08 November 2019

Weekly Economic Update

Growth slowed down, but how much?

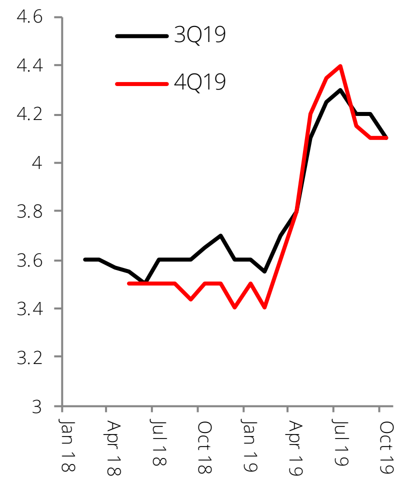
What's hot next week

- The coming trading week in Poland will be shorter owing to The Independence Day on Monday. However, some important events will take place later on. Abroad, we will see some macro data, including flash 3Q GDP estimates for the European countries that could help verify the global economic outlook. We expect that Germany avoided a recession with the quarterly pace of growth falling to zero. Also, speeches of some of the FOMC members – including Governor Powell – are scheduled.
- In Poland we will also see **flash 3Q GDP** (on Thursday). This release should not have any big market impact if the headline is in line with our forecast and market consensus (at 4.1% y/y). Unfortunately, recently some worrying signals emerged as regards the outlook for the economic growth and its components. Only to mention some of them, like signal from the central bank credit survey showing a sharp drop of the companies demand for the investment loans. In the previous years, this was an omen of a strong deceleration of investment outlays. GDP growth breakdown will be released in late November.
- On Wednesday the balance of payments numbers are due for release. **We are expecting a markedly wider current account balance** than the consensus and this could be PLN-negative. **Inflation data** will be overshadowed by other events, but should confirm that CPI slowed to 2.5% and core inflation steadied at 2.4% y/y The inflation peak is still ahead (1Q20), but this has already been priced-in.
- We will be able to learn more about inflation outlook on Tuesday morning, when the **Inflation Report** is presented. We already know, however, that temporarily higher inflation is not treated by the MPC as an argument to change monetary policy parameters.
- **The first meeting of the new parliament** is set for Tuesday. We will get to see whether PiS actually lost control over the Senate. After the weekend also the PM and his cabinet are likely to be sworn in.

Market implications

- Lack of the zloty's positive response to the obvious global mood improvement (amid hopes for the US-China trade deal) suggest there are minor chances for the EURPLN down move to resume in the short-term. Moreover, it seems that the global optimism could ease after the weekend for a while – the market has apparently priced in more positive news regarding the trade deal than justified, taking risk factors under consideration. The upcoming data would have to beat consensus noticeably to help optimism stay on the market. The data about big Poland C/A deficit will not help the zloty either. Bonds yields after having risen sharply in the last days make a small correction more plausible but overall the market shall hold in the "risk-on" mood which favours weaker debt.

Bloomberg consensus – GDP growth in 3Q and 4Q19



Source: Bloomberg, Santander

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Last week in economy

Data released last week confirmed the Polish economy is slowing down, with PMI index falling, banks tightening credit criteria and major institutions trimming their forecasts. Still, the MPC stance remained unchanged.

Polish PMI for manufacturing declined to 45.6pts from 47.8pts, while a rebound was widely expected. The index posted its biggest drop in 3.5 years and reached the lowest level since mid-2009. The fall was driven by all main subindices – new orders (12th decline in a row and the lowest reading since April 2009), output (12th decline in a row and the lowest reading since June 2009) and employment. Weaker sentiment was explained by slowing demand from Europe (export shrank for 15 months in a row, at the fastest pace since June 2009) and rising competition from China. Expectations about output fell to the lowest level in the history of the survey (2012). The data confirmed that the Polish economy was slowing down in 4Q19, but the pessimistic picture drawn by the PMI survey is in our view exaggerated and is giving guidance about the direction of the economy, not about the scale of the slowdown.

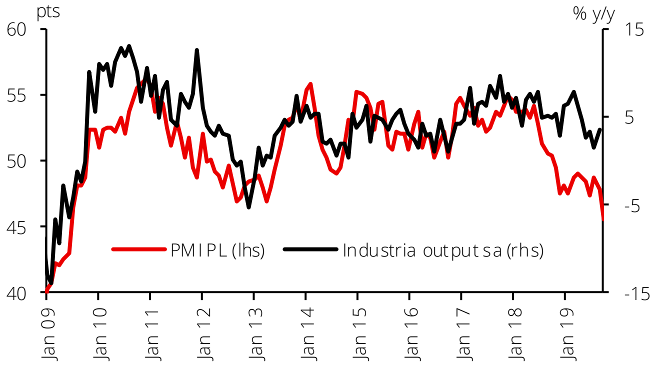
According to **the NBP credit survey**, in 3Q commercial banks tightened their SME, mortgage and consumer lending criteria. Banks intend to further tighten criteria in these areas in 4Q. As a reason for actions taken in 3Q in respect of SMEs, banks mentioned their capital situation and strong emphasis on the higher industry risk. As for both SMEs and consumer loans, the reason for tighter criteria was the deterioration of the loan book quality. In 3Q, the demand for loans to finance fixed investments, inventories and working capital fell markedly. Overall, the results of the survey spur concerns about the pace of investments growth but suggest the households are doing fine.

In the autumn forecasting round, **the European Commission lowered GDP forecast for Poland** for years 2019/2020 to 4.1%/3.3% from 4.4%/3.6%. Polish general government sector is expected to show a result of -1% GDP this year, -0.2% next year (improvement mostly due to the one-off transformation charge on households from open pension funds reform) and -0.9% in 2021. However, the EC based its calculations on what it found in the 2020 budget draft, which most likely is no longer valid.

Minister of Finance Jerzy Kwieciński informed that **the planned date for transfer of funds from OFE** (public pension funds) to IKE (private pension accounts) is 1 July 2020. It means that for the first 6 months of 2020, the FUS (social security fund) will be receiving transfers from OFE (thanks to so called „zipper" mechanism – transfer of funds of savers who are shortly before the retirement age to FUS) and simultaneously will be paying current contributions to OFE. Historically speaking, in 2018 the "zipper" payments equalled PLN7.8bn, while current contributions amounted to PLN2.8bn (net PLN5.0bn). That having said, we estimate that the delay will support public finance balance by PLN2.5bn. We would like to stress that the asymmetric nature of the transformation fee (PLN13.5bn in 2020, PLN5.5bn in 2021), which was unveiled recently in the regulatory assessment, was already fully taken under consideration in the budget draft. As a result, it will not help to fill the potential gap in public finance, which is likely to occur after the proposal to resign from the limit on social insurance contributions has been scrapped.

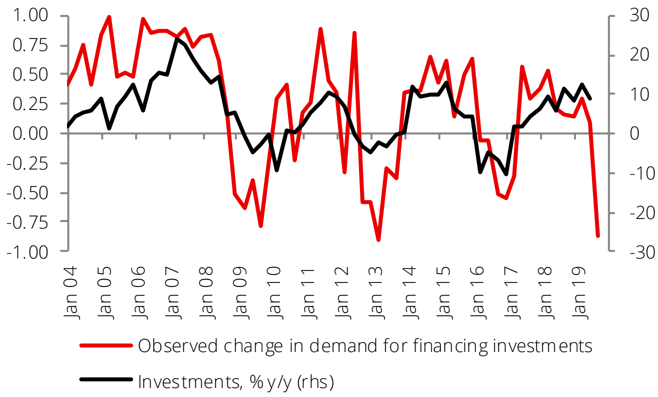
The MPC left interest rates unchanged and the statement did not differ significantly in the key points vs the previous one. The relatively slow economic growth abroad and uncertainty related to the future developments were stressed again. The MPC – relying on the new NBP projections – still thinks that despite some expected economic slowdown in 2020 the pace of Poland's GDP growth shall remain decent and inflation should not leave the range of allowed fluctuations around the target. Majority of the MPC members support the wait-and-see approach and we do not expect any rate changes in 2019 and 2020.

PMI and industrial output



Source: GUS, Santander

Signals from credit survey vs investment growth



Source: European Commission, Santander

Quote of the week:

Łukasz Hardt, MPC member, PAP, 06/11/2019: There are many inflationary factors in play right now (...) but on the other hand there is the economic slowdown in Germany, uncertainty about electricity prices and about the fiscal policy in 2020. This is not the right moment to react with change in monetary policy parameters.

Adam Glapiński, NBP Governor, PAP, 06/11/2019: There is a majority stance in the Council that inflation will remain to the target in the upcoming two years. That is why I think that with high probability the rates will not go up (...) If rates are to be changed, then a rate cut is more probable, but by private path is that rates will not be changed. Slowdown will be minor and inflation will remain curbed.

Rafał Sura, MPC member, PAP, 06/11/2019: I think that the current level of interest rates is optimal for the Polish economy. Let me add that inflation forecasts are prone to downward risk, given that the NBP staff assumed electricity price hike by 8% y/y.

	GDP growth			
	Nov 18	**Mar 19**	**Jul 19**	**Nov 19**
2019	3.55 (±0.85)	4.0 (±0.7)	4.5 (±0.6)	4.3 (±0.4)
2020	3.25 (±0.95)	3.65 (±0.95)	3.9 (±0.9)	(3.55±0.85)
2021	-	3.35 (±0.95)	3.35 (±0.95)	(3.25±0.95)
	CPI inflation			
2019	3.25 (±0.65)	1.7 (±0.5)	2.0 (±0.3)	2.3 (±0.1)
2020	2.9 (±1.0)	2.65 (±0.95)	2.8 (±0.9)	2.85 (±0.75)
2021	-	2.4 (±1.1)	2.4 (±1.1)	2.6 (±1.0)

Source: NBP, Santander

FX and FI market

Last week on the market

FX Decent data released in the US and Europe together with positive remarks regarding the US-China trade talks pushed the global equity indexes significantly up on the course of the passing week. This helped the majority of the EM currencies to gain vs the euro while the dollar index rose. However, the zloty did not benefit from the higher appetite for the risky assets and it underperformed its EM peers (only the forint and Brazilian real lost more). To some extent, this might have been due to the much worse than expected Poland's manufacturing PMI. Please note that in October, the zloty gained the most in the EM universe.

In the case of the other CEE currencies, the Russian ruble performed the best while the forint lost noticeably vs the euro. The koruna lost but was temporarily supported by the outcome of the Czech central bank's meeting. In line with expectations, interest rates were left unchanged but two members voted for a 25bp hike amid still high inflation pressure.

FI Significant improvement on the global market sentiment amid weaker worries about the global economic slowdown and positive news related to the trade talks have weighed heavily on the global debt market. Polish IRS and bond yields jumped by c10-20bp on the belly and long end. Last week, we mentioned that the 10Y bond yield trading range was narrowing and soon some bigger (and a rather upside) move could take place. Indeed, in the last few days the yield broke the 2.05% resistance and rose above 2.10%, its highest since early September. The bond and IRS curves steepened – the 2-10 spreads rose to their highest since July and early-August, respectively.

Key events

Next week, we will see numerous macro data – including first estimates of 3Q GDP growth in European countries. Also, speeches of some of the FOMC members – including Governor Powell (Wednesday and Thursday) – are scheduled.

In Poland, the trading week will be shorter due to The Independence Day on Monday. On Thursday, we will see the flash 3Q GDP release and this would be the most awaited publication in Poland next week.

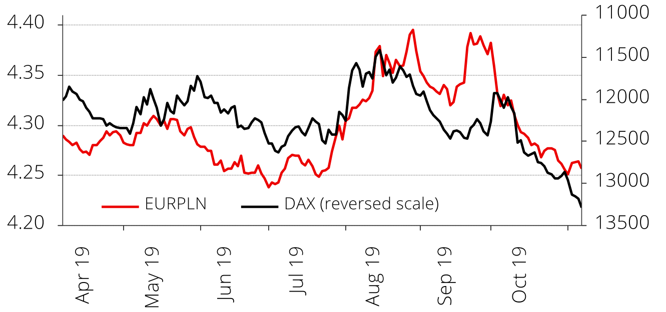
Market implications

FX Lack of the zloty's positive response to the obvious global mood improvement suggest there are minor chances for the EURPLN down move to resume in the short-term. Our forecast of the 3Q GDP is in line with the market consensus and this release should not have a meaningful impact on the zloty. The recent days saw global equities rallying and already this Friday we saw some profit taking despite the surprisingly strong German trade data. Thus, it seems that the global optimism could ease for a while allowing EURPLN to rise.

FI Polish 10Y bond yield reached the next reference level – 2.20%, the local peak recorded in July. At the same time, the 10Y Bund and UST yield are also trading near the next resistance levels of -0.22% and 2%, respectively. We expect some relief on the debt market in the short term. The recently released soft indicators surprised to the upside and seem to have already been largely priced in by the market. Thus, the data released in the coming days would have to surprise well to the upside to push yields further up. However, we think this will rather not be the case, particularly in case of the GDP prints.

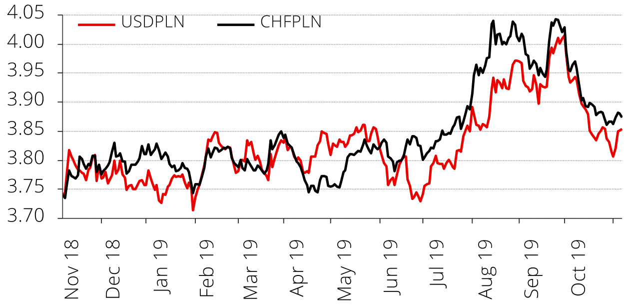
In mid-October, the PL-DE 10Y bond yield spread broke the 240bp support level and is now trying to come back above it.

EURPLN and German DAX index



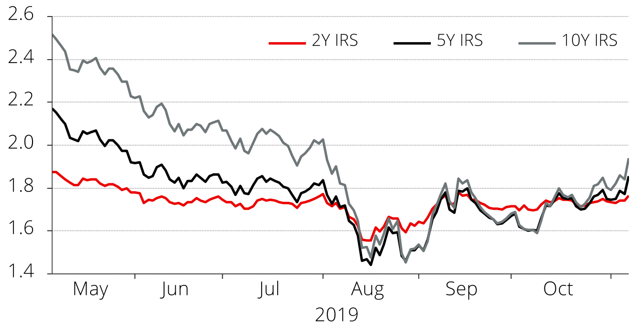
Source: Refinitiv Datastream, Santander Bank Polska

USDPLN and CHFPLN



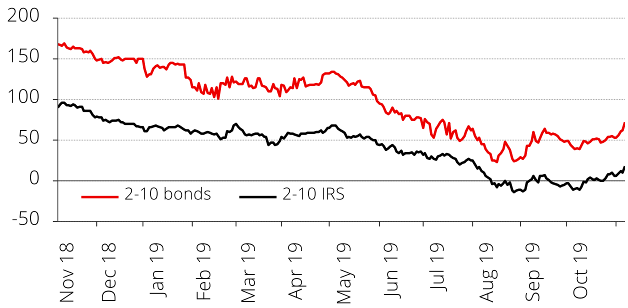
Source: Refinitiv Datastream, Santander Bank Polska

PLN IRS



Source: Refinitiv Datastream, Santander Bank Polska

2-10 spreads (bp)



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
		MONDAY (11 November)					
	PL	**The Independence Day – market holiday**					
09:00	CZ	CPI	Oct	% y/y	2.7	-	2.7
		TUESDAY (12 November)					
11:00	DE	ZEW Survey Current Situation	Nov	pts	-25.0	-	-25.3
		WEDNESDAY (13 November)					
08:00	DE	HICP	Oct	% m/m	0.1	-	0.1
11:00	EZ	Industrial Production SA	Sep	% m/m	-0.3	-	0.4
14:00	**PL**	**Current Account Balance**	**Sep**	**€mn**	**-219**	**-826**	**-606**
14:00	**PL**	**Trade Balance**	**Sep**	**€mn**	**7.5**	**-366**	**-55**
14:00	**PL**	**Exports**	**Sep**	**€mn**	**19 291**	**19 049**	**17 646**
14:00	**PL**	**Imports**	**Sep**	**€mn**	**19 265**	**19 415**	**17 701**
14:30	US	CPI	Oct	% m/m	0.3	-	0.0
		THURSDAY (14 November)					
08:00	DE	GDP WDA	3Q	% y/y	0.4	-	0.4
09:00	CZ	GDP SA	3Q	% y/y	2.6	-	2.8
09:00	HU	GDP	3Q	% y/y	4.2	-	4.9
10:00	**PL**	**CPI**	**Oct**	**% y/y**	**2.5**	**2.5**	**2.5**
10:00	**PL**	**Flash GDP**	**3Q**	**% y/y**	**4.1**	**4.1**	**4.5**
11:00	EZ	GDP SA	3Q	% y/y	1.1	-	1.1
14:30	US	Initial Jobless Claims	week	k	215	-	211
		FRIDAY (15 November)					
11:00	EZ	HICP	Oct	% y/y	0.7	-	0.7
14:00	**PL**	**CPI Core**	**Oct**	**% y/y**	**2.4**	**2.4**	**2.4**
14:30	US	Retail Sales Advance	Oct	% m/m	0.1	-	-0.3
15:15	US	Industrial Production	Oct	% m/m	-0.3	-	-0.4

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg