07 August 2020

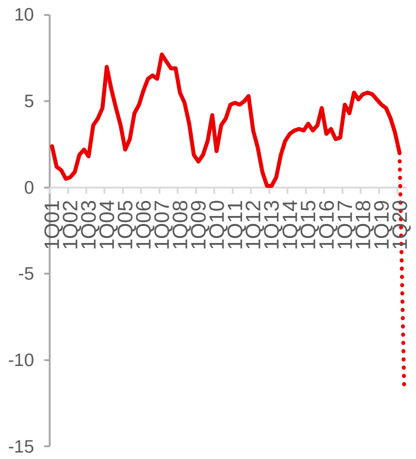
Weekly Economic Update

Fall of Polish GDP and reintroduced restrictions

What's hot next week

- August started with still strong positive momentum of economies recovering after spring lockdowns. At the same time COVID-19 statistics of daily cases show that the world is facing the second wave of the pandemic. As a result there is pressure to reintroduce restrictions, also in Poland, albeit shaped in such a way not to curb activity in the recovering economies. Still, it is worth to track current data, especially the US ones – July output and retail sales, August consumer sentiment – in search of negative impact of the intensifying pandemic.
- In Poland we will get to see the first GDP for 2Q20 data and we are expecting a decline by 11.7% y/y. i.e. stronger than expected by the market. Still, as we know that the economy was rebounding quite fast in the recent weeks, the reading for 2Q20 does not matter that much. Markets could pay more attention if the reading surprises markedly to the upside, in our view. We will also get to see balance of payments data for June, most likely with another major surplus in current account and trade balances.
- This week also numerous inflation readings will be released, among others in the USA, Germany and in CEE region, including Poland final CPI data. Persistently high inflation in CEE countries compared to euro zone inflation already sinking to around zero is an interesting phenomenon but likely without much impact on the monetary policy in the region and not that much important for the market as the issue how economies deal with rising number of new COVID-19 infections.

Polish GDP, % y/y



Source: GUS, Santander

Market implications

- Summer holiday mood on the FX market as measured by low realized volatility may persist for another week. If the dollar regains some ground, however, this might weaken EM currencies, including zloty, a bit. August seasonality also will not help the zloty – EURPLN increased in most of the previous Augusts.
- Bond yield curve might remain stable at the front end (with FRA and IRS continuing their slow gradual declines). Long end of the curve is likely to follow core market closely (the 10Y yield spread is stable at 180bp). On Thursday PFR will issue PLN 3-5bn worth of bonds with maturities 7Y and 10Y.

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Last week in economy

The week started with Polish PMI pushing well above 50 pts. Relatively strong German data releases complemented the picture of a recovery in Polish industry. The focus then switched to a quick rise of new Covid cases, urging government response.

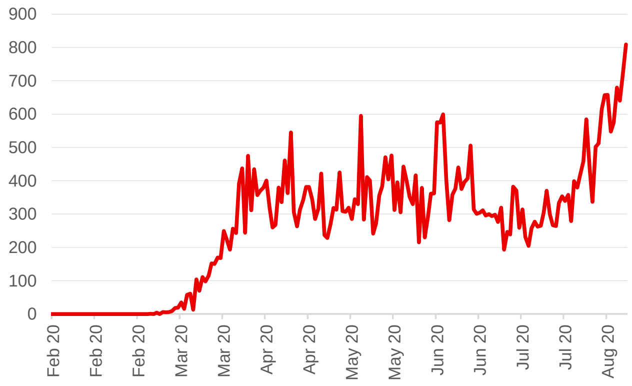
On 8th August **epidemic restrictions will be reintroduced** in some powiats (second-level local government units). Powiats will be divided into three classes: "red" the most threatened, "yellow" the medium threatened and "green" least threatened. The "colours" are to be updated on a regular basis, with "red" status attained after new infections exceed 12 per 10k people and "yellow" after exceeding 6. In "green" zones there are no changes in restrictions. In "yellow" zones there will be a limit of people in restaurants, congresses, fitness clubs (1 person per 4 m2), in cinemas and at sport events (up to 25% of seats), at private events like weddings (100 people). In "red" zones all congresses, cultural and sports events are to be called off, fitness clubs and cinemas to be closed. There will be limits on number of people in restaurants and churches (1 person per 4 m2), on public transport (50% of seats), on private events like weddings (50 people). Moreover, masks are to be worn in all public places. The "red" list includes 9 powiats with total population above 1 million (2.7% of country's population), producing 2.5% of total PIT income and 1.3% of total CIT income. The "yellow" list includes 10 powiats inhabited by over 800 thousand people (2.1% of country's population), producing 2.2% of PIT income and 1.3% of CIT income.

Polish manufacturing PMI rose again in July, to 52.8pts from 47.2 pts, the highest reading in almost two years and much above the long-term average of 50.3pts. Current output and new orders components increased, resulting in the first indication in 20 months that purchasing activity went up. The report signals however that external demand rose only marginally and that manufacturers kept adjusting their staff numbers down despite improved current activity, albeit the levels of the PMI employment index are already back to the pre-crisis trend. The impact of suppliers' delivery times (+0.6 pts) was not key to the further July rebound. The July PMI report seems to confirm a V-shaped rebound.

Complementing the positive picture, the data from most important partners for Polish industry also came better than expected. Final July manufacturing PMI readings for the euro zone and Germany added 0.7pp to 51.8pt and 1.0pp to 51.0 flash estimates, respectively (and these flash estimates were already above expectations at the time of their release). June Germany factory orders (at -11.3% y/y) were over 6pp better than expected. There were more better-than-expected data from Germany: exports and industrial production rebounded in m/m terms even more than in May – exports by 14.9% after 8.9% and output by 8.9% after 7.4%.

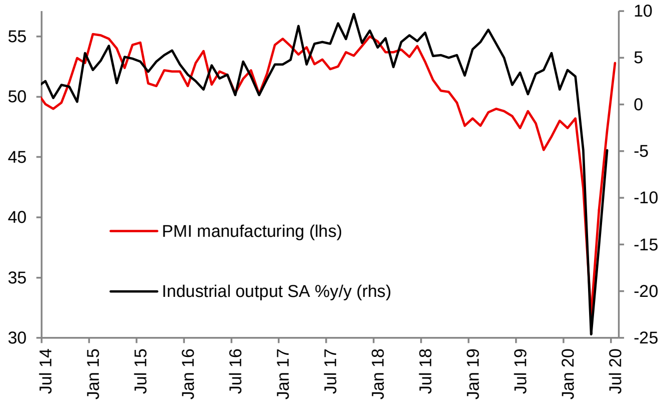
General government sector deficit in Q1 2020 stood at PLN -14.7bn, after PLN +14.4bn in Q1 2019. Looking at the budget data it seems that worsening of the GG deficit was only to a little extent attributable to the increase of the deficit of the central budget (PLN -9.4bn in Q1 2020 vs PLN -4.5bn in Q1 2019). This quarter was the worst Q1 since the data are available (1999). In our opinion, the GG deficit for the whole year might increase significantly above PLN200bn.

New daily cases of COVID-19 in Poland



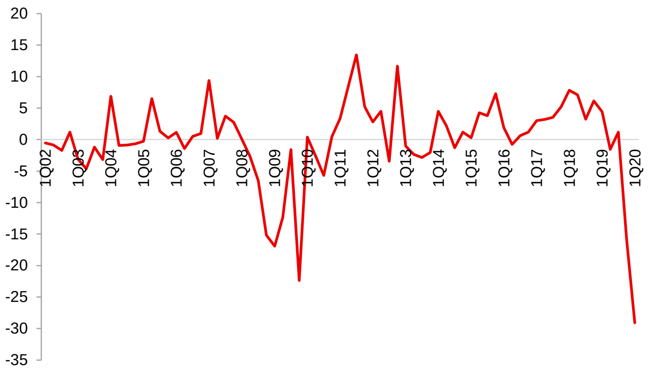
Source: Ministry of Health, Santander

Polish manufacturing PMI vs industrial output



Source: GUS, Bloomberg, Santander

General government balance, y/y change in PLNbn



Source: Eurostat, Santander

FX and FI market

Last week on the market

FX The passing week encompassed first trading days of the new month. EURPLN, currently at 4.413, has barely changed week on week, however in the meantime fell to and briefly remained below the 4.40 level (0.6% lower). The EURUSD kept increasing, however, and this lead to even lower USDPLN – currently at 3.729, or -0,5% over week. The realized volatility of the EURPLN has been very low (around 4% annualized) which is not surprising given lack of significant macroeconomic publications.

As for the other regional currencies, both forint and koruna lost vs euro by 0.7% and 0.2% respectively. Macroeconomic data in Hungary mostly beat estimates (PMI manufacturing at 50.8, industrial production) except for the retail sales. In Czechia CNB has left rates unchanged while the data were relatively weak (PMI manufacturing at 47.0, retail sales). USDRUB fell 0.75% with likely reasons being higher oil (Brent +4% w/w) and significant improvement in PMI services which beat estimates by a noticeable 8.4pp (to 58.5).

FI Polish bond yields have not changed much over week even with stronger than expected Polish manufacturing PMI (increase by 5.6pp to 52.8). 10Y bond yields close the week at 1.29% in the meantime having traded in the 1.26%-1.31% narrow range. Front end of the bond curve remained unchanged (2Y at 0,10%), however 1Y IRS and FRA (e.g. 9x12) declined by 2-3pb possibly catching up or hedging against the gradual decline in the 3 month Wibor.

The Ministry of Finance at a switch auction sold bonds of six series (OK0423, PS0425, WZ0525, WZ1129, DS1030) for PLN3.54bn. It bought back DS1020, WZ0121, PS0421, OK0521 worth PLN3.48bn in total. What is more, the ministry informed that at the end of July it held PLN127bn on its PLN and foreign exchange accounts..

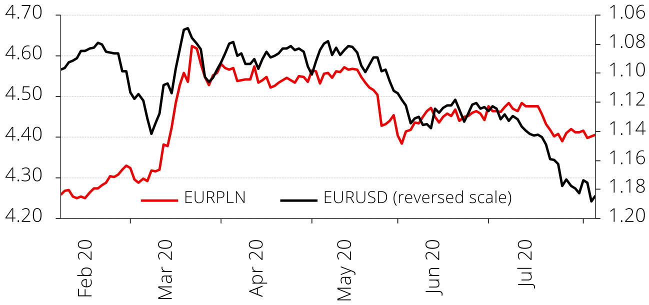
Key event of the upcoming week could be the Friday publication of Polish Q2 GDP where we expect a decline of -11.7 y/y (vs market consensus of -9.0%) and final July CPI reading (3.1% y/y). On Thursday current account data will be published. Abroad, in Germany August ZEW will be published on Tuesday and inflation on Thursday. In the Eurozone industrial production on Wedesday and Q2 GDP on Friday. In the US July inflation (Wednesday), retail sales and industrial production (Friday).

Market implications

FX In the upcoming week, due to subdued trading activity related to the to summer holiday period we expect EURPLN to remain in the 4.40-4.44 narrow range. There is however a non-negligible likelihood of the EURPLN move higher. Here is why: firstly, we perceive the dollar weakness (lost 5% in July alone) as stretched, and expect the dollar strengthening in the short term. Were it to happen, the EM currencies, including the zloty, would depreciate a bit. Secondly, seasonality analysis on EURPLN suggests that the month of August is usually the one in which EURPLN increases. Given still high uncertainty in the macroeconomic data being published (current account, GDP, CPI) only if the actual number significantly deviates from the market consensus will it have a chance to impact the zloty.

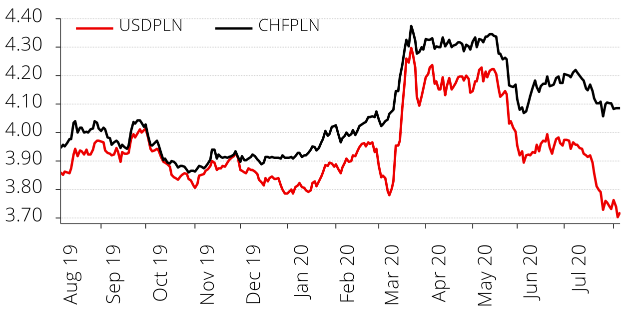
FI The front end of the bond curve is likely to remain stable as the bond yields (2Y at 0.10%) seem to have found a temporary equilibrium. Front end IRS and FRA however may continue a slow grind lower. At the long end of the bond curve yields are likely to depend fully on the core markets (with spread to Bund stable at slightly above 180bp). Polish Development Fund (PFR) informed that the next issuance of its bonds will be on August 13 (so next Thursday, usually these auctions were held on Fridays). PFR will offer 7Y and 10Y bonds with planned supply of PLN3-5bn. PFR issued bonds worth PLN62bn so far and according to its July indications, the whole program could reachPLN85-90bn.

EURPLN and EURUSD



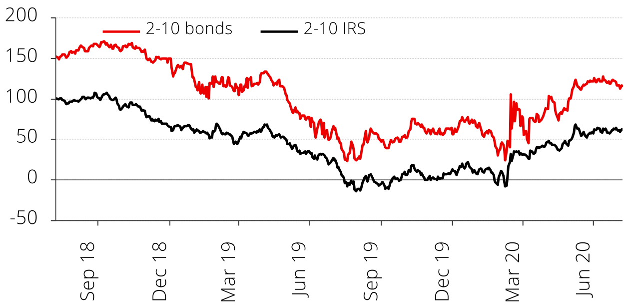
Source: Refinitiv Datastream, Santander Bank Polska

USDPLN and CHFPLN



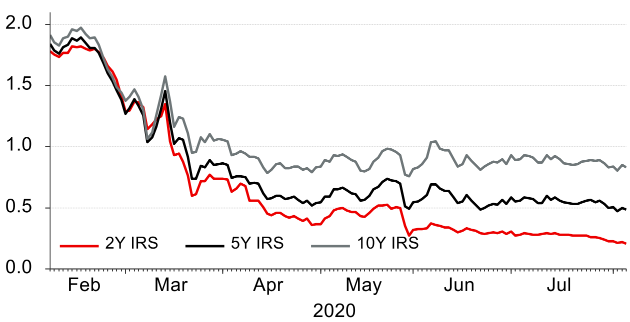
Source: Refinitiv Datastream, Santander Bank Polska

Slope of Polish curves



Source: Refinitiv Datastream, Santander Bank Polska

Poland IRS



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
		TUESDAY (11 August)					
09:00	HU	CPI	Jul	% y/y	3.4		2.9
11:00	DE	ZEW Survey Current Situation	Aug	pts	-69.5		-80.9
		WEDNESDAY (12 August)					
11:00	EZ	Industrial Production SA	Jun	% m/m	12.0		12.4
14:30	US	CPI	Jul	% m/m	0.3		0.6
		THURSDAY (13 August)					
08:00	DE	HICP	Jul	% m/m	0.0		-0.5
09:00	CZ	CPI	Jul	% y/y	3.1		3.3
14:00	**PL**	**Current Account Balance**	**Jun**	**€mn**	**2074**	**1767**	**2455**
14:00	**PL**	**Trade Balance**	**Jun**	**€mn**	**1148**	**1059.0**	**1250**
14:00	**PL**	**Exports**	**Jun**	**€mn**	**17691**	**18099**	**15700**
14:00	**PL**	**Imports**	**Jun**	**€mn**	**16474**	**17040**	**14450**
14:30	US	Initial Jobless Claims	Aug.20	k	1400		1186
		FRIDAY (14 August)					
09:00	HU	GDP	2Q	% y/y	-10.7		2.2
10:00	**PL**	**CPI**	**Jul**	**% y/y**	**-**	**3.14**	**3.1**
10:00	**PL**	**GDP**	**2Q**	**% y/y**	**-9.0**	**-11.7**	**2.0**
11:00	EZ	GDP SA	2Q	% y/y	-15.0		-15.0
14:30	US	Retail Sales Advance	Jul	% m/m	1.65		7.5
15:15	US	Industrial Production	Jul	% m/m	2.7		5.41
16:00	US	Michigan index	Aug	pts	71.0		72.5

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

Additional information is available on request. Please contact Santander Bank Polska S.A. Financial Management Division. Economic Analysis Department. al. Jana Pawła II 17. 00-854 Warsaw. Poland. phone +48 22 534 18 87. email ekonomia@santander.pl. http://www.santander.pl.