19 February 2021

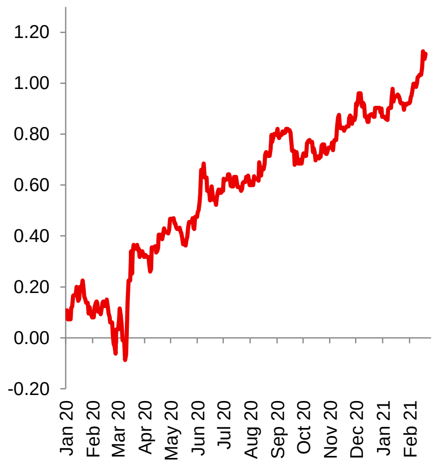
Weekly Economic Update

Forging the package

What's hot next week

- The passing week was full of local macroeconomic data. The yearly dynamics of January retail sales, industrial output and construction output were significantly weaker than the December ones, however this resulted mainly from the negative impact of the working day effects and base effects. After adjusting for seasonality, the dynamics looks decently. That the situation in the Polish economy at the start of the year is better than might seem at first is also supported by the labour market data, which showed that y/y wages fell only within the sectors which were hit the most by the pandemic-related restrictions.
- We already know that the economy is in a decent shape. Next week we will find out how exactly the end of the 2020 looked like. On Friday there is a final reading of Q4 GDP. The preliminary reading showed a contraction of 2.8%, which translated to only a slight decline on a q/q basis. The final reading is unlikely to differ by much from the preliminary one hence its market impact should rather be neutral.
- Abroad there will be **a lot of data from the US**, including consumer sentiment and trends in the real estate sector. The work on the final shape of President Joe Biden's **fiscal package** is under way and soon (it is rumoured to be the first half of March) one should expect to see the actual final version and the start of the implementation process. Recently, both equity and rates markets have already priced in a big chunk of the news, hence the approval of the package might actually be a good reason for markets to correct. Markets will still be watching **how the pandemic situation evolves** and especially how the vaccines get produced, distributed and applied.

PLN IRS rates, 2x10 spread, %



Source: Bloomberg, Santander

Market implications

- **EUR/PLN is likely to trade horizontally for another week in the 4.47-4.51 range**. The global mood is supportive for EM currencies, but investors and traders are reluctant to build larger zloty bullish bets as that might backfire in case NBP returns to the FX market to purchase EURPLN - which in theory can happen anytime as long as EURPLN trades below 4.50. Recall that 4.47 was most likely the level when NBP entered the market for the second round of interventions in late 2020.
- **Polish bond yields and IRS rates are likely to follow global rates markets closely** in the following week as the local macro data are of less importance. Despite some recent hawkish voices from the MPC (Kropiwnicki, Gatnar) we still think the NBP rates will remain unchanged, with the main one at 0.1%, till the end of the current MPC's term (early 2022). Hence the long end of the Polish IRS and bond yield curve might react the most to the global reflationary trend.

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Last week in economy

Inflation beat market consensus in line with our view. Retail sales and construction showed strong drops. Industrial output was depressed by calendar effects and employment registered a worrying decline.

Polish **January CPI** inflation hit 2.7% y/y, in line with our forecast and above market expectations (2.4% y/y). Based on the limited available information, we estimate that inflation went up mostly due to hike in petrol prices, electricity tariffs and higher core inflation (we believe it rebounded to 4.0% vs 3.7% in December). In our view, in the upcoming months the CPI will oscillate around the NBP target (2.5%), with a possible jump towards 3.0% in April. Find more here. **PPI** climbed to 0.7% y/y in January from 0.1% on weaker PLN and higher commodity prices, but the core part of the index also accelerated.

In January Polish **industrial output** rose by 0.9% y/y vs market expectations at 1.9% and our 0.1% forecast. In SA terms production was up 5.7% y/y, less than in December (7.1%), but more than in any other month of 2020. We think the industry could post a double-digit growth on average this year. Find more here.

Construction fell by 10.0% y/y in January vs our call at -12.8% y/y, market consensus at -2.8% y/y and previous reading at +3.4% y/y. The reading looks very disappointing but actually it is not: the output was dragged lower by the negative working day effect and by the high statistical base effect. We think that output in construction will continue to post negative annual growth rates in the nearest months, but should improve in 2H21 as investment will be reviving.

In January, Polish **retail sales** dropped by 6% y/y in real terms. The market had expected -6.6% y/y and we -4.5%. The large deterioration vs -0.8% y/y in December was due to closed shopping malls. Also, the restrictions on leisure activities discouraged travelling. However, durables goods sales rose 1.4% y/y. Epidemic restrictions remain the key obstacle to a major rebound in consumption – we expect a quick normalisation as soon as these end. Find more here. In February, Polish **consumer confidence** was stable m/m, but households' financial situation expectations were the highest in four months.

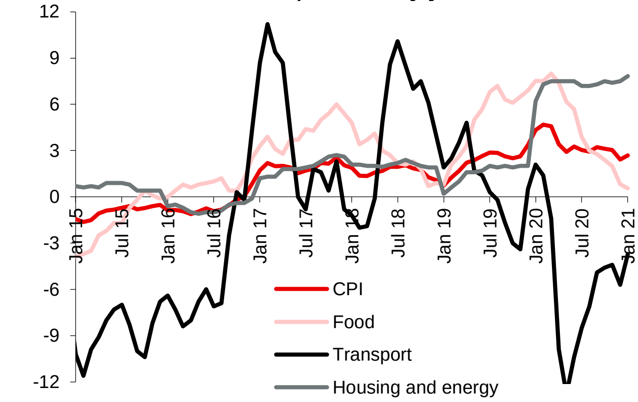
Poland January **employment** fell by 2.0% y/y vs our call at -1.3% y/y and market expectations at -1.5% y/y, while wages rose by 4.8% y/y in January, close to our call (4.7%) and market expectations (4.8%). Decline in employment was mostly due to annual adjustment of GUS statistical sample, in our view. We are expecting employment and wage growth to improve in the months to come. Find more here.

Current account balance showed +€0.43bn in December, below our and market expectations (at €1.08 and €1.01 respectively). The turnover was very strong. Exports was up by +14.8% y/y (the highest growth since Jan'18) while 11.6% had been expected. Imports rose by 13.6% y/y (the highest growth since Oct'18) instead of 9.3% expected. 12m current account surplus rose to 3.5% of GDP from the previous record-high 3.4% in November.

According to a **new draft, the Open Pension Funds (OFE) conversion**, will take place on 28 January 2022. The insured will have to decide between 1 June 2021 and by 2 August where to transfer their OFE pension capital: to the state-owned social insurance system (ZUS, no charge now, but future payouts come under PIT) or private individual pension accounts (IKE, 15% haircut, no PIT later). Main financial consequences for the general government sector assuming 50% choosing IKE are estimated at +PLN4.6bn in 2021, +12.5bn in 2022.

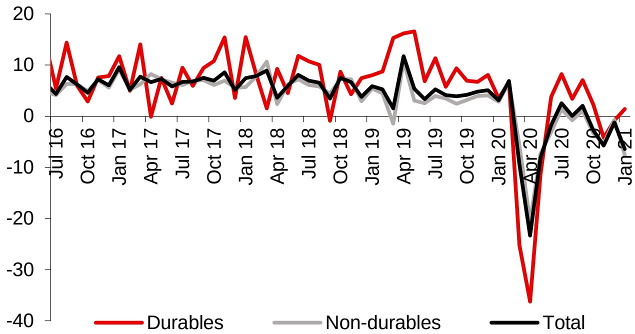
MPC member **Jerzy Żyżyński** said that a rate cut ,but by only 10bp, still could not be ruled out. **Jerzy Kropiwnicki** thinks that in 2H21 a small rate hike may be considered if inflation goes above NBP forecasts. **Eugeniusz Gatnar** said that in 2H21 one should consider a rate hike that would take the main rate to 0.5%, because inflation may accelerate to even 4% and by the end of the MPC term in early 2022 the main rate should be at 1.0%.

CPI inflation and selected components, % y/y



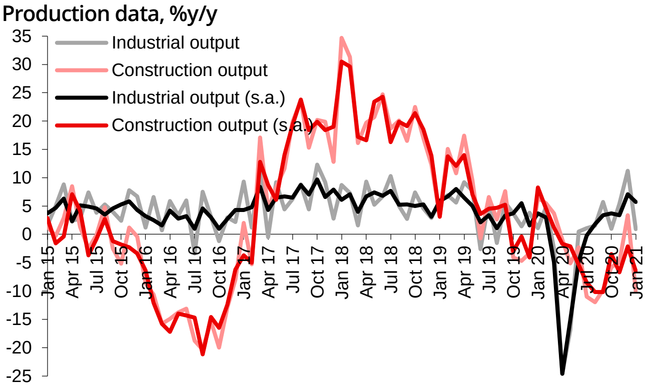
Source: GUS, Santander

Retail sales, in constant prices, main categories, %y/y



Source: GUS, Santander

Production data, %y/y



Source: GUS, Santander

Poland's foreign trade, in EUR, %y/y

Source: NBP, Santander

FX and FI market

Last week on the market [not edited]

FX EURPLN was pretty stable for another week (down -0.2% w/w). The currency pair has been trading horizontally within the 4.47-4.51 range for almost the whole February now. The subdued volatility of EURPLN was partly a function of lower volatility globally where most currencies (except for the rising GBPUSD) and main equity indices were stable on a w/w basis as well. USDPLN declined to 3.71 by 0.2%. CHFPLN to 4.14 by 0.5% and it was only GBPPLN which increased by 0.8% to 5.18. Elsewhere in the CEE region, EURCZK stabilized after the down trend observed since the start of the year paused a week before. EURCZK increased 0.3% to 25.83. Czech December current account printed worse than expected at CZK -3.2bn. EURHUF was simply stable in the passing week and most of the time remained within the narrow 358.0-359.5 range. Hungarian Q4 GDP surprised to the upside and expanded (vs expected contraction) on a q/q basis. USDRUB increased by 0.4% w/w to 73.9. Russian retail sales and PPI both surprised significantly to the upside, unemployment rate fell to 5.8%.

FI Polish January CPI reading on Monday at 2.7% y/y beat expectations by 0.3pp. FRA markets started to price in hikes (e.g. 9x12 to 0.34% from 0.25%; 21x24 to 0.70% from 0.55% vs 3M Wibor at 0.21%) but later in the week retraced a bit (e.g. 9x12 to 0.31%). IRS closed the week 7bp higher at 1.53% for 10Y (after briefly overshooting to 1.60%) and 5bp higher at 0.97% for 5Y (the mid-week overshoot to 1.04%). The MTD increase of both IRS stand near 30bp now. Bond curve has not increased that much. As a result the 10Y spread to Bund narrowed to 167bp while the 10Y ASW became even more negative (now at -19bp). On Wednesday NBP purchased PLN 1.05bn worth of government bonds (PS0425, DS0727, WS0428, DS1029, DS1030). On Thursday, Ministry of Finance sold a total of PLN 5.5bn bonds amid demand of PLN 7.9bn (OK0423, PS1026, DS1030, WZ1126, WZ1131). After the auction the gross borrowing needs for 2021 are met in 53%, the MinFin said.

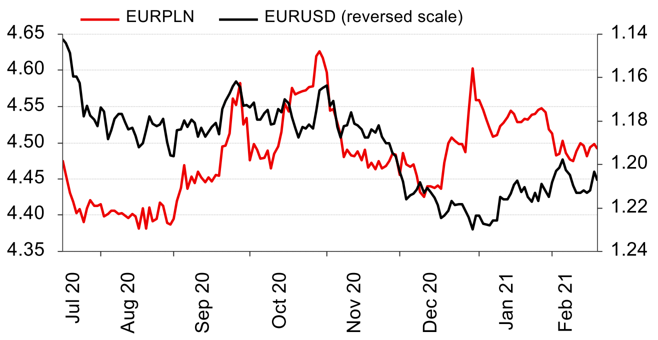
Next week in Poland there is M3 money supply on Monday and unemployment rate on Tuesday as well as detailed Q4 GDP breakdown on Friday. Abroad there are German IFO (Monday), Eurozone HICP, Hungarian central bank rate decision (Tuesday), German Q4 detailed GDP and US new home sales (Wednesday), Eurozone ESI, US durables and Q4 GDP (Thursday); US personal income and spending (Friday).

Market implications

FX EUR/PLN is likely to trade horizontally for another week in the 4.47-4.51 range. The higher than expected January CPI reading (which we foresaw) and slightly higher yields make zloty more an attractive investment, on the margin. The global mood is supportive for EM currencies but investors and traders are reluctant to build larger zloty bullish bets as that might backfire in case NBP returns to the FX market to purchase EURPLN which in theory can happen anytime as long as EURPLN trades below 4.50. That is also one of the reasons why realized volatility is so low (e.g. 1WK below 3%).

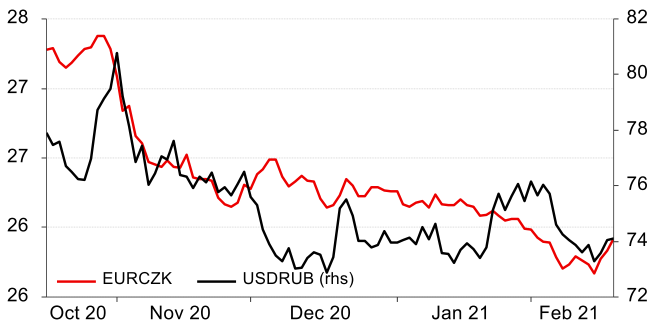
FI Polish fixed income is likely to follow global rates markets closely in the following week as the local macro data (M3, unemployment, final GDP Q4) are of less importance. The Polish economy and inflation keep recovering from the pandemic. However despite some recent hawkish voices from the MPC (Kropiwnicki, Gatnar) we still think the NBP rates will remain unchanged at 0.1% till the end of the current MPC's term (early 2022). Hence 2Y IRS at 0.44% might seem like a stretch (the FRA 21x24 implies 40bp hikes). The bond supply is still slightly smaller than the market would wish for. That is why it is the long end of the Polish IRS curve which might react the most to the global reflationary trend.

EURPLN and EURUSD



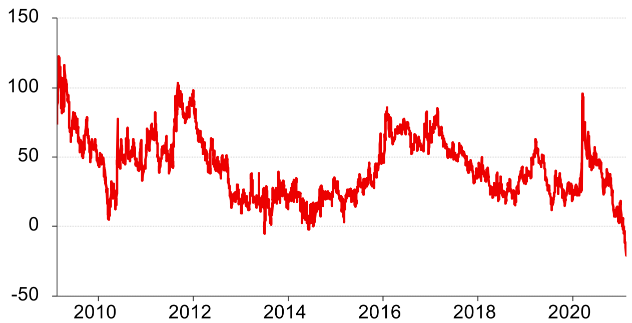
Source: Refinitiv Datastream, Santander Bank Polska

EURCZK and USDRUB



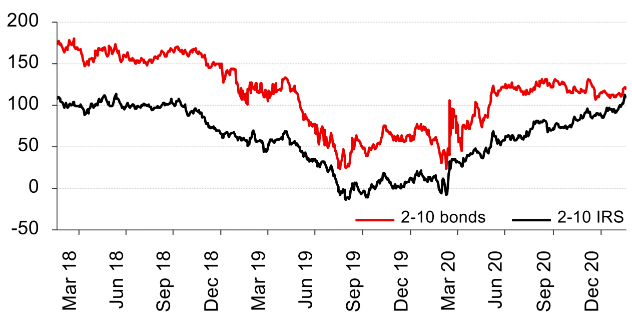
Source: Refinitiv Datastream, Santander Bank Polska

Poland 10Y asset swap spread



Source: Refinitiv Datastream, Santander Bank Polska

Poland 2-10 spreads



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
			MONDAY (22 February)				
10:00	DE	IFO Business Climate	Feb	pts	89.7		90.1
14:00	**PL**	**Money Supply M3**	**Jan**	**% y/y**	**16.4**	**16.5**	**16.4**
			TUESDAY (23 February)				
10:00	**PL**	**Unemployment Rate**	**Jan**	**%**	**6.5**	**6.5**	**6.2**
11:00	EZ	HICP	Jan	% y/y	0.0		0.9
14:00	HU	Central Bank Rate Decision	Feb.21	%	0.6		0.6
16:00	US	Consumer Conference Board	Feb	pts	90.0		89.3
			WEDNESDAY (24 February)				
08:00	DE	GDP WDA	4Q	% y/y	0.0		-3.9
16:00	US	New Home Sales	Jan	% m/m	2.0		1.6
			THURSDAY (25 February)				
11:00	EZ	ESI	Feb	pct.	-		91.5
14:30	US	Durable Goods Orders	Jan	% m/m	1.3		0.5
14:30	US	GDP Annualized	4Q	% Q/Q	4.1		4.0
14:30	US	Initial Jobless Claims	Feb.21	k	772.5		861.0
16:00	US	Pending Home Sales	Jan	% m/m	-		-0.3
			FRIDAY (26 February)				
10:00	**PL**	**GDP**	**4Q**	**% y/y**	**-2.8**	**-2.8**	**-1.5**
14:30	US	Personal Spending	Jan	% m/m	0.7		-0.2
14:30	US	Personal Income	Jan	% m/m	10.0		0.6
14:30	US	PCE Deflator SA	Jan	% m/m	0.2		0.4
16:00	US	Michigan index	Feb	pts	76.2		76.2

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.