Weekly Economic Update

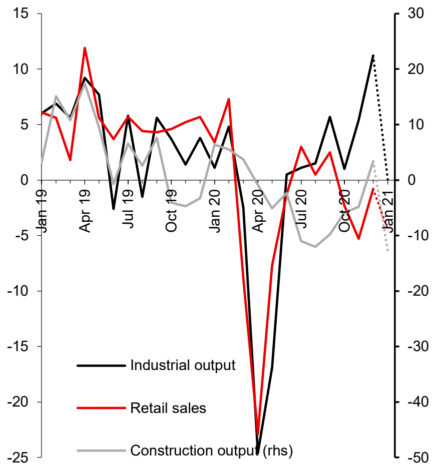
12 February 2021

Week of important data

What's hot next week

- Week packed with **important data ahead**. Abroad we will get to see a lot of economic activity indices: new GDP releases for 4Q20 in Europe, results of industry and retail trade in Europe and the USA, US housing market numbers and flash PMIs to conclude the week, and these will show the February reaction of managers' sentiments to prolonging troubles with the pandemic (the consensus sees some deterioration of moods).
- In Poland, the week will start with **CPI inflation and balance of payments**, then **wages and employment, output in industry and construction, retail sales, PPI inflation.**
- Our forecast of January CPI (2.7% y/y) is well above the market consensus (more details here) which means **Polish inflation would fit the trend of the above-expectations CPI readings in Europe**. In Poland, this would be largely owing to higher fees and taxes effective since the start of the year. On the other hand, **our forecasts of industrial and construction output are well below the market expectations** (strong effect of the number of working days effect that has been obviously underestimated by the other analysts). While we do doubt that these releases will set the trends for the rest of the year – we expect inflation to stay close to the target and industrial and construction output to regain momentum – they might cause temporary fluctuations of market sentiment. Our intuition tells us that at in the current circumstances an upside surprise with inflation could be more meaningful to investors than weak output.

Output and sales, % y/y



Source: GUS, Santander

Market implications

- Monday's above-consensus inflation could support the zloty. Longer appreciation impulse could be prevented by the risk of an another central bank intervention, but EURPLN may ease somewhat, at least at the start of the week.
- Polish bond yields and IRS jumped in the last weeks, partly following the core markets and so some extent amid unwinding bets for negative interest rates in Poland after the comments of the central bank's governor and recent decent macro data. High inflation reading could boost reflation trend, particularly it yields abroad stay in the up-trend. On the other hand, after a substantial rise of yields we should finally see a bigger demand from banks and the Thursday's auction could be a good opportunity to do so.

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

Last week we got to see flash 4Q20 GDP data, some data on fiscal performance in 2020 as well as new forecasts of the European Commission and IMF recommendations for Poland.

According to flash estimate, **GDP growth** was at -2.8% y/y in 4Q20 vs -1.5% y/y in 3Q and -8.4% in 2Q, confirming that the second dip was much shallower than the first one. The flash release did not offer the growth breakdown, but the whole-year estimate suggested that private consumption growth turned negative again in 4Q but to a much lesser extent than in spring (c.-3% y/y vs -10.8% in 2Q), while fixed investments were still falling at a similar pace as in 2Q (-10.7% y/y). The full GDP data for 4Q20 will be released on 26 February. The spread of the pandemic in 1Q and the January trade restrictions might make the 1Q21 show only a limited rebound, to c.-2% y/y. We may need to wait for strong economic revival until 2H21, but this still requires the vaccination rollout to accelerate to a level that removes much uncertainty regarding future lockdowns. Our full-year 2021 growth forecast sits at 4.6%.

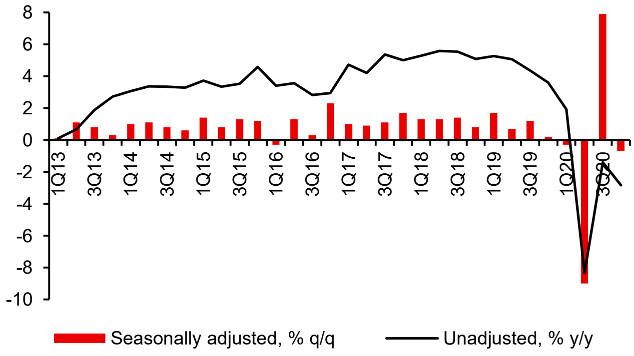
According to new **European Commission forecasts** (link), the short term economic outlook is worse than indicated in the Autumn round, but the longer term economic outlook improved due to start of the vaccination rollout. As a result, 2021 GDP growth forecast of EU countries went mostly down, while 2022 GDP forecasts went up. Polish 2021 GDP growth forecast went down to 3.1% from 3.3%, but 2022 growth was increased to 5.1% from 3.5%, it is worth noting that the forecasts do not include the impact of the Next Generation EU package. As for the inflation, the 2021 HICP figure was moved up to 2.3% from 2.0%, while the one for 2022 went down to 2.9% from 3.1%.

IMF presented its article IV report on Poland (link). The report recommended to use the available large fiscal space to extend the current support to sectors not affected directly by the pandemic. Monetary policy should remain in the current shape, according to the Fund, until the economic recovery strengthens. Any potential easing should be based on QE extension. IMF recommends to change the banking tax to another instrument in time of post-pandemic recovery, as it distorts the credit supply.

Local governments ended 2020 with PLN5.6bn surplus versus plan of PLN21bn deficit. In 4Q20 their revenues rose by a healthy 6.2% y/y, with CIT adding 7.6% y/y and PIT 5.5% y/y. Spending rose by 2.3% y/y with investment outlays going down by 7.6% y/y (deducting about 1 pp from total investment growth). **The central budget deficit in 2020** equalled PLN85bn, and in December alone it grew by PLN72bn and it was the highest jump for this month ever. This development was mostly caused by a spike in expenditure, which stood at PLN109bn vs the range of PLN40-60bn in a few last Decembers. The entire 2020 revenues stood at PLN419.8bn vs the plan of PLN398.7bn and this improvement is pretty surprising in light of the pandemic and related restrictions. In December alone, the revenues were firm in VAT (increase by c.11% y/y), CIT (up 18.4% y/y however this is a volatile time series) and PIT (up 14.0% y/y). In our opinion, **the general government deficit** stood in 2020 at around 8% GDP, the most since the Global Financial Crisis of 2008.

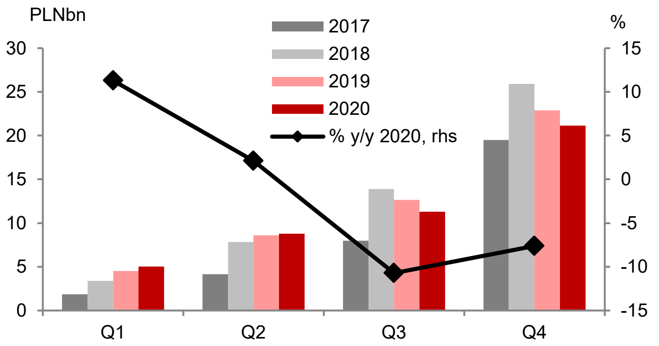
Numerous **MPC members** spoke last week. Łukasz Hardt said that in the case of more lockdowns the central bank should boost the QE size rather than cut interest rates. In the positive scenario, the QE program should be maintained, reserve requirement ratio should be normalized and only then interest rates should be raised but no higher than 0.50% for the main refi rate. Eryk Łon said that it is likely that in 2021 there would be no need for interest rate cuts. If the economic situation deteriorates, rates should be cut and QE programme be extended to cover other asset classes. Grażyna Ancyparowicz said that there are no reasons to expect the inflation rate to rise above the NBP inflation target at 2.5%. Cezary Kochalski thought that the recent data from the economy lower the rate cut probability, but not to zero. He did not support cutting rates below zero, however. Kochalski assumed that the CPI will remain in 1Q21 near the 2.5% NBP target and slightly above the level in the remaining part of the year, but with core CPI declining significantly. We are expecting rates to remain flat in 2021.

GDP growth, % y/y



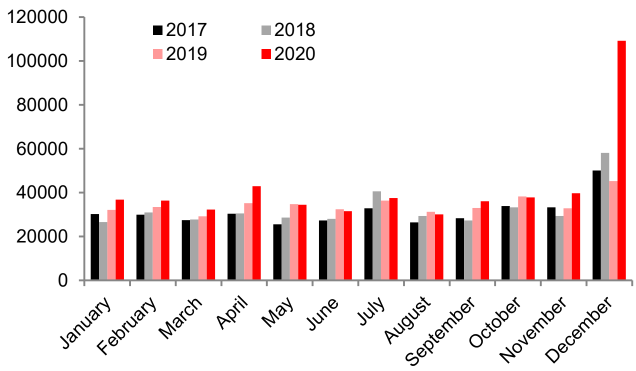
Source: GUS, Santander

Local governments - investment



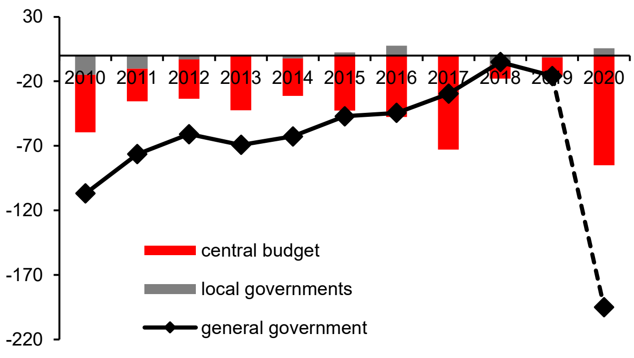
Source: Finance Ministry, Santander

Central government spending by months, PLNbn



Source: Finance Ministry, Santander

Budget balances, PLNbn



Source: Ministry of Finance, Eurostat, Santander

FX and FI market

Last week on the market

FX EURPLN was quite stable hovering within the tight 4.47-4.51 range during the last five sessions with the weekly trading range being the second lowest since April 2020. The zloty's stabilization was coherent with what we have seen in the EUR/USD market – the exchange rate's weekly high-low spread was the third lowest so far this year. USDPLN was hovering in a c1.5% range and closed the week flat at c3.73. The zloty lost somewhat vs the pound (GBPPLN +0.7% to 5.12) and Swiss franc (CHFPLN +1% to 4.17).

Elsewhere in the CEE region, EURCZK down trend observed since the start of the year paused with the exchange rate fluctuating around 25.75. The Czech January CPI beat expectations (2.2% vs 1.7%) but yet well before this release the market has been pricing chances for a rate hike this year in Czechia. Thus, the inflation release failed to provide fresh appreciation impulse for the koruna. EURHUF was trading in a 356-360 range. The Hungarian inflation was in line with the consensus (2.7% y/y). USDRUB fell 0.6% thanks to the rising oil price weaker dollar and higher than in the previous month Russian trade surplus.

FI Polish bond yields remained at an elevated levels reached at the end of the previous week, the 10Y yield stayed close to 1.28%. IRS moved further up slightly with the 10Y rate reaching its fresh YTD high. Dovish signals from the USA (lower than expected CPI, higher weekly jobless claims and Powell's speech) pushed core yields slightly down bringing the 10Y PL-DE bond yield spread to c175bp. Respective asset swap spread remained at -10bp. Since the start of the year, the 2-10 bond spread is trading in a horizontal trend while the IRS curve is steepening with its spread above 100bp (its highest since October 2018).

Key factors for the market in the coming week may be data releases. The passing week's calendar was light while the in next days we will see important data.

Flash February PMIs for the euro zone and Germany will show how the slow progress of vaccinating affects the business mood. The consensus points to only marginal drop of PMIs.

There will be numerous data releases in the USA, with the January retail sales and industrial output, among others.

The market shall remain focused on any news related to distribution of the Covid-19 vaccines.

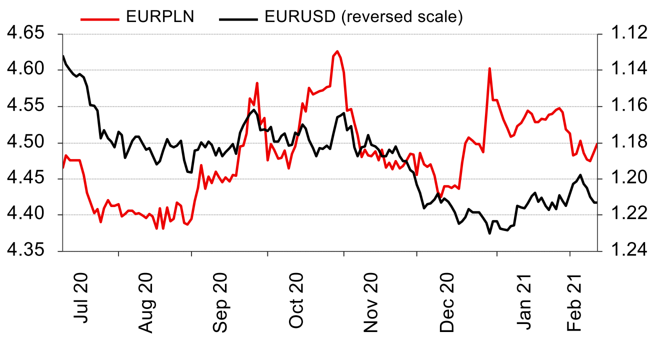
There will be also some data releases in Poland. The most awaited by the market could be the Monday's January CPI – our forecasts (2.7%) is above the consensus (2.4%). On the other hand, our estimate of the industrial output is below of what the market expects.

Market implications

FX EUR/PLN has stabilized in a tight range after the late January drop awaiting the impulse. The Monday's Poland CPI release could support the zloty since after the above-average reading the market may recall NBP's governor comment that rates could go up if needed. However, any EUR/PLN drop after this release should be short-lived. We think the bias for EUR/PLN in the coming weeks is tilted rather to the upside given the risk of the central bank intervention.

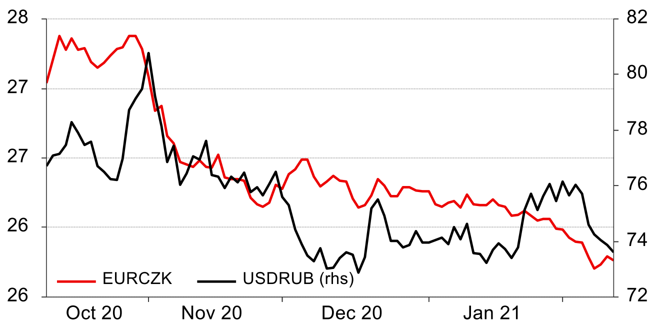
FI Polish rates did not benefit from a slight decline of core yields last week. The 10Y PL-DE bond yield spread has been testing 170bp support but did not manage to break it for good and now we could see some correction. This could actually be the case if Poland January CPI comes above the consensus, like we expect. Thus, we think Polish yields and IRS may stay at an elevated level or even climb slightly further.

EURPLN and EURUSD



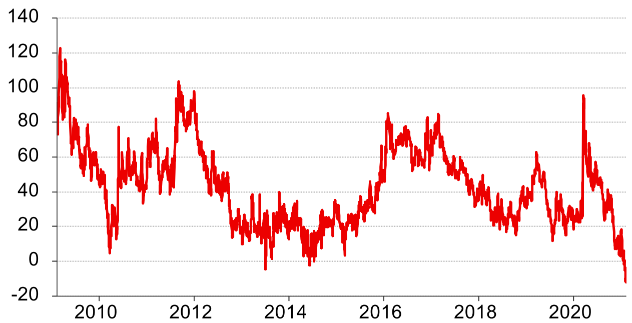
Source: Refinitiv Datastream, Santander Bank Polska

EURCZK and USDRUB



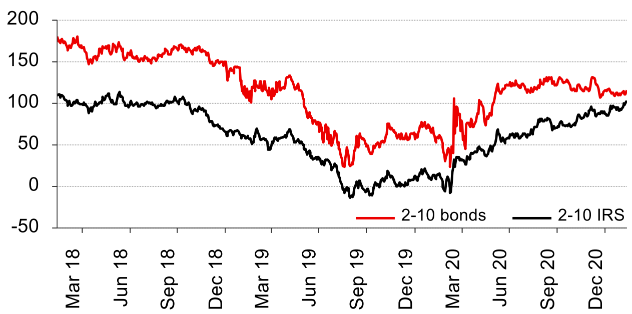
Source: Refinitiv Datastream, Santander Bank Polska

Poland 10Y asset swap spread



Source: Refinitiv Datastream, Santander Bank Polska

Poland 2-10 spreads



Source: Refinitiv Datastream, Santander Bank Polska

Santander

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
			MONDAY (15 February)				
10:00	**PL**	**CPI**	**Jan**	**% y/y**	**2.4**	**2.7**	**2.4**
11:00	EZ	Industrial Production SA	Dec	% m/m	-0.5	-	2.5
14:00	**PL**	**Current Account Balance**	**Dec**	**€mn**	**1 005**	**1085**	**1 725**
14:00	**PL**	**Trade Balance**	**Dec**	**€mn**	**580**	**999**	**1 756**
14:00	**PL**	**Exports**	**Dec**	**€mn**	**19 271**	**19 421**	**22 965**
14:00	**PL**	**Imports**	**Dec**	**€mn**	**18 740**	**18 422**	**21 209**
			TUESDAY (16 February)				
09:00	HU	GDP	4Q	% y/y	-6.0	-	-4.6
11:00	EZ	GDP SA	4Q	% y/y	-5.1	-	-5.1
11:00	DE	ZEW Survey Current Situation	Feb	pts	-66.3	-	-66.4
			WEDNESDAY (17 February)				
10:00	**PL**	**Employment in corporate sector**	**Jan**	**% y/y**	**-1.5**	**-1.3**	**-1.0**
10:00	**PL**	**Average Gross Wages**	**Jan**	**% y/y**	**4.8**	**4.7**	**6.6**
14:30	US	Retail Sales Advance	Jan	% m/m	0.8	-	-0.7
15:15	US	Industrial Production	Jan	% m/m	0.4	-	1.57
20:00	US	FOMC Meeting Minutes					
			THURSDAY (18 February)				
10:00	**PL**	**Sold Industrial Output**	**Jan**	**% y/y**	**1.9**	**0.1**	**11.2**
10:00	**PL**	**PPI**	**Jan**	**% y/y**	**0.4**	**0.5**	**0.0**
11:00	EZ	HICP	Jan	% y/y	0.9	-	0.9
14:30	US	Initial Jobless Claims	week	k	760	-	793
14:30	US	Housing Starts	Jan	% m/m	-1.1	-	5.8
14:30	US	Index Philly Fed	Feb	pts	22.0	-	26.5
			FRIDAY (19 February)				
09:30	DE	Flash Manufacturing PMI	Feb	pts	57.0	-	57.1
09:30	DE	Flash Markit Services PMI	Feb	pts	46.5	-	46.7
10:00	EZ	Flash Manufacturing PMI	Feb	pts	54.6	-	54.8
10:00	EZ	Flash Services PMI	Feb	pts	46.0	-	45.4
10:00	**PL**	**Construction Output**	**Jan**	**% y/y**	**-2.8**	**-12.8**	**3.4**
10:00	**PL**	**Retail Sales Real**	**Jan**	**% y/y**	**-6.6**	**-4.5**	**-0.8**
16:00	US	Existing Home Sales	Jan	% m/m	-3.0	-	0.8

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.