

17 January 2020

Weekly Economic Update

Negative data surprises coming

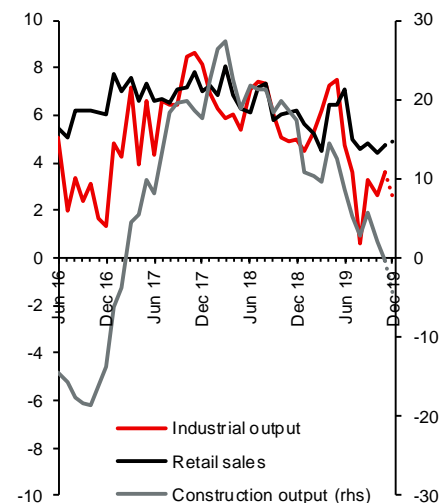
What's hot next week

- Signing the phase one deal by the US and China did not trigger any profit taking on the market and the global mood is still positive, supported by data showing that foreign trade volumes have picked up recently (last data about Asian countries exports).
- In the coming week, the data release calendar abroad will not be too heavy. The market attention is likely to focus on the sentiment indexes (**flash PMIs, German ZEW**) and if the releases do not disappoint (consensus assumes no further deterioration) then expectations for a gradual economic activity improvement should be sustained.
- A few central banks will hold their meetings - the Peoples Bank of China (Monday) and the ECB (Thursday) – but we do not expect the outcomes to deliver impulses important for the markets and economies.
- Polish economic cycle (like we have already underlined) is slightly delayed vs the euro zone and we think domestic data will not look too encouraging in the coming months. During the coming week, we will see **December output, retail sales, wages and employment data**. In all cases our forecasts are below the market consensus. If we are right, market pricing of a rate hike (that has started after the December CPI print at 3.4%) could fade. Data releases could be accompanied by **more comments of the MPC members** that might be in line with the central bank's governor Glapiński view of no need to hike rates (Jerzy Żyżyński has already confirmed he shares governor's opinion). However, if the upcoming releases beat expectations, against our forecasts, then in our view the wage growth could have the biggest impact on the market – strengthening of the wage pressure still before the hike of the minimum wage would rise chances that jump of CPI could have secondary and more long-lasting consequences. At the end of the week, we will see money supply that in our view shall show continuation of deceleration of M3 and loans growth – clearly not a reason to build expectations for a rate hike.

Market implications

- We expect the zloty could depreciate (with EURPLN heading towards 4.26-4.27) amid below-consensus Polish macro data, stronger dollar and technical analysis signals.
- On the domestic interest rate market, the yields up trend could now decelerate amid below-consensus Polish data.

Output and retail sales, 3M mov.av., %/y



Source: GUS, Santander

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Last week in economy

CPI details suggested that some of the quick December rise could be Christmas holiday-related. Still, inflation is likely to push above 4% y/y in the next reading. The large positive deviation from forecasts of November C/A was due to imports showing weakness once again.

December CPI inflation was confirmed at 3.4% y/y with food, fuels and the core component all contributing more than previously to the headline growth. Some of the rapid rise of core inflation could be a one-off factor in transport services, similar to what happened in 2019 around Easter. The January CPI print might be 4.1% y/y (as the large electricity price hike will kick in and other administered prices will also go up). More in our [Economic Comment](#).

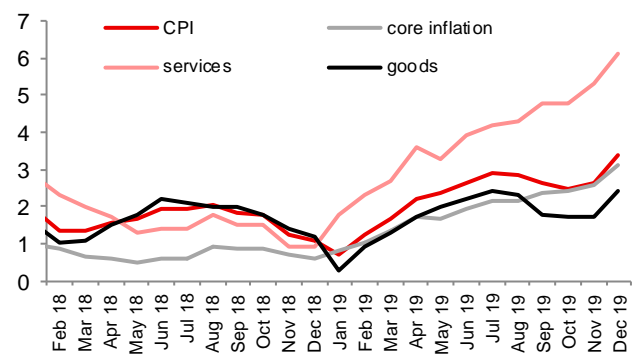
All measures of **core inflation** increased in December. CPI excluding prices of food and energy reached 3.1% y/y, up from 2.6%, re-establishing the record-high level reached earlier in December 2011. Inflation excluding administered prices surged most, to 3.6% y/y (its highest level since June 2012), inflation excluding most volatile prices rose to 3.1% (highest since July 2012, and 15% trimmed mean reached 2.5% (highest since December 2012). We expect core inflation to stabilise at the current high level in 1Q2020, and then to start descending gradually, to around 2.5% at the year-end.

Additional information provided by December **HICP inflation** data (headline inflation up from 2.5% y/y to 3.1%, core inflation up from 2.6% y/y to 2.9%) is that the non-tradable part of core inflation reached 4.9% y/y – the highest level in 10.5 years, while the tradable part rose to 0.3% y/y which happens to be its highest level in seven years and the second positive reading since early 2013.

November **current account balance** was much above forecasts: €+1457mn vs €+451mn consensus and our €+521 forecast. Compared to our estimates half of the large surprise comes from income balances, half from trade balance of goods: both exports and imports came below expectations, but imports much more so (-4.6% y/y while we expected -0.9% y/y; export growth was -1.0% y/y while we expected +0.3%). This is not the first time recently that monthly imports look poor and this may signal a deeper slowdown in domestic demand than we were assuming (although NBP comment stressed that import weakness was due to cheaper energy commodities and fuels). On the other hand our estimate of net exports' contribution to GDP may need to be raised given that the November trade balance outcome was almost €0.5bn better than we assumed. We think the data increase the probability that 4Q GDP growth will not be much worse than 3.9% y/y recorded in 3Q. 12M rolling sum of C/A balance grew to 0.6% GDP in November from 0.4% previously.

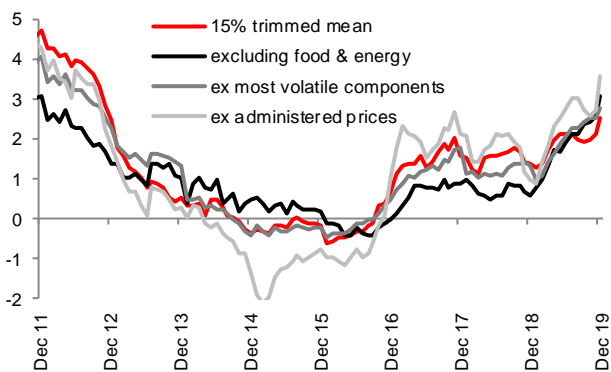
According to **MPC's Eugeniusz Gatnar**, considered one of the most hawkish members, the Council should hike rates by 15bp or 25bp to prevent speculative bubbles (strong credit activity and real estate market) and to support saving. The MPC member is worried about negative real interest rates and expects inflation to go above 4% at the start of the year and to stay for the whole year above the band of tolerable deviations from the NBP target. On the other hand, **Jerzy Żyżyński**, considered one of the most dovish members, argued that inflation rise is only temporary and in 4Q20 CPI will return to the 2.5% y/y target. In his view if the council does not react to higher inflation, it signals to the public that there is no reason to panic and as a result inflation expectations calm down. He also stated, repeating NBP governor Adam Glapiński's view, that the next move on interest rates could be a cut, but stabilisation is the most probable scenario. NBP informed that in December the motion to cut rates was once again supported only by Eryk Łon. In our view the MPC will not change rates this year although the rise of inflation will be fuelling market speculation about such a scenario.

CPI Inflation, % y/y



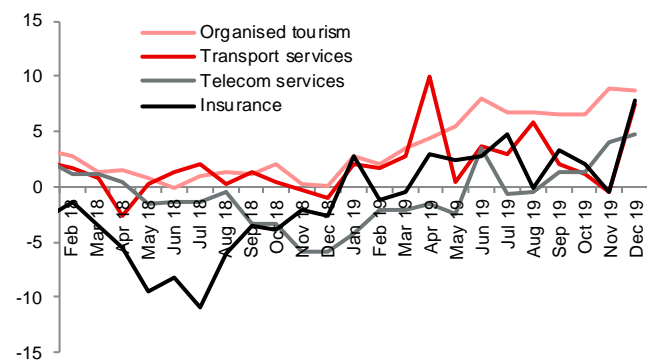
Source: GUS, NBP, Santander

Core inflation measures, %y/y



Source: NBP, Santander

CPI Inflation –selected categories, % y/y



Source: GUS, Santander

Poland, international trade, %y/y



Source: NBP, Santander

FX and FI market

Last week on the market

FX Emerging market currencies (CEE3) realized volatility has picked up last week above the long term average. This is in contrast to the developed market ones which still remain relatively muted. As to the price level the EURPLN has not changed week over week (at 4.237), however on Tuesday the pair saw a significant squeeze lower down to 4.2126 after which it rebounded to 4.244 on early Friday. In the passing week the global factors, like the signing of the US – China “phase 1” trade deal have had not much influence on the zloty. As to the zloty’s crosses, the USDPLN and GBPPLN also remained unchanged in the vicinity of 3.81 and 4.98, while CHFPLN gained 0.5% to 3.944 after US Treasury department put Switzerland on the currency manipulators watch list. In the case of the other CEE currencies, the forint and Russian rouble weakened – EURHUF +0.6% w/w to 335.6 and is just one step away from breaching the all time high of 336.7. USDRUB +1.0% w/w to 64.7 after the Russian government change (and despite the stable oil price). It was only Czech koruna that strengthened by 0.3% to 25.15 (low 25.05) after still higher inflation print on Monday and increasing expectations of a CNB rate hike.

FI Polish bond yields increased albeit not as much as in a previous week of 7-10 Jan (where 10Y moved by c 20bp higher). So in the previous week the long end of the curve (10Y) traded briefly around 2.35% (highest since July 2019) only to correct lower afterwards and close the week almost unchanged w/w at 2.30%. The front end of the curve (FRAs and 2Y bond yields) marched slowly but consistently higher as the market kept pricing in an interest rate hike: 2Y bond yields went up by 4bp to 1.57% while 21x24 FRA by 6bp to 1.89%.

Key events

Next week, PBoC (Monday) and ECB (Thursday) decide on interest rates, there is German PPI and ZEW data in the beginning of the week and a PMIs in the US and Europe on Friday. There is quite a lot of data being published in Poland, Santander is mostly below market consensus (see calendar at the end of the document for details).

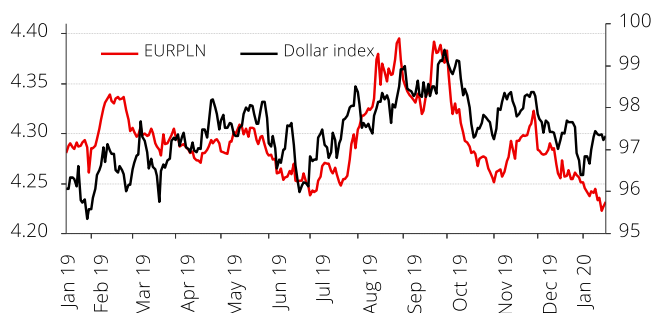
Market implications

FX EURPLN fell below the 4.24 lower band level mostly, we reckon, as a result of the yuan whose strength accompanied the signing of the trade deal. Local Polish macroeconomic fundamentals – slowing growth and accelerating inflation the latter of which contributes to even more negative real rates both warrant a medium term depreciation pressure on the zloty. Next week if the data turn out to be as week as we expect, the zloty might march higher towards 4.26, 4.27. The biggest risk to our forecast would be overly dovish PBoC which would support the risk on the global markets early next week.

FI After the abrupt rise in Polish bond yields 2 weeks ago, and a spike higher and a subsequent correction lower in the passing week, we expect a stabilization of yields in the following week. It might very well be that the 10Y will ultimately reach 2.50% within the next month or so (we believe the medium term trend in yields is upwards), however given the slowing economy and negative surprises to macroeconomic data which we expect next week, yields might pause for a while in the vicinity of 2.30%. The German Bund yields struggle to rise above the current -0.20% hence it is likely that the 10Y PL-DE spread remains c250bp.

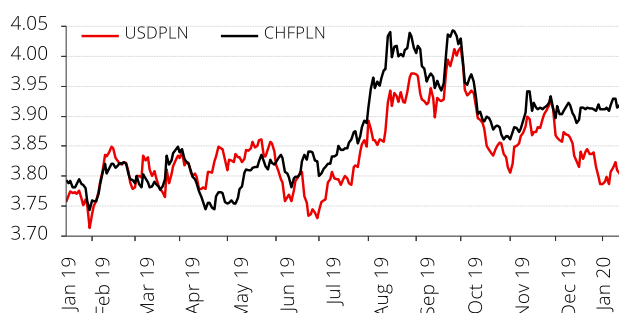
The market still tries to estimate how long, after the recent high December CPI print, the CPI would remain above the target. Tuesday wages data might be crucial here. If the print is weaker than market consensus the reaction should be muted. However if we are wrong and the print will be above market consensus then the market is likely to price and even higher probability of a rate hike and the 2Y yields should increase further.

EURPLN and dollar index



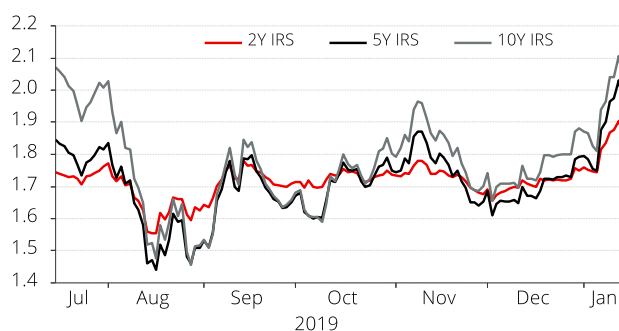
Source: Refinitiv Datastream, Santander Bank Polska

USDPLN and CHFPLN



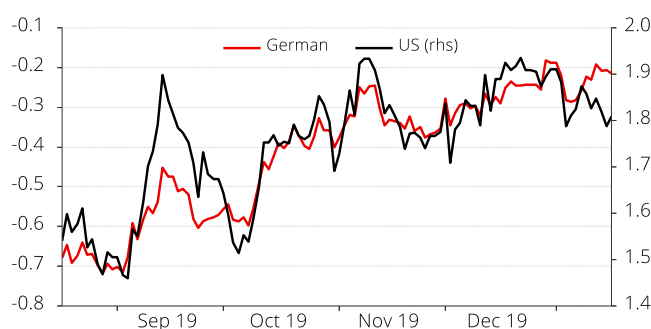
Source: Refinitiv Datastream, Santander Bank Polska

Poland IRS



Source: Refinitiv Datastream, Santander Bank Polska

10Y Bund and UST yields



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE	
				MARKET	SANTANDER		
TUESDAY (21 January)							
10:00	PL	Employment in corporate sector	Dec	% y/y	2.6	2.6	2.6
10:00	PL	Construction Output	Dec	% y/y	1.3	-1.6	-4.7
10:00	PL	Average Gross Wages	Dec	% y/y	6.1	5.6	5.3
11:00	DE	ZEW Survey Current Situation	Jan	pts	-10.0	-	-19.9
WEDNESDAY (22 January)							
10:00	PL	Sold Industrial Output	Dec	% y/y	6.1	4.8	1.4
10:00	PL	PPI	Dec	% y/y	0.9	1.0	-0.1
16:00	US	Existing Home Sales	Dec	% m/m	1.5	-	-1.65
THURSDAY (23 January)							
10:00	PL	Retail Sales Real	Dec	% y/y	6.6	5.7	5.2
13:45	EZ	ECB Main Refinancing Rate	Jan.20	%	0.0	-	0.0
14:30	US	Initial Jobless Claims	Jan.20	k	218	-	204
FRIDAY (24 January)							
09:30	DE	Flash Germany Manufacturing PMI	Jan	pts	44.2	-	43.7
09:30	DE	Flash Markit Germany Services PMI	Jan	pts	52.9	-	52.9
10:00	EZ	Flash Eurozone Manufacturing PMI	Jan	pts	46.7	-	46.3
10:00	EZ	Flash Eurozone Services PMI	Jan	pts	52.8	-	52.8
14:00	PL	Money Supply M3	Dec	% y/y	9.4	8.9	9.4

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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