

22 May 2020

Weekly Economic Update

Output and sales reached the bottom

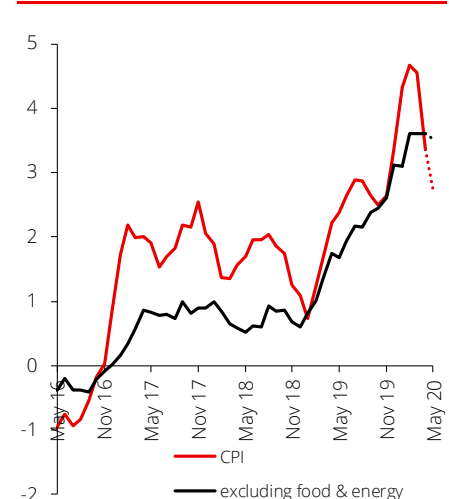
What's hot next week

- It seems that May was the month during which both consumers and corporates started to shrug off the shock caused by the pandemic and the painful restrictions for business and social activity that followed – this is what flash PMIs are suggesting. If so, then in the coming week there is a handful of sentiment indicators being published (Ifo, ESI, Michigan, Conference Board) which might prove useful in sustaining positive market mood. The refreshed conflict between the US and China poses a risk to market sentiment however – Hong Kong has already been influenced by it (China plans to limit the country's liberties under national security concern). In the coming week we will get more details regarding Q1 GDPs in Germany and the US.
- The details of Polish 1Q GDP growth (the flash reading of which surprised us positively) will also be out, but we feel it may be difficult to revise up the forecasts for the following quarters on this information, knowing how deep was the April fall of industrial output and retail sales. On Friday, flash CPI for May is due – the further decline of fuel prices and some of food components as well as the easing of lockdown measures (which potentially allowed GUS to record prices in economic areas that were closed in April) should help bring CPI growth below 3% y/y.
- One-day MPC meeting is scheduled next week (postponed from the early May). We do not know whether the press conference will follow the meeting, nor whether the next MPC meeting scheduled just a week later will take place. Also we do not know which of the two meetings will be followed by a communique. We are more convinced about MPC not planning to cut rates further for now than we are about the exact date when this will be announced.

Market implications

- Last week, rising prices of stocks, commodities and weakening dollar helped emerging market currencies gain, including the zloty, which rose 1% vs euro and 2% vs dollar. The EURPLN exchange rate has not reacted to very poor industrial production data, which might indicate that the bearish PLN positioning is excessive. In the short term we do not expect EURPLN to break out of the horizontal 4.50-4.60 range in either way. However as long as the weakening dollar and elevated stock indices allow, the EURPLN might test 4.50 in the nearest future.
- Bond yields and IRS increased more than the core market yields. This might partially be explained by decent bond supply which came to market in the passing week, a total of PLN 29.2bn (Ministry of Finance PLN 5bn, BGK PLN 9bn, PFR PLN 15bn). In the coming week we expect the yields to continue marching higher and this despite the expected NBP asset purchasing auction on Thursday. We expect the 10Y POLGBs to end the next week above 1.50% and the spread vs Bund to widen to 200+bp.

CPI inflation in Poland, % y/y



Source: GUS, Santander

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Last week in economy

Given the better-than-expected 1Q20 GDP reading on one hand and the dramatically worse industrial output for April on the other posing a downward risk for our 2Q20 GDP growth forecast (-11.7% y/y), we prefer to hold on to our entire year estimate at about -4%.

Industrial output tumbled by 24.6% y/y in April, way more than we and the market had feared (-12.9% and -12.4%, respectively). This is the strongest blow the Polish industry has taken after 1990, bringing the output back to levels seen 7 years ago. The industry suffered due to full-scale Covid-19 lockdowns, staff absences and reduced demand. We hope that April marked this year's trough and we are going to see a gradual recovery in the months to come. Read more in our [Economic comment](#).

In April Polish **employment** in the corporate sector fell by 2.1% y/y and 2.4% m/m, while **wage growth** slowed down to 1.9% y/y from 6.3% y/y in March – both were deeply below expectations (-0.6% y/y and 4.4% y/y, respectively). The momentum of changes is unprecedented in Poland's modern economic history. Clearly, the SARS-CoV-2 epidemic was taking its toll on the labour market much faster than we had anticipated. As some restrictions were eased in May, we are expecting the negative tendencies to milden markedly. Meanwhile, consumer confidence improved somewhat in May. More in [Economic Comment](#).

April **retail sales** in constant prices fell by 22.9% y/y, more or less in line with our forecast and market consensus. Durable goods suffered more than non-durables. Sales are likely to improve in May, but remain deep in the negative territory. The erosion of households' incomes is likely to put negative pressure on consumer consumption in the months to come. More in [Economic Comment](#).

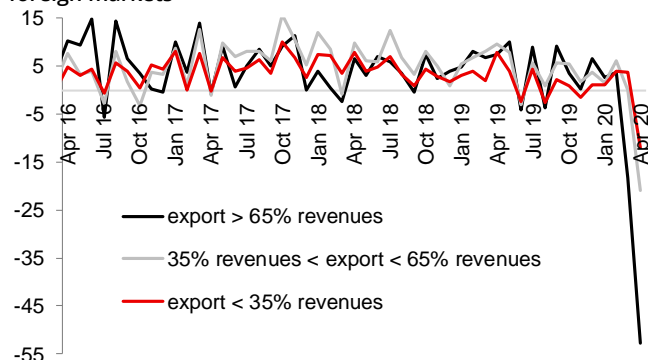
Construction output surprised positively in April, showing only a marginal y/y decline of 0.9% vs +3.7% previously, thanks to a robust civil engineering performance, while the housing market clearly stepped on the brakes in April.

New anti-crisis tools prepared by the government that were mentioned during the week include 3-month long credit instalment holidays for those who have lost job during lockdown, PLN300mn of subsidies for corporate loans interest payments for up to 12 months this year, PLN270mn next year. Unemployment benefits are to go up by 40% to PLN1200 and, on top of that, another benefit for those who lost their job, worth PLN1300 monthly, may be paid out for 3 months.

Ministry of Finance wants to broaden the list of events that switch off the **stabilising expenditure rule** (SRW) to include an epidemic. Spending limits derived from the rule could be temporarily suspended and there would be 2-4 years transition period before the return to the limits, depending on the condition of state finances and economic growth.

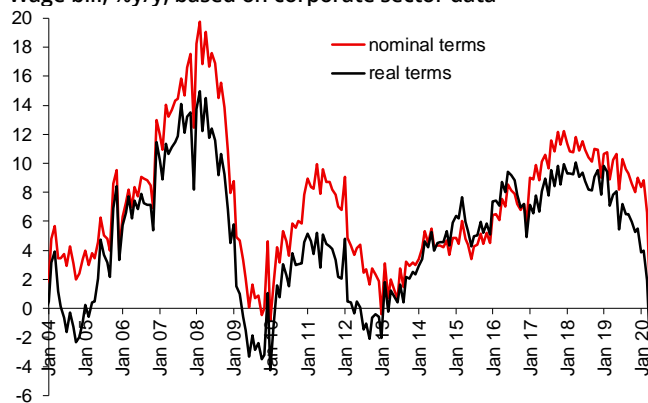
MPC's Jerzy Kropiwnicki wants a slow come back of rates to the levels from before the pandemic, in steps every 2-3 months, but not yet at the May meeting. He thinks there are not many negative rates' supporters (he is strongly against). Grażyna Ancyparowicz has not excluded further rate cuts, but rather in 2H20. Eryk Łon would like to keep rates stable for at least a year from now. We think majority of MPC will be voting for keeping rates unchanged this year, while in the case of unexpected weakness in the economy and another wave of the coronavirus, more cuts cannot be excluded

Manufacturing output, % y/y, sectors divided by exposure to foreign markets



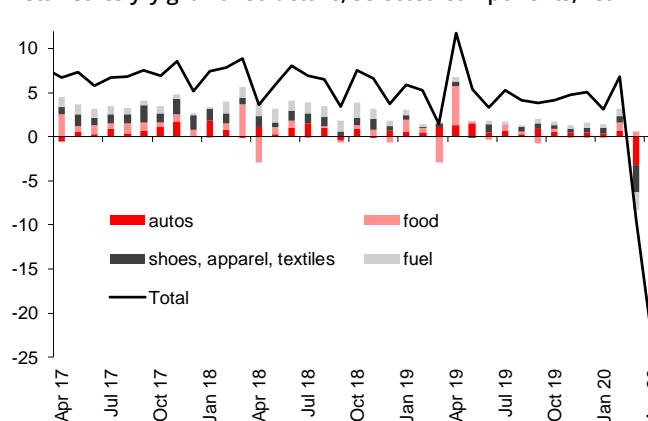
Source: GUS, Santander

Wage bill, %y/y, based on corporate sector data



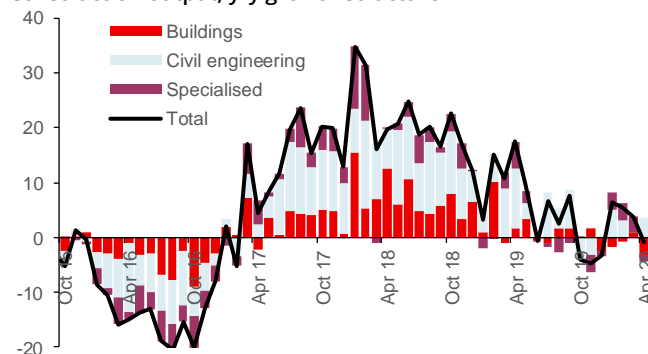
Source: GUS, Santander

Retail sales y/y growth structure, selected components, real



Source: GUS, Santander

Construction output, y/y growth structure



Source: GUS, Santander

FX and FI market

Last week on the market

FX During last week the dollar weakened (dollar index fell 0.8% to 99.6) while commodities, especially energy ones, continued their upward march e.g. WTI gained another 9%. Also risky assets increased in price (SP500 +2.4%). As a result, emerging market currencies gained for the first time in many weeks. Zloty as much as 1% vs euro (4.523), 2% vs the dollar (4.144) and 2% vs the frank (4.268). FX options implied volatilities declined and the volatility surface slope became normal again. Regional currencies behaved in a similar fashion – EURHUF and EURCZK moved lower by 1.7% (to 348.8 and 27.2) while USDRUB dropped to 71.9 which is as much as 2%.

FI Over the course of the passing week POLGBs yields increased and by more than those at the core markets – there the US curve edged higher by 1bp, while the German one by 3bp. In Poland the bond yield curve moved higher by 5bp at the front end (2Y to 0.55%) while 7bp at the long end (10Y to 1.40%). Even larger increases were observed on the IRS curve: 2Y closed the week at 0.52% (2Y ASW almost back to zero) while 10Y to 0.95%. The increases in yields (which were larger than those on the core markets) might have resulted, at least partially, from a decent bonds supply this week – Ministry of Finance sold PLN 5bn worth of bonds, BGK issued 7Y bonds worth PLN 9bn, while PFR 5Y ones worth more than PLN 15bn. The weekly total issuance reached PLN 29.2bn. As investors repriced lower the likelihood of the next rate cut, the FRAs were increasing.

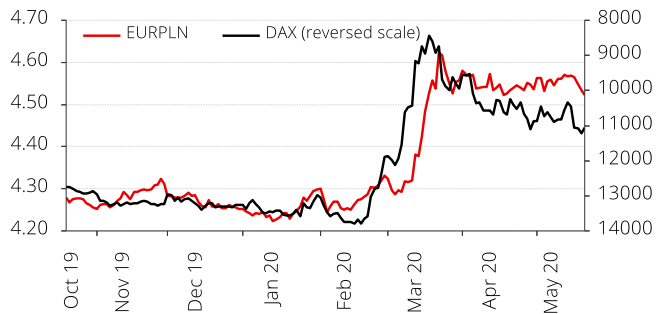
Key events in Poland there is unemployment rate data on Tuesday, while on Thursday the MPC meeting. In Germany IFO index will be published on Monday, while retail sales on Wednesday. In the Eurozone flash HICP for May will be published on Wednesday. In the US the Q1 GDP data and durables good orders get published on Thursday while Michigan index on Friday. On Tuesday Hungarian central bank decides about interest rates (0.9% unchanged).

Market implications

FX EURPLN declined in line with other emerging markets currencies in the context of rising stock and commodity prices. The exchange rate has not reacted to very poor industrial production data, which might point to overly bearish zloty positioning. During the decline the only technical level that the EURPLN managed to breach was the relatively unimportant 50-day moving average (at 4.54) while the important level of 4.50 has not been reached so far. It seems that EURPLN remains in the new horizontal range 4.50-4.60. We do not expect the currency pair to move outside of the range either way in the short term. However in the coming week, as long as the weaker dollar and stock indices remaining at the elevated levels will allow, the EURPLN might test 4.50. We do not think the level will be broken for good.

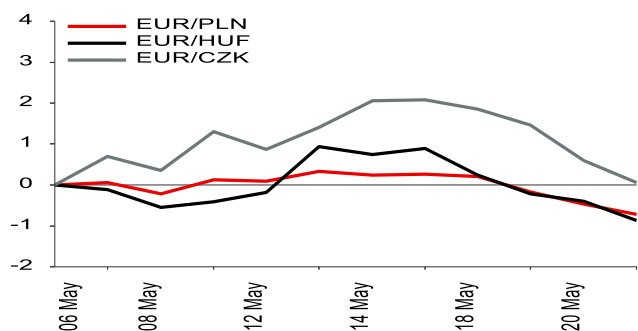
FI Polish bonds were being sold in the passing week, during the same period the yields on the core markets increased but only very slightly. Polish FRAs increased signalling that market expectations towards further rate cuts weakened. In the coming week we expect bond yields further to rise as a result of the quite significant yield supply – roughly PLN 29.2bn – and even despite incoming NBP purchasing auction on Thursday. Last time BGK and PFR issued bonds, NBP bought around 50% and 20% of the bonds, respectively. We expect the 10Y POLGBs to increase to 1.50% in the coming week while the spread to Bund might widen to 200bp or above. IRS which have recently been used to hedge the bonds positions might continue marching upwards and this should help narrow the asset swap spreads a bit.

EURPLN and German DAX index



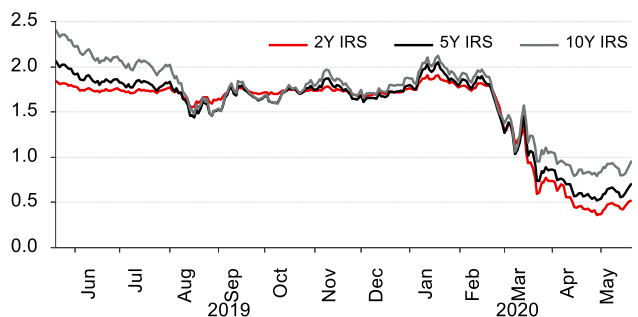
Source: Refinitiv Datastream, Santander Bank Polska

EM currencies (% change since May 1)



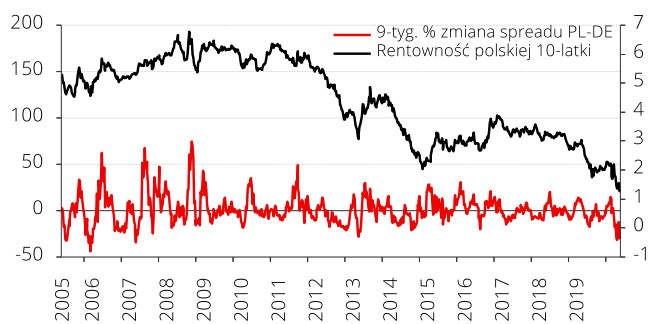
Source: Refinitiv Datastream, Santander Bank Polska

Poland IRS



Source: Refinitiv Datastream, Santander Bank Polska

Poland 10Y bond yield and 9-week % change of PL-DE spread



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

| TIME CET | COUNTRY | INDICATOR | PERIOD | FORECAST | | LAST VALUE |
|---------------------------|-----------|----------------------------|------------|--------------|-------------|---------------|
| | | | | MARKET | SANTANDER | |
| MONDAY (25 May) | | | | | | |
| 08:00 | DE | GDP WDA | 1Q | % y/y | -2.3 | -2.3 |
| 10:00 | DE | IFO Business Climate | May | pts | 78.3 | 74.3 |
| 14:00 | PL | Money Supply M3 | Apr | % y/y | 12.3 | 12.4 |
| TUESDAY (26 May) | | | | | | |
| 10:00 | PL | Unemployment Rate | Apr | % | 5.7 | 5.8 |
| 14:00 | HU | Central Bank Rate Decision | May.20 | % | 0.9 | 0.9 |
| 16:00 | US | Consumer Conference Board | May | pts | 87.0 | 86.9 |
| 16:00 | US | New Home Sales | Apr | % m/m | -21.85 | -15.4 |
| WEDNESDAY (27 May) | | | | | | |
| | DE | Retail Sales | Apr | % m/m | -10.0 | -4.0 |
| THURSDAY (28 May) | | | | | | |
| | PL | MPC decision | | % | 0.5 | 0.5 |
| 11:00 | EZ | ESI | May | pct. | 72.5 | 67.0 |
| 14:00 | DE | HICP | May | % m/m | 0.2 | 0.4 |
| 14:30 | US | Durable Goods Orders | Apr | % m/m | -18.0 | -15.3 |
| 14:30 | US | GDP Annualized | 1Q | % Q/Q | -4.8 | -4.8 |
| 14:30 | US | Initial Jobless Claims | May.20 | k | 2400.0 | 2438.0 |
| 16:00 | US | Pending Home Sales | Apr | % m/m | -15.0 | -20.8 |
| FRIDAY (29 May) | | | | | | |
| 09:00 | HU | GDP | 1Q | % y/y | 0.0 | 2.2 |
| 10:00 | PL | Flash CPI | May | % y/y | - | 2.7 |
| 10:00 | PL | GDP | 1Q | % y/y | 1.9 | 1.9 |
| 11:00 | EZ | Flash HICP | May | % y/y | 0.35 | 0.4 |
| 14:30 | US | Personal Spending | Apr | % m/m | -12.55 | -7.5 |
| 14:30 | US | Personal Income | Apr | % m/m | -7.0 | -2.0 |
| 14:30 | US | PCE Deflator SA | Apr | % m/m | -0.7 | -0.3 |
| 16:00 | US | Michigan index | May | pts | 73.7 | 73.7 |

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg
**estimate after CPI inflation data

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