

1 August 2019

Eyeopener

Markets not satisfied with FOMC rhetoric

Fed cut rates by 25bp but did not signal more easing
 July inflation beat forecasts, PMI down
 Zloty supported by CPI, but hit by FOMC decision
 Today PMIs from Europe

On Wednesday the trade on global markets was rather calm, as investors were holding breath ahead of the evening Fed decision. As we assumed and wrote in our newest *MACROscope*, investor expectations about the FOMC's dovishness were exaggerated. Fed funds rate went down by 25bps with two FOMC members voting against, while some market players were betting for a 50bps cut. The market enthusiasm was also muted by comments of Jerome Powell, who said that the cut is only a mid-term adjustment in the cycle, a form of risk management. Further cuts were not ruled out, but there was no clear suggestion that an easing cycle is starting. These events supported the dollar, undermined the stock markets and US bonds.

Flash estimate of Polish CPI for July showed a much stronger reading than expected: 2.9% y/y vs 2.6% market consensus and our 2.7% call. The rise of inflation from 2.6% was caused mainly by food price inflation pushing to 6.8% y/y (the highest since mid-2011) and by +0.3% m/m (the last time m/m food inflation was positive in July was in 2000). Fuel prices also surprised us to the upside in the flash reading by dropping less m/m than we estimated. As a result, our estimate of core CPI points to 2.1% y/y in July vs 1.9% in June. The internal pressure due to strong domestic demand should push it even further up, to significantly above 2.5% by the end of the year. Headline CPI should reach (or even breach) 3% y/y in December and if household electricity prices are freed next year it would go above 4% y/y in January. We think such path will make MPC hawks feel uncomfortable, but we do not expect them to build a majority for rate hikes this year or next.

High CPI encouraged **numerous MPC members** to speak. Jerzy Osiatyński said that inflation growth is worrying and it may reach 3.5% y/y soon. According to him, the MPC was not expecting CPI to go that high and it should react if this rise proves persistent. Łukasz Hardt stated there is a rising probability that inflation will run above the July projection. He also reiterated his opinion that a rate hike may be necessary at the end of 2019. Eugeniusz Gatnar expressed a similar opinion: if inflation and core inflation go further up, the MPC should react in the autumn. Kamil Zubelewicz restated that interest rates in Poland should already be going up, but he is not expecting the MPC to hike rates in this term. On the other hand Rafał Sura said that CPI running slightly above the projection is not enough to change the MPC bias. Today Adam Glapiński wrote in a column for *Rzeczpospolita* daily that the MPC should react flexibly to shocks, even if inflation exits the tolerance band around the target, adjusting to the reason and persistence of the shock, and taking into account the long-term consequences of its decision on the macroeconomic and financial stability. This shows that the NBP president feels very comfortable with keeping rates on hold. In our view, the rising inflation will be a major support for the hawkish faction and it is possible that a vote for hikes will come in late 2019. We still think however, that the majority led by Governor Glapiński will keep rates unchanged. Monetary easing by main central banks is actually a strong argument against cuts.

According to **flash estimates of agricultural output**, this year the output of root vegetables will fall by 9% y/y (mind that last year's output was historically low due to drought), output of fruit from trees decreased by 25% y/y and output of berries by 20% y/y. Lower supply of vegetables and fruit will be supporting price growth in these categories in 2019.

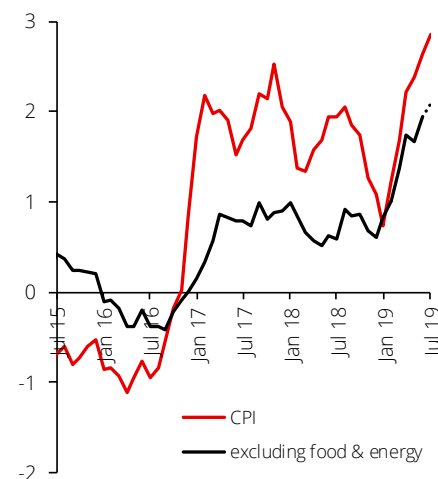
Polish manufacturing PMI disappointed by dropping more than expected in July, to 47.4 pts, due to the employment index. New orders indexes remained below 50 pts signalling that domestic and foreign demand is shrinking. The purchasing activity component was the lowest in six years.

EURPLN started the day slightly below 4.30, but started to move down after the CPI release, and at the end of local trading hours the pair was just below 4.29. EURHUF fell to 326.2 from 327.5 at the opening, EURCZK was quite stable at c25.65 and the ruble was losing somewhat (USDRUB up to 63.5 from 63.4). After the FOMC decision, CEE fx weakened sharply vs the dollar (USDPLN jumped from 3.85 to 3.88 and this morning is seen close to 3.89) and much less vs the euro. Today their losses may continue.

Yesterday **EURUSD** was consolidating slightly below 1.115. At the end of the day the dollar gained, pushing the pair down to 1.113. The Fed decision quickly sent the exchange rate below 1.11 and this morning it is at 1.104. Today's PMI indices are unlikely to support the euro so we see a risk of further decline in EURUSD.

The **domestic interest rate market** rebounded yesterday after recent rises in yields. On the longer end of the curve yields fell by about 2bps, while the shorter end was stable. The disappointment about FOMC has put upside pressure on domestic yields, a response is already seen on the core markets. The Finance Ministry informed that it financed 83% of borrowing needs at the end of 2019. There is one switch auction planned for August (08.08). 3Q19 the Ministry want to offer debt worth PLN13bn in total.

Inflation, %/y



Source: GUS, NBP, Santander

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FX market

Today's opening

EURPLN	4.2916	CZKPLN	0.1669
USDPLN	3.8858	HUFPLN*	1.3148
EURUSD	1.1044	RUBPLN	0.0609
CHFPLN	3.8993	NOKPLN	0.4378
GBPPLN	4.7076	DKKPLN	0.5747
USDCNY	6.8989	SEKPLN	0.4015

*for 100HUF

Last session in the FX market 31/07/2019

	min	max	open	close	fixing
EURPLN	4.284	4.299	4.298	4.286	4.2911
USDPLN	3.847	3.856	3.854	3.851	3.8504
EURUSD	1.112	1.116	1.115	1.113	-

Interest rate market 31/07/2019

T-bonds on the interbank market**

Benchmark (term)	%	Change (bps)	Last auction	per offer	Average yield
PS0721 (2L)	1.53	0	21 mar 19	OK0521	1.633
PS1024 (5L)	1.88	-2	21 mar 19	PS0424	2.209
DS1029 (10L)	2.17	-2	21 mar 19	DS1029	2.877

IRS on the interbank market**

Rates on the interbank market						
Term	PL		US		EZ	
	%	Change (bps)	%	Change (bps)	%	Change (bps)
1L	1.72	1	2.05	-2	-0.42	-1
2L	1.76	1	1.86	-3	-0.45	-2
3L	1.76	1	1.79	-3	-0.44	-2
4L	1.79	0	1.77	-3	-0.40	-2
5L	1.82	0	1.78	-3	-0.34	-3
8L	1.95	0	1.87	-4	-0.14	-4
10L	2.02	-1	1.94	-4	0.01	-4

WIBOR rates

Term	%	Change (bps)
O/N	1.52	-3
T/N	1.55	0
SW	1.57	-1
2W	1.60	0
1M	1.64	0
3M	1.72	0
6M	1.79	0
9M	1.81	0
1Y	1.86	0

FRA rates on the interbank market**

Term	%	Change (bps)
1x4	1.72	0
3x6	1.72	1
6x9	1.72	1
9x12	1.70	1
3x9	1.78	0
6x12	1.78	1

Measures of fiscal risk

Measures of financial risk				
Country	CDS 5Y USD		10Y spread*	
	Level	Change (bps)	Level	Change (bps)
Poland			2.60	-3
France	21	0	0.26	0
Hungary			2.72	1
Spain	41	-1	0.74	1
Italy	165	3	2.00	2
Portugal	42	0	0.80	1
Ireland	31	-1	0.53	0
Germany	11	-1	-	-

* 10Y treasury bonds over 10Y Bunds

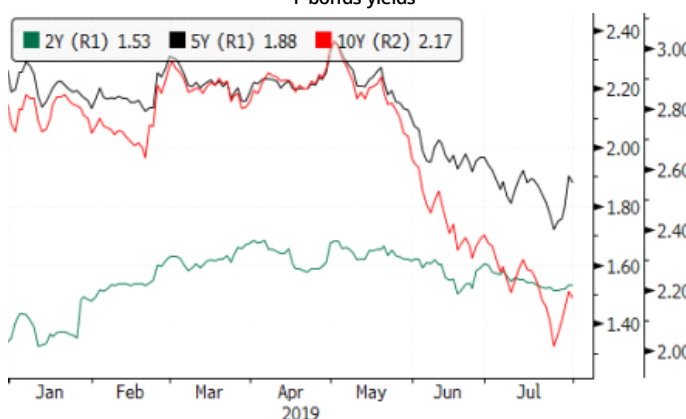
**Information shows bid levels on the interbank market at the end of the trading day

Source: Bloomberg

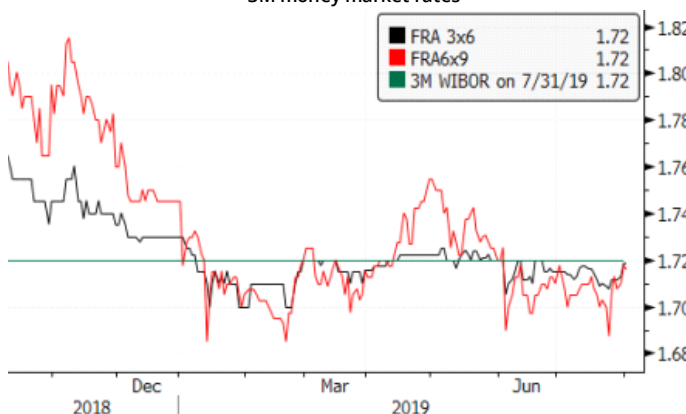
Zloty exchange rate



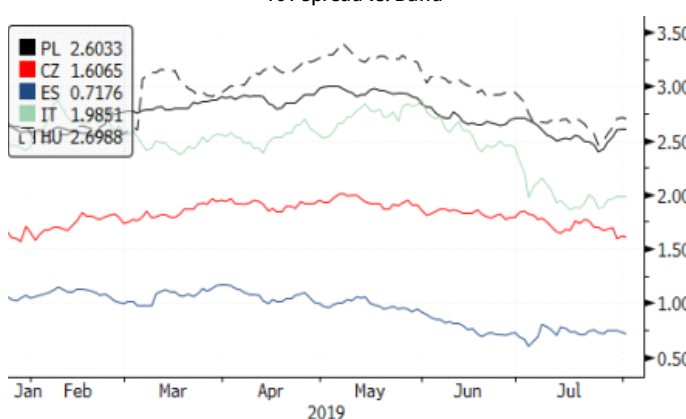
T-bonds yields



3M money market rates



10Y spread vs. Bund



Economic Calendar

Economic calendar								
TIME	COUNTRY	INDICATOR	PERIOD	FORECAST		ACTUAL	LAST	
CET				MARKET	SANTANDER	VALUE	VALUE*	
FRIDAY (26 July)								
14:30	US	GDP Annualized	2Q	% Q/Q	1.8	-	2.1	3.1
MONDAY (29 July)								
No important data releases								
TUESDAY (30 July)								
11:00	EZ	ESI	Jul	pct.	103.0	-	102.7	103.3
14:00	DE	HICP	Jul	% m/m	0.3	-	0.5	0.3
14:30	US	Personal Spending	Jun	% m/m	0.3	-	0.3	0.5
14:30	US	Personal Income	Jun	% m/m	0.3	-	0.4	0.4
14:30	US	PCE Deflator SA	Jun	% m/m	0.1	-	0.1	0.1
16:00	US	Consumer Conference Board	Jul	pts	125.0	-	235.7	124.3
16:00	US	Pending Home Sales	Jun	% m/m	0.4	-	2.8	1.1
WEDNESDAY (31 July)								
10:00	PL	Flash CPI	Jul	% y/y	2.6	2.7	2.9	2.6
11:00	EZ	Flash HICP	Jul	% y/y	1.15	-	1.1	1.2
11:00	EZ	GDP SA	2Q	% y/y	1.0	-	1.1	1.2
11:00	EZ	Unemployment Rate	Jun	%	7.5	-	7.5	7.5
14:15	US	ADP report	Jul	k	150	-	156	102
20:00	US	FOMC decision		%	2.00-2.25	-	2.00-2.25	2.50
THURSDAY (1 August)								
09:00	PL	Poland Manufacturing PMI	Jul	pts	48.0	48.8	47.4	48.4
09:55	DE	Germany Manufacturing PMI	Jul	pts	43.1	-		43.1
10:00	EZ	Eurozone Manufacturing PMI	Jul	pts	46.4	-		46.4
13:00	CZ	Central Bank Rate Decision		%	2.0	-		2.0
14:30	US	Initial Jobless Claims	week	k	218	-		206
16:00	US	ISM manufacturing	Jul	pts	52.0	-		51.7
FRIDAY (2 August)								
11:00	EZ	Retail Sales	Jun	% m/m	0.0	-		-0.3
14:30	US	Change in Nonfarm Payrolls	Jul	k	160	-		224
14:30	US	Unemployment Rate	Jul	%	3.7	-		3.7
16:00	US	Michigan index	Jul	pts	98.5	-		98.4
16:00	US	Durable Goods Orders	Jun	% m/m	0.7	-		2.0
16:00	US	Factory Orders	Jun	% m/m	0.6	-		-0.7

Source: Santander Bank Polska, Bloomberg, Parkiet

* in the case of a revision the data is updated

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