21 August 2020

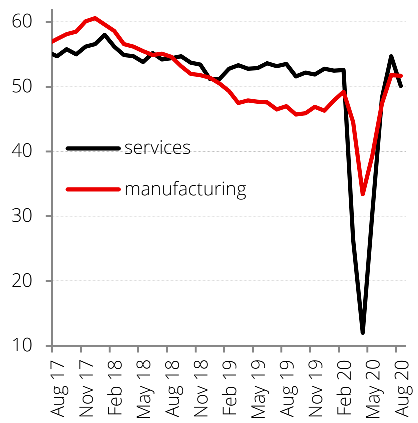
Weekly Economic Update

Nice data plus a fly in the ointment

What's hot next week

- First hard data from the third quarter, i.e. July's readings of wages, output in industry and retail sales were generally aligned with our view that they will surprise to the upside. However, there were some numbers, which cooled our eagerness to revise the 2020 economic growth path more than it has resulted from the flash 2Q GDP data (which came much above our estimate). First, construction output dropped by a whole 5 percentage points more than the market had expected. Second, August consumer and business confidence showed worries about future – it seems optimism is unlikely to return to pre-covid levels just like that. A similar conclusion could be drawn from flash August PMIs for the euro zone services.
- Among the incoming data the LFS unemployment could prove the most interesting one (quarterly data) – this measure of readiness to take up a job in 1Q did not really react to the crisis and the 2Q reading can draw picture differing from registered unemployment data. We are expecting a further acceleration in M3 money supply. Minutes from the July MPC meeting, due for release on Friday are unlikely to reveal new discussions in the Council: most central bankers stick to the view that rates should remain unchanged in 2020 and 2021, while the minority would see rates going up next year, but not above the pre-covid level.
- If one wants to follow central bankers' views with market-moving potential, then we suggest focusing on Jackson Hole symposium, and Jerome Powell's speech in particular where he is to discuss a new communication strategy of the Fed.

Euro zone PMI indexes



Source:: Bloomberg, Santander

Market implications

- EURPLN currently still resides near the 200 day moving average and this despite a few positive macroeconomic data in a row. We interpret this behaviour as a sign that indicates that EURPLN is oversold. We think in the nearest time the balance of risks points to higher probability of EURPLN rise (especially in the coming week). The lack of significant macroeconomic data in the coming week implies that the local bond yields are likely to follow those at the core markets closely.

Economic Analysis Department:

al. Jana Pawła II 17, 00-854 Warszawa
email: ekonomia@santander.pl
website www: skarb.santander.pl
Piotr Bielski +48 22 534 18 87
Marcin Luziński +48 22 534 18 85
Grzegorz Ogonek +48 22 534 19 23
Wojciech Mazurkiewicz +48 22 534 18 86
Marcin Sulewski, CFA +48 22 534 18 84

Last week in economy

The first hard data for 3Q offered many positive surprises. However, the survey-based indexes for August signalled renewed worries of consumers and doubts in some sector about the outlook.

Retail sales grew by 3.0% in July vs -1.3% in June, in line with our forecast (2.8%) and above the market consensus (-0.7% y/y). Retail sales turned positive on an annual basis for the first time since pre-epidemic February. We think however that some factors pushing sales up are temporary and effects of end of stimulus are likely to jump in, making us expect the retail sales to show only a slight improvement in the months to come. **Construction output** dropped much more than expected, 10.9% y/y vs 5.5% consensus. While housing construction output was still recording high growth rates, the indicator of running projects in housing was also depressed. August **business sentiment** indexes improved again in all sectors, but with some expectations components deteriorating. More in Economic Comment.

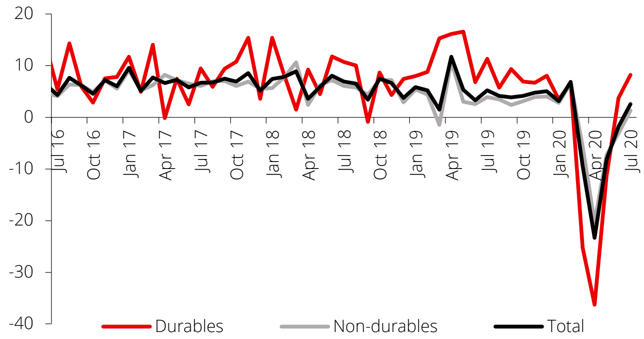
July's **industrial output** rose by 1.1% y/y, less than our optimistic forecast (+3.7%), but above market expectations of a decline (-1.2%). Industry came above the water also in seasonally-adjusted terms, showing +0.2% y/y and +6.2% m/m. While we are expecting a further recovery in industry in the months to come, it will become more demanding: economic situation in Poland's main economic partners is likely to improve but remain subdued, and this could weigh on sectors producing intermediate goods, while enhanced demand for durable consumer goods is probable to be satiated soon. More in Economic Comment.

In July **employment** in the corporate sector was down only 2.3% y/y vs -3.0% y/y consensus and our -3.1% call. In m/m terms, employment rose by 66k, the most ever, ex Januaries. **Wage** growth accelerated to 3.8% y/y from 3.6% while market expected it to slow to 3.4%. While these numbers are quite promising in regard to private consumption outlook, the **consumer confidence** deteriorated in August, most probably due to rising Covid-19 restrictions. The latter factor could be a risk factor for the consumption recovery in Poland. More in Economic Comment.

After July, the **central budget deficit** stood at PLN 16.3bn, which is a slight improvement versus June (PLN 17.1bn). Tax incomes are slightly better than expected. Especially optimistic are incomes from the VAT (+9.5% y/y, the first positive reading since Feb), which might indicate a quick rebound of the economic activity and/or that Ministry of Finance has used up the ability to quicken tax returns.

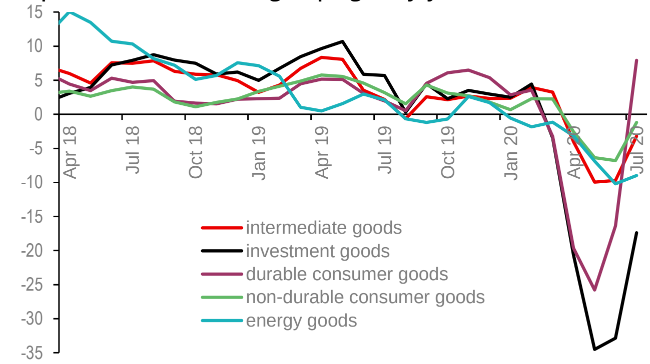
The government has proposed **amendment to the 2020 budget**. It increased the budget limit to PLN109.3bn (4.9% of GDP) from zero planned earlier. Budget incomes were planned at PLN398.7bn (PLN36.7bn less than in the original version), more or less in line with our expectations. Spending was planned at PLN508bn, i.e. by PLN72.7bn more than in the previous version. It is worth noting that until July the central budget spending rose only by PLN18.5bn y/y, which means that in August-December period the government is willing to spend PLN256bn as compared to PLN181bn in the corresponding period of 2019 (rise by PLN75bn). We do not yet know how is the government willing to spend these means, given that so far the Covid-related spending (about PLN130bn) was almost completely offshored outside the main budget and the planned sum was almost totally disbursed already. So, either the government wants to leave space in case there is a need to launch a second lifeline package, or is planning to move some spending from 2021 into 2020 in order to reach better fiscal metrics in the future more easily.

Retail sales in constant prices and main components, % y/y



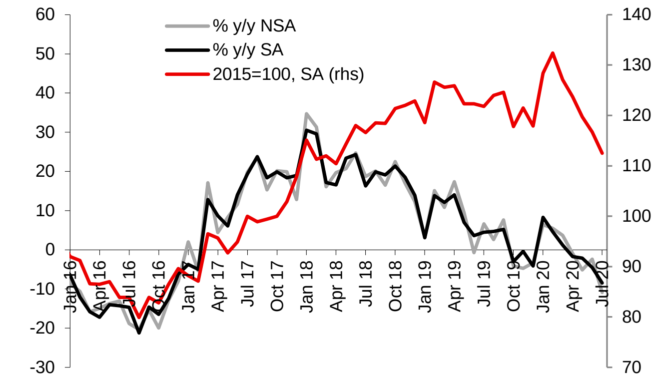
Source: GUS, Santander

Output of main industrial groupings, % y/y



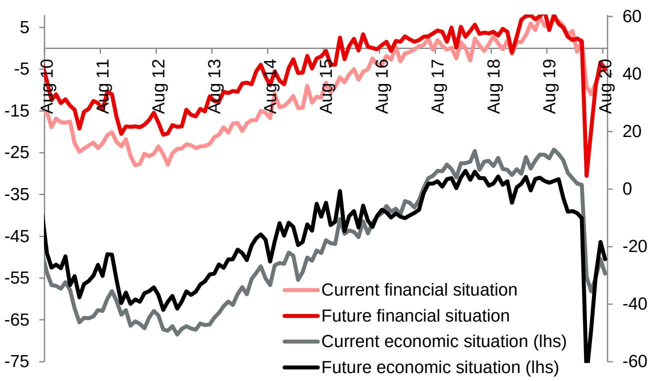
Source: GUS, Santander

Construction output



Source: NBP, Santander

Consumer confidence, selected components



Source: GUS, Santander

FX and FI market

Last week on the market

FX EURPLN was slowly declining in the passing week and ended the week at 4.39, 0.2% lower w/w. In the meantime the pair traded as low as 4.375 (on Wednesday – after decent Polish labour market data) and as high as 4.412 (Wednesday/Thursday evening – after Fed not-so-dovish minutes) however calmed down later in the week and on Friday closed just at the 200 day moving average. EURUSD declined by 0.3% w/w while EURCHF by 0.1% w/w hence the CHFPLN declined but less so – just 0.1% to 4.08, while USDPLN even increased a bit – by 0.1% to 3.716. Thanks to the higher cable (c+0.9%), GBPPLN moved up almost 1 pp to 4.905. Elsewhere in the CEE region, only EURCZK moved lower – by 0.2% to 26.04 – and currently resides at the 200 day moving average as well. EURHUF and USDRUB increased significantly by 1.25% to 350.7 and 74.3, respectively.

FI July core CPI in Poland surprised to the upside and increased to its highest level in years – to 4.3% y/y. As a result of this reading and positive labour market data the FRA contracts started to price in a small chance of rate hikes over the next 2 years (FRA 21x24 to 0.33% vs Wibor 3m at 0.23%) while the IRS curve moved noticeably higher e.g 5Y to 0.66% , 10Y to 1.02% (bond yields increased as well but less so). The behaviour of Polish rates contrasted with that of the core markets where yields declined after some of the data was not as good as hoped (declines in Empire manufacturing, Philly Fed indices and increases in initial jobless claims in the US, for example). As a result the 10Y spread vs Bund widened by 12bp to 184bp.

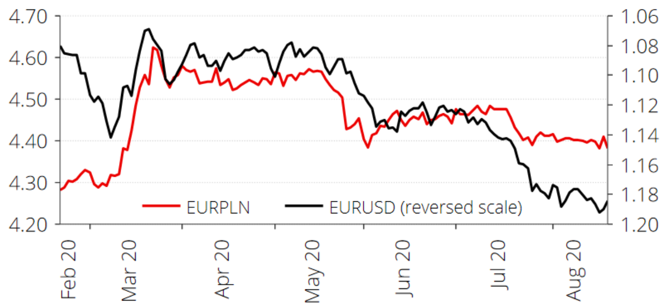
Key event Jackson Hole summit which starts on Thursday and lasts for 2 days is likely to be the most important event. Fed Chair Powell is to speak on Thursday. In Poland NBP minutes are due on Friday, while earlier in the week other data are published like M3 (Monday) and unemployment rate (Tuesday). In Eurozone less busy week data-wise, ESI indices on Thursday. In Germany, final Q2 GDP reading and IFO indices (Tuesday), retail sales (Thursday). In the USA: consumer confidence and new home sales (Tuesday), durables (Wednesday), second Q2 GDP reading, pending home sales (Thursday) and PCE on Friday. Hungarian central bank decides on rates on Tuesday.

Market implications

FX EURPLN comfortably resides near the 200 day moving average. Stronger than expected labour market data have not managed to push the currency pair lower, which we interpret as a sign that the EURPLN has become a bit oversold and is more likely than not to rebound in the nearest future (and the coming week in particular). Also the USDPLN is likely to increase, and even by more, thanks to the likely dollar strengthening before the Jackson Hole summit (only if the Fed chairman Powell delivers on the dovish hopes will the USD resume weakening, in our opinion). The EURPLN up move, if materialises, should not be very significant – the breach of the 4.435 level (50 day moving average) is unlikely in our opinion.

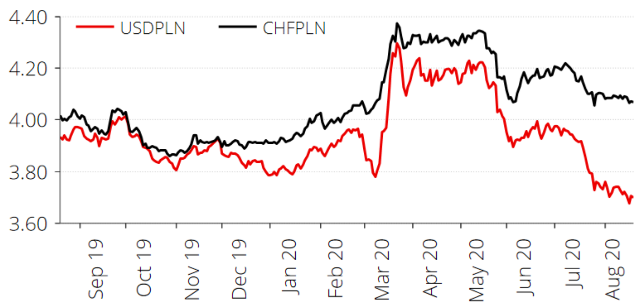
FI Lack of significant data from Poland in the coming week implies that the Polish yield curve is likely to follow core markets, especially at the long end. At the front end of the bond curve the fact that 2Y yields temporarily increased in the passing week (from 0.13% to 0.16% and back) might suggest that the initial demand for short term bonds from the banking sector has been satiated and further yield declines are less likely (the size of the NBP 7-day bills auction has stabilised around PLN170bn). We expect no rate changes over the next 2 years, hence the current 21x24 FRA pricing of some hikes is probably a stretch, but the move back closer to the Wibor3m level does not have to happen next week. As for the long end bonds, as long as the core markets do not move much, there are few reasons to expect POLGBs to move significantly either way. Friday NBP minutes might give some clues about the way the MPC sees evolution of the CPI in the context of pandemic.

EURPLN and EURUSD



Source: Refinitiv Datastream, Santander Bank Polska

USDPLN and CHFPLN

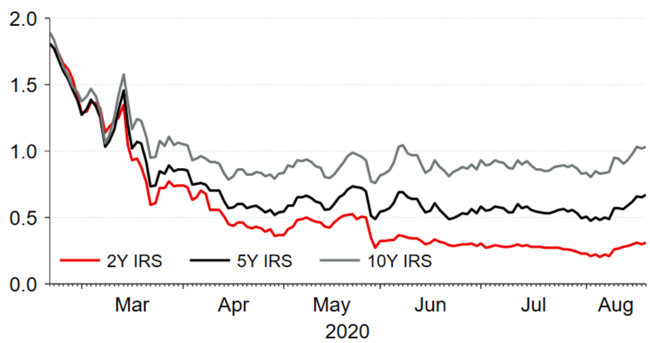


Source: Refinitiv Datastream, Santander Bank Polska

PL-DE bond yield spread

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
			MONDAY (24 August)				
14:00	**PL**	**Money Supply M3**	**Jul**	**% y/y**	**18.5**	**18.6**	**18.1**
			TUESDAY (25 August)				
08:00	DE	GDP WDA	2Q	% y/y	-11.7		-11.7
10:00	DE	IFO Business Climate	Aug	pts	92.5		90.5
10:00	**PL**	**Unemployment Rate**	**Jul**	**%**	**6.1**	**6.1**	**6.1**
14:00	HU	Central Bank Rate Decision	Aug.20	%	0.6		0.6
16:00	US	Consumer Conference Board	Aug	pts	93.0		92.6
16:00	US	New Home Sales	Jul	% m/m	-0.13		13.8
			WEDNESDAY (26 August)				
14:30	US	Durable Goods Orders	Jul	% m/m	4.0		7.6
			THURSDAY (27 August)				
	DE	Retail Sales	Jul	% m/m	0.5		-2.0
14:30	US	GDP Annualized	2Q	% Q/Q	-32.5		-32.9
14:30	US	Initial Jobless Claims	Aug.20	k	920.0		1106.0
16:00	US	Pending Home Sales	Jul	% m/m	5.5		16.6
			FRIDAY (28 August)				
11:00	EZ	ESI	Aug	pct.	85.0		82.3
14:00	**PL**	**MPC minutes**	**Jul.14**				
14:30	US	Personal Spending	Jul	% m/m	1.5		5.6
14:30	US	Personal Income	Jul	% m/m	-0.3		-1.1
14:30	US	PCE Deflator SA	Jul	% m/m	0.4		0.4
16:00	US	Michigan index	Aug	pts	72.8		72.8

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.