been partly priced in. The December's seasonal pattern supports the zloty but in the short-term the market direction could rely on the outcome of the Brexit talks. UK is one of the Poland's biggest trading partners and lack of a deal could push EURPLN up.
- Polish bond yields were roughly stable after the previous Friday's jump despite the EU budget deal and strengthening of the German debt. The 10Y PL-DE bond yield spread rose to 200bp, its highest for weeks, and this could help Polish long-term yields to ease.

Economic Analysis Department:

al. Jana Pawła II 17, 00-854 Warszawa
email: ekonomia@santander.pl
website www: skarb.santander.pl
Piotr Bielski +48 22 534 18 87
Marcin Luziński +48 22 534 18 85
Grzegorz Ogonek +48 22 534 19 23
Wojciech Mazurkiewicz +48 22 534 18 86
Marcin Sulewski, CFA +48 22 534 18 84

Last week in economy

Deal on EU budget was the most important piece of news of the week. Moreover, we got to see comments of MPC members (and minutes) as well as some minor economic data and reports from rating agencies.

The first day of European Council summit brought a **deal on EU budget** and on the Recovery and Resilience Facility, opening the way to about EUR170.0bn earmarked for Poland in 2021-2027 period.

The flash **registered unemployment rate** in November stood at 6.1%, unchanged since June. The number of the unemployed increased over the month by 7.8 thousands, which is less than in the same period of the previous two years.

The report by GUS about the **3Q labour demand** showed that the labour market behaved pretty well given the economic shock. In Q3 the pace of job shedding decreased to -24% y/y (during the quarter 64k jobs were destroyed, of which 16k due to Covid-19) from 14.3% y/y in Q2 (93.6k, of which 31k Covid-19 related ones). Job creation was lower by 16.4% than a year earlier, while in Q2 it was as much as 44.2% lower. Also, at the end of Q3 the share of workers working remotely from home equalled 5.8%, while 3 months earlier it was 10.2%.

Moody's rating agency expressed concerns that the institutional framework will be still deteriorating in Poland in the coming years. S&P rating agency said it is not concerned about the Polish fiscal performance even if the debt to GDP ratio does not start to fall before 2023. Meanwhile, **Fitch rating agency** has updated the Polish GDP forecast for 2021 down to 3.3% from 4.5%, while the 2022 one up to 5.1% from 3.3%.

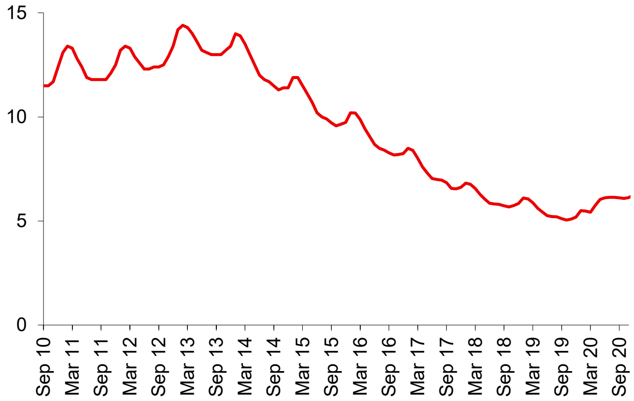
Head of the Energy Regulatory Office (URE) approved the **new energy tariffs** for 2021 for 3 out of 4 suppliers. Prices for households will go up by c3.5% on average, which in our view adds 0.1pp to inflation (assuming that the approved hike for the fourth company will be similar). Since January also other energy fees are changing, in particular the "power surcharge", which will additionally boost energy bills – by c9% in total, according to our estimate (+0.35pp to inflation rate).

NBP **released a calendar of MPC meetings for 2021** which confirmed this week's media reports that next year there will be one-day meetings. The new NBP communication includes also new tools: the NBP Governor Glapiński posted a video recording with his answers to questions raised by journalists. There was no important information in the recording.

MPC member Łukasz Hardt said that in 2021 it would be necessary to consider hiking rates to 0.50% from current 0.10% along continuing the non-standard measures and extending them (e.g. adding long term repo operations). In his opinion, the 2021 inflation in Poland will be higher than implied by the recent NBP projection, due to growth recovery, possible supply chain shortening, as well as possible increase of money velocity in the economy. Hardt also supports hike of the reserve requirement ratio to 3.5% in order to decrease liquidity in the Polish banking sector. **Eryk Łon** reiterated that in his opinion no reasons for rate hikes will occur before the end of the current MPC term (in early 2022).

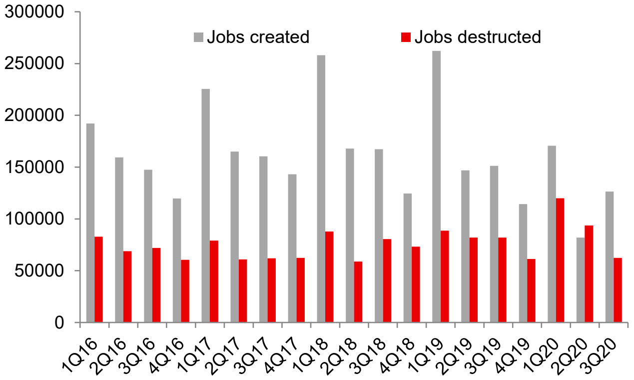
November MPC meeting's minutes underscored the uncertainty regarding the economic outlook. The Council agreed that the risks to the current economic projection are to the downside - deterioration of business conditions in Poland's trading partners and lack of zloty's further depreciation during the pandemic were noted as reasons. Majority of the MPC agreed on CPI projection showing CPI at the inflation target (2.5%) next year, but some had doubts and thought the inflation would be higher due to minimum wage hike and possible maintained high inflation of services prices.

Registered unemployment rate, %



Source: GUS, Ministry of Development, Labour and Technology, Santander

Job creation and destruction



Source: GUS, Santander

FX and FI market

Last week on the market

FX The passing week somewhat more volatile than the previous ones since EURPLN fell below 4.45 and neared 4.42, its lowest since early September. The main factor behind zloty strength was a EU budget deal. USDPLN fell below 3.64 for a while, CHFPLN was trading in a wide range around 4.13 and GBPPLN plummeted to 4.83 from 4.95 amid weak pound owing to no positive Brexit news.

The other CEE currencies also should end the week stronger. The forint also benefited from the EU budget deal, koruna was supported by the decent Czech data and hawkish comment of CNB member, ruble took advantage of weaker dollar and higher oil price. EURHUF fell for a while below its November bottom of 353.7, EURCZK retreated from c26.5 resistance and USDRUB approached its 72.5 support.

FI After the Friday's sharp jump of IRS and the bond yields, the next five days brought a stabilization or slight recovery. The 10Y benchmark yields eased 5bp to 1.35%, 5Y by c10bp to 0.50%. The IRS rates remained at an elevated levels, their highest since March/April for 5Y (0.75%) and 10Y (1.20%) tenors. The 10Y PL-DE bond yield spread widened by 5bp to 200bp (its highest since May) after +20bp in the previous week.

Key factors for the market in the coming days could be the Brexit talks, FOMC decision and flash PMIs. Until mid-December, there has still been no positive news flow and there is a risk that EU-UK talks will end without an agreement.

During the election period, the US central bank refrained from any bold declarations and it seems that the last meeting of the year shall not bring any decisions on the monetary policy front. However, it will be interesting to see how the GDP and CPI forecasts have changed since September.

European manufacturing PMIs are holding at high levels comfortably above 50pts while services indexes are in a down trend. The market expects some deterioration of an economic activity in December.

The year-end is nearing and perhaps the upcoming week could be the last one with at least average investors' activity and that could bring any material changes on the market.

Market implications

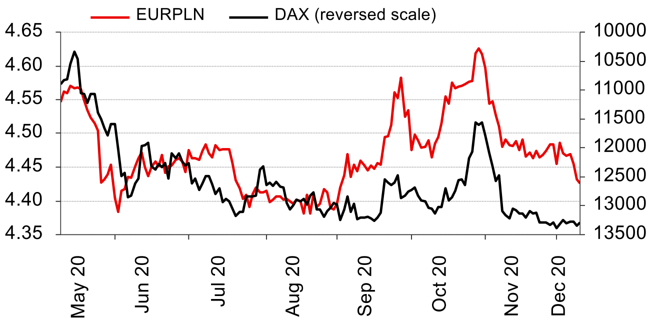
Outcome of the UK-EU talks could determine the mood at the start of the week. The United Kingdom is one of the biggest Poland trading partners so the perspective of no trade deal since the start of 2021 could generate a pressure on Polish assets. Let's hope that after the successful Poland/Hungary-EU talks, the European leaders will strive to continue the series of a happy-end negotiations.

FX There has been no big zloty's reaction to the EU budget approval. This might have been due to the two reasons. First, the Polish currency did not depreciate after Poland and Hungary said they could veto the budget indicating that the market has not been seriously concerned that there would be no deal by the end of the year. Second, the room for larger zloty's appreciation could have been limited by the unsolved Brexit case.

FI Polish bond yields will likely end the week lower vs the last Friday's close but the scale of move appears to be disappointing given the EU budget deal and the ECB decision to expand its PEPP program. In our view, the zloty may show bigger adverse/positive reaction to the Brexit talks than bonds.

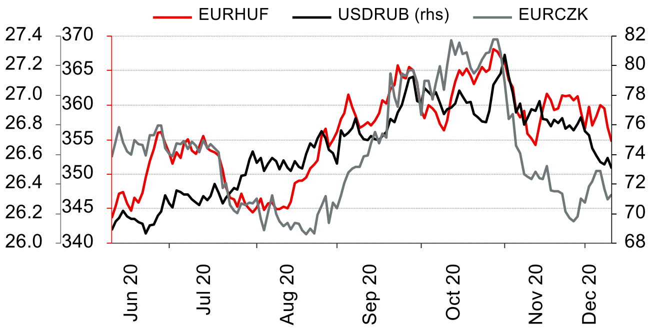
The 10Y PL-DE bond yield spread has widened to the level last time seen weeks ago. We would like to note not only the value it has reached but also the speed of the rise. The 4-week % change of the spread has reached >10% and as seem on the chart, this has not happened very often in the past. However, when it appeared, on a several occasions it preceded at least short stabilization of the Polish 10Y bond.

EURPLN and German DAX equity index



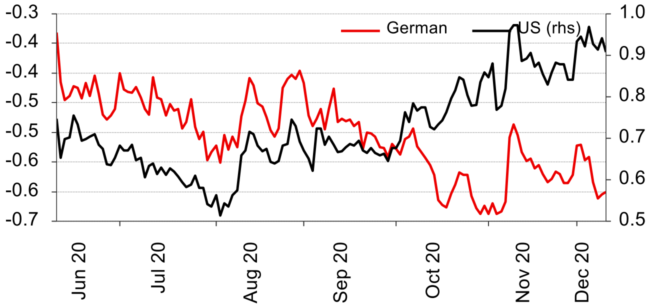
Source: Refinitiv Datastream, Santander Bank Polska

EURHUF, EURCZK and USDRUB



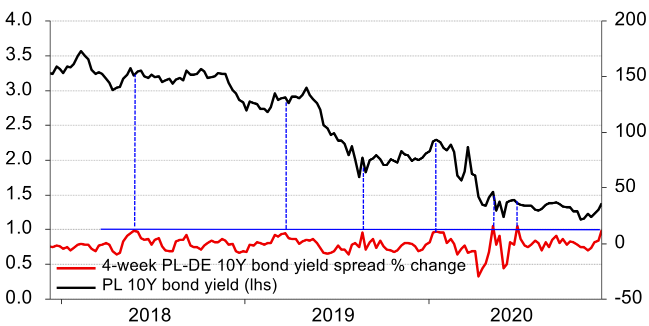
Source: Refinitiv Datastream, Santander Bank Polska

10Y German and US bond yields



Source: Refinitiv Datastream, Santander Bank Polska

4-week 10Y PL-DE yield spread % change and PL 10Y bond yield



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
		MONDAY (14 December)					
11:00	EZ	Industrial Production	Oct	% m/m	1.8	-	-0.4
14:00	**PL**	**Current Account Balance**	**Oct**	**€mn**	**1 235**	**1 022**	**1 072**
14:00	**PL**	**Trade Balance**	**Oct**	**€mn**	**1 114**	**923**	**1 238**
14:00	**PL**	**Exports**	**Oct**	**€mn**	**22 448**	**21 637**	**21 109**
14:00	**PL**	**Imports**	**Oct**	**€mn**	**21 277**	**20 714**	**19 871**
		TUESDAY (15 December)					
10:00	**PL**	**CPI**	**Nov**	**% y/y**	**3.0**	**3.0**	**3.1**
14:00	HU	Central Bank Rate Decision		%	0.6	-	0.6
15:15	US	Industrial Production	Nov	% m/m	0.5	-	1.1
		WEDNESDAY (16 December)					
09:30	DE	Flash Germany Manufacturing PMI	Dec	pts	56.5	-	57.8
09:30	DE	Flash Markit Germany Services PMI	Dec	pts	44.0	-	46.0
10:00	EZ	Flash Eurozone Manufacturing PMI	Dec	pts	53.1	-	53.8
10:00	EZ	Flash Eurozone Services PMI	Dec	pts	41.5	-	41.7
14:00	**PL**	**CPI Core**	**Nov**	**% y/y**	**4.2**	**4.2**	**4.2**
14:30	US	Retail Sales Advance	Nov	% m/m	-0.1	-	0.3
20:00	US	FOMC decision		%	0.25	-	0.25
		THURSDAY (17 December)					
10:00	**PL**	**Employment in corporate sector**	**Nov**	**% y/y**	**-1.5**	**-1.2**	**-1.0**
10:00	**PL**	**Average Gross Wages**	**Nov**	**% y/y**	**4.7**	**4.5**	**4.7**
11:00	EZ	HICP	Nov	% y/y	-	-	-0.3
14:30	US	Initial Jobless Claims	week	k	-	-	853
14:30	US	Housing Starts	Nov	% m/m	-0.3	-	4.9
14:30	CZ	Central Bank Rate Decision		%	0.25	-	0.25
14:30	US	Index Philly Fed	Dec	pts	21.7	-	26.3
		FRIDAY (18 December)					
10:00	DE	IFO Business Climate	Dec	pts	90.3	-	90.7
10:00	**PL**	**Sold Industrial Output**	**Nov**	**% y/y**	**3.5**	**3.8**	**1.0**
10:00	**PL**	**PPI**	**Nov**	**% y/y**	**-0.1**	**-0.5**	**-0.4**

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.