

23 November 2018

Weekly Economic Update

Strength of GDP and weakness of CPI

What's hot next week

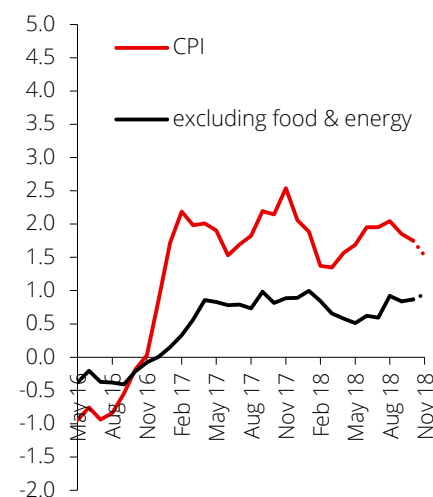
- The EU summit will be held this Sunday when the UK-EU Withdrawal Agreement is to be signed. This should be a non-event if everything goes well but the Brexit tensions are far from over since the British parliament needs to approve the Agreement. The governments faces tough fight to win votes needed to form a majority.
- At the end of the week, the stat office will publish detailed 3Q GDP data and flash CPI for November. We shall see what caused the flash GDP reading coming out well above the consensus. Some clues point to a stronger-than-expected rebound of investments. We think consumption stayed close to 5% y/y while net exports started to weigh on growth. We expect inflation data will show it sinking from 1.8% to 1.5% y/y due to the highly negative base effect (there was a spike of food and fuel prices a year ago).
- Globally, market attention should focus on the German and US data. Recent days saw some FOMC members suggesting that in 2019 there could be less rate hikes than expected so far and perhaps the minutes from the November meeting will reflect some concerns about the economic outlook after the last subdued macro readings. Markets will also be waiting for the US-China trade talks to be held later in the week.

Market implications

We think that the coming week will be yet another with EURPLN holding within the 4.26-4.34 range observed since August. Correlation with EURUSD looks to be still meaningful and the number of the data due to be released abroad could play the main role on the Polish FX market.

We think Polish yields/IRS could fall in the coming days amid strong core markets. The 10Y bond spread vs Bunds could widen as the outlook for the bond auction could curb gains of the domestic debt. Short-end may benefit from the low CPI reading.

Inflation measures, % y/y



Source: GUS, NBP, Santander Bank Polska

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What's hot next week

We will learn the solution to the puzzle of surprisingly strong GDP growth in 3Q. The flash print was 5.1% y/y vs. 4.7% market consensus. Some clues point to a stronger-than-expected rebound of investments. We think consumption stayed close to 5% y/y while net exports started to weigh on growth.

We will also get 3Q LFS data, with our focus on employment (after corporate data showed unexpected drop in August and September) and participation rate (response to very tight labour market).

Flash CPI reading for November may show inflation sinking from 1.8% to 1.5% y/y – at the time when the market is trying to guess how strongly it will rebound with the start of next year. The low estimate for November is due to the highly negative base effect in that month (there was a spike of food and fuel prices a year ago), while core CPI might have moved a notch higher.

Last week in economy

In Q3, revenues and costs of Polish enterprises rose 8.3% and 8.2% y/y, respectively. Profit before tax and net profit turned out to be higher by 9.5% and 11.1% vs the previous year after two quarters of weakening performance in y/y terms. Average margin improved in 3Q (from 4.7% to 5.3% after seasonal adjustment), suggesting that the pressure to increase own prices did not rise. Nevertheless, we expect that 2019 will see a rapid growth in energy costs, compressing margins.

In 3Q, investments on enterprises employing 50+ persons, accelerated to 15.7% y/y from 13.2% y/y, with construction of buildings increasing c23.5% y/y (vs 18.7% previously) and purchases of machinery by 16% (vs 17%). Summing these data with local governments investments (+74% y/y), in 3Q total investments might have grown at above 10% rate. We should mention, however, that in 2Q the investments of big companies and local governments were also very robust but the total headline disappointed as the SMEs underperformed.

Poland October industrial output beat expectations rising 7.4% y/y vs market consensus at 6.6% and our forecast at 6%. However, output grew only 5% y/y in seasonally adjusted terms – close to the September and August figures and well below 1H18 average of 6.4%. More in the [economic comment](#). Another positive surprise was October wage growth in the corporate sector, which accelerated from 6.7% y/y to 7.6% vs. market expectations of 6.7%. Employment growth stayed at 3.2% y/y.

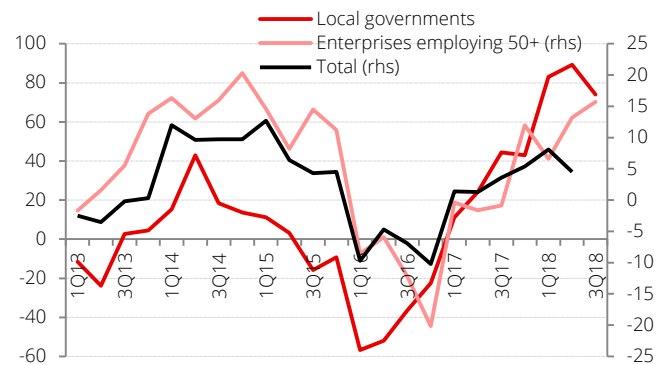
In October, Poland real retail sales growth surged from the disappointing 3.6% y/y for September to 7.8% vs market consensus at 5.8%. The headline figure beat expectations partly thanks to revival of auto sales. Outlook for sales seems positive - November's reading of business sentiment in retail sector was the highest since February while a sub-index showed that sales are expected to hold high in the months to come.

Sectoral business sentiment indexes showed a significant broad-based rise, advancing above the readings seen in the previous two months – the ones that had suggested the economy was already slowing down. Consumer sentiment remained very positive.

Quote of the week

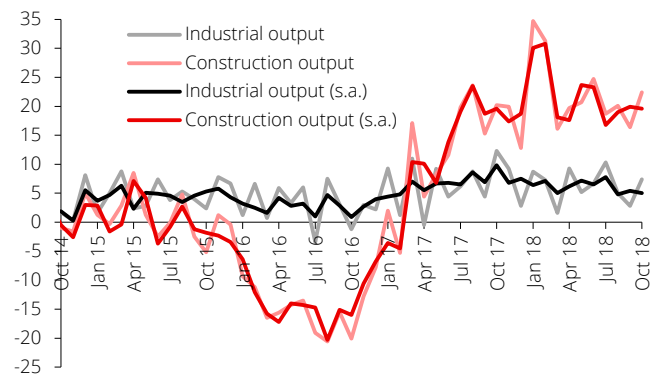
We assume that what the MPC needs to discuss rates hikes is inflation pushing above the target in line with NBP projection and staying there for longer than the MPC could tolerate. For some what the November projection showed was already unbearable and there was a failed motion to raise rates by 25bp. The hawkish minority stressed (in the minutes) that what should be watched now is whether the energy impulse to CPI coming next year pushes inflation up for longer, against the November projection which had no second round effects included. However, in general, the consensus view of the MPC has not changed. We think rates could go up in late 2019 at the earliest.

Investment growth, %/y



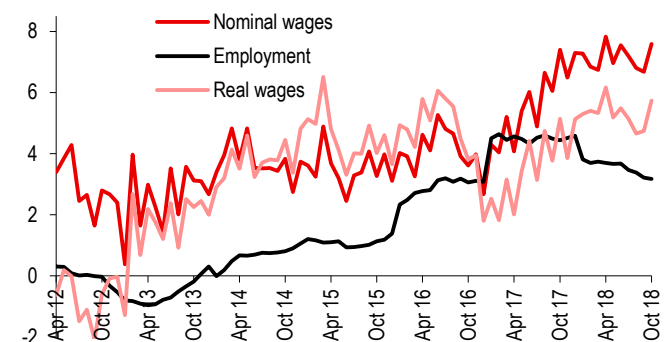
Source: GUS, Santander Bank Polska

Output growth in Poland



Source: GUS, Santander Bank Polska

Corporate sector data, %/y



Source: GUS, Santander Bank Polska

Rafał Sura, MPC member, Bloomberg, 19 November

This situation does not require from the MPC any automatic move as we need to see first if those barely outlined trends will become entrenched.

Jerzy Żyżyński, MPC member, Bloomberg, 21 November

The outlook for Polish inflation supports a prolongation of the period of stable interest rates. Raising rates in response to inflation pickup coming from energy and fuel prices would be ineffective and would harm the economy.

November MPC meeting minutes, NBP, 22 November

An argument was raised that the upward revision of the inflation forecast for the coming year, increasing the risk of inflation running above 2.5% in the longer term, spoke in favour of a rise in interest rates at the current meeting. In the opinion of [some] Council members, an assessment of the rationale for raising interest rates should, in particular, include the scale and persistence of the transmission of higher energy prices on the growth of other prices and inflation expectations.

FX and FI market

Last week on the market

FX Only at the beginning of the week the zloty was still under pressure of market concerns about liquidity of some small Polish banks. Later, as the top state and central bank officials said they are ready to help if needed, EURPLN returned to 4.30 from 4.34. EURUSD was on the rise for the better part of the week also helping the zloty to recover despite poor global market sentiment. There was no outright market reaction to the information that a rate hike motion was filled at the MPC November meeting. GBPPLN remained stable around 4.85 after it had fallen from 4.93 in the previous week. CHFPLN recorded only a temporary rise to 3.82 from 3.78.

FI Polish bond yields and IRS are likely to end the week slightly below levels seen last Friday. Debt recovered after the weekend as the NBP calmed investors fearing about the liquidity situation of some small banks. In mid-week the yields down move stopped and a correction was seen after the surprising information about a rate hike motion at the MPC last meeting.

Key events

The EU summit will be held this Sunday when the UK-EU Withdrawal Agreement is to be signed. This should be a non-event if everything goes well but the Brexit tensions are far from over since the British parliament needs to approve the Agreement. The governments faces tough fight to win votes needed to form a majority.

At the end of the month, the stat office will publish detailed 3Q GDP data and we shall see what caused the flash reading coming out well above the consensus. We will also see flash November CPI.

On Thursday, the Ministry of Finance will hold a bond auction.

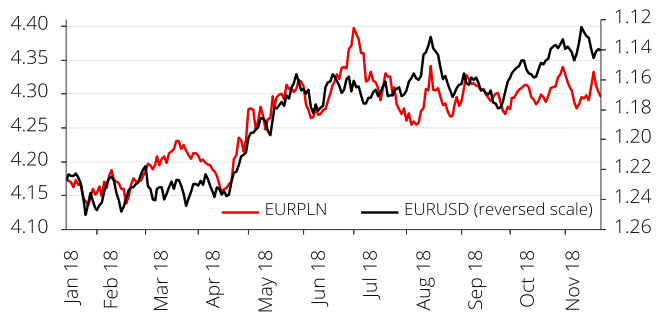
Globally, market attention should focus on the German and US data. Recent days saw some FOMC members suggesting that in 2019 there could be less rate hikes than expected so far and perhaps the minutes from the last meeting will reflect some concerns about the economic outlook after the last subdued macro readings.

Market implications

FX We think that the coming week will be yet another with EURPLN holding within the 4.26-4.34 range observed since August. Correlation with EURUSD looks to be still meaningful and the number of the data due to be released abroad could play the main role on the Polish FX market. The upward move of EURUSD started in mid-November is the biggest rise in the downtrend observed since mid-September which may indicate the euro could continue to gain vs the dollar in the coming weeks. This trend could gain steam if the recent reserved FOMC members' comments are followed by the below-consensus US data. Higher EURUSD would allow EURPLN to near the 4.26 support level.

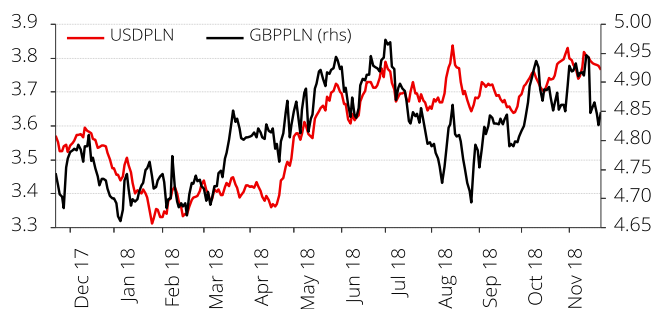
FI We believe that the impact of the information about the rate hike attempt on the Polish bonds/IRS will likely be short lived and the trends on the core markets should be key. The recent data (like euro zone flash November PMIs) disappointed which pushed Bund yields down. Also, the recent cautious comments of the FOMC members may allow core debt gains. We think Polish yields/IRS could fall in the coming days but the bond spread vs Bunds could widen as the outlook for the bond auction could curb gains of the domestic debt. At the same time, the 2Y bonds might benefit from the low CPI reading.

EURPLN and EURUSD



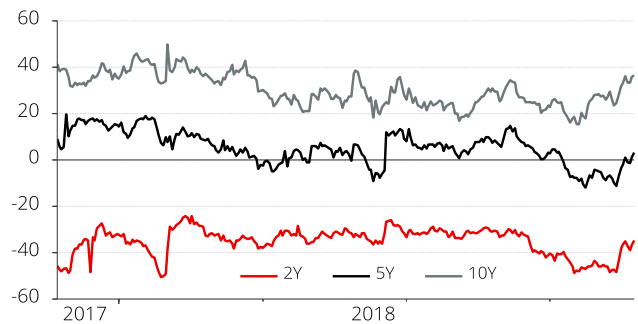
Source: Thomson Reuters Datastream, Santander Bank Polska

USDPLN and GBPPLN



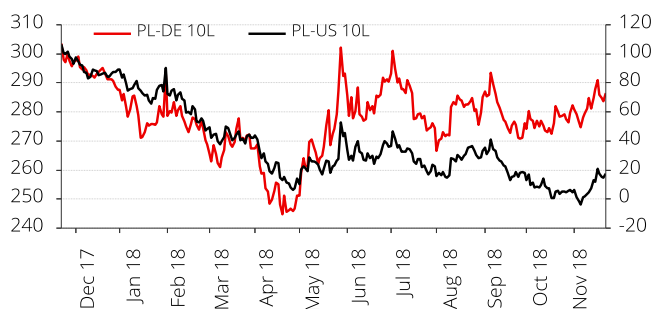
Source: Thomson Reuters Datastream, Santander Bank Polska

Asset swap spreads



Source: Thomson Reuters Datastream, Santander Bank Polska

10Y bond yield spreads



Source: Thomson Reuters Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD	FORECAST			LAST
				MARKET	SANTANDER	VALUE	
MONDAY (26 November)							
10:00	PL	Unemployment Rate	Oct	%	-	5.7	5.7
10:00	DE	IFO Business Climate	Nov	pts	102.5	-	102.8
TUESDAY (27 November)							
16:00	US	Consumer Conference Board	Nov	pts	136.2	-	137.9
WEDNESDAY (28 November)							
14:30	US	GDP Annualized	3Q	% Q/Q	3.6	-	3.5
16:00	US	New Home Sales	Oct	% m/m	5.3	-	-5.5
THURSDAY (29 November)							
11:00	EZ	ESI	Nov	pct.	-	-	109.8
14:00	DE	HICP	Nov	% m/m	-	-	0.1
14:30	US	Initial Jobless Claims	week	k	215	-	216
14:30	US	Personal Spending	Oct	% m/m	0.4	-	0.4
14:30	US	Personal Income	Oct	% m/m	0.4	-	0.2
14:30	US	PCE Deflator SA	Oct	% m/m	0.2	-	0.1
16:00	US	Pending Home Sales	Oct	% m/m	1.0	-	0.5
20:00	US	FOMC Meeting Minutes					
FRIDAY (30 November)							
09:00	CZ	GDP SA	3Q	% y/y	-	-	2.3
10:00	PL	Flash CPI	Nov	% y/y	1.5	1.5	1.8
10:00	PL	GDP	3Q	% y/y	5.1	5.1	5.1
11:00	EZ	Flash HICP	Nov	% y/y	-	-	2.2
11:00	EZ	Unemployment Rate	Oct	%	-	-	8.1

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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