Bank Zachodni WBK
Grupa Santander

WEEKLY ECONOMIC UPDATE

21 – 27 May 2018

Global market has been pretty volatile ion the course of the past week. Rising oil prices spurred concerns about faster monetary policy normalization which boosted the dollar, hit the EM currencies and pushed bond yields up. In Poland, flash 1Q GDP surprised to the upside adding pressure on bonds and failing to support the zloty. The MPC rhetoric remained dovish and did not trigger any material investors' reaction.

This week, we will see Polish economic activity data. We are expecting positive data from industry in April, after weak results in March. However, this will be mostly thanks to statistical base effect and our estimates are below consensus for industrial output and only a fraction above for retail sales. The zloty did not gain after the strong 1Q flash estimate and we think this means it could actually not respond positively to this week's macro releases. As far as bonds are concerned, we expect yields might move slightly down amid macro data releases. Globally, we will see numerous European and US data, especially flash PMI as well as GDP data, and many central bankers will deliver their speeches.

Economic calendar

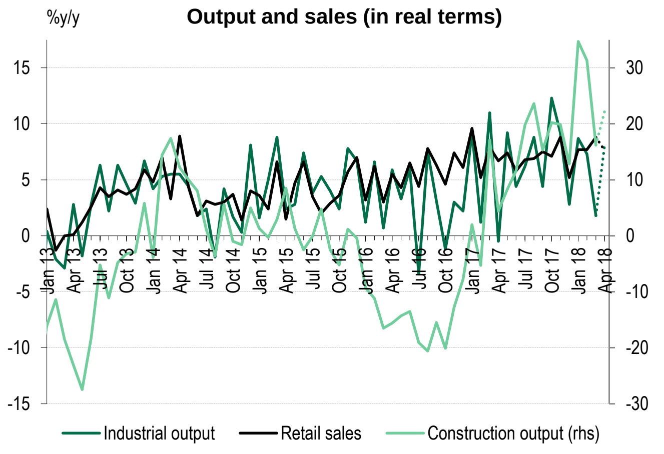
TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST BZWBK	LAST VALUE
		MONDAY (21 May)					
10:00	**PL**	**Sold Industrial Output**	**Apr**	**% y/y**	**8.5**	**8.1**	**1.8**
10:00	**PL**	**Construction Output**	**Apr**	**% y/y**	**24.5**	**22.2**	**16.2**
10:00	**PL**	**PPI**	**Apr**	**% y/y**	**0.9**	**1.0**	**0.3**
		TUESDAY (22 May)					
14:00	HU	Central Bank Rate Decision		%	0.90		0.90
		WEDNESDAY (23 May)					
09:30	DE	Flash Germany Manufacturing PMI	May	pts	-	-	58.1
09:30	DE	Flash Markit Germany Services PMI	May	pts	-	-	53.0
10:00	EZ	Flash Eurozone Manufacturing PMI	May	pts	-	-	56.2
10:00	EZ	Flash Eurozone Services PMI	May	pts	-	-	54.7
10:00	**PL**	**Retail Sales Real**	**Apr**	**% y/y**	**7.5**	**7.6**	**8.8**
16:00	US	New Home Sales	Apr	% m/m	-2.0	-	4.0
20:00	US	FOMC Meeting Minutes					
		THURSDAY (24 May)					
08:00	DE	GDP WDA	1Q	% y/y	2.4	-	2.3
11:30	**PL**	**Bond auction**					
14:00	**PL**	**Money Supply M3**	**Apr**	**% y/y**	**-**	**5.9**	**5.8**
14:30	US	Initial Jobless Claims	week	k	215	-	211
16:00	US	Existing Home Sales	Apr	% m/m	-0.5	-	1.1
		FRIDAY (25 May)					
10:00	DE	IFO Business Climate	May	pts	-	-	102.1
10:00	**PL**	**Unemployment Rate**	**Apr**	**%**	**6.3**	**6.3**	**6.6**
14:30	US	Durable Goods Orders	Apr	% m/m	-1.5	-	2.6
16:00	US	Michigan index	May	pts	98.8	-	98.8

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

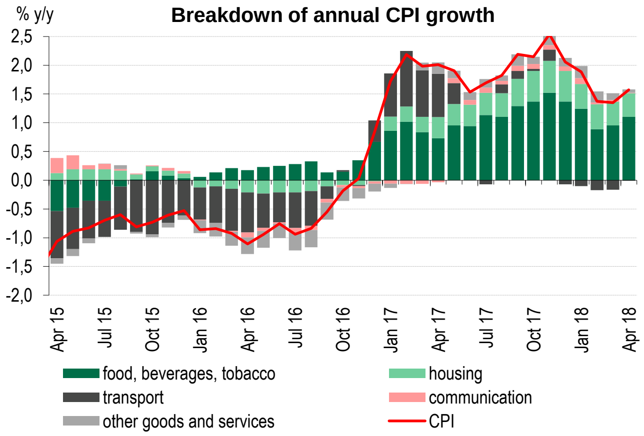
TREASURY SERVICES:
Poznań +48 61 856 5814/30
Warszawa +48 22 586 8320/38
Wrocław +48 71 369 9400

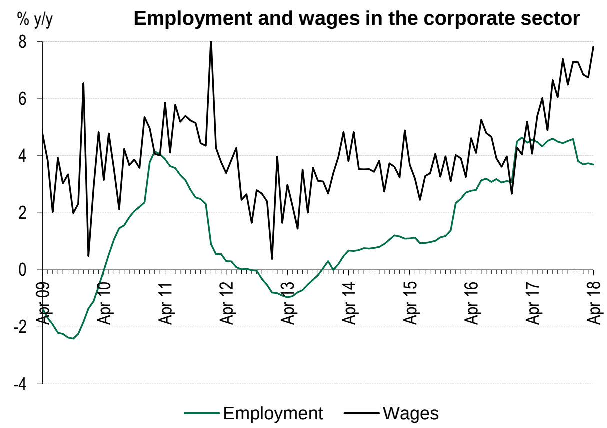
What's hot next week – Important data from real economy



▪ We are expecting positive data from industry in April, after weak results in March. However, this will be mostly thanks to statistical base effect, given that April 2017 was a month with Easter and one working day less. In the following months, we are expecting the industry to slow down to 5% y/y on average, given weaker demand from the euro zone.
▪ Construction is likely to show a 20+ result. This sector is operating at high growth rates, partially thanks to low base effect, but more and more companies report there are cutting their sales and backlog growth as they are approaching their capacity limits.
▪ Retail sales for April will be an interesting reading, given high base effect of Easter in April 2017 and only one trading Sundays. We are expecting some slowdown versus March, but are generally more optimistic than the market.
▪ We are expecting Statistics Poland to confirm April unemployment rate at 6.3%, in line with the data from the Labour Ministry.

Last week in economy – GDP and wages beat expectations





▪ The flash release showed GDP growth at 5.1% y/y vs 4.9% in 4Q17, while a slowdown was expected by the market and our forecast was 4.9% y/y. We think the economy will gradually decelerate in the rest of the year, with 2Q around 4.5% y/y.
▪ CPI in April was confirmed, growing from 1.3% to 1.6% y/y/ CPI went up mostly due to higher prices of fuels and food. Core CPI inflation ex food and energy decreased in April from 0.7% to 0.6% y/y, while the Eurostat measure HICP excluding food, energy, alcohol and tobacco, went from -0.1% y/y to -0.2%. In our view, the decrease of core inflation came from lower price changes of car insurance, airline fares and broadcasting services. We think that core inflation will accelerate above 1.5% y/y this year. CPI may temporarily surpass 2.0% in mid-2018, but will retreat below this level at the end of the year.
▪ Current account in March showed a deficit of €1.0bn. Exports fell by 2% y/y, driven by negative working day effect and by decelerating exports of cars. Import rose by 1.6% y/y with increasing fuel purchases and a purchase of an airplane. In our view, there is a downward risk for exports in the upcoming months in the light of weaker signals from the euro zone, while imports will remain strong driven by robust domestic demand. Net exports contribution was most likely negligible in 1Q, but in the following quarters it might turn slightly negative.
▪ Wage growth surprised to the upside in April, rising by 7.8% y/y vs our expectations at 7.4% y/y and market consensus at 7.2% y/y. In our view, wage growth was underpinned by positive working day effect and pay rises in mining. We gather that a further acceleration of wages is possible. Employment growth was flat at 3.7% y/y, in line with expectations. Wage bill rose by 10.0% y/y in real terms, the fastest pace since 2008. Strong growth of disposable income will warrant strong growth of private consumption (near 5% y/y).

Quote of the week – No reasons to change rates, maybe even in 2020

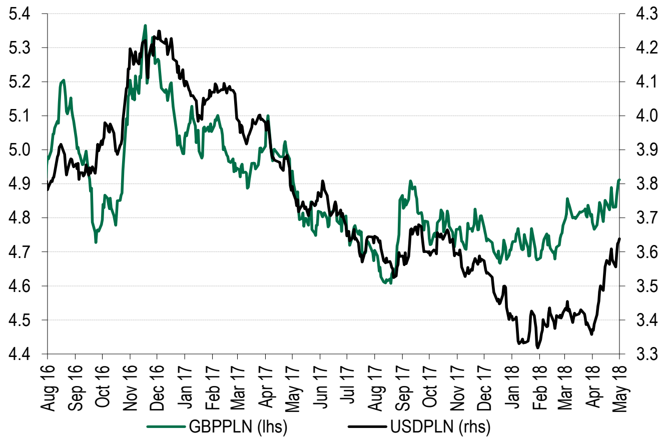
Adam Glapiński, NBP governor, MPC press conference, May 16
I am almost sure this year and next there will be no reason to change rates, maybe even longer, I think about 2020 (…) I am talking about the dominating view inside the Council and my own. (…) High growth, but inflation is absent, wage pressure is absent (…) wage growth decreased.
Jerzy Osiatyński, MPC member, MPC press conference, May 16
We wish there was no tightening [into 2020] but this is a long time frame. Wage pressure exists.
Kamil Zubelewicz, MPC member, MPC press conference, May 16
For the majority of MPC rates stability is a value, so the probability of rate changes is low. I assume that with the current knowledge rates will be stable even beyond 2019.

The MPC kept rates on hold, with no significant changes in the statement. The Council still sees the current rates level as adequate, given the economic outlook, promoting macroeconomic stability and return of inflation to the 2.5% target. In the statement a hope is expressed that slowdown in the euro zone in 1Q is temporary. During the press conference, governor Adam Glapiński extended his claim that rates will most likely stay unchanged through 2018 and 2019, also to cover 2020, based on his intuition. MPC hawk Kamil Zubelewicz admitted it is possible, albeit absolutely against his view. Jerzy Osiatyński also in general did not question the governor's opinion on how long rates could stay intact. Adam Glapiński also stated that wage growth surprises to the downside and there is no wage pressure, but his words were quickly falsified. We still assume that inflation processes and wage pressure will intensify this year, but rates will stay flat until late 2019.

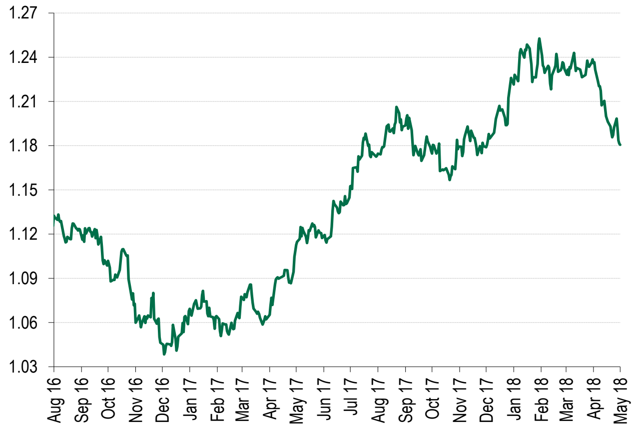
Foreign exchange market – Zloty still under pressure

EURPLN

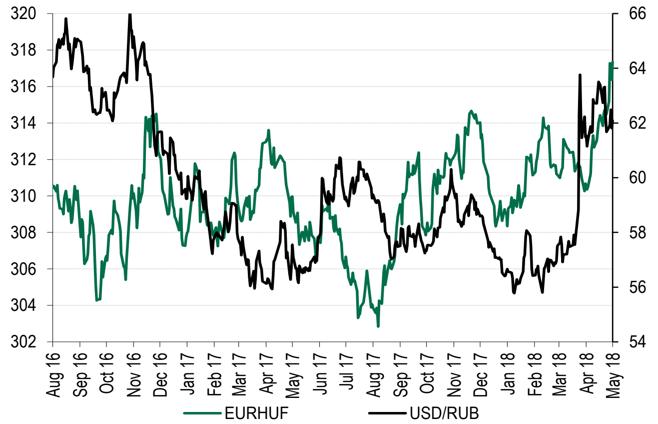
USDPLN I GBPPLN



EURUSD



EURHUF and USDRUB



Global factors hit zloty

- Last week, the zloty extended losses vs main currencies as the dollar resumed its appreciation trend and oil prices jumped making the market pricing in faster monetary policy normalization by the global central banks. Poland flash 1Q18 GDP estimate surprised to the upside but failed to boost the zloty. As a result, EURPLN, USDPLN and GBPPLN reached fresh 2018 peaks at c4.30, c3.65 and 4.92, respectively. Since last Friday, nearly all EM currencies depreciated vs the dollar and half of them vs the euro. The zloty was one of the weakest of them and in Europe only the Turkish lira performed worse than the zloty.
- This week, we will see Polish economic activity data. In our view, industrial output might disappoint while our estimate for retail sales is only a fraction above the consensus. The zloty did not gain after the strong 1Q flash estimate and we think this means it could actually not respond positively to this week's macro releases.
- Globally, we will see numerous European and US data and many central bankers will deliver their speeches. The recent rise in oil price has turned the market attention to the monetary policy issues and if the upcoming events push the balance towards the hawkish side, the zloty may remain under pressure.
- According to Reuters, this week is the fifth in the row of PLN weakening. Such a long streak was recorded last time in mid-2017 and, earlier, in mid-2012. According to this data, since 1993, EURPLN has never gone up for more than 7 weeks in a row. In our view, short-term chance for a more persistent zloty strengthening (below 4.23 per euro) is very little. At the same time, we do not expect EURPLN to rise much above 4.30.

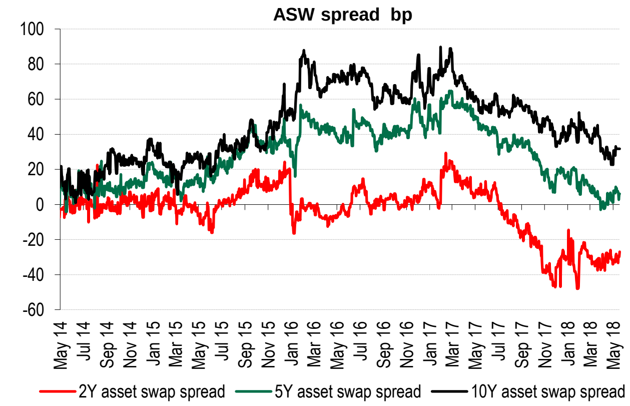
Italy weighs on euro

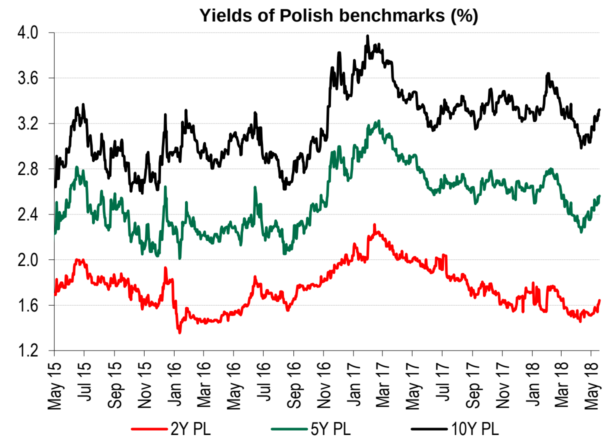
- Dollar appreciation resumed amid rising oil prices, decent US data and political uncertainty related to the situation in Italy. As a result, EURUSD fell for the fifth week in a row, reaching fresh 2018 low at c1.175. Such a long streak was last time observed at the turn of 2014 and 2015.
- We still think the dollar could remain strong in the short term. The most recent signals from Italy were not too encouraging (potential coalition parties question the EU budget rules and said that plan to ask the ECB to forgive Italy €250bn of debt) likely limiting the room for stronger euro. At the same time, we think the flash PMIs could be positively received by the market preventing EURUSD from falling below 1.17.

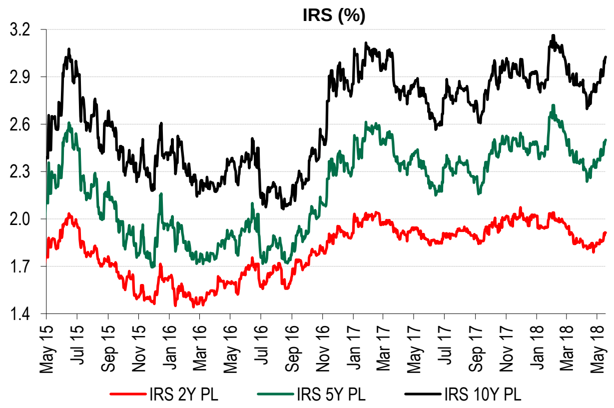
Strong ruble, forint under pressure

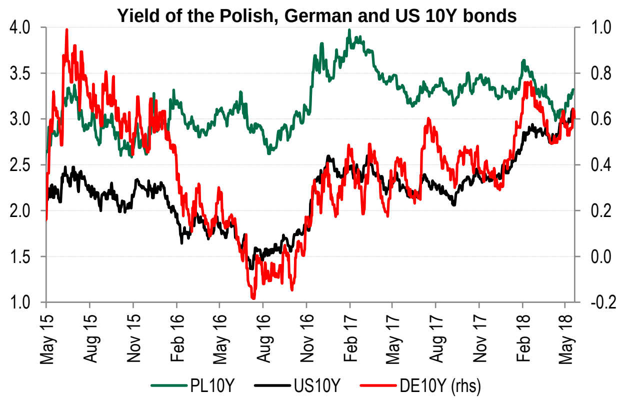
- Among the other CEE currencies, Hungarian forint performed the worst despite better-than-expected flash 1Q GDP reading with EURHUF rising to c318 from 315, to its highest since mid-2016. EURCZK and USDRUB stayed in the ranges set in the previous weeks, and the room for weaker ruble was limited by rising oil prices.
- This week, Hungarian central bank will decide on the interest rates. Recent macro data was mixed: robust 1Q GDP but poor April PMI and industrial output. The forint is under strong negative pressure and this might encourage the central bank to adopt a somewhat less dovish stance to stabilize the currency, in our view.

Interest rate market – Bond prices melted by high oil prices









GDP and US readings negatively affected domestic sovereign bonds

- Last week we observed progressing decreasing on the core bond markets and domestic sovereign bonds market. As a consequence, the Polish bonds yield curve was shifted up by 6-8 bp, while the IRS by 5-10 bp. In both cases, the stronger move was visible on the long end of the curves. The scale of the move of the domestic yield curve was comparable to the Bund curve move and significantly less than the US curve. The changes were fueled by stronger US retail sales data (an upward revision of March reading) and the hawkish sound of ECB member remarks. On the domestic front, the unexpectedly high reading of 1Q18 GDP pressured the yield curve up. This effect could not be offset by the dovish tone of MPC conferences. As usual, the rising oil prices negatively affected sovereign bonds.

PMI and industrial/retail sales in the spotlight

- The next week will be dominated by key domestic (industrial production and retail sales) and PMI Euro-zone indices data release. We think that the solid yields increases observed last time were mainly driven by central bankers' statements and remarks, who presented a positive assessment of European economy. We believe if this week data releases confirm the central bankers' view, the investors will decide to take profit. In our opinion, the bond market will be sensitive mainly to the Euro-zone PMI – manufacturing and -services data releases (scheduled for Wednesday). We think that PMI reading will be close or slightly lower than March's readings, which is likely lead to the profit-taking and yields slide. We think that weakening of euro, which we witnessed over the last 4-6 weeks will positively influence PMI- new orders component (the strong Euro was blamed for the weaker new orders in the PMI reports from the turn of quarters). Moreover, we believe that rebound visible in some ESI-manufacturing components (production expectations) and slower pace of decreases of assessment of stocks of finished products will be reflected in the inhibition of PMI declines. We believe that rebound of ESI retail sales business activity assessment will help to stabilise the next PMI readings.
- We expect the neutral influence of domestic data release (industrial production and retail sales) on the domestic bond market. In our opinion, the main readings will be well above or (industrial production) and slightly below (retail sales) March readings. However, the seasonally adjusted forecasts show slow subduing of the pace of growth in the both of these categories. Moreover, we believe that Fed members speeches (announced for the next week) will not affect negatively US sovereign bonds, which will potentially help to stabilized domestic market. The element of risk is still the prices of crude oil, which in the case of continuation of upward trend may temporarily negatively affect domestic debt.

Regular auction

- At the auction planned for 24 May, we expect a supply at the level of upper limit of the range announced by the MF (PLN 3-6bn). We think that the demand for both OK0720 and WZ0524 among the offered OK0720, PS0123, WZ0524, WS0428, WZ0528. We expect lower demand for fixing-coupon bonds WS0428.

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