

31 October 2019

Weekly Economic Update

New projection, same conclusions

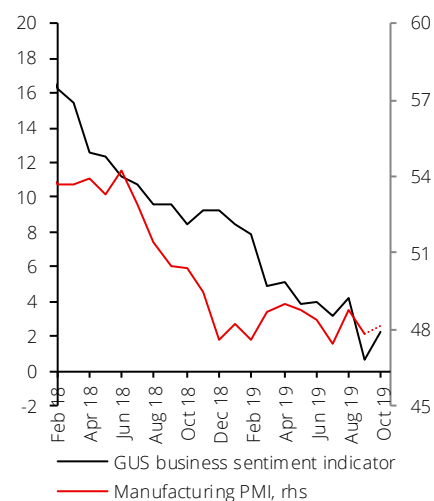
What's hot next week

- After the UK parliament has agreed for snap elections on December 12th, the Brexit issue will disappear from the radar for a while. In the coming week investors are likely to focus on a mix of statistical data from main economies, looking for hints about the global growth outlook. Any news regarding the US-China trade negotiations will be also important for sentiment.
- **MPC meets next week** and will analyse the updated NBP economic projection. Governor Adam Glapiński already signalled the new projection will be a tad higher for CPI (but not exceeding 3.5% i.e. the upper end of tolerance band) and a tad lower for GDP, and in his view should be no argument for rate changes in any of the directions. We guess that – by analogy to what was the case in November 2018 – the projection will assume that retail energy tariffs will not be frozen in 2020. So, the risks for the projection will be probably asymmetric to the downside. We think it is possible that ultra-dovish Eryk Łon will file a motion to cut interest rates again, for the third time in a row. But at the same time we do not rule out that the hawkish camp will propose a small policy tightening at November's meeting. Some MPC members (Gatnar, Hardt) suggested earlier they may back a rate hike by 15bp. Still, neither cuts nor hikes are likely to get majority support, so **interest rates are expected to remain unchanged**. The NBP governor is likely to reiterate his view that monetary policy parameters can stay unchanged until the end of the MPC term in early 2022.
- **Polish manufacturing PMI** might have gone a bit higher in October given the surprising stabilisation of business sentiment in German industry. Other indicators (by GUS and European Commission) showed the industry as positively standing out vs others sectors of the Polish economy when it comes to m/m behaviour of sentiment indexes.

Market implications

- EURPLN downtrend has been in the working for 5th week in a row now, a pretty rare occurrence. If history is any guide (and we think it is) we might expect at least some consolidation at the current levels in the 4.24 – 4.28 range as the market tries to test the important technical support and simultaneously awaits important news from the US-China trade talks. The dolar index might test the recent lows at 97.3 and if the level does not hold the next important level is at 96.0, 1.2% lower. This implies USDPLN might visit the mid-3.70s area before moving elsewhere.
- Polish 10Y bond yields are currently within a technical pattern called pennant meaning the consolidation is close to being over and we might expect a move either direction in the weeks to come. Economic activity data from Europe next week are surely going to help set the direction. We expect, however that given the length and size of the rally YTD, the more likely direction both in German yields and in Polish yields is higher and expect Polish 10Y yields to increase to 2.15% towards the end of the year.

Polish industry sentiment indicators



Source: Bloomberg, GUS, Santander

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Last week in economy

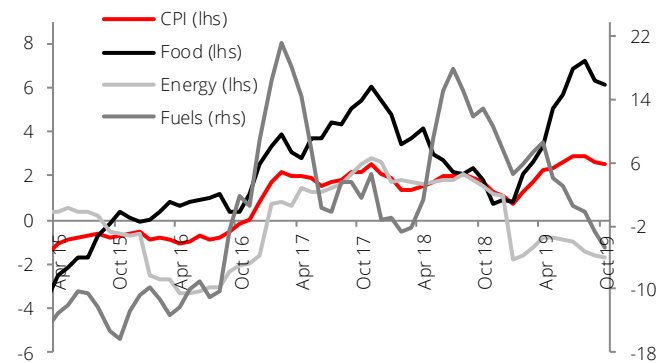
Inflation declined some more in October and so did economic sentiment indicators. Budget deficit remained tiny after September and the government has still not decided on issues like social security contributions' limit or extension of electricity price freeze for 2020.

According to flash estimate, Polish **CPI** went down again in October, to 2.5% y/y from 2.6% in line with our forecast. For the second time in a row the headline inflation decreased due to non-core elements. We estimate that the core inflation stayed at 2.4% y/y and expect it to climb to c3% y/y at the turn of the year. Decision on electricity prices will most likely determine if CPI stays below 4% y/y early next year (deputy energy minister said it is too early to declare further electricity price freeze). The data do not change the monetary policy outlook: interest rates in Poland are likely to remain on hold for long. More in the [economic comment](#).

European Commission's **ESI indicators for Poland** showed a deterioration in October. The main indicator dropped from 102.1 to 100.2, its lowest since December 2016, and was only slightly above the long-term average (99.8). The sub-indicators for services, construction, retail trade and consumer sector have decreased, while manufacturing improved slightly. Manufacturing indicator improved mainly due to better expectations regarding future prices and output, but at the same time companies' employment expectations kept falling (the index is already the lowest in 3.5 years). The index of consumer confidence has started deteriorating, following worse sentiment in other sectors. Consumers expressed less confidence in particular in future economic situation. They were also less eager to make major purchases and to save. This was accompanied by continued pessimism of the retail trade sector, the orders expectations of which are now at the lowest level in almost six years. The consumer confidence indicators by GUS published earlier also signalled some worsening in October. ESI indices herald further slowdown of economic growth in Poland in 4Q19.

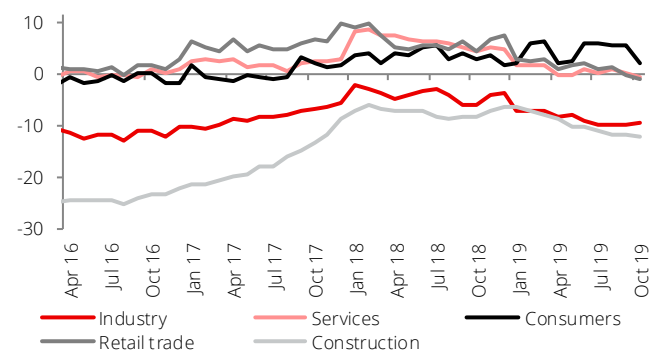
Year-to-date result of **central budget** amounted to -PLN1.8bn after September. September alone saw a surplus of PLN0.2bn. In January-September total revenues grew by 8.5% y/y (VAT +6.4% y/y, CIT +17.7% y/y, PIT +12.7% y/y) and spending by 10.4%. In our view, tax revenues are likely to grow at solid rates in the months to come (yet PIT will be under negative spell of lowered tax rates introduced in October) and spending will be reined in, so the year is likely to close with deficit markedly below PLN20bn.

CPI and non-core components, % y/y



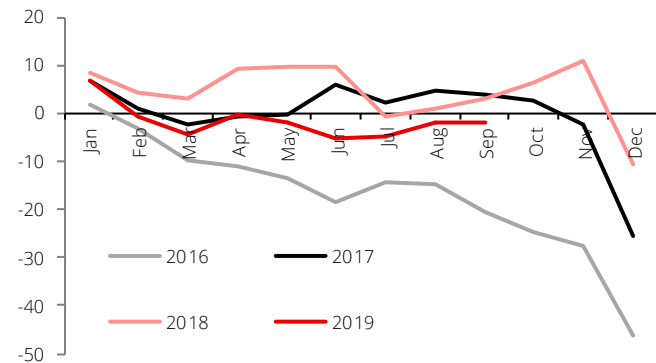
Source: GUS, Santander

ESI, sectoral sentiment indicators



Source: European Commission, Santander

Central budget performance, year-to-date, PLNbn



Source: Ministry of Finance, Santander

FX and FI market

Last week on the market

FX Having taken advantage of the positive global sentiment towards the risky assets including EM currencies, the zloty continued its appreciating trend and gained another 0.4% vs the euro (and the Swiss franc) in the passing week and a total of 3% in October. The rally offset almost all of the August sell-off. EURPLN closes the month on a 4.26 handle. Given the EURUSD rallied 0.7% w/w, the USDPLN fell even stronger, by 0.9% to 3.82. Only GBPPLN remained flat on the week, as GBPUUSD rallied after the risk of hard Brexit has been significantly diminished.

In the case of the other CEE currencies, the forint has not changed on the week at 329.6, the koruna gained 0.3% vs euro on CNB's Holub hawkish comments (discussions within CNB whether to pause or hike further). The Russian ruble has not changed in weekly terms (despite lower Brent oil by 1.3%), but has traded temporarily stronger after CBR cut rates 50 bp, more than expected, to 6.50% and the fixed income rally followed.

FI Polish bond yields fell for a second week in a row as the increase in core yields apparently have paused (and the German yield curve actually corrected lower) and thanks to soft preliminary CPI reading for October. Polish bonds 2Y yield fell to 1.46%, down 2bp, while 10Y to 1.98%, down 5bp. On the swap curve the 2Y has not changed w/w at 1.73%, while 10Y actually increased by 4bp to 1.80% helping narrow the 10Y asset swap spread to 17bp. The 10Y PL-DE yield spread widened from 235 to 238, up by 3bp.

Key events

With the prospect of hard Brexit on 31 October out of the way, and Fed having cut rates for the 3rd time this year, global markets' focus turns to the plausibility and the details of a potential US-China negotiations which touch on a wide range of topics from FX manipulation to intellectual property rights to market access to tariffs. While the negotiations progress (and are expected to conclude in H2 of November) markets will be particularly wary of tariffs-related news with events like further tariffs escalation on the one end or tariffs cuts on the other being the likely biggest potential market movers.

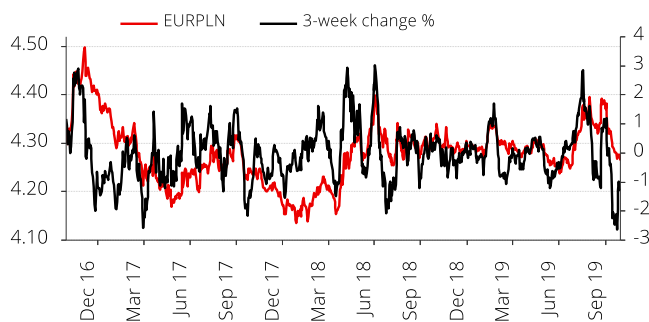
On 1 November Polish markets are closed for holidays and are likely to remain volatile given lower liquidity and important data from the US (NFP, ISM manufacturing). Next week markets will focus on the next round of PMIs in Asia, Europe (including in Poland, on Monday) and the US (ISM non-manufacturing on Tuesday). On Wednesday, in Poland there is the MPC rate decision (we expect no change to interest rates at 1.5%) and publication of CPI/GDP projection.

Market implications

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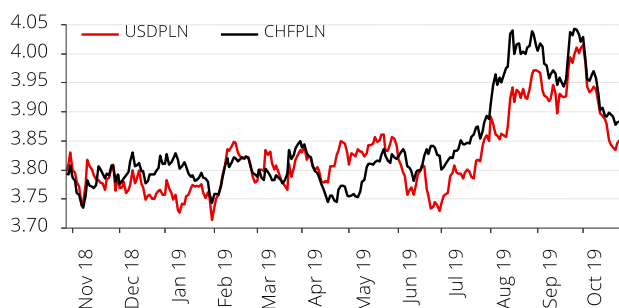
FI Polish 10Y bond yields are currently within a technical pattern called "the pennant" meaning the consolidation is close to being over and we might expect a move either direction in the weeks to come. Economic activity data from Europe next week are surely going to help set the direction. We expect, however, that given the length and size of the rally YTD, the more likely direction both in German yields and in Polish yields is higher and expect Polish 10Y yields to increase to 2.15% towards the end of the year.

EURPLN



Source: Refinitiv Datastream, Santander Bank Polska

USDPLN and CHFPLN



Source: Refinitiv Datastream, Santander Bank Polska

PLN IRS



Source: Refinitiv Datastream, Santander Bank Polska

10Y bond yield spreads (bp)



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST		LAST VALUE
					MARKET	SANTANDER	
FRIDAY (1 November)							
13:30	US	Change in Nonfarm Payrolls	Oct	k	85.0		136,0
13:30	US	Unemployment Rate	Oct	%	3.6		3.5
15:00	US	ISM manufacturing	Oct	pts	49.0		47.8
MONDAY (4 November)							
09:00	PL	Poland Manufacturing PMI	Oct	pts	48.1	48.1	47.8
09:55	DE	Germany Manufacturing PMI	Oct	pts	41.9		41.7
10:00	EZ	Eurozone Manufacturing PMI	Oct	pts	45.7		45.7
16:00	US	Durable Goods Orders	Sep	% m/m	-		-1.1
16:00	US	Factory Orders	Sep	% m/m	-0.5		-0.1
TUESDAY (5 November)							
02:45	CN	Caixin China PMI Services	Oct	pts	51.5		51.3
16:00	US	ISM services	Oct	pts	53.4		52.6
WEDNESDAY (6 November)							
	PL	MPC decision		%	1.50	1.50	1.50
08:00	DE	Factory Orders	Sep	% m/m	0.5		-0.6
09:00	CZ	Industrial Production	Sep	% y/y	4.6		-3.8
09:55	DE	Markit Germany Services PMI	Oct	pts	51.2		51.4
10:00	EZ	Eurozone Services PMI	Oct	pts	51.8		51.6
11:00	EZ	Retail Sales	Sep	% m/m	0.1		0.3
THURSDAY (7 November)							
08:00	DE	Industrial Production SA	Sep	% m/m	-0.5		0.3
13:00	CZ	Central Bank Rate Decision	Nov.19		2.00		2.00
FRIDAY (8 November)							
08:00	DE	Exports SA	Sep	% m/m	0.5		-1.5
09:00	HU	Industrial Production SA	Sep	% y/y	-		2.7
09:00	HU	CPI	Oct	% y/y	-		2.8
16:00	US	Michigan index	Nov	pts	96.0		95.5

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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