CEE Economics

Poland

19 June 2020

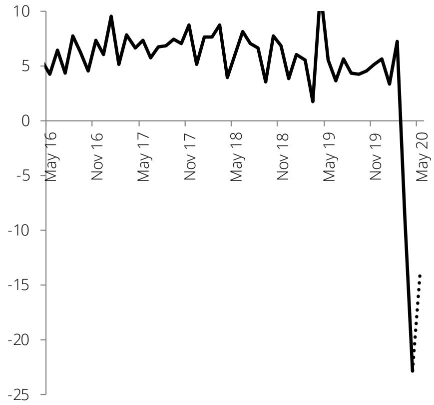
Weekly Economic Update

Symptoms of recovery

What's hot next week

- The available data for May seem to confirm our earlier assumption that April was the worst month in this economic crisis and next months should see a gradual rebound from the bottom, both in Poland and abroad.
- After the weekend we will see the first hints on economic activity in June, including flash PMIs in Europe, German Ifo, next regional Fed's activity trackers, and in Poland business climate indicators from GUS. Most of them should confirm further improvement, which has been already priced-in by the financial market.
- In Poland we will see some more data for May, including retail sales, unemployment, money supply, detailed information in the GUS Statistical Bulletin.
- The agenda includes central bank meetings in Czechia, Hungary, China. Market consensus does not assume any rate changes, but we would not rule out a small rate adjustment from CNB that could negatively affect the koruna (and indirectly the zloty).
- It will be the last week of the presidential election campaign in Poland. So far it does not look likely that it will end in the first round. Markets may start paying attention to the issue if the result is much different from the recent polls.
- Today the European Council meeting was held. EU leaders were to discuss the new recovery programme and EU budget but the meeting was arranged as a videoconference and hardly anyone expected it could bring a breakthrough in negotiations without a face-to-face backstage meetings. We will have to wait for decisions in this matter until late summer or even autumn.

Retail sales, % y/y



Source: GUS, Santander

Market implications

- We maintain the view that EURPLN would gradually march upwards – recently this view was additionally reinforced by the MPC's verbal intervention. If this form of intervention would not work, bigger NBP's activity cannot be ruled out. Additional argument for weaker PLN could be possible correction in EURUSD and the fact that as regards the new daily COVID-19 infections Poland is slowly becoming the European black sheep.
- In the debt market the short end of the curve should remain under the pressure of rising excess liquidity, which before the end of June may at least partly shift from the NBP bills (almost PLN160bn of assets, which effectively yield below zero for commercial banks) to POLGBs. The long end will be more dependent on core debt markets.

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Last week in economy

First data from May confirmed that the Polish economy was shrugging of the epidemic effects, with a rebound in industrial output and confidence indicators, slowing decline of employment. We are expecting more positive news in the upcoming months.

In May **Polish industrial output** fell by 17.0% y/y vs -24.6% y/y in April. In seasonally-adjusted terms this means a 12.2% m/m rebound from the April trough. The largest decline was seen among industries producing investment goods, -38.4% y/y vs -50.9% previously, output growth of consumer durables improved the most, to -13.7% y/y from -47.8%, and consumer non-durables again saw the smallest decline (-8.7% y/y). Cars, machinery and equipment and furniture were still the most depressed industries, together with coal mining. We expect production growth to improve in the following months, possibly entering single-digit y/y declines area as we move to 2H20.

Central budget showed a PLN26.0bn deficit after May, as compared to PLN18.9bn after April. Bear it in mind, however, that currently the central budget does not say much about the state of the public finance, as the government has pushed the bulk of the epidemic-related spending out from the central sector. As of the end of May, the government spent PLN62.35bn on covid-related programmes (about PLN60bn in May alone) and in our view only an insignificant part of this sum is already visible in the central government balance, as government spending amounted to PLN34.5bn in May (vs. PLN28.5bn in May 2019). VAT revenues tumbled in May by 35% y/y, while PIT and CIT were stable or even increased in annual terms. The two latter are however affected by the government decision to prolong payment deadlines, so timeline shifts are making it difficult to interpret the data.

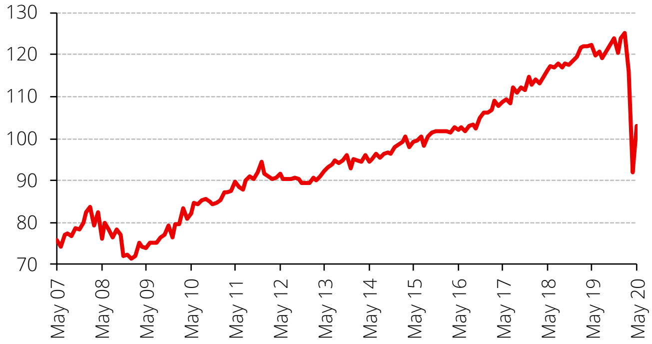
Local governments recorded a PLN9.8bn surplus in 1Q20 after PLN11.0bn one year earlier. Sector's investment increased by 11.3% y/y, but we think it is mostly due to favourable weather conditions. We are generally pessimistic as regards outlook for local governments' investment this year and expect declines in annual terms, especially given Covid-related slump in PIT and CIT receipts as well as delays in realisation of EU-financing contracts. We expect a major deterioration of local government's balances in 2Q20.

Poland's **labour market statistics** for May were roughly in line with expectations: employment declined further, but at a slower pace than in April (-1.4% m/m vs -2.4% in the previous month), and wage growth eased to 1.2% y/y from 1.9% y/y. We expect June statistics to see some rebound on the labour market. Meanwhile, consumer confidence improved markedly, but remained way below pre-covid levels. Read more in our Economic Comment.

In May **Polish CPI** fell to 2.9% y/y from 3.4%. The slowdown was caused mainly by falling fuel prices and slower growth of food prices, while **core inflation** rose to 3.8% y/y from 3.6% (highest in 18 years). The effect of the epidemic is becoming more visible in the data: in some categories it is causing price cuts (footwear, tourism), in some - their rise (medical services, hairdressing). We expect CPI inflation to keep falling this year, to c1.5% in December, with core inflation also going down but slower and unlikely below 2% this year. Poland **HICP inflation** rose to 3.4% y/y in May from 2.9% Core HICP inflation rose to 4.6% from 2.8% - the biggest acceleration since data is available (1997).

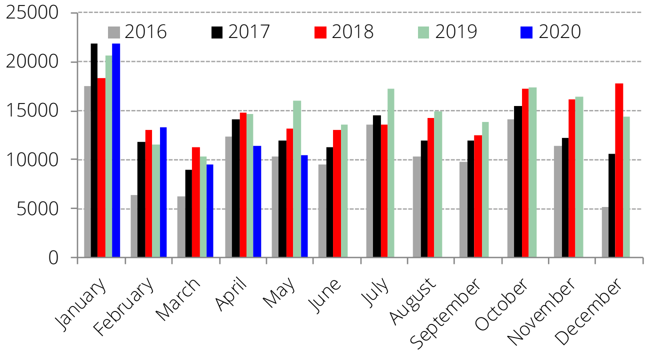
The **NBP** kept interest rates unchanged, in line with expectations. The official statement included an important addition stating that "the pace of economic recovery could be mitigated by the lack of visible zloty exchange rate adjustment". It looks like in the Council's opinion the FX channel does not work effectively as a macroeconomic policy instrument in this recession phase - zloty should have been weaker, which would support Polish exporters. Let us remind words of MPC's Rafał Sura, who said at the beginning of June that the NBP would analyse reasons behind mild PLN weakening and this could affect its future actions (EURPLN neared 4.40 at that time). Rafał Sura usually shares views of NBP President Adam Glapiński and the new sentence in the official statement suggests that the issue brought the Council's attention. We still believe interest rates are about to stay on hold for a long time, at least until the end of 2021. The next meeting is scheduled for 8 July, with new NBP staff economic forecasts.

Industrial output, seasonally adjusted, 2015 = 100



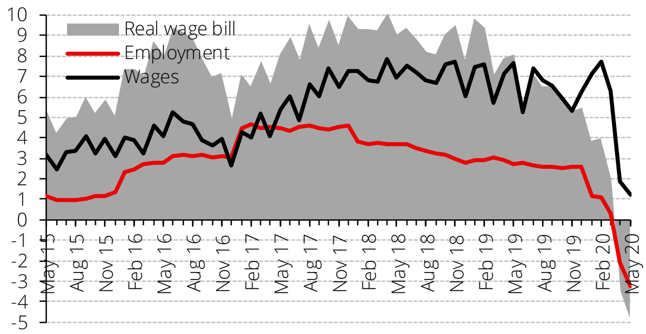
Source: GUS, Santander

VAT revenues, PLNmn



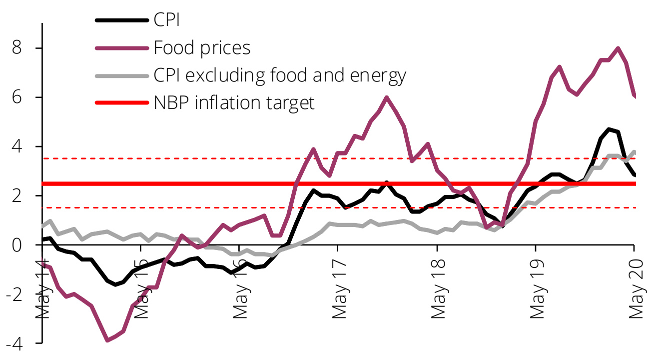
Source: Ministry of Finance, Santander

Labour market statistics, % y/y



Source: GUS, Santander

Inflation measures and NBP target, % y/y



Source: GUS, NBP, Santander

FX and FI market

Last week on the market

FX The passing week has been the third in a row when EURPLN was hovering around 4,43-4,44 for most of the time. The dollar appreciation and the sentence in the MPC post-meeting statement saying that in the central bank's view the zloty is not weak enough did not have a long-lasting impact on the Polish currency. USDPLN, CHFPLN and GBPPLN did not move much either.

The other CEE currencies also remained fairly stable in the recent days. EURCZK was hovering around 26,7, EURHUF near 346, and USDRUB in a tight range slightly below 70.0.

FI The IRS and bonds yields on the front end and belly of the curves did not move much in the passing week. The short-term rates were virtually flat while the 5Y were trading within a 10bp range. Only on the long end rates recorded a meaningful change with the 10Y yield climbing 7bp on weekly basis. The asset swap spreads and spread vs Bund remained roughly stable.

Last week was also pretty calm on the core markets while yields of the euro zone peripheral bonds fell slightly.

Key events of the next would be flash PMIs and the numerous US data, in our view. In our region, the Czech central bank will decide about the interest rates and in Poland retail sales data will be released.

Market implications

After the last FOMC meeting when message was again rather reserved and not too optimistic, the upside trend on the equity market lost steam somewhat. However, there seems to be little concern about information about a rise of COVID-19 cases in regions that have reopened recently, at least for the time being. This week, we will see flash June euro zone PMIs that rose slightly in May after the severe plunge in April. The market is hoping for a noticeable rebound that could help justify pricing a V-shape growth revival, in contrast to what central bankers say.

FX We remain our view of EURPLN moving up towards 4.50 in the coming weeks. In the recent days, one more factor supporting this bet joined the list, namely the verbal intervention from the central bank. Since it provided only short-lived and limited effect, we think that in the coming weeks the NBP might step up its effort to weaken the zloty.

Also, the coronavirus pandemic still does not look to be contained in Poland, similarly to many other EM countries. Should the market notice a divergence on this front vs developed countries, the EM currencies may perform poor with the zloty being more prone to depreciation given low interest rates in Poland.

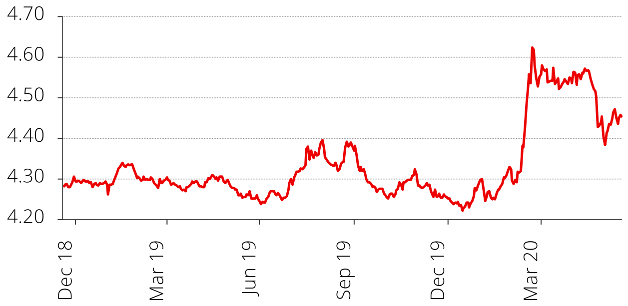
The pressure on the Polish currency could come from EURUSD. In the previous week, the exchange rate failed to break 1.14 resistance again and looks heavy for now. In our view, EURUSD could correct lower after a noticeable mid-May/mid-June rally and stronger dollar might pressure the zloty.

Finally, there is a non-zero probability that the Czech central bank will actually cut rates, in contrast to the market expectations. Such surprise could hit the koruna and to some extent weight on the zloty as well.

FI We think Polish IRS and bond yields should at least not rise or may even drop this week. The end-of-month period could encourage banks to buy tax-free Treasury bonds instead of parking excess cash in taxed central bank's bills. Also, the room for higher rates could be limited by the option of QE expansion, that next to stabilizing the market, might have a desired impact on the zloty's exchange rate.

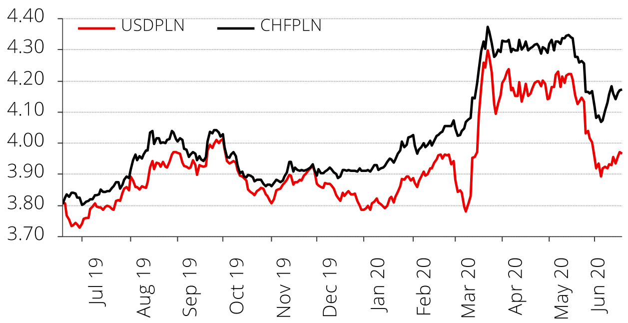
Since the beginning of June, the 10Y PL-DE bond yield spread rose by more than 20bp to c183bp. Should the global market sentiment stay positive, the Bund yields might rise but this may not automatically mean Polish rates should rise as well. There seems to be room for the PL-DE spread to drop first.

EURPLN



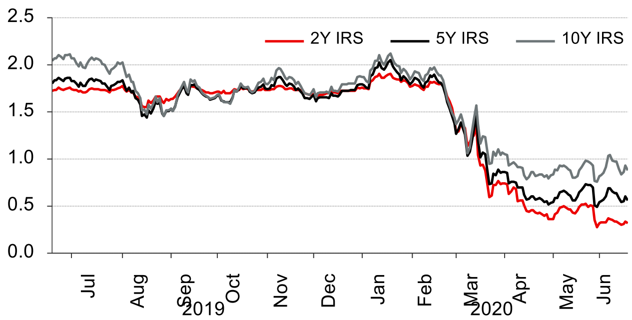
Source: Refinitiv Datastream, Santander Bank Polska

USDPLN and CHFPLN



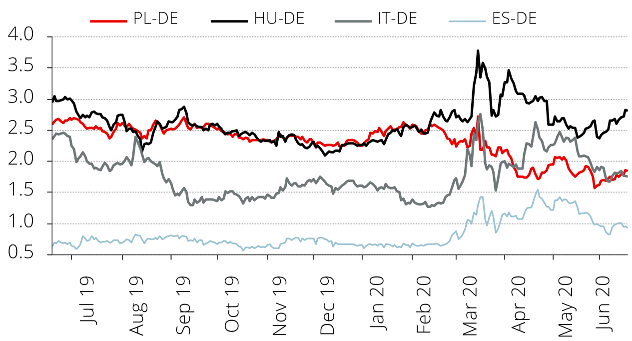
Source: Refinitiv Datastream, Santander Bank Polska

Poland IRS



Source: Refinitiv Datastream, Santander Bank Polska

10Y yield spreads vs Bund



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
			MONDAY (22 June)				
10:00	**PL**	**Real retail sales**	**May**	**% y/y**	**-11.7**	**-14.0**	**-22.9**
16:00	US	Home sales	May	% m/m	-4.2	-	-17.8
			TUESDAY (23 June)				
9:30	DE	Flash PMI – manufacturing	Jun	pts	44.0	-	36.6
10:00	EZ	Flash PMI – manufacturing	Jun	pts	43.2	-	39.4
14:00	**PL**	**Money supply**	**May**	**% y/y**	**14.6**	**16.2**	**14.0**
16:00	US	New home sales	May	% m/m	1.1	-	0.6
			WEDNESDAY (24 June)				
10:00	**PL**	**Unemployment rate**	**May**	**%**	**6.1**	**6.0**	**5.8**
10:00	DE	Ifo index	Jun	pts	85.0	-	79.5
13:00	CZ	Central bank decision		%	0.25	-	0.25
			THURSDAY (25 June)				
14:30	US	GDP third estimate	Q1	% q/q	-5.0	-	-5.0
14:30	US	Durable goods orders	May	% m/m	12.0	-	-17.7
14:30	US	Initial jobless claims	week	k	-	-	1 508
			FRIDAY (26 June)				
14:30	US	Consumer incomes	May	% m/m	-5.8	-	10.5
14:30	US	Consumer spending	May	% m/m	8.7	-	13.6
16:00	US	Michigan index	Jun	pts	78.9	-	78.9

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

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