12 March 2021

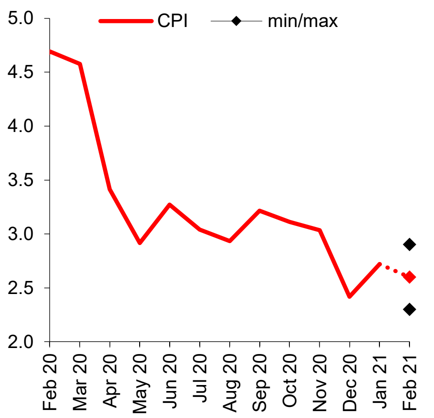
Weekly Economic Update

A lot of data and Fed meeting

What's hot next week

- After a week almost devoid of local events, comes one crammed with new stats: on Monday CPI data are out, on Tuesday core CPI and balance of payments, on Wednesday wages and employment, on Thursday industrial production and PPI, on Friday retail sales and construction output. The new data may prove important indicators of economic activity in 1Q and inflation tendencies.
- As usual in March GUS will release **CPI data for January and February** recalculated using updated weights. Our forecast is a mild decline of inflation to 2.6% y/y in February (in line with consensus) from 2.7% in January. Uncertainty regarding the reading is quite big due to the hard-to-estimate impact of CPI basket weights update (the forecast range is 2.3%-2.9% according to Parkiet daily newspaper which prepares consensus of local economists). In our view the review of the CPI basket weights (which may cause particularly large shifts in a pandemic-stricken year) will lead to both readings going up by no more than 0.1pp. We think that core inflation decreased in February to 3.3% after a rise to 3.8% y/y in January. This would be markedly below consensus, which is pointing to 3.7% y/y for February, so the release might be a market-moving one (if our estimate proves correct).
- In case of other forecasts we are more optimistic than the market median when it comes to February **wage growth** (5.3% y/y) and **industrial output** (4.7% y/y), but more pessimistic about **retail sales** (-4.3% y/y). **Balance of payments** data will in our view show a very high surplus on current account in January (€3.1bn), but poor growth of exports and imports (less working days, respite after high activity in late 2020). In sum, the combination of the data coming throughout the week will be a mixed bag and might not give investors a clear indication if they should head towards pricing a scenario of quicker growth plus higher inflation and rate hikes or in the opposite direction.
- The key event abroad will be the **Thursday Fed meeting**. The accompanying forecast update will most likely show higher paths of GDP and inflation while the dot chart will still be highlighting no intensions in FOMC to raise interest rates in near future. For the markets a key issue will be if the central bank signals shrinking tolerance to rising bond yields in a more convincing manner than recently. A more dovish message from the central bank could help slow down any further upside moves of bond yields.

CPI – our forecast and range of Parkiet forecasts



Source: GUS, Parkiet, Santander

Market implications

- The 4.60 level proved an effective resistance for the EURPLN so far. However, the zloty did not react positively to the theoretically positive factors: slightly weaker dollar, higher equity indexes or stronger Polish bonds. Meanwhile, the factors ahead are hardly supportive for the currency: the possible increase in the scale of NBP's QE, the approaching Supreme Court ruling on FX-loans (25 March) possibly boosting intraday volatility. Summing up, we think 4.60 level will be tested, and most likely breached, in the next 1-2 weeks.
- Polish market rates declined in the course of the passing week, but showed no big positive reaction to the central bank's statement regarding QE program which did not even prevent a rebound. It seems that trends on the core markets shall remain key. The overall message from the meeting should be rather dovish and help yields on the core markets and in Poland to stay below their recent peaks.

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Last week in the economy

Last week was not rich in macro data: we only got to see the quarterly report on demand for labour and details of NBP March forecasts. Moreover, the government decided to tighten restrictions in new regions and the NBP said it is worried about rising yields.

Starting on 15 March the Mazowieckie and Lubuskie voivodships will be covered by **stricter anti-pandemic regulations**, as Warmińsko-Mazurskie and Pomorskie already are (out of 16 total voivodships). This means a closure of shopping centres, sports facilities, cultural and recreation institutions. The health minister said that it may happen that another expansion of restrictions will be country-wide.

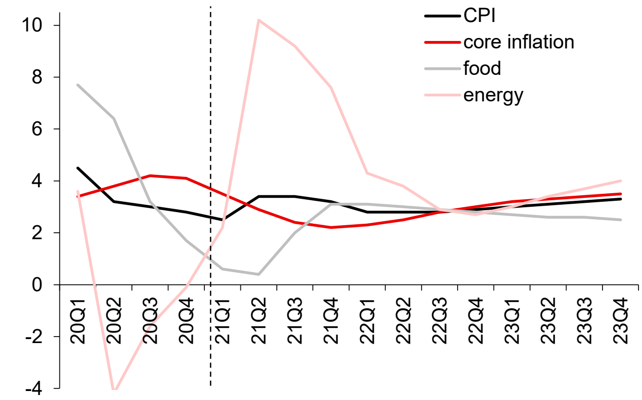
NBP Inflation Report showed that the upward revision vs the November inflation projection in 2021 came from energy prices. In 2022 core inflation is expected to contribute less to headline CPI than in the previous projection, but quicker rise of food and energy components more than offset this decline. Core inflation is expected to weaken throughout 2021 to 2.2% in 4Q21 and to change direction in early 2022 as the output gap switches to positive values. The positive GDP path revision was based on stronger contribution of private consumption (c.0.5pp more in 2021 and 2022, thanks to wage growth accelerating systematically to 7.5% in 2023 from 5.3% in 2022 amid unemployment rate low enough to provide wage pressure throughout the whole projection). However, according to the authors the balance of risks is negative for both GDP and CPI paths.

In 4Q20 **the demand for labour** in the Polish economy still seemed muted. The difference between newly created and destroyed workplaces amounted to 37.6k versus 64k in 3Q and this was the weakest result (apart from 2Q20) – since the 2013 slowdown. In annual terms, this measure fell by 29.2% while one quarter earlier it was -7.4%. Job creation was slower than in 3Q (-20% y/y vs -16.4% earlier), whole job destruction was somewhat faster in annual terms (-12.1% y/y versus -24% in 3Q). In 4Q20, the pandemic was blamed for layoffs less often than before – in 12% of cases versus 26% in 3Q20.

MPC member Eryk Łon said that interest rate hikes will not be needed till the end of the current MPC's term. Another MPC member **Eugeniusz Gatnar** is of the opinion that the current inflation projection, despite being higher than the November 2020 one, is "too cautious". He thinks that in the MPC there is no majority to support a possible rate hike.

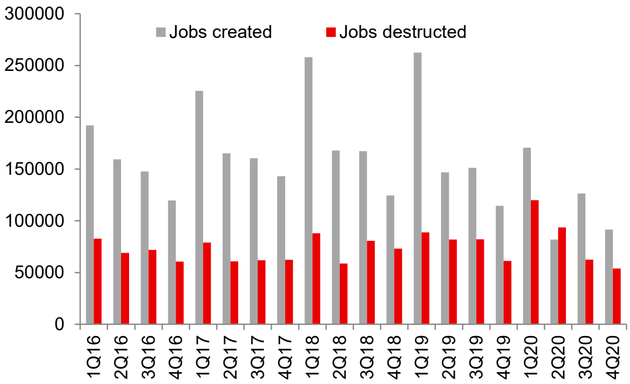
On Thursday **the NBP released a statement** informing that due to rising bond yields it is mulling whether to increase flexibility and frequency of bond tenders, i.e. probably to increase the scale of bond purchases. On one hand this comes as a surprise, as during the press conference on March 5th the NBP governor Glapiński calmed down that rise of yields is no reason to worry, as it reflects higher optimism about economic outlook (seemingly following the Fed guidance). Moreover, yields declined since this conference. On the other hand, Glapiński pointed recently a few times that the divergence between the QE pace in Poland and abroad is among sources of the excessive zloty strength, and the NBP was promoting articles stating that increase of asset purchases could be a feasible option.

NBP inflation forecasts, % y/y



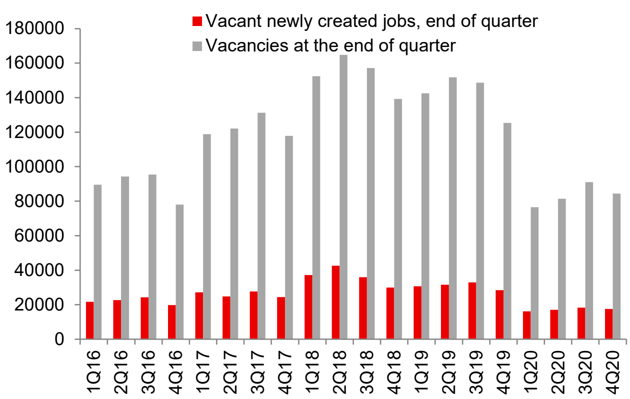
Source: NBP, Santander

Jobs creation and destruction



Source: GUS, Santander

Vacancies



Source: GUS, Santander

FX and FI market

Last week on the market

FX EURPLN was hovering at an elevated level despite a EURUSD rise, drop of Polish bond yields and rebound of the European stock indexes. The exchange rate set the weekly peak at c4.60 but at the end of the week was slightly below this level, roughly flat on weekly basis. Room for stronger zloty was limited by climbing number of new Covid-19 cases in Poland that resulted in more restrictions (regional, for now) and signal from the central bank that the QE program could be intensified. USDPLN also did not change much in weekly terms though it managed to reach 3.885 for a while, its highest since November. GBPPLN remained at an elevated level of c5.36, its highest since late 2016. CHFPLN was trading sideways around 4.13.

The other CEE currencies gained slightly. EURCZK fell 0,25%, EURHUF 0.3% and USDRUB 1.5% on weekly basis. The inflation readings from Czechia (unexpected CPI drop) and Hungary (expected rise) failed to generate any material market reaction. EURCZK and EURHUF remain relatively close to their local peaks while USDRUB neared the lower end of the 73-75 range in which it has been trading since mid-February.

FI Dovish message from the NBP governor at his last Friday's speech and stable yields on the core markets allowed Polish market rates to fall last week. Bond yields and IRS rates fell 5-10bp which allowed the 10Y spread vs Bund to fall c5bp to 185bp and vs UST 10bp to -5bp. At the end of the week, the Polish central bank announced that it could consider increased frequency of bond tenders but this did not prevent bonds from slight weakening owing to higher yields on the core markets on Friday.

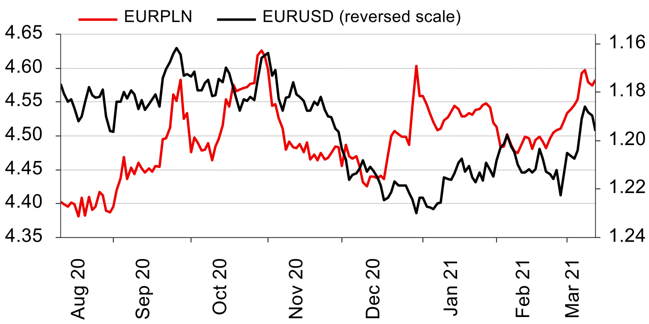
Next week we will see important Polish data, mainly February inflation, retail sales and industrial output. Our CPI forecast is marginally above the consensus (2.6% y/y vs 2.5%), industrial output as well (4.7% y/y vs 4.5%), while in case of the real retail sales we are below (-4.3% y/y vs -2.7% y/y). Abroad the market will be waiting for the FOMC decision. Recall, that in the recent weeks Jerome Powell and his Fed colleagues tried to intervene verbally to pause or slow the yield's upside trend but without much success.

Market implications

FX The 4.60 level proved an effective resistance for the EURPLN so far. However, the zloty did not react positively to the slightly weaker dollar, higher equity indexes or stronger Polish bonds. Meanwhile, the factors ahead are hardly supportive for the currency: It is already less than two weeks until the Civil Chamber of the Supreme Court announces its ruling regarding important issues regarding the FX-loans case, and as we approach March 25, the uncertainty about the verdict may get to the forefront, boosting intraday volatility. Second, the recent signal from the central bank that the pace of bond buying may be boosted is not a good news for the zloty either. Also looking at the chart, we see that EURPLN tends to return to 4.60 quite often in the recent weeks while the down waves are getting shorter in price terms. Summing up, the short-term outlook for the zloty is not favourable, in our view. We think 4.60 level will be breached in the next 1-2 weeks.

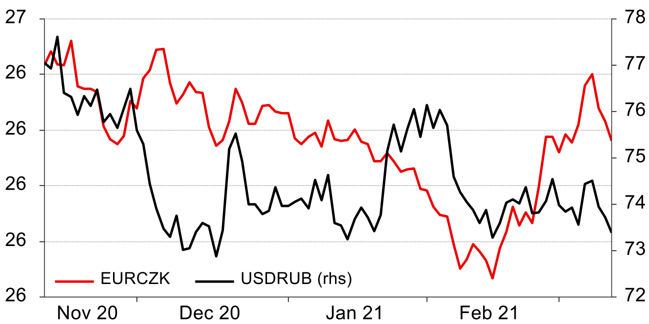
FI Polish market rates showed no big positive reaction to the central bank's statement regarding QE program and it seems that trends on the core markets shall remain key. The main event after the weekend would be the FOMC decision. We will have updated dot plot and this should show that chances for any rate hikes in the coming years are very low. We think the Committee will try to be more convincing it is not planning to tighten monetary policy anytime soon. Thus, the overall message from the meeting should be rather dovish and help yields on the core markets and in Poland to stay below their recent peaks.

EURPLN and EURUSD



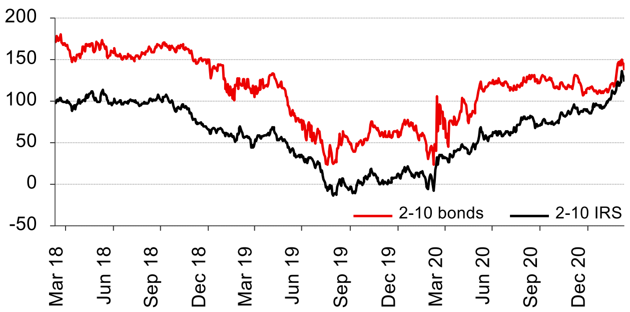
Source: Refinitiv Datastream, Santander Bank Polska

EURCZK and USDRUB



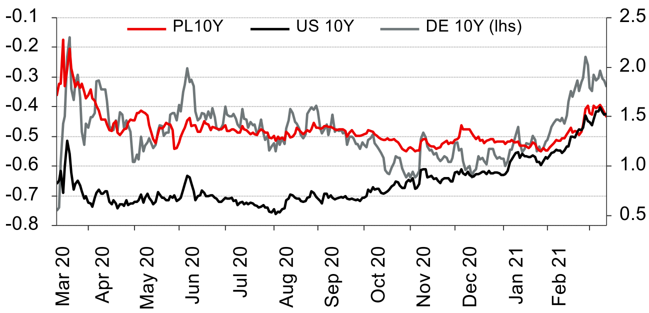
Source: Refinitiv Datastream, Santander Bank Polska

Poland 2-10 spreads



Source: Refinitiv Datastream, Santander Bank Polska

10Y bond yields



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
		MONDAY (15 March)					
09:00	CZ	Retail sales	Jan	% y/y	-4.9	-	3.7
10:00	**PL**	**CPI**	**Feb**	**% y/y**	**2.5**	**2.6**	**2.7**
		TUESDAY (16 March)					
11:00	DE	ZEW index	Mar	pts	73.1	-	71.2
13:30	US	Retail sales	Feb	% m/m	-0.4	-	5.3
14:00	**PL**	**Current account**	**Jan**	**€m**	**2416**	**3144**	**430**
14:00	**PL**	**Exports**	**Jan**	**€m**	**3.7**	**1.9**	**14.8**
14:00	**PL**	**Imports**	**Jan**	**€m**	**1.2**	**-0.6**	**13.6**
14:00	**PL**	**Core inflation**	**Feb**	**% y/y**	**3.6**	**3.3**	**3.8**
14:15	US	Industrial output	Feb	% m/m	0.5	-	0.9
		WEDNESDAY (17 March)					
10:00	**PL**	**Employment in corporate sector**	**Feb**	**% y/y**	**-1.9**	**-1.9**	**-2.0**
10:00	**PL**	**Wages in corporate sector**	**Feb**	**% y/y**	**4.7**	**5.3**	**4.8**
11:00	EZ	HICP	Feb	% y/y	0.9	-	0.9
13:30	US	House starts	Feb	k	1 540	-	1 580
19:00	US	Fed decision		%	0.0-0.25	-	0.0-0.25
		THURSDAY (18 March)					
10:00	**PL**	**Industrial output**	**Feb**	**% y/y**	**4.5**	**4.7**	**0.9**
10:00	**PL**	**PPI**	**Feb**	**% y/y**	**1.4**	**1.2**	**0.7**
13:30	US	Philly Fed index	Mar	pts	-	-	23.1
13:30	US	Initial jobless claims	week	k	-	-	712
		FRIDAY (19 March)					
10:00	**PL**	**Construction output**	**Feb**	**% y/y**	**-9.5**	**-9.3**	**-10.0**
10:00	**PL**	**Retail sales**	**Feb**	**% y/y**	**-2.7**	**-4.3**	**-6.0**
	PL	**Fitch rating update**					

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg