

19 April 2019

Weekly Economic Update

Happy Easter!

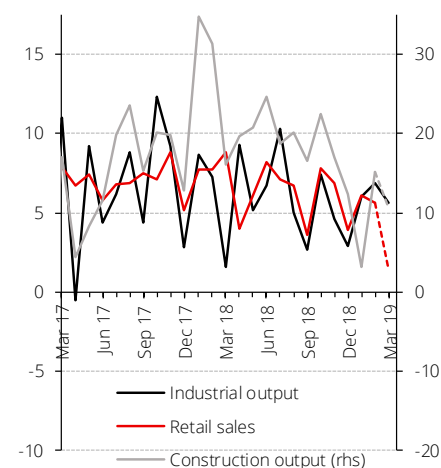
What's hot next week

- Next week in Poland is not only shorter (holiday on Monday) but also situated right between Easter and the long May weekend. It does not have to mean, however, that it will be dull and inactive period for markets. First of all, we will see a number of new data releases, and secondly the election campaign for the European Elections is entering its crucial stage, so it could be a hot period in terms of political news and events. Please recall that not so long ago the politicians from the ruling party were suggesting that the government reshuffle is possible before the end of April (although recently Polish media suggested it may be delayed due to teachers' strike).
- Right after the Easter Monday the statistical office may surprise us with the **quarterly GDP data revision** for 2017-2018. One year ago a similar revision showed a substantial reduction (by -6pp) of investment growth in the last quarter of 2017.
- Additionally, in the Polish calendar we have retail sales, construction output, unemployment rate, money supply, the release of the Statistical Bulletin and maybe the data about the state budget performance in March. The data could shed more light in terms of the economic growth in 1Q19. Recently released data about trade deficit widening in February suggested lower optimism about 1Q GDP forecast, but the March industrial output improved the outlook again. We forecast **pretty decent construction and assembly output growth (by more than 10% y/y) and weaker reading of the retail sales (below +1.5% y/y in constant prices)** mainly due to the different time of Easter than in the previous year). Overall, the upcoming data shall allow us to expect the GDP grew c4.5% y/y in 1Q19.
- Abroad, we will see German Ifo and some US data (GDP, durable goods orders, real estate data). The German index could show some rebound though the source of this move could not be much optimistic. There are also small chances that the first estimate of the US 1Q GDP would surprise to the upside.

Market implications

- After the drop of yields in the passing week (mainly on the core market), the coming days may also be positive for bonds. This could be thanks to the data releases (relatively weak Polish retail sales, no meaningful improvement in the global macro data) and the bond auction (with possibly quite positive results due to PLN8bn of bonds maturing on April 25). On the FX market, EURPLN could rise (due to the macro data).

Production and retail sales, constant prices, % y/y



Source: GUS, Santander

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Last week in economy

The government has found a way to deliver the costly election promises without breaching the expenditure rule or even without halting the fiscal consolidation. This was achieved through (1) indication of new sources of revenues with the upfront taxation of pension savings playing the key role (as part of the **OFE overhaul**), (2) trimming room for expenditures other than those linked to the pre-election promises, except maybe for a few areas where increases are obligatory from the legal point of view. The fiscal trajectory presented in the **Convergence Programme Update (CP)** suggests that (our) worries about fiscal easing and increased debt issuances were overblown. More in our [Economic Comment "Redistribution rather than easing"](#).

S&P rating agency assessed Poland before the release of the CP and the OFE overhaul proposal. Still, the agency confirmed the rating of Poland at A- with stable outlook, judging that the strong economic growth allows for looser fiscal policy. The CP scenario (if implemented) and the creation of PPK (Employee Capital Plans) this year meet some of the criteria S&P mentioned as prerequisites for higher credit score (quicker debt reduction, rise of private savings).

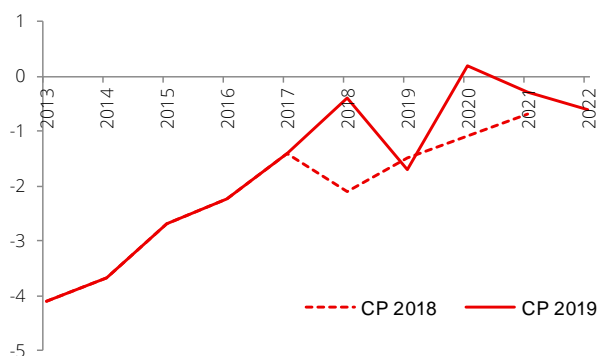
Polish industry showed more signs of resilience to the euro zone slowdown with March **output** beating market expectations (5.6% y/y vs 4.4%). The seasonally and working day adjusted growth showed an acceleration from 6.5% y/y to 7.8% y/y – the strongest reading since July 2018. The data seem to confirm our view that economic slowdown this year will be mild. PPI growth was 2.5% y/y in March, down from 2.9% y/y, vs 2.6% market expectations and our 2.4% call. We expect the PPI to ease some more in the following months.

The labour market remains tight, judging by the record-low unemployment levels, which should lead to wage pressures and slower employment growth, in our view. However, this was not seen in the March data, which we think was due to some one-off effects. **Wage growth** in the corporate sector was just 5.7% y/y vs 7.3% expectations while **employment** showed one of the strongest m/m March changes in recent years. Very high consumer confidence indicators for April (especially when it comes to assessment of financial situation) also suggest that wage growth has not entered a deceleration phase yet.

The final March **CPI** inflation reading was in line with the flash estimate, 1.7% y/y, up from 1.2%. Core CPI jumped to 1.4% y/y from 1.0% - this has been the highest reading since October 2013. Services prices inflation rose to 2.7% y/y from the December low of 0.9%. We have recently observed more and more factors suggesting that our CPI forecast reaching c2.5% y/y in December will need to be revised higher. These factors are: strong rebound of pork and gasoline prices in April, weather conditions that could threaten this year's crops, fiscal stimulus, uncertainty if companies will be compensated for higher energy prices, no compensation next year).

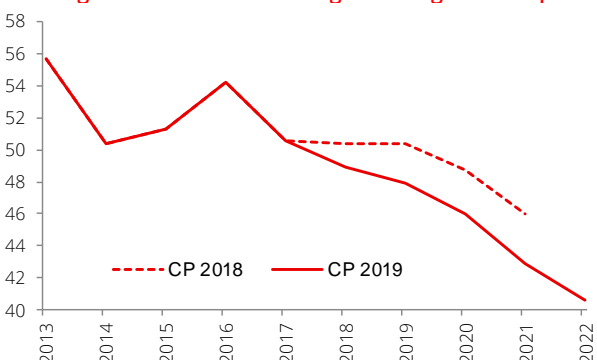
So far, the **MPC** is quite relaxed about inflation outlook. According to the minutes from the April MPC meeting, the majority of the Council's members was of the opinion that there is a limited risk of CPI permanently deviating from the target and that slower growth abroad generates uncertainty regarding the scale of GDP growth deceleration in Poland. Some members said that rate hikes could be considered if there is a significant inflation rise. We believe there is a growing probability that the pace of inflation growth in 2019 and 2020 will be faster than the central bank currently assumes.

GG deficit – gov't forecasts in Convergence Programme Updates



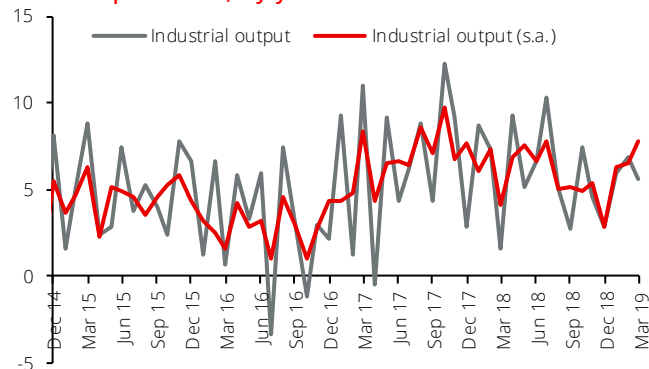
Source: Ministry of Finance, Santander

GG debt – gov't forecasts in Convergence Programme Updates



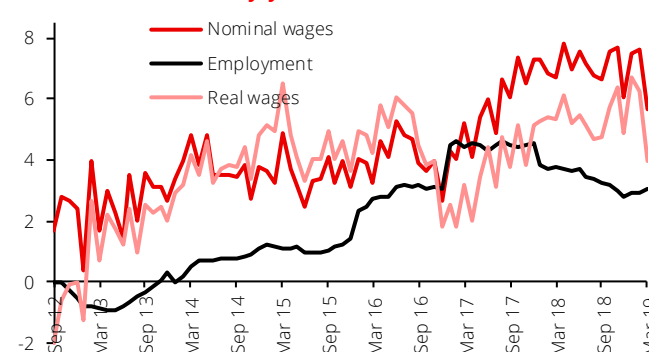
Source: Ministry of Finance, Santander

Industrial production, %y/y



Source: GUS, Santander

Labour market data, % y/y



Source: GUS, Santander

FX and FI market

Last week on the market

FX EURPLN was decreasing at the beginning of the last week, fuelled by better mood on the global markets and information about the OFE (Open Pension Funds) reform. In the later part of the week EURPLN rebounded, which almost levelled the earlier falls. This upward move was a reaction to the dramatic slide of EURUSD which was affected by PMI data that painted a gloomy prospect for the European economy.

FI Over the last week the yields of domestic bonds were declining pushing the entire domestic curve down by 7bp. At the beginning of the week the bonds market was impacted by the information about the OFE (Open Pension Funds) reform which implied a reduction of the debt supply. In the second part of the week POLGBs were supported by poor Eurozone PMI data. The domestic bonds ignored the much-better-than-expected domestic industrial production data for March. Despite the bonds market going up, the IRS rates increased by 4-5bp, following the core markets peers, which was reflected in the ASW spread narrowing to the level last seen in February.

Key events

This week we are expecting German Ifo data (on Wednesday) and US GDP advance reading for 1Q19 (on Friday). On Thursday regular POLGBs auction is on the agenda. The German data is likely to show some uptick, however we think that their structure will be rather pessimistic. The US 1Q19 GDP reading has a small chance to surprise us on the positive side.

The markets may get inspired with the domestic retail sales data release (on Tuesday), where we expect a negative surprise.

On the auction we expect supply at PLN8bn (the upper end of Ministry of Finance announced PLN4-8bn supply).

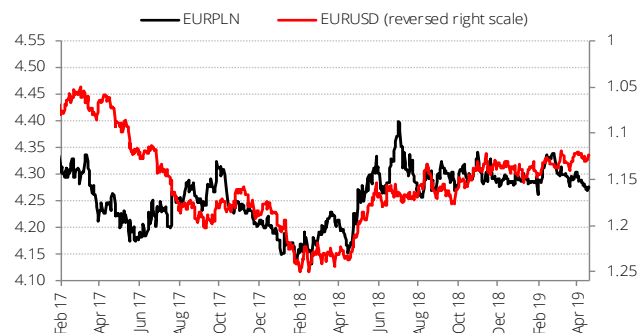
Market implications

FX This week we expect EURPLN to increase in reaction to the series of poor macro data, domestic retail sales and US GDP. The German Ifo data is not likely to disturb this move. Similarly as in the case of PMI data, we expect a marginal rebound but Ifo data structure will rather suggest the weakening of economic outlook.

FI The substantial decreases in yields over the last week will most likely encourage investors to take the profit. However the OK0419 bond redemption, scheduled for 25 April (cPLN8bn) together with regular auction should support the domestic bonds market.

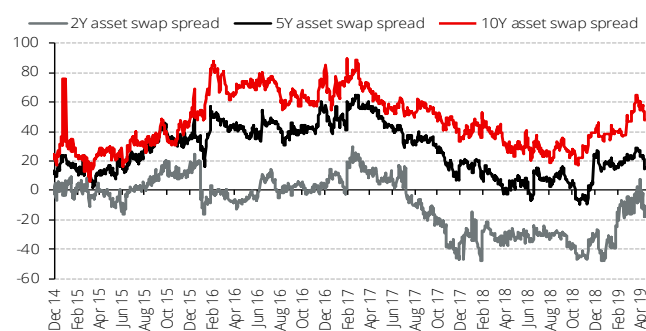
In the next week we anticipate the yields to gradually decrease as a response to the release of Eurozone flash 1Q19 GDP which in our opinion will be weak. Moreover, the bonds are likely to be supported by FOMC conference, where we expect further wave of comments emphasizing a negative influence of trade wars on the economy.

EURPLN and EURUSD



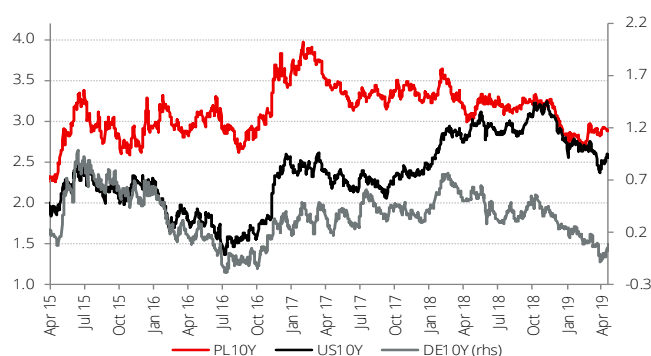
Source: ThomsonReuters, Santander Bank Polska

ASW spreads (bp.)

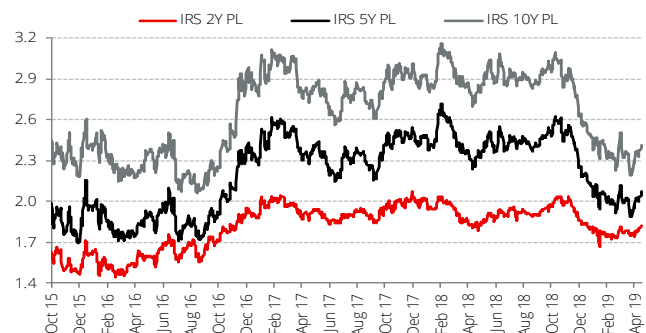


Source: ThomsonReuters, Santander Bank Polska

Yield of the Polish, German and US 10Y bonds



PLN IRS (%)



Source: Thomson Reuters, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE
				MARKET	SANTANDER	
MONDAY (22 April)						
16:00	US	Existing Home Sales	Mar	% m/m	-3.99	11.8
TUESDAY (23 April)						
	PL	Central Budget Cumul.	Mar	mn PLN	-	-792.87
10:00	PL	Retail Sales Real	Mar	% y/y	0.0	5.6
14:00	PL	Money Supply M3	Mar	% y/y	9.6	9.8
16:00	US	New Home Sales	Mar	% m/m	-3.3	4.9
WEDNESDAY (24 April)						
10:00	DE	IFO Business Climate	Apr	pts	99.9	99.6
10:00	PL	Construction Output	Mar	% y/y	9.0	10.64
10:00	PL	Unemployment Rate	Mar	%	5.9	5.88
THURSDAY (25 April)						
14:30	US	Durable Goods Orders	Mar	% m/m	0.5	-1.6
14:30	US	Initial Jobless Claims		k	205.0	196.0
FRIDAY (26 April)						
14:30	US	GDP Annualized	1Q	% Q/Q	1.8	2.2
16:00	US	Michigan index	Apr	pts	96.9	96.9

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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