Bank Zachodni WBK
Grupa Santander

WEEKLY ECONOMIC UPDATE

11 – 17 December 2017

The event of the week abroad will be the Fed meeting and the likely interest rate hike. Even more important than the decision itself will be the post-meeting press conference and the change the in FOMC members' expectations about the pace of future tightening. ECB meeting is also in the agenda, but potentially much less exciting. There will be also a few data releases, including European flash PMIs.

In Poland the data about inflation will help to understand what fueled sharp CPI rise in November to 2.5% y/y (in our view, it was mainly food and fuel, while core inflation inched up only slightly to 0.9%). Also, the balance of payments data will be released, potentially positive for the zloty (high export growth, sizeable surplus in trade and current account).

The politics will probably continue dominating discussions in Poland. The change of PM from Beata Szydło to Mateusz Morawiecki failed to influence markets, and the Sejm's confidence vote for the new government is unlikely to change anything. In our view, the PM replacement will not change the course of government's policies substantially, but in general may be slightly positive for Polish assets, as it gives some hope for less confrontational policy versus EU and better coordination of work on some projects (for example, changes in OFE, new capital plans). At the bond switching auction the Ministry of Finance may offer more short-term bonds, after the last information about extension of average duration in their portfolio.

Economic calendar

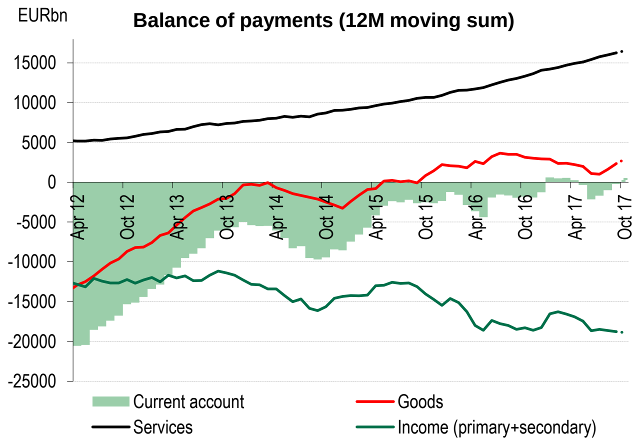
TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
			MONDAY (11 December)				
14:00	**PL**	**CPI**	**Nov**	**% y/y**	**2.5**	**2.5**	**2.5**
			TUESDAY (12 December)				
11:00	DE	ZEW Survey Current Situation	Dec	pts	88.45	-	88.8
14:00	**PL**	**CPI Core**	**Nov**	**% y/y**	**0.9**	**0.9**	**0.8**
			WEDNESDAY (13 December)				
11:00	EZ	Industrial Production	Oct	% m/m	-0.3	-	-0.6
14:30	US	CPI	Nov	% m/m	0.4	-	0.1
20:00	US	FOMC decision		%	1.25-1.5	-	1-1.25
			THURSDAY (14 December)				
09:30	DE	Flash Manufacturing PMI	Dec	pts	62.1	-	62.5
09:30	DE	Flash Services PMI	Dec	pts	54.5	-	54.3
10:00	EZ	Flash Manufacturing PMI	Dec	pts	59.7	-	60.1
10:00	EZ	Flash Services PMI	Dec	pts	55.9	-	56.2
13:45	EZ	ECB Main Refinancing Rate		%	0.0	-	0.0
14:00	**PL**	**Current Account Balance**	**Oct**	**€mn**	**147**	**702**	**-100**
14:00	**PL**	**Trade Balance**	**Oct**	**€mn**	**609**	**748**	**764**
14:00	**PL**	**Exports**	**Oct**	**€mn**	**17800**	**18478**	**17207**
14:00	**PL**	**Imports**	**Oct**	**€mn**	**17371**	**17730**	**16443**
14:30	US	Initial Jobless Claims	week	k	240	-	236
14:30	US	Retail sales	Nov	% m/m	0.3	-	0.2
			FRIDAY (15 December)				
11:30	**PL**	**Bond Switch Auction**					
15:15	US	Industrial Production	Nov	% m/m	0.2	-	0.9

Source: BZ WBK, Reuters, Bloomberg

ECONOMIC ANALYSIS DEPARTMENT:
al. Jana Pawła II 17, 00-854 Warszawa fax +48 22 586 83 40
email: ekonomia@bzwbk.pl Web site: http://www.bzwbk.pl
Piotr Bielski +48 22 534 18 87
Marcin Luziński +48 22 534 18 85
Grzegorz Ogonek +48 22 534 19 23
Konrad Soszyński +48 22 534 18 86
Marcin Sulewski +48 22 534 18 84

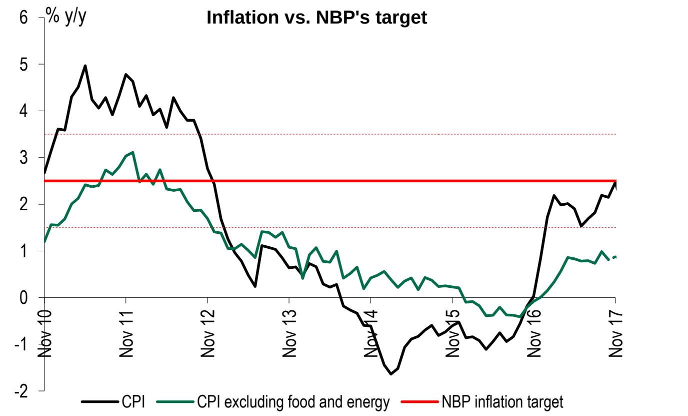
TREASURY SERVICES:
Poznań +48 61 856 5814/30
Warszawa +48 22 586 8320/38
Wrocław +48 71 369 9400

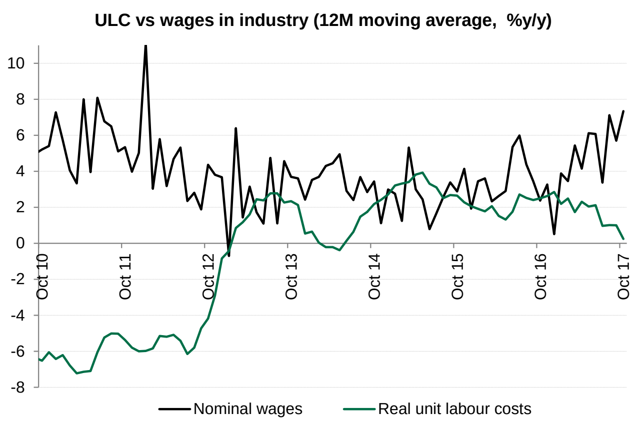
What's hot next week – Final CPI and Fed rate hike



- This week will start with the final release of November CPI. Flash headline estimate surprised to the upside hitting the target for the first time in five years. We think the final figure should not differ much from the flash one and we forecast that the main driver for acceleration from 2.1% were food and energy prices. On Tuesday the NBP will release core CPI and we estimate it rose to 0.9% y/y from 0.8% in October.
- We forecast the October balance of payments data to show the second highest C/A surplus this year mainly thanks to lower deficit at primary income account. Positive working day effect shall boost exports and imports pace of growth – to 19% y/y (from 10.2% y/y) and 15.6% y/y (from 5.7%), respectively.
- As regards global events, the FOMC is likely to deliver its third 25bp rate hike. However, from the market's point of view the updated "dot chart" should prove more important.

Last week in economy – MPC immune to strong data, Fitch raises forecasts





- The MPC kept the main interest rates unchanged, with the reference rate at 1.5%, in line with expectations. The MPC communique was relatively soft and the press conference was even softer as governor Glapiński repeated his claim that interest rates should remain on hold until the end of 2018 and argued that the recent data (which we considered good arguments for the MPC hawks, not doves) solidify his view on rates. Rafał Sura and Eryk Łon who accompanied NBP head at the press conference expressed similar opinion.
- It seems that doves are still in majority in the rate-setting panel, with no desire to change the monetary policy stance in the foreseeable future. We guess that more hawkish Council members will be more vocal in expressing their concerns in the coming weeks. For now, we assume that the first interest rate hike is still likely in 2H18. We elaborate on this decision more in our Instant comment.
- The MPC decided to reduce interest on the mandatory reserve to 0.5% (from 1.35%), effective from Jan-18. The NBP governor said the decision was of a technical nature.
- Fitch raised GDP forecasts for Poland: for 2017 from 4% to 4.4%, for 2018 from 3.2% to 3.6% and the main risk to its forecasts comes from labour shortage. Fitch sees 100bp of interest rate hikes next year (market consensus is 25bp) and additional 50bp in 2019. According to the agency the expectations of tighter financing conditions will be among the key reasons of GDP growth slowdown after 2017. In 4Q17 alone, the agency estimates the GDP growth to be 3.9% y/y (in our view it will exceed 4%). We think that the release of these forecasts may mean that the rating review due Friday 8 could prove neutral or the agency could even refrain from releasing the report.

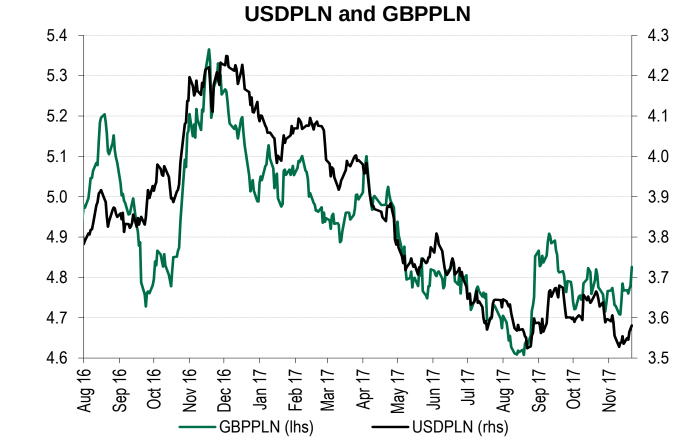
Quote of the week – Morawiecki replaced Szydło as prime minister

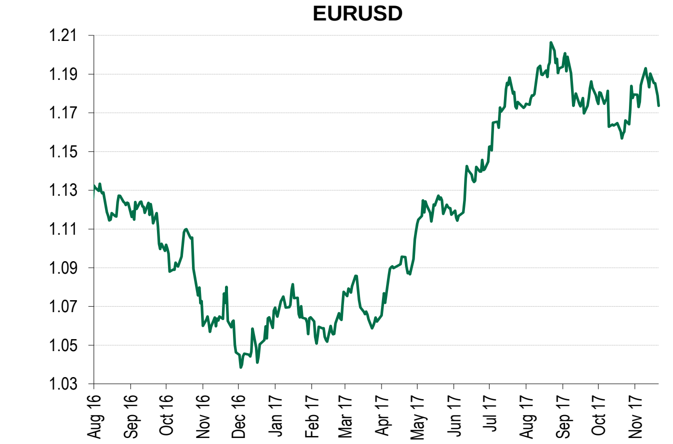
Beata Szydło, Prime Minister, Twitter, 8 December
These two years were an extraordinary time for me. It was an honor to serve Poland and Poles. Thank You.

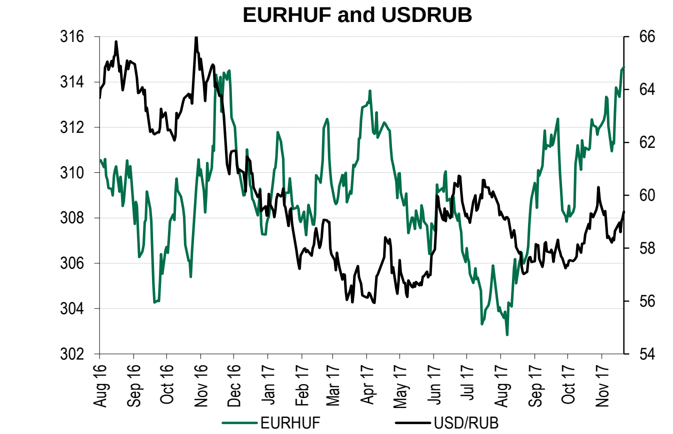
Beata Mazurek, Law and Justice spokeswoman, PAP, Bloomberg, 7 Dec
The new situation at home and abroad requires a change in management. The ruling party is to change the prime minister. PM Beata Szydło is to step down. Finance Minister Morawiecki is a candidate for new prime minister. People are being replaced but the programme is not changing.

President Andrzej Duda has designated Mateusz Morawiecki as new Prime Minister to replace Beata Szydlo, whose resignation has been accepted by the president. The new PM has 14 days to deliver introductory speech and win a confidence vote in the Sejm. The media report that for the time being, the composition of the government will remain almost intact and it is probable that Beata Szydło will become a deputy prime minister for social affairs. So far no candidates were named to head the Ministry of Finance and the Ministry of Development. In our view, replacing the PM will not change the general direction of the government policy; but it gives hope for a less confrontational stance towards the EU and improved coordination of some projects (for instance, changes in the pension system).

Foreign exchange market – Waiting for FOMC







Polish FX market still calm

- EURPLN stayed above the local low at below 4.20 oscillating near 4.21. In our previous reports, we were pointing to the low (and falling) volatility on the Polish FX market and now we have another proof for that: the last week's high-low spread is the lowest since late 2013. There was no meaningful market reaction to the dovish MPC and the change of Polish PM. At the same time, USDPLN rose to 3.58 from 3.55 (amid lower EURUSD) and GBPPLN climbed above 4.83 from 4.74 (owing to stronger pound after progress in Brexit negotiations).
- The outcome of the ECB meeting should not be a breaking event for the Polish currency. We see bigger potential for the FOMC to deliver a trigger for a sustainable move. The interest rate market has already priced the 25bp hike but the dollar is much weaker than in June when it was the last time when the FOMC raised rates. The outcome of the Committee's meeting could boost the US currency while could weigh on the EM currencies.
- As regards internal events, the recent week confirmed that the market seems to have largely priced-in the positive news-flow from Poland. Thus, the release of final CPI and more information about government reshuffle shall be neutral for the zloty in the coming days.

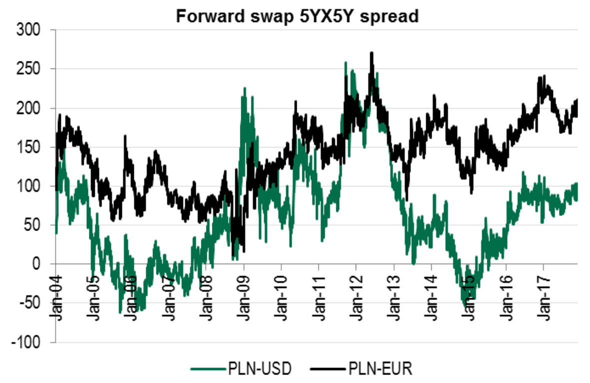
Fed could support dollar

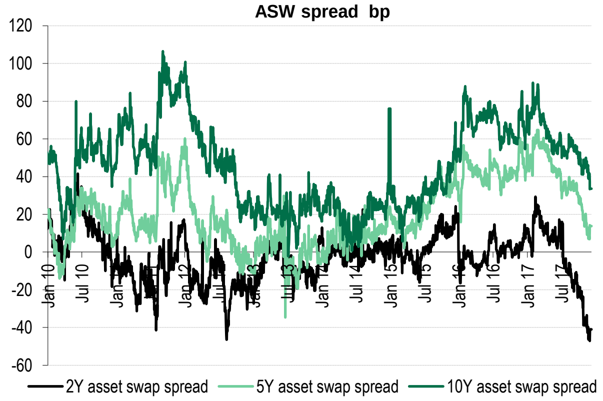
- EURUSD fell for the second week in a row, nearing 1.17 vs 1.19. The dollar gained thanks to some better-than-expected US figures and talking about a progress in negotiations on the tax reform.
- The European Commission and the United Kingdom informed about an agreement that allows them to take Brexit negotiations to the second stage. This information provided some support for the pound vs the euro.
- This week both the ECB and Fed hold meetings and in our view the updated "dot chart" should be crucial from the market perspective. We think there is still room for the dollar to gain in the short-term, owing to the Fed monetary policy outlook. The ECB is not expected to take any actions after it cut the size of monthly bond purchases but will also release the updated economic forecasts.

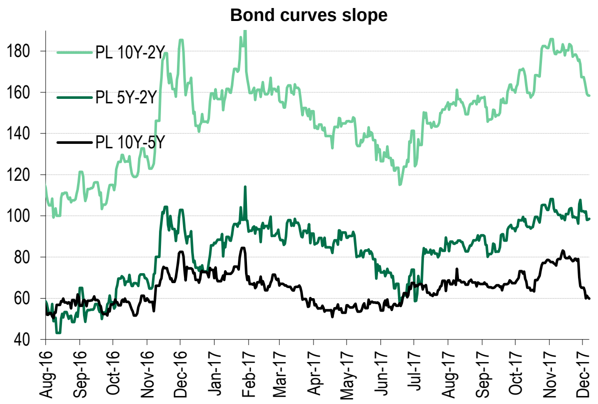
Forint weakest this year

- Hungarian forint remained under pressure vs the euro with EURHUF rising temporarily above 315, breaking this year's peak and reaching its highest since late 2016. The currency continued to depreciate after the recent central bank decision. Additional pressure was generated by weaker-than-planned budget performance and lower than expected CPI data.
- USDRUB rose to nearly 59.4 despite higher oil prices. The ruble was pressured by dovish signals from the central bank and dollar's appreciation on the global market.
- The upside trend of EURCZK paused as the expectations for a December rate hike revived after comments of central bankers and the exchange rate ended the week near 25.56 after a temporary rise to c25.7.

Interest rate market – ASW and yield curves flatter







Last week on the debt market

- On the debt market, the MPC conference was the most important last week event. At the beginning of the week, the bond market stabilized. The PMI data, as well as US new order data (weaker than expected), did not affect debt prices. The domestic market reacted to the MPC conferences. On the conference, the NBP president confirmed that in his opinion the rates will remain at the current level till the end of 2018. In reaction, the domestic yield curve decreased by 3-4 bp on the long end and by 1 bp on the short end. Over the week, the yields curve slide by 7 bp on the long end by 2 bp in the middle and rose by 2 bp on the short end. The yields drop was supported by weak ISM data and industrial production data from Germany.

Switch auction and Fed in the spotlight

- In our opinion, the most important event of the next week will be bond switch auction and Fed conference. The auction result will likely “setup” the domestic bonds market at the beginning of the next year. We expect the bigger share of shorter bonds (OK0720) on the auction. According to the last Ministry of Finance (MoF) statement, average debt maturity at the end of November in PLN was 4,52. This gives the issuer the greater flexibility of distributions maturity issue (so far MoF accordingly to their statement it sought to extend average maturity to c5 years). As a consequence we forecast further yields increases in the front end of the curve by 2-5 bp. The remaining part of the curve should be dependent on the core markets. In the next week, the key events for the core market will be: Wednesdays’ Fed conference (where the rate hike is almost certain), the US retail sales data release and European flash PMI data. The first two events will likely negatively affected the core bonds market (however moderately), the last should support the bonds market (we anticipate a little lower reading compare to the November one). As a result, we see 1-2 bp downshift in the belly and on the long end of the curve compared to the current level.

ASW curve will flatten

- On the asset swap (ASW) market, we expect the belly and the long end of the curve to remain on the slightly lower than the currently observed level. We anticipate further spread decompression on the short end of the ASW curve which will be triggered by the higher supply of short bonds on the switch auction.

Bond auction

- On the switch bond auction, MoF will plan to sell zero-coupon OK0720, fixed-coupon PS0123, DS0727, and floating-coupon WZ1122 and WZ0528 bonds.

End of the year perspectives

- At the end of the year perspectives, we see some upward shift, above the current level. In our opinion, the upward move will be supported by domestic economy solid macro data for November and the prospects to increasing debt supply at the beginning of the next year. However, taking into account the last released and expected European data (generally weak), the scale of growth will be insignificant.

Additional information is available on request. Please contact Bank Zachodni WBK S.A., Economic Analysis Department, al. Jana Pawła II 17, 00-854 Warsaw, Poland, phone +48 22 534 18 87, email ekonomia@bzwbk.pl