

02 October 2020

# Weekly Economic Update

## Rising tide

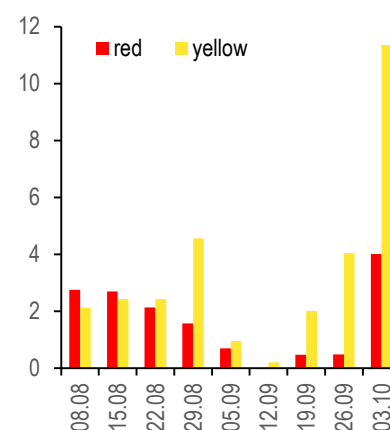
### What's hot next week

- The main theme for markets is still the rising tide of Covid-19 infections and considerations how strongly it may affect economic outlook. Global risk aversion, which triggered EM currencies' selloff at the end of September, has apparently eased in the last few days and it looks like the next few days may see some relief. But it does not mean that the risk factors have disappeared: Covid-19, Brexit, Armenia-Azerbaijan conflict, row about the next round of stimulus in the USA, and now Donald Trump tested positive for coronavirus – if we see negative news in one of those subjects, market volatility may rise again.
- Calendar of data releases is not particularly thick, but we will see some information abroad hinting on the pace of economic revival, including: services PMI/ISM, data about production and retail sales in Europe (incl. Germany, Czechia, UK). Also, Fed and ECB minutes will be released.
- Agenda in Poland includes only the MPC meeting, which is unlikely to bring any change in monetary policy. The advocates of keeping interest rates stable for a long time are still in majority, we think. For investors it will be interesting whether the MPC will refer in any way to the recent currency depreciation (as the currency selloff in Hungary has pushed the central bank towards the unexpected rate hike recently). We think the MPC is still very far from worrying about zloty weakness. First of all, the depreciation was not very significant and not persistent, secondly the MPC was in fact worried a few months ago about the insufficient zloty depreciation, worsening the economic outlook.

### Market implications

- Zloty and other CEE currencies have regained much of the late September losses. In case there would be no yet another wave of risk aversion globally, EURPLN should stabilize close to 4.48 in the coming days, in our opinion.
- On the fixed income market, the relative steepness of the Polish yield curve, lower core market yields as well as low supply of the POLGBs help long end yields to remain stable and head lower. Of the factors which might possibly stop or even reverse the move would be a signal of less dovish MPC (not very likely) or a fresh wave of a global EM bond sell-off.

Share of Poland's population in yellow and red zones, %



Source: Health Ministry, Santander

### 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

Inflation refused to fall in September and its persistence most likely came from core components. Industrial sentiment indicators suggested the rebound kept losing steam in September.

**September CPI** was 3.2% y/y, up from 2.9%. Data imply a rise of core inflation is to c4.2% y/y from 4.0% and this comes as the biggest surprise of this release as it seemed after August data that the core measure embarked on a downward trend, depressed by reduced domestic demand. This means that core inflation may end the year closer to 3.5% than 3% we indicated earlier, and headline CPI is still likely to be much lower in 2021 than this year, pressured by negative output gap. The starting point will be higher than we previously thought though.

**Polish manufacturing PMI** improved only marginally in September, to 50.8 from 50.6 seen in August. Subindices of employment, new orders and stock purchases improved slightly, while output and delivery times subindices worsened. Production was up but only marginally, supported by slight export expansion. Labour market improved, with the first employment rise recorded since June 2019. Cost inflation eased slightly but remained high, partly due to weaker PLN, while prices of finished goods rose for the first time in 6 months. Overall, the survey confirms that the pace of recovery in Polish manufacturing slowed down at the end of 3Q.

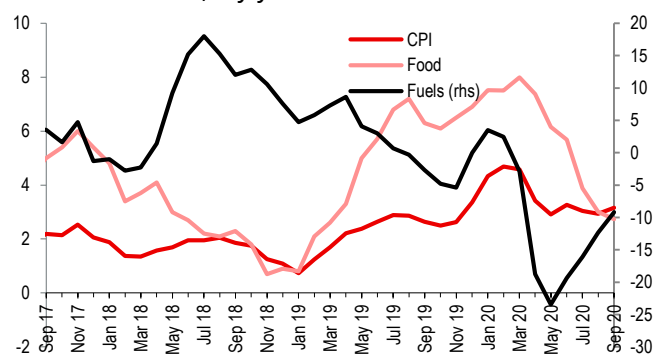
**The ESI economic sentiment** indices for Poland showed a further improvement in business sectors, especially in services and retail trade. The improvement in the manufacturing was modest – the much better assessment of the current trend was accompanied by the lack of improvement in new orders. Current activity was seen as improving in both the construction and retail trade sectors. The consumer sentiment worsened, mostly due to deterioration in the current financial situation (the worst reading in almost 6 years) and economic one (worst since 2004, or 16 years).

NBP revised the **balance of payments** data since 2004. Almost the entire data series saw an upward revision of goods imports, which dragged the total C/A balance down by about 0.3% of GDP each year until 2018. 2019 saw an downward revision of services exports and upward of primary incomes, improving the whole balance by EUR0.4bn. Total sum of errors and omissions balance improved to -EUR58bn from -EUR72bn. Export of services in 2Q20 was revised up by €2.2bn, import by €1.3bn, so the change was quite major, exceeding 15%. The data show foreign travel was hit the most – export fell by 64.9% y/y, import by 69.6%. Export of transport services fell 19% y/y, import by 15.8% y/y. IT services proved immune to pandemic – export rose 1.9% y/y, import 6.7% y/y. This month there will be a benchmark revision of GDP data and the changes described above suggest lower GDP growth in 2019 and higher in 1H20. Note however that we have no information about revisions in other categories.

Poland's **gross external debt** rose in 2Q20 to 57.1% of GDP from 56.4% in 1Q20, while **net investment position** fell to -44.4% of GDP from -44.1%. Deterioration of both statistics was due to lower denominator (nominal GDP), while nominator improved.

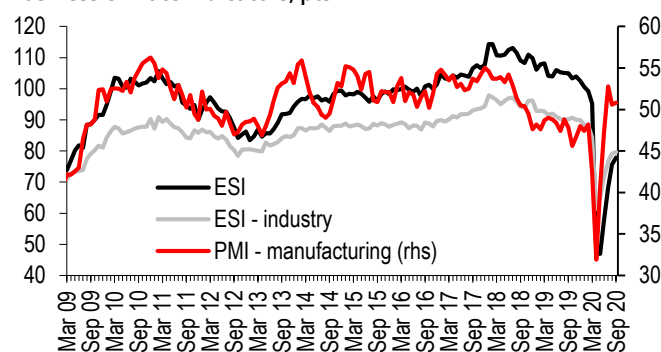
According to the **MPC's Eryk Łon** it is important for the "interest rates to remain at a moderate level", which will support investments. He added that lack of rate hikes will help the zloty to remain at the weak level, which will support exports. It is intriguing that the lowest NBP rate level in history at 0.10% is barely "moderate" for Mr. Eryk Łon. Jerzy Kropiwnicki said that rate cuts have had only mediocre impact and repeated that in mid-2021 the MPC should consider hikes. Proponents of rate are currently in minority in the MPC and we do not think it would be likely for them to gather a majority next year

Inflation measures, % y/y



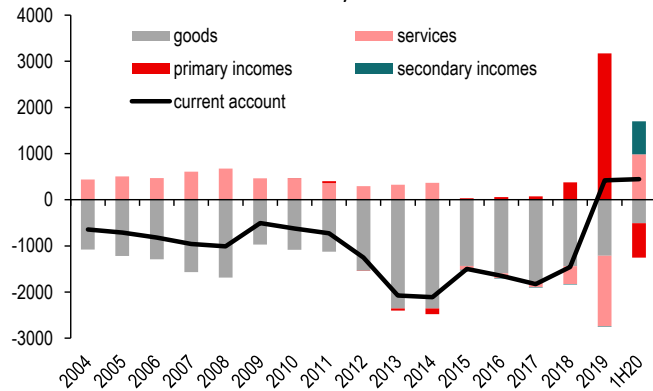
Source: GUS, Santander

Business climate indicators, pts



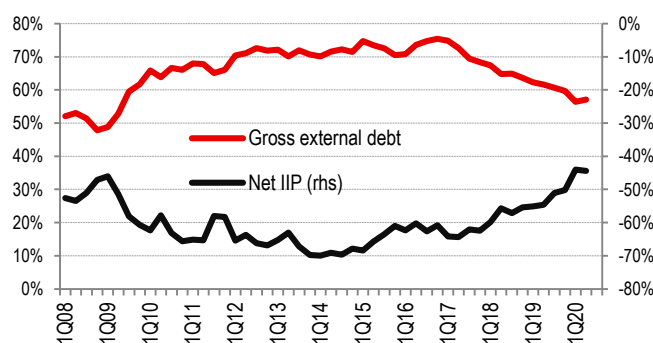
Source: Markit, European Commission, Santander

Revision of current account data, EURmn



Source: NBP, Santander

Gross external debt and net international investment position, % of GDP



Source: GUS, NBP, Santander

## FX and FI market

### Last week on the market

**FX** The last five sessions were quite volatile on the Polish FX market. EURPLN jumped to 4.60 (only slightly below its 4.63 COVID-peak seen in March) but at the end of the week was at c5.00. USDPLN plummeted to 3.83 from weekly high of 3.94, CHFPLN to 4.17 from 4.26 and GBPPLN to 4.95 from 5.06. In the first part of the week, the zloty was pressured by the still unstable global market mood and Armenia-Azerbaijan fights that weighed on the ruble and Turkish lira and in turn deteriorated mood in the CEE region. In the next days, when the global stocks rose, the zloty got an additional boost from the higher-than-expected Poland flash September CPI.

**FI** Domestic IRS rose 5-6bp while the bond yields remained near their recent low or even continued to decline. The 10Y bond closed the week near 1.32%, c5bp above its local support (August low). The 5Y bond yield fell c10bp on weekly basis to its new all-time-low of c0.55%. The 10Y PL-DE bond yield spread is fluctuating around 185bp since mid-June and nothing has changed in this regard last week. Polish 2-10 IRS and bond yield spreads remained at an elevated levels.

The Ministry of Finance announced its bond supply plan for 4Q20. In the final three months of the year, the Ministry plans only one standard auction (for PLN5bn) and four-five switch auctions. Two of them will take place this month: 8 and 22 of October.

**Key factor** for the market to follow shall not change at least in the next few days. Pandemic dynamics might determine the performance of risky assets but we think that the potential negative impact of the number of new COVID-19 cases is diminishing.

On the macro data front, we will see September services ISM for the US and PMI for the euro zone. In August, services indexes fell slightly and this might have continued in September. The FOMC will release its minutes from the last meeting.

In the CEE region, Polish MPC will hold a rate-decision meeting and some macro data will be released in Czechia and Hungary. After the recent zloty weakening, we may see less reference to the exchange rate in the post-meeting statement.

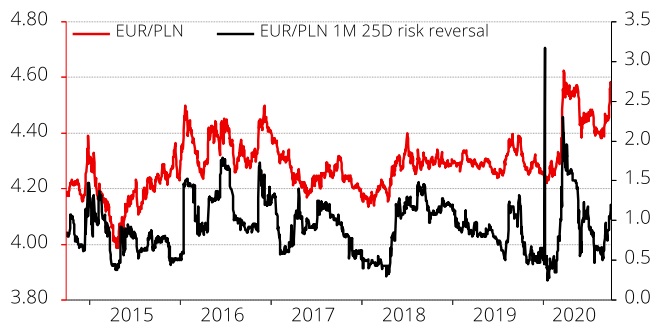
### Market implications

**FX** EURPLN, EURCZK, EURHUF and USDRUB have recently reached or were only slightly below their multi-month peaks reached in March during the full-blown global risk aversion driven by the coronavirus pandemic outbreak. Noticeable recovery seen at the end of this week suggests that the CEE currencies sell-off was utilized by investors for purchase. In our view, regional currencies at levels seen in March was not coherent with the main global stock indexes suffering a down correction that was smaller than the previous ones or paused at important support levels. Also, EUR/USD returned above the 1.17 support level that it broke in the previous week.

The abovementioned global circumstances may create a supportive environment for the zloty and its CEE peers at least in the short term, in our view. Also, the recent Polish CPI print, together with deposit rate hike in Hungary and no rate cut in Russia, may also work in favour of the CEE currencies in the coming days. In the coming days we expect EURPLN to stabilize near 4.48.

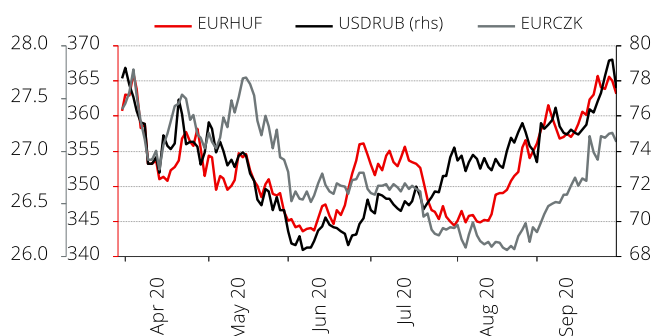
**FI** Relative steepness of the Polish bond curve (compared to Bund and Treasuries) still favours lower yields on the long end. However, if the positive mood stays on the global market, the German bond yields may climb somewhat preventing Polish 10Y benchmark from a bigger strengthening. We think the 10Y bond yield may stay above 1.25% in the coming days though the room for an increase looks limited thanks to the scarce bond issuance plans for 4Q20.

### EURPLN and risk reversal implied volatility



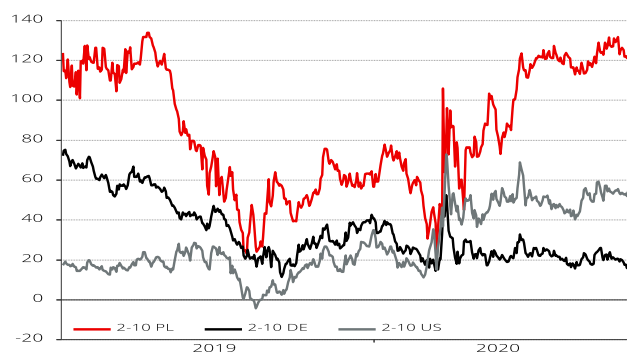
Source: Refinitiv Datastream, Santander Bank Polska

### EURHUF, EURCZK and USDRUB



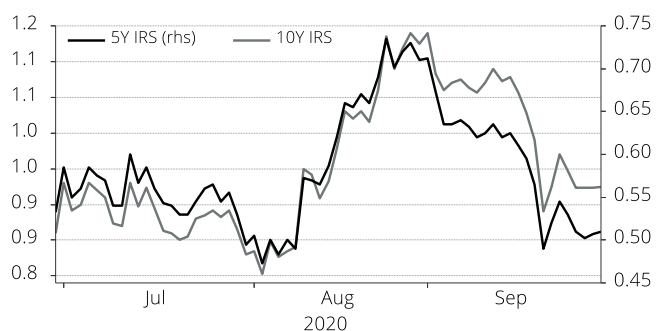
Source: Refinitiv Datastream, Santander Bank Polska

### Slope of the bond curves



Source: Refinitiv Datastream, Santander Bank Polska

### Poland IRS



Source: Refinitiv Datastream, Santander Bank Polska

## Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD	FORECAST		LAST VALUE
				MARKET	SANTANDER	
<b>MONDAY (5 October)</b>						
09:55	DE	Markit Germany Services PMI	Sep	pts	49.1	49.1
10:00	EZ	Eurozone Services PMI	Sep	pts	47.8	47.6
11:00	EZ	Retail Sales	Aug	% m/m	2.5	-1.3
16:00	US	ISM services	Sep	pts	56.3	56.9
<b>TUESDAY (6 October)</b>						
08:00	DE	Factory Orders	Aug	% m/m	3.0	2.8
09:00	HU	Industrial Production SA	Aug	% y/y	-3.0	-7.71
<b>WEDNESDAY (7 October)</b>						
	<b>PL</b>	<b>MPC decision</b>		<b>%</b>	<b>0.1</b>	<b>0.1</b>
08:00	DE	Industrial Production SA	Aug	% m/m	1.95	1.2
09:00	CZ	Industrial Production	Aug	% y/y	-6.2	-4.9
20:00	US	FOMC Meeting Minutes	Sep.20		-	0.0
<b>THURSDAY (8 October)</b>						
03:45	CN	Caixin China PMI Services	Sep	pts	54.25	54.0
08:00	DE	Exports SA	Aug	% m/m	0.0	4.7
09:00	HU	CPI	Sep	% y/y	3.8	3.9
14:30	US	Initial Jobless Claims	Oct.20	k	850.0	837.0

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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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.