Monthly Pulse Check

Economy. FI. FX

March 12th 2021

mBank Research

For contact details and classification of the report see the last page.

Our view in a nutshell (≥1Y horizon) & major forecasts

Macro

- The pace of vaccinations controls the third wave outcomes. Europe is lagging behind the U.S. and the UK. However, it is highly likely that we observe the last wave of economic restrictions and economic growth is set to restart in H2 2021 for good.
- Polish economy behaves better than expected. We expect 3.8% recovery in 2021. Current epidemic restrictions may linger also in Q2. However, once the 60+ population is inoculated, GDP growth is set to resume. Due to the disbursement of the new EU funds, Polish cycle is seen as longer and possibly stronger than in the U.S. and euro zone as a whole. It may also be more inflationary since labor market survived 2020 very well.

Monetary policy: Fed. ECB. NBP

- Fed: ZIRP + QE + direct loans to firms. Rather done with easing.
- ECB: NIRP (already there) + QE Expansion (maximum flexibility) + new LTRO. Using flexibility of the programs.
- NBP: Rates cuts (total 140bp). QE already in place (govvies + bonds with state guarantees). Over to fiscal policy now. Not out of ammo, though. FX channel (interventions), QE expansion (flexibility), forward guidance stay on the table if need be. Negative rates unlikely. On hold in either way in 2021.

FX Market

- Weak zloty in H1 2021 (negative real rates, strong dolar). The return to modest appreciation is likely in H2 2021 as euro zone recovers, the drive for stronger dolar wanes and (cyclical) recovery trades kick in, helped by current account surplus (flows).

		2020 Q1 F	2020 Q2 F	2020 Q3 F	2020 Q4 F	2021 Q1 F	2021 Q2 F	2021 Q3 F	2021 Q4 F	2020 Q1-Q4	2021 Q1-Q4	2022 Q1-Q4
GDP y/y	%	1,9	-8,4	-1,5	-2,8	-2,2	9,0	2,5	5,3	-2,8	3,8	5,1
Individual consumption y/y	%	1,2	-10,8	-0,4	-3,2	-1,2	11,5	0,5	5,4	-3,0	4,1	4,6
Investment y/y	%	0,9	-10,7	-9,0	-10,9	-8,0	3,1	1,8	7,7	-8,4	1,2	7,8
Inflation rate (eop)	%	4,6	3,3	3,2	2,4	2,8	3,3	3,6	4,1	2,4	4,1	4,0
Unemployment rate (eop)	%	5,3	6,1	6,1	6,2	6,5	6,0	5,9	5,9	6,2	5,9	5,1
NBP repo rate (eop)	%	1,00	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,25
EUR/PLN (eop)	%	4,56	4,45	4,53	4,56	4,55	4,50	4,45	4,40	4,56	4,40	4,30
USD/PLN (eop)	%	4,13	3,96	3,87	3,73	3,79	3,75	3,71	3,67	3,73	3,67	3,58

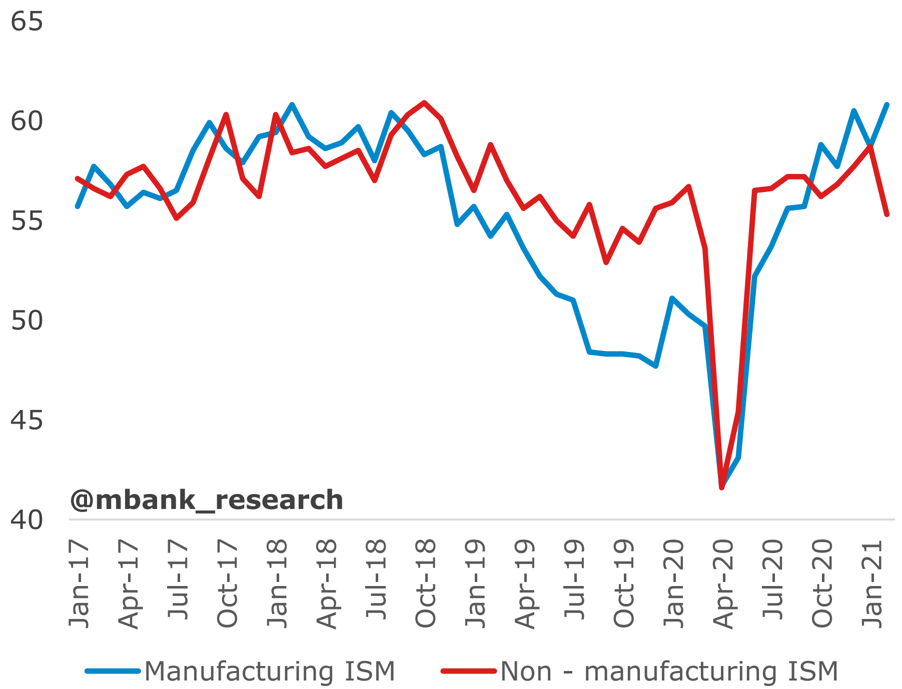
F - forecast

Highlights

- Third wave of COVID-19 infections is unfolding in Poland. Upcoming weeks will possibly bring more epidemic restrictions as the number of vaccinated people is too low to stop the spread. However, as the most vulnerable part of the population gets a jab (late Q2), restrictions will be lifted and will not return. See the monitor here.
- The U.S. is faring much better than the euro zone (see here and here). The U.S. is also the source reflationary story that is roiling through the markets worldwide (see here).
- The consensus for Poland is not moving much (see here). We may see more adjustment after the publication of the complete set of numbers for the first quarter, i.e. in April/May. Next week's upcoming releases (see here) are mostly for February data.
- We expect 3.8% GDP growth in 2021 (see here). Labor market survived 2020 in quite decent shape (see here) making a good foundation for further GDP acceleration (more than 5% in 2022). So far the economy is balancing between restrictions-driven consumption (see here for more detailed tracking) and mostly immune (and powering ahead) manufacturing (see here). Mobility indicators are showing the slow return to normality (see here) but this may change in the very short term due to epidemic situation.
- Inflation is coming off elevated levels. We can, however, abandon assumption that inflation in 2021 will be substantially lower than in 2020. Actually it may be on average matching the levels seen in 2020 (see here). We think that the new NBP projection is on knife's edge in that respect (see here).
- Short end market rates are anchored by dovish MPC. Longer rates follow global developments. Reflation story increased longer-term-rates. It is unlikely to be reversed and the most likely outcome is still up, albeit in a more orderly manner (see here for recent developments).
- NBP purchases are at low levels for now (see here and here). Recently NBP announced it may step up purchases (just after the similar ECB announcement). It may smooth market fluctuations but the trend in rates comes from abroad.
- We expect weak PLN in H1. Some appreciation may happen in H2. See here.

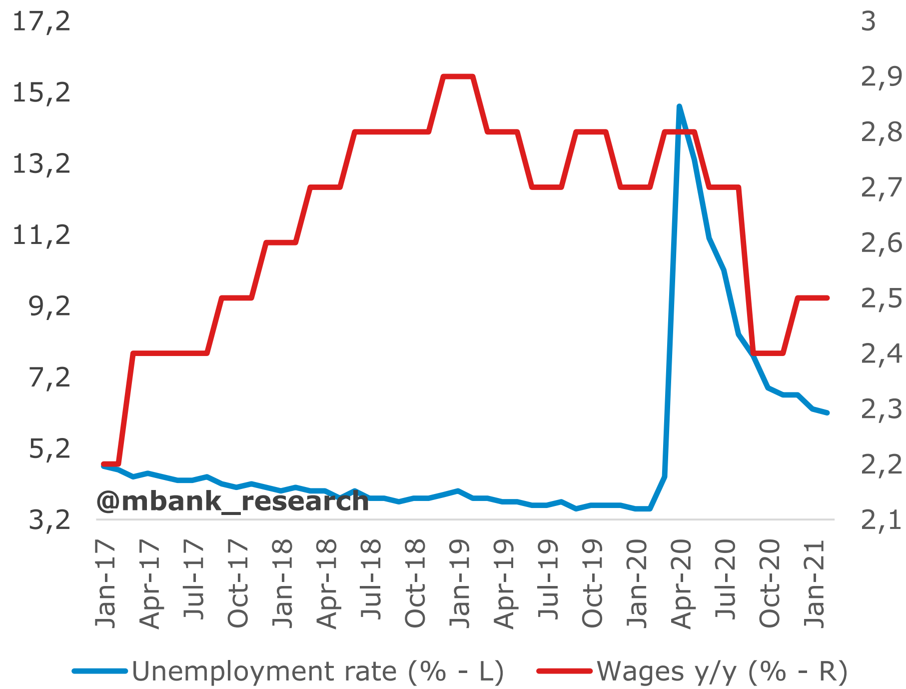
U.S. economy health check

ISM PMI: manufacturing & non-manufacturing



Source: ISM

Labor market: wages & unemployment rate

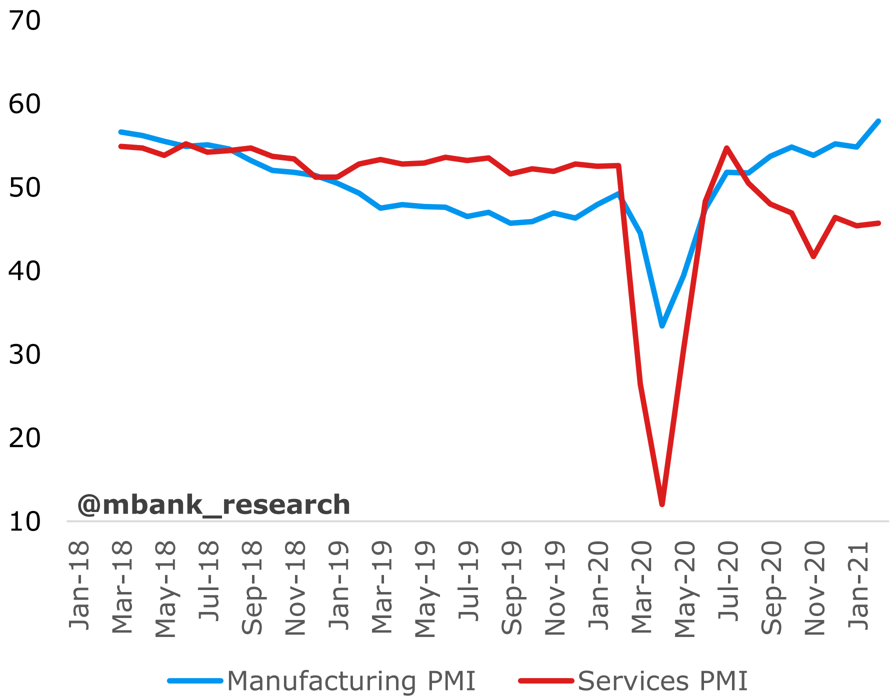


Source: FRED

- Business activity better than in the euro zone. Vaccination rate much faster. Fiscal stimulation larger. Reopening after the third wave. Poised to outperform the rest of the world in 2021.
- Although current inflation remains subdued, reflation story originated in the U. S. and is reflected in much higher yields and rates. However, in proper perspective, the mild tightening of financial conditions guarantees a bit of a cushion before the incoming excess in demand (in times of supply scarcity).
- The Fed is expected to stick to its communication story that inflation increase is going to be temporary. At this very moment (unless there is a fresh specualtion on another fiscal package, this time addressing the infrastructure deficiencies), current inflation story boils down to closely following the data on labor market and prices. Expectations for improvement are already high. Monetary policy tightening expectations have – in our opinion – reached its closest possible date.

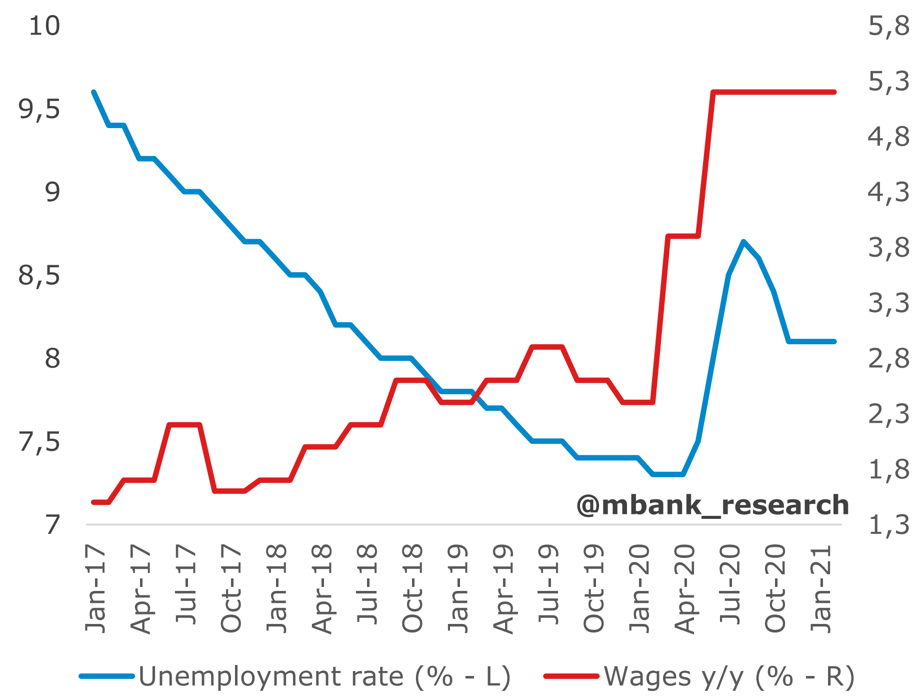
Euro area economy health check

Markit PMI: manufacturing & services



Source: Markit

Labor market: wages & unemployment rate

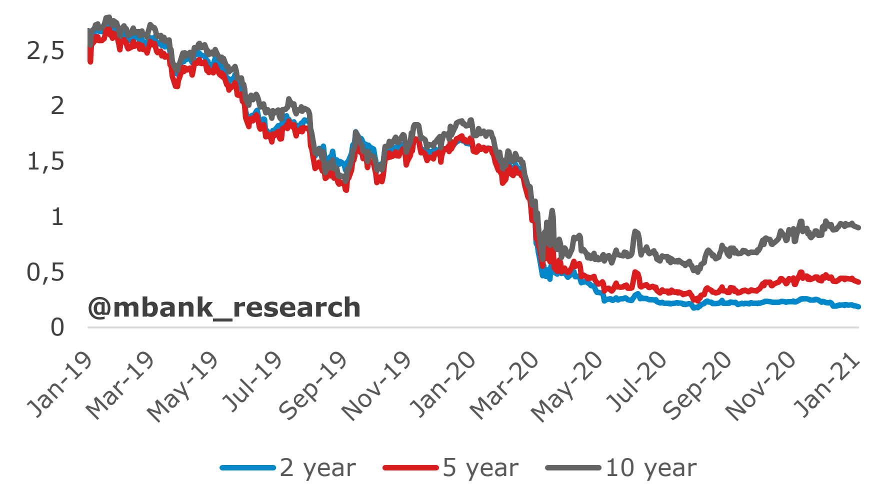


Source: Eurostat

- Slow start of vaccination campaing makes the third infection wave less bearable than in the U.S. and demands more drastic lockdown measures. It is already visible in the difference in business activity in manufacturing and services. Divergence is here to stay for a while since there is no direct fiscal stimulation on the horizon at the moment (or in other words, the NGEU is unlikely to exert any meaningful impact before 2022). Spill-overs from the U.S. package are estimated at +0.5-0.6pp (OECD calculations).
- Reflationary story imported from the U.S. generates unwaranted tightening of financial conditions. Therefore ECB decided to act front-loading the pace of PEPP purchases. It is rather unlikely that ECB would decide to expand the overall level of stimulation.
- Structurally low growth in euro zone is here to stay making substantial monetary policy stimulation warranted for a long period of time after the pandemic ends. Hence, we do not expect any interest rate hikes for many, many years.

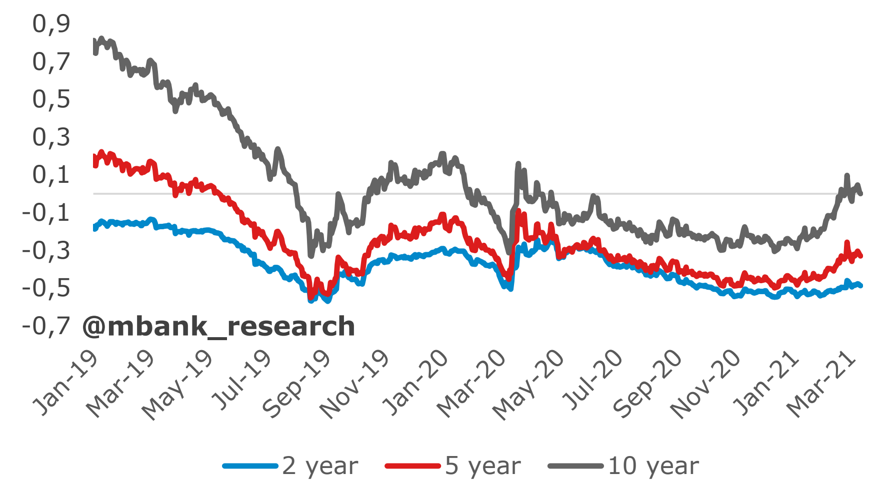
Global rates: move higher unlikely to be reversed in longer tenors; short end much better anchored by easy central bank's policy.

US swap rates (%)



Source: Bloomberg

EU swap rates (%)



Source: Bloomberg

Swap spreads (10Y-2Y. p.p.)

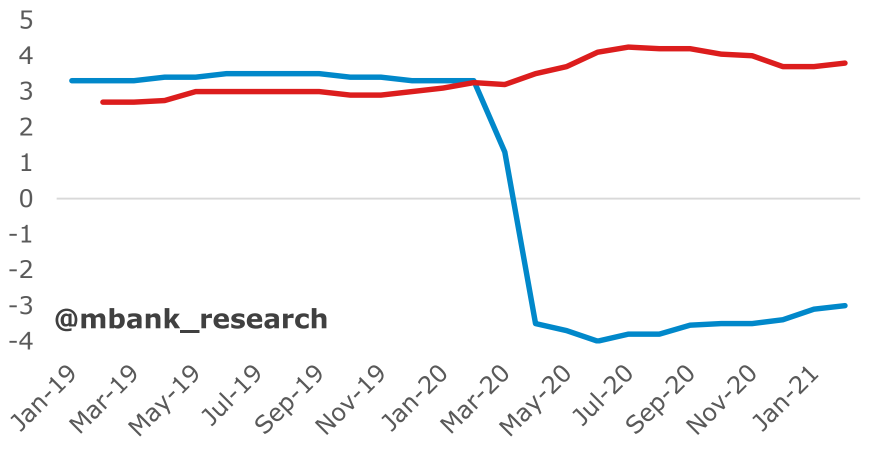
Source: Bloomberg

US and EZ inflation expectations (%)

Source: Bloomberg

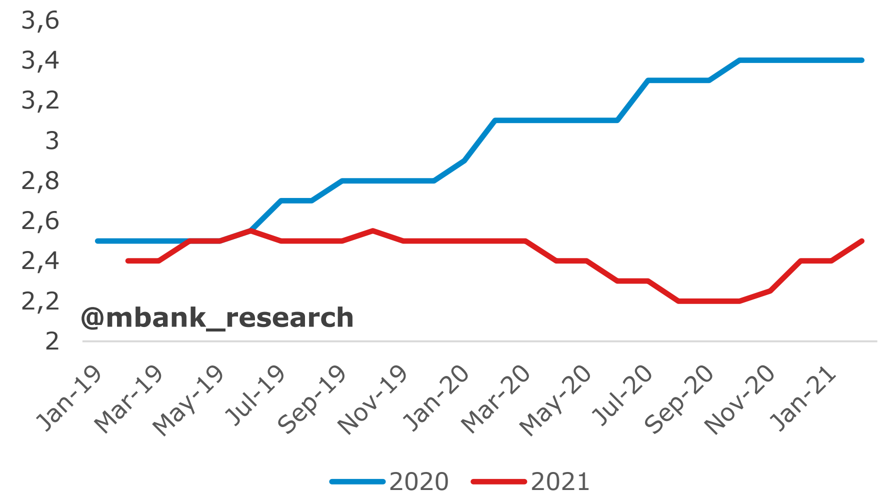
Consensus: what is expected in Poland?

Consensus tracker: GDP growth (% y/y. annual avg)



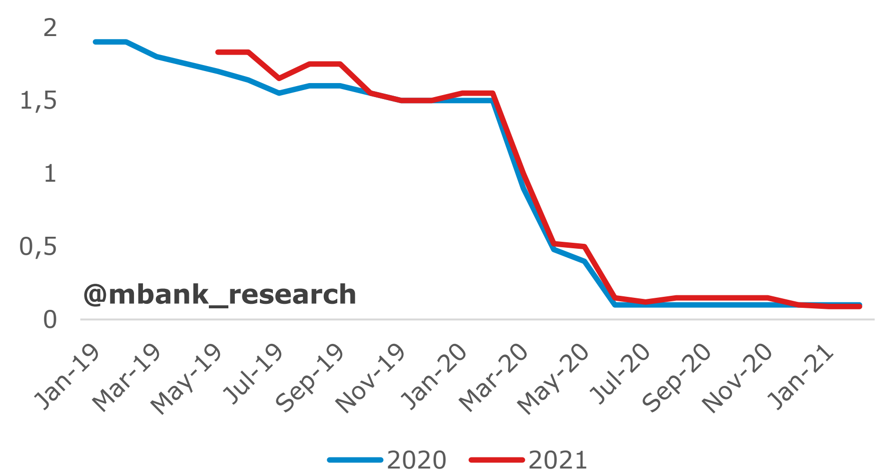
Source: Bloomberg

Consensus tracker: CPI inflation (% y/y. annual avg)



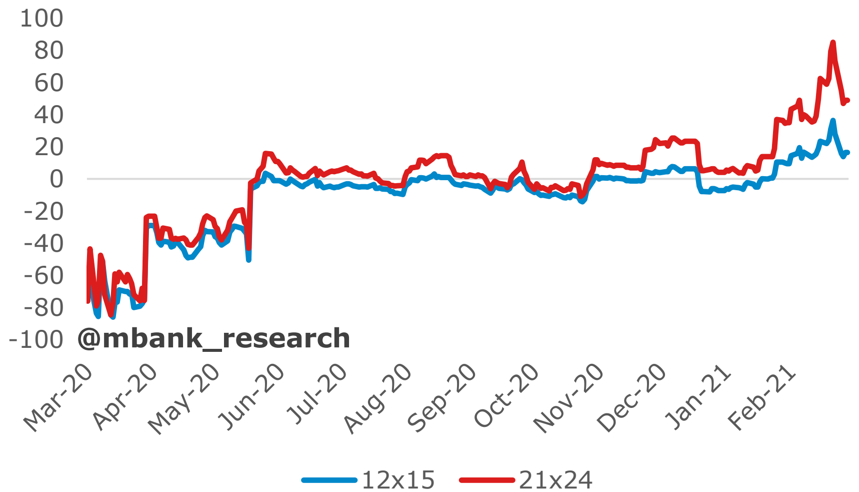
Source: Bloomberg

Consensus tracker: NBP ref. rate (%. end of period)



Source: Bloomberg

Rate changes priced in by FRA (bps)



Source: Bloomberg

Upcoming Polish macro releases: March 2020

Publication	Date	Period	mBank	Consensus	Actual	Prior
PMI (pts.)	01.03	Feb	52,2	52,8	53,4	51,9
Unemployment rate (%)	04.03[3] 23.03[4]	Feb	6,5%	6,5%	6,6%	6,5%
CPI y/y (%)	15.03[2]	Feb	2,5%	2,5%		2,7%
Current account (m EUR)	16.03	Jan	2880	2416		430
Employment y/y (%)	17.03	Feb	-1.9%	-1.9%		-2.0%
Wages y/y (%)	17.03	Feb	4.9%	4.7%		4.8%
Industrial output y/y (%)	18.03	Feb	4.4%	4.5%		0.9%
PPI y/y (%)	18.03	Feb	1.5%	1.4%		0.7%
Retail sales y/y (%)	19.03	Feb	-2.1%	-2.7%		-6.0%
Construction output y/y (%)	19.03	Feb	-5.0%	-9.5%		-10.0%
M3 y/y (%)	22.03	Feb	16.5%	16.5%		16.8%

[1] Flash estimate

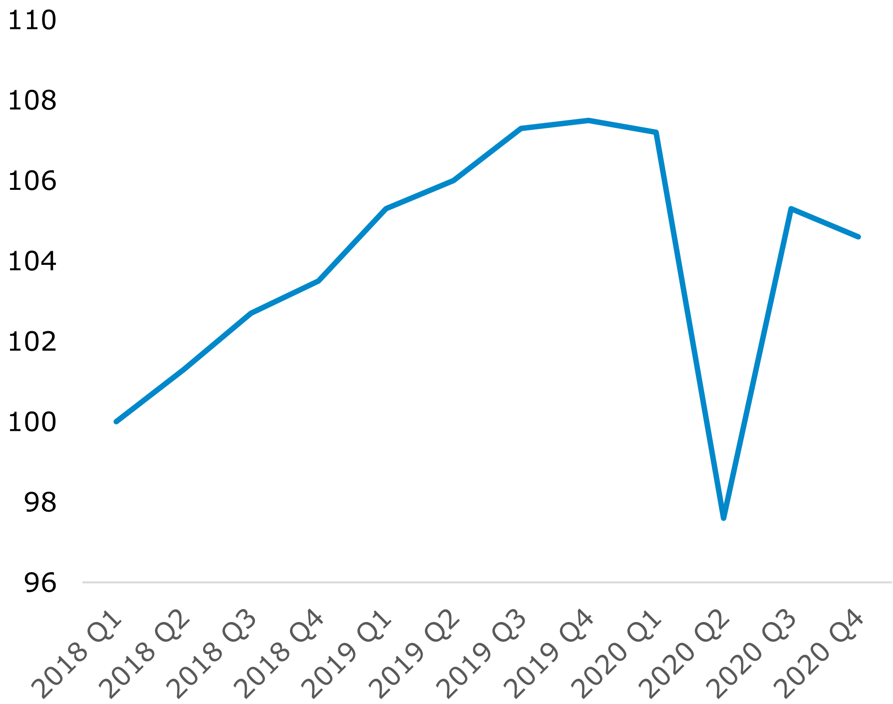
[3] Ministry of Economic Development, Labour and Technology estimate

[2] Final reading

[4] Statistics Poland final reading

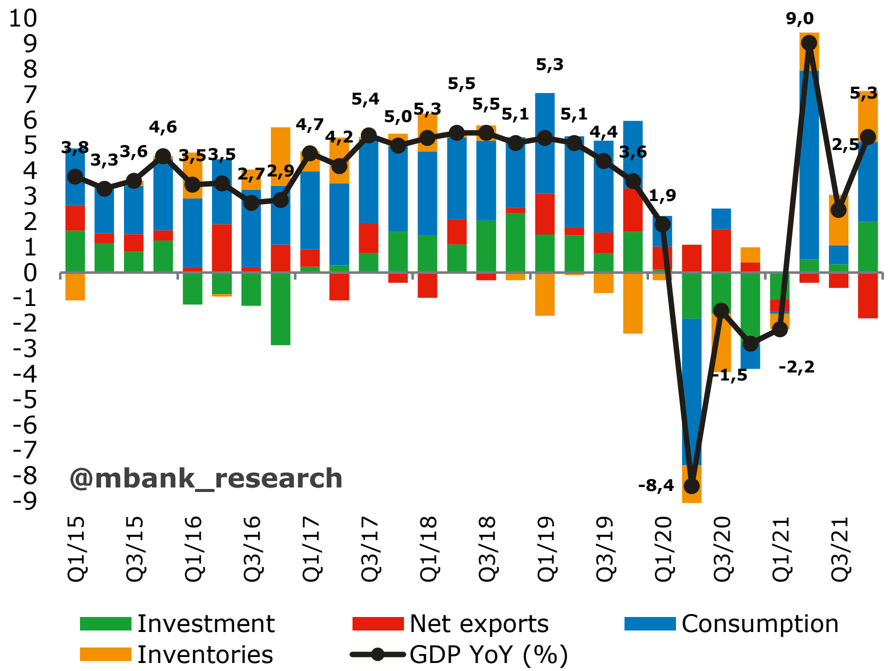
GDP: the big picture

GDP. Q1 2018 = 100.



Source: Statistics Poland. own elaboration

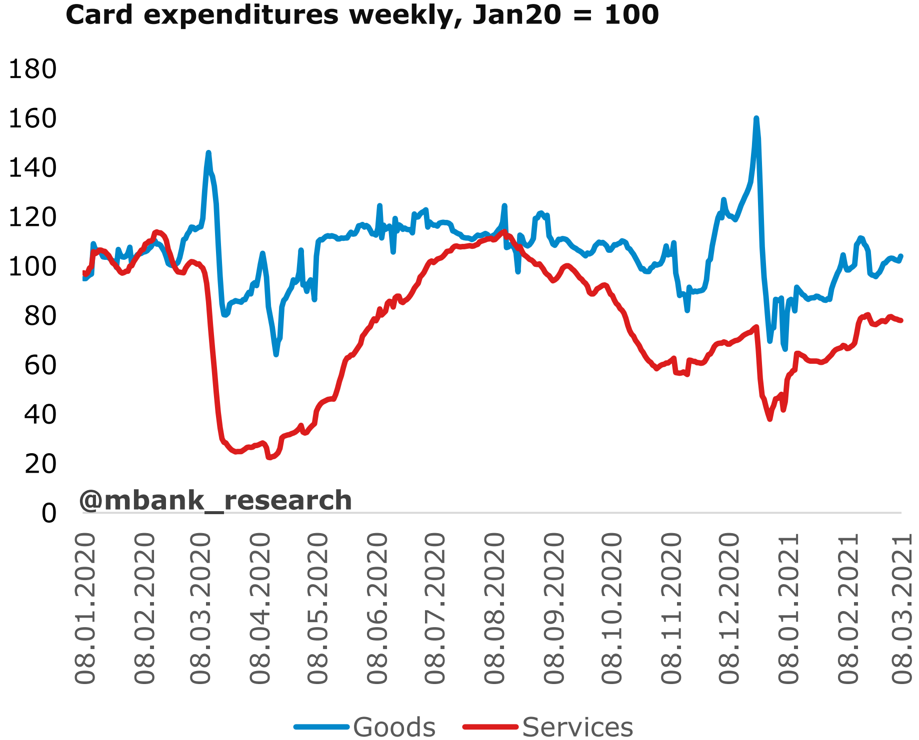
GDP breakdown



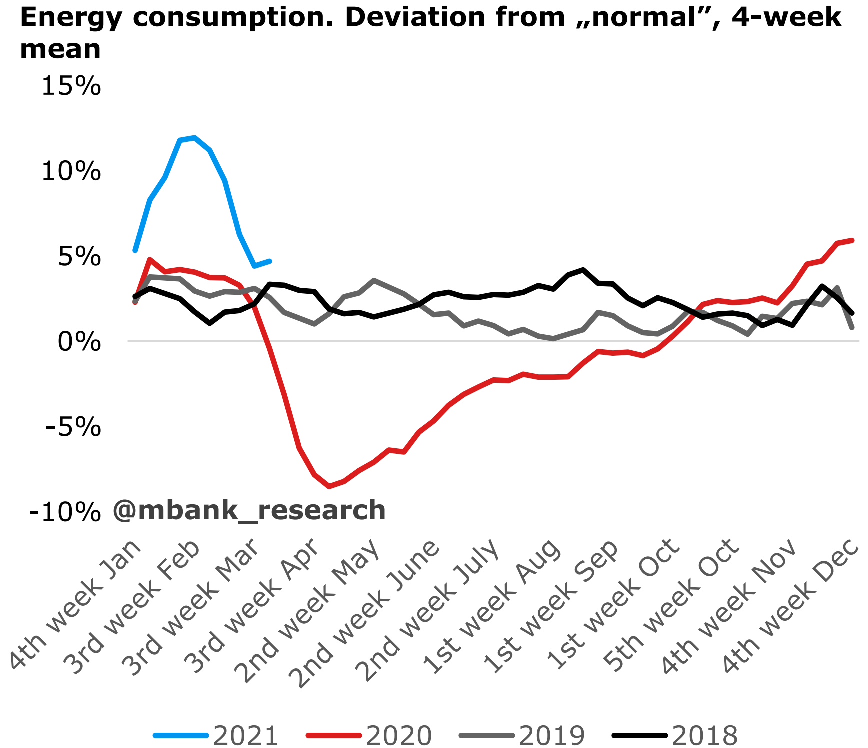
Source: Statistics Poland. own elaboration

- We do not change our view. The best for the economy is set to come in 2022+. 2021 is going to be an interim year.
- Last data show that – indeed – we had double dip in GDP growth, atlhough the Q4 results were much better than experienced during the first wave of infections.
- We expect slow (but nevertheless proceeding) start of investment, strong exports and quite strong consumption. However, due to the fact that consumption is not going to be supported by new fiscal programmes (as in the U.S.) and the bulk of state aid was channeled to firms, savings did not burst like in the U.S. Moreover, we do not expect consumers to draw down wealth soon. We think the imporovement in labor market is more imporant and therefore we expect the ultimate acceleration of consumption to be postponed to later years. In the meantime we will only see base effects connected to some service types that will return to life. It is in our opinion not a no brainer to expect the return of services to be correlated also higher lower spending on goods. They already thrived in 2020.

Consumption following restrictions, industrial output proceeding forward



Source: mBank transaction data. Own elaboration.

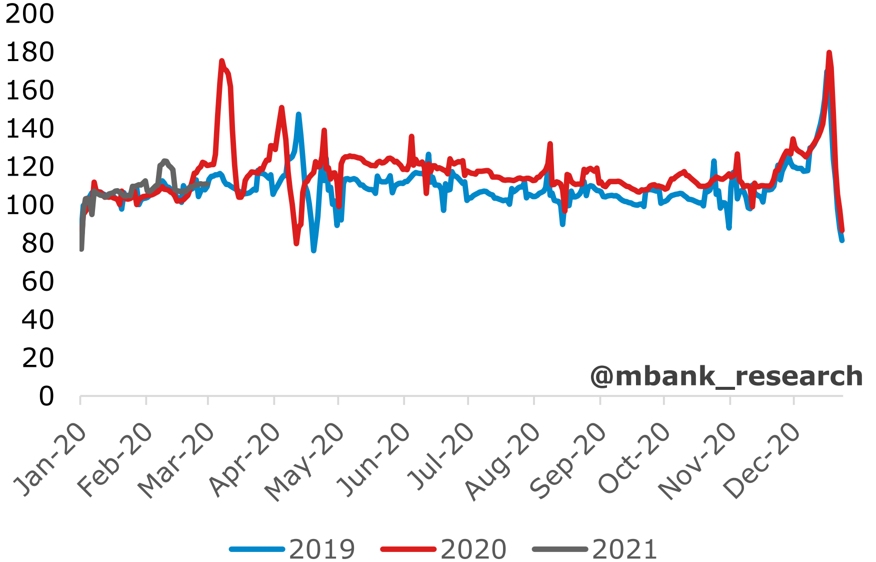


Source: electricity grid data & own elaboration

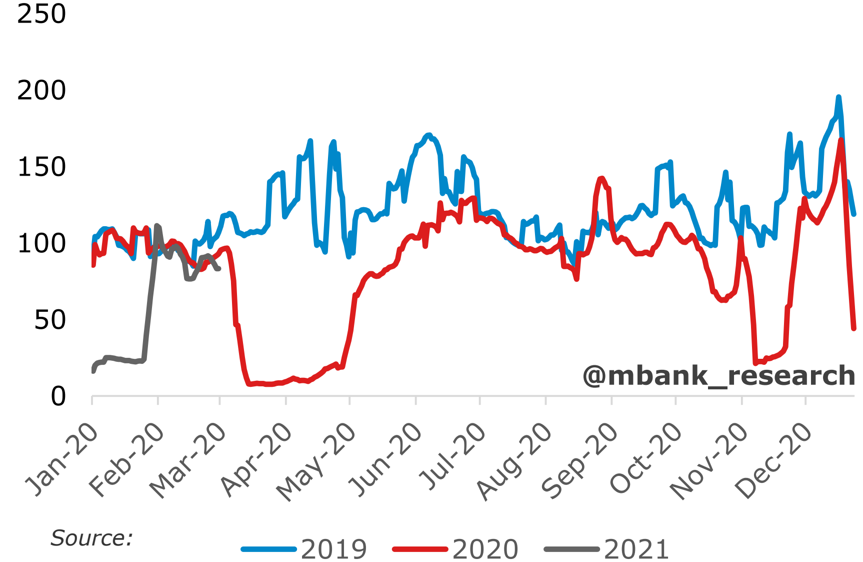
- Industrial production remains strong (but not as strong as energy consumption presented above suggest – this maybe our failing to account for the new norm of energy consumption at low temperatures while many people work from home) and is on the pre-pandemic trend. In the short-term we can see some troubles with deliveries, higher material costs and possible lockdowns in other European countries but in the longer term there are no major threats for industrial production to march upwards.
- Retail sales and services follow the pandemic restrictions. After a slight decline in January (closed shopping centers), in February retail sales rebounded (according to card expenditures, we do not know the official data yet). But it was still lower than in previous year. Restrictions returned in March (only in some regions, but we expect some nationwide solutions) therefore both services and retail sales will decline again before they re-accelerate.

Card expenditures, 7-day average

Food, beverages and non-specialized stores, Jan20 = 100

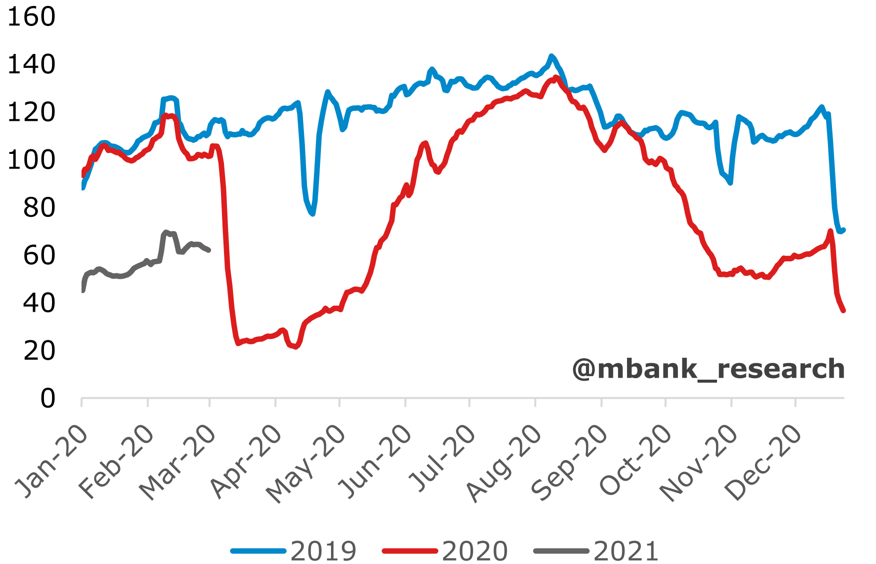


Clothing, footwear, Jan20 = 100

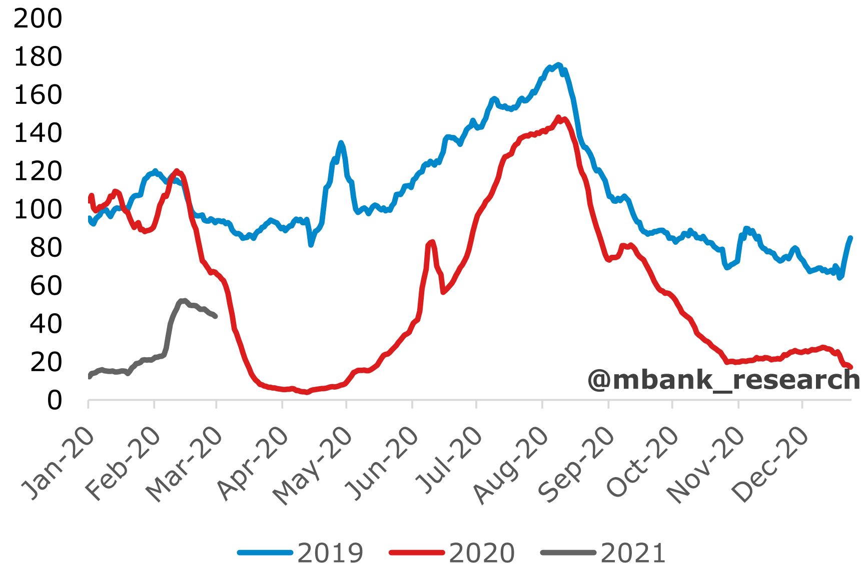


Source:

Restaurants etc., Jan20 = 100



Tourism, Jan20 = 100

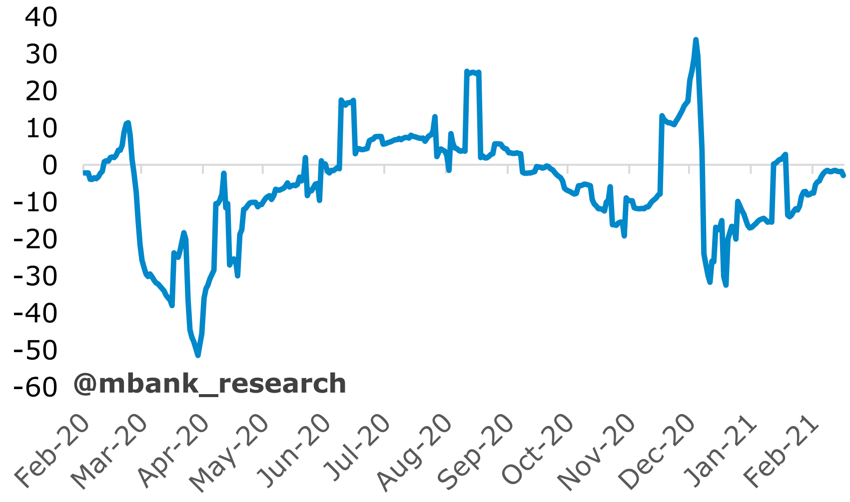


Source: mBank transaction data. Own elaboration.

Google mobility, 7-day average

Retail & recreation (% change from Jan20)

Grocery & pharmacy (% change from Jan20)



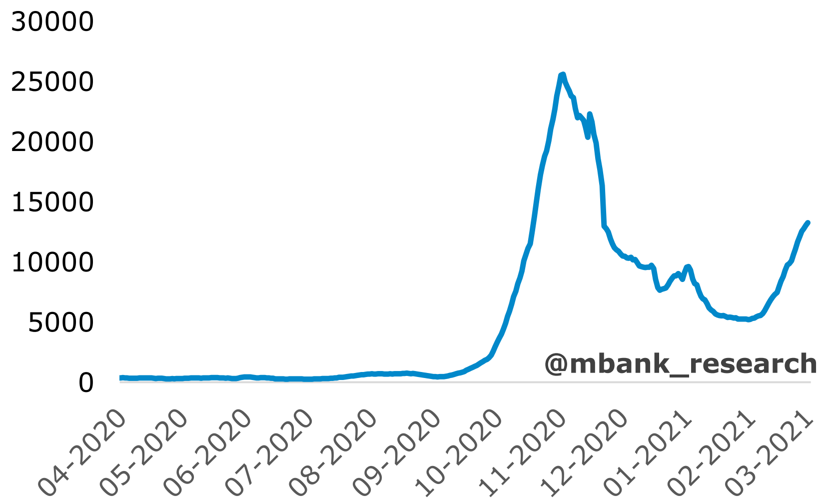
Workplaces (% change from Jan20)

Residential (% change from Jan20)

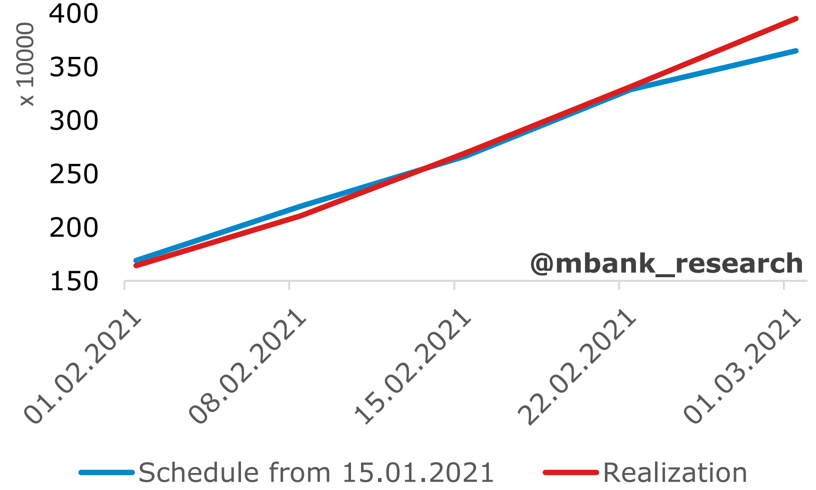
Source: Google mobility data. Insights in these reports are created with aggregated, anonymized sets of data from users who have turned on the Location History
The baseline is the median value, for the corresponding day of the week, during the 5-week period Jan 3–Feb 6, 2020

COVID-19 situation in Poland

Daily new cases (7day average)



Government schedule of vaccination vs realization



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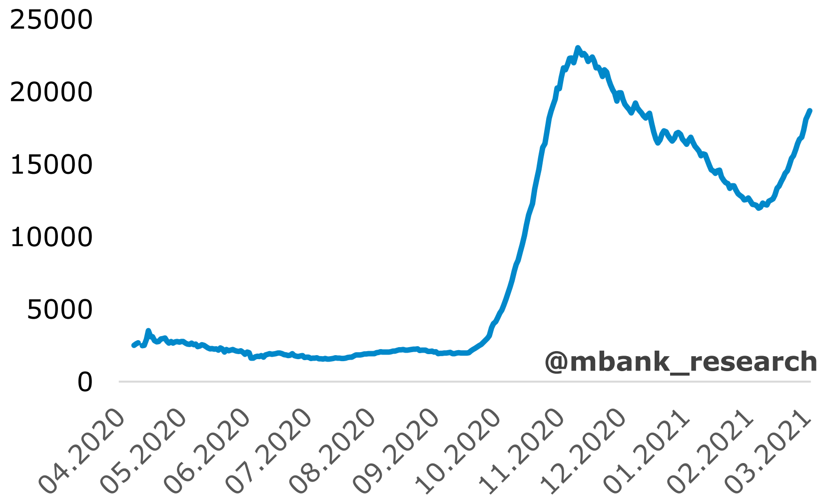
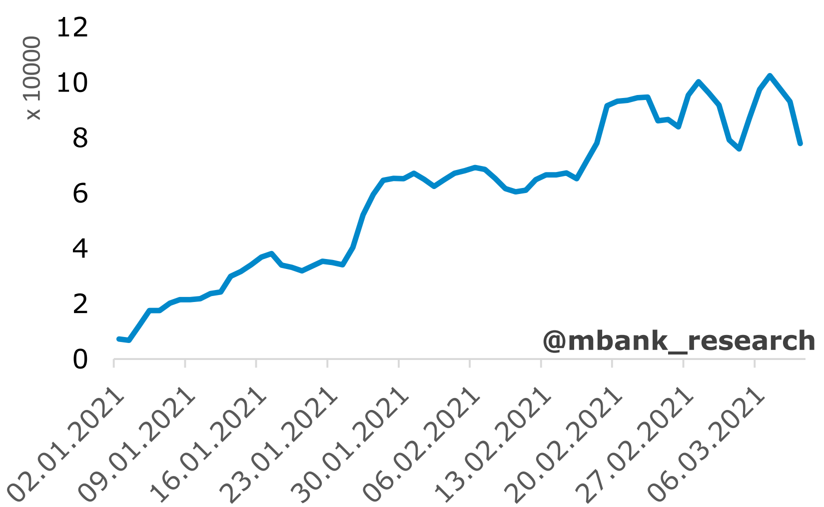
Hospitalized patients



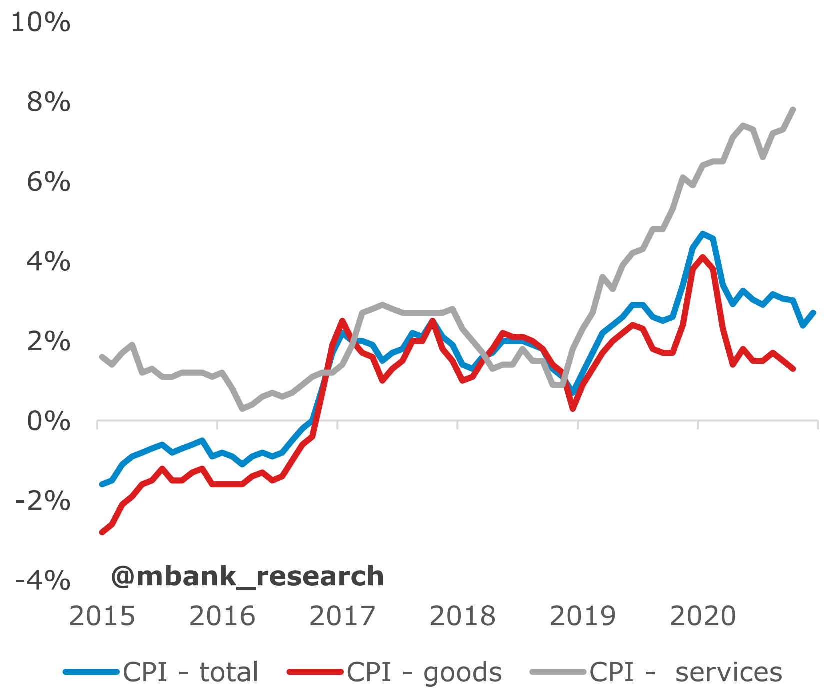
Daily new vaccinations (7day average)



Source: Our World In Data, Covid-19 excel sheet by Michal Rogalski, gov.pl

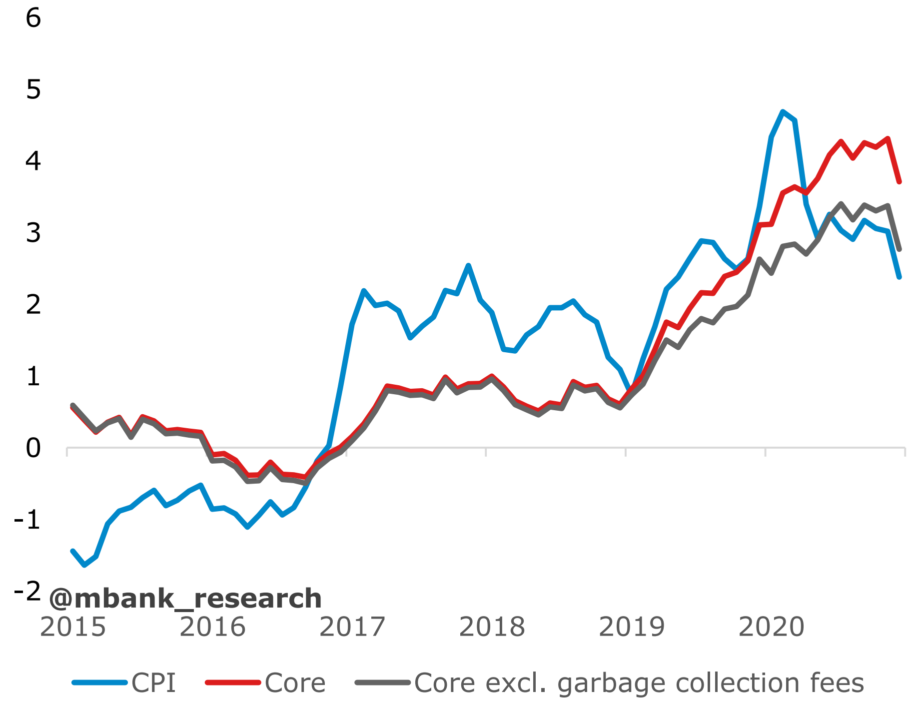
Short-term inflation tracker

Still little respite in services



Source: Statistics Poland. own elaboration

Inflation excluding garbage collection fees (in %)

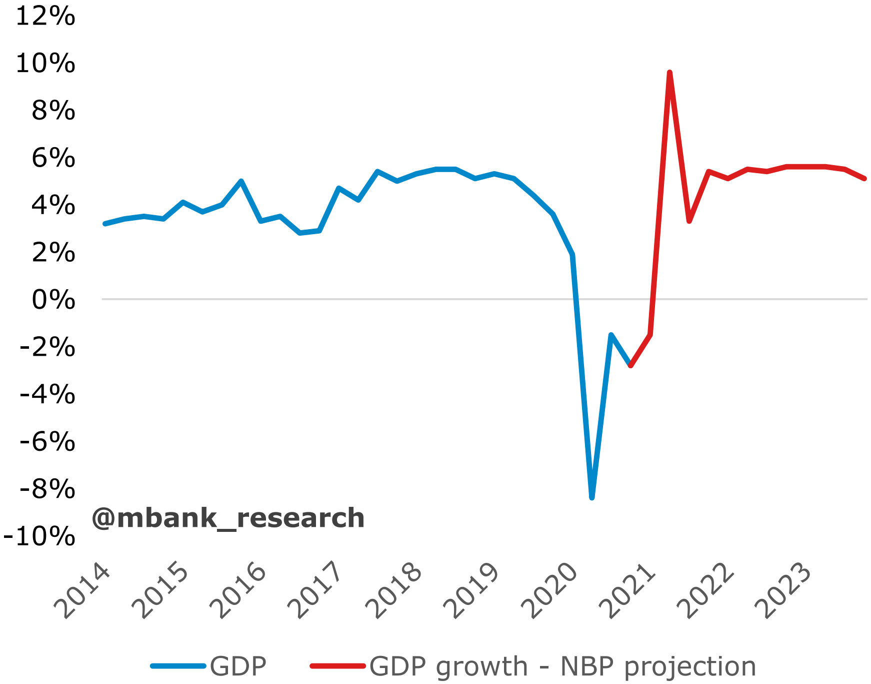


Source: Statistics Poland. own elaboration

- Inflation surprised to the uspide at the start of the year. Mechanically it pushes (already quite steep) inflation path for 2021 even higher. Core inflation stays elevated as well.
- 2021 will be market with inflation propelled mostly by fuels, food and base effects. Core inflation is going to fall during the course of the year. However, once it proved to be more sticky than modelled so it has to be monitored closely.
- Stripping the effects of garbage collection (widely communicated as an imporant source of price growth) does not really change the picture. Core inflation is still running high and with upcoming period of strong growth (>4.5% in the next 4 years), the potential of overshooting inflation target is very high.
- 2021 higher inflation can be (correctly) attributed to some temporary effects connected with reopening of the economy. We argue, however, that this inflation burst is not going to be transient and inflationary pressure is here to stay in 2022 and later years. We therefore keep our expectations for the start of monetary policy normalization in late 2022 intact.

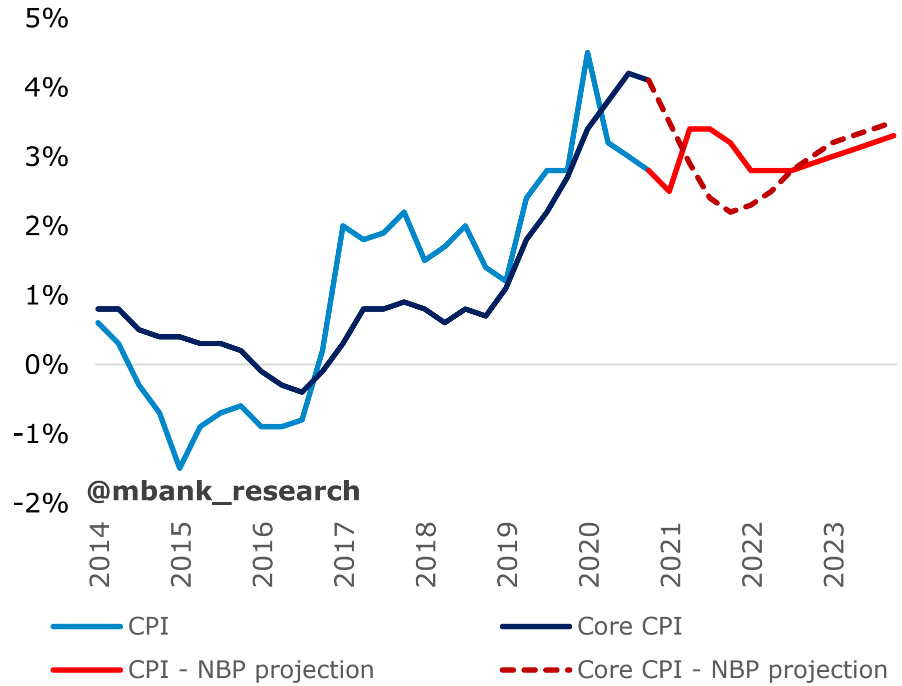
NBP new forecasts

GDP growth >5% in 2022-2023



Source: NBP, own elaboration

Inflation path subject to upside risks (in our opinion)

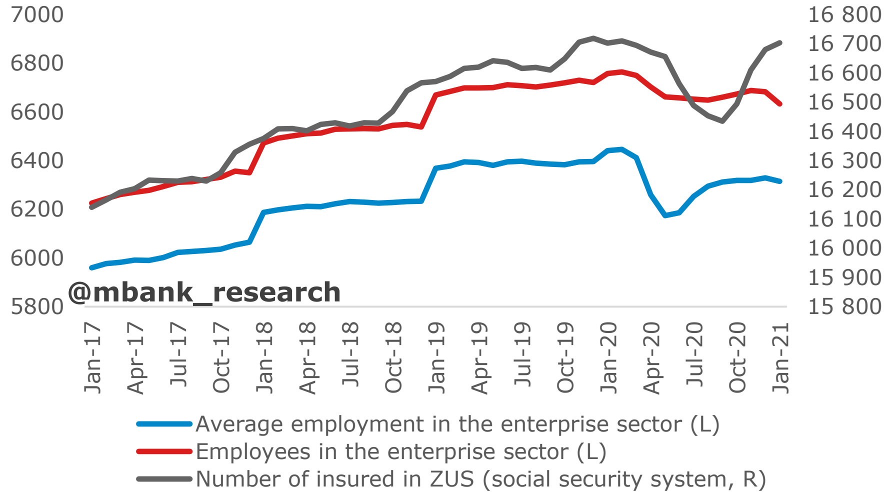


Source: NBP, own elaboration

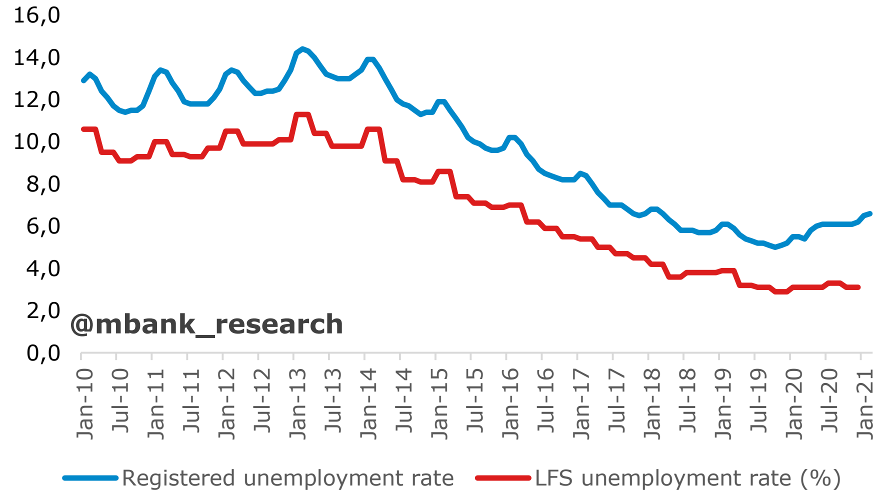
- March GDP forecasts in NBP projections are much more optimistic compared to the November ones. There are few reasons: weaker COVID-19 impact on economic activity in Q4, faster recovery abroad, launching new anti-crisis programs in January and absorption of Next Generation EU funds (not included in the previous forecasts).
- Despite better growth perspectives inflation will remain within the range for deviations from target (3.1% y/y in 2021, 2.8% in 2022 and 3.2% in 2023). Inflation forecast for 2021 is higher compared to the November one because of increase in energy prices. NBP analysts project that next year inflation will decrease due to lower core inflation (lagged effect of output gap, and expiring one-off effects from this year).

Labor market trackers

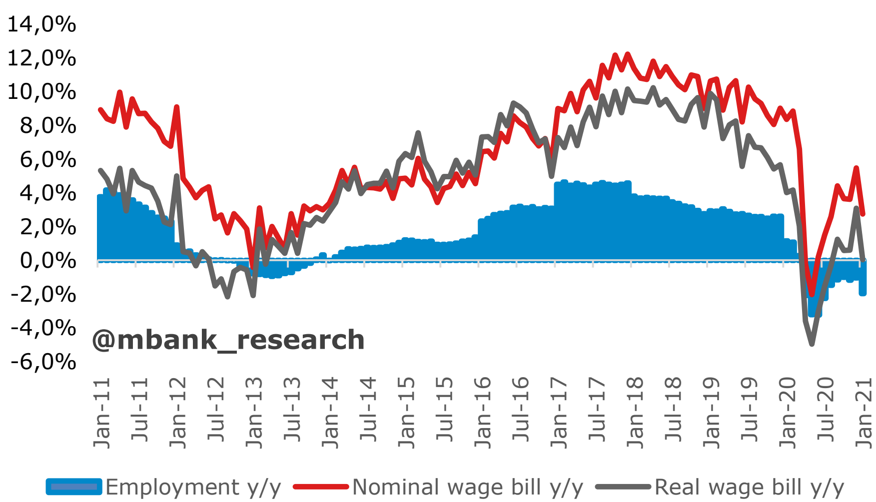
Employment



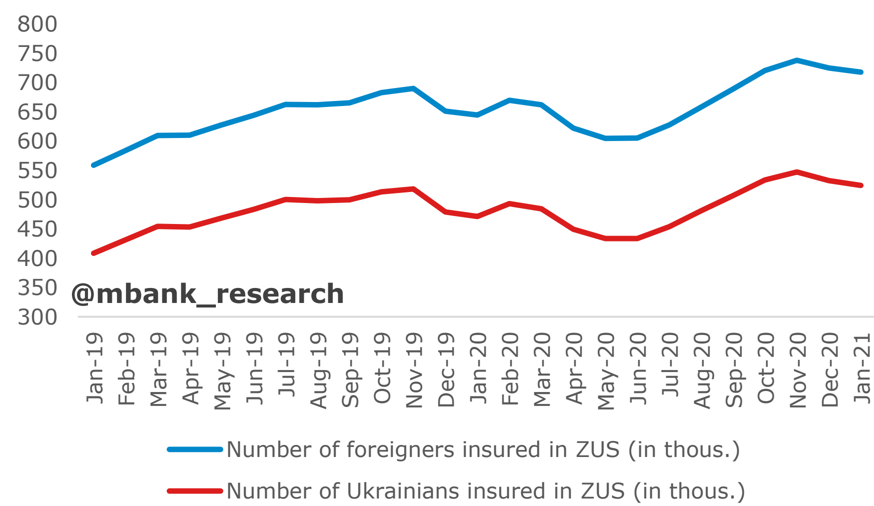
Unemployment rate



Wage bill



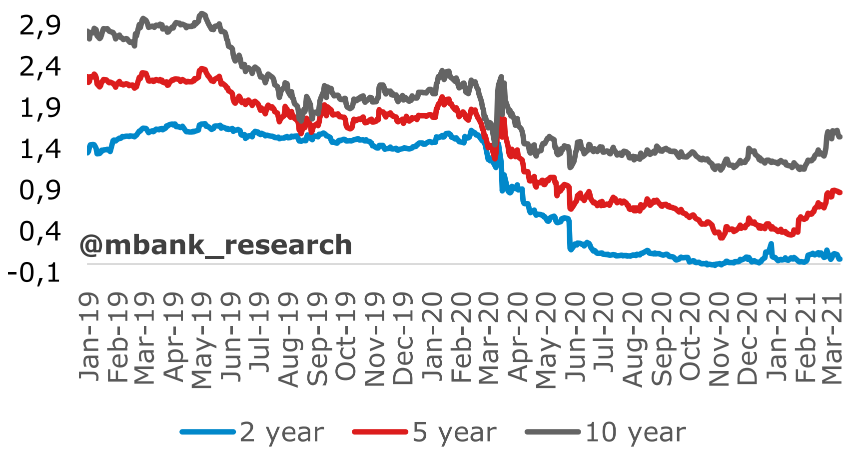
Immigration in the labor force



Source: Statistics Poland, ZUS Statistical Portal, own elaboration

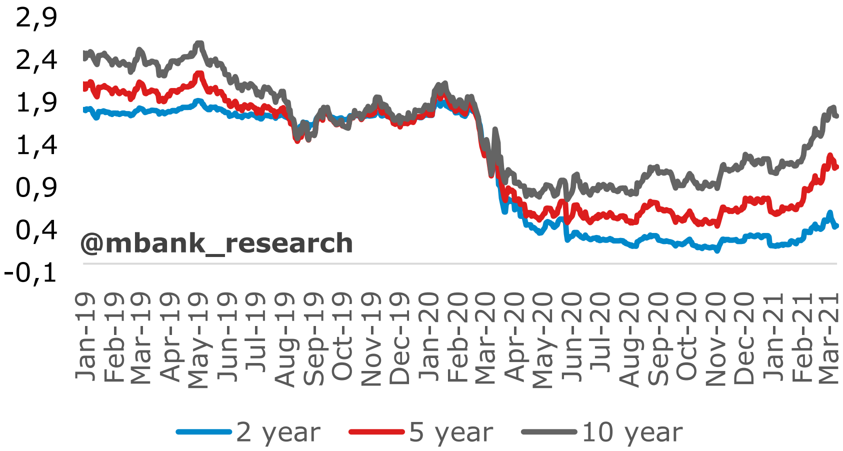
Polish rates, yields and spreads:

POLGBs



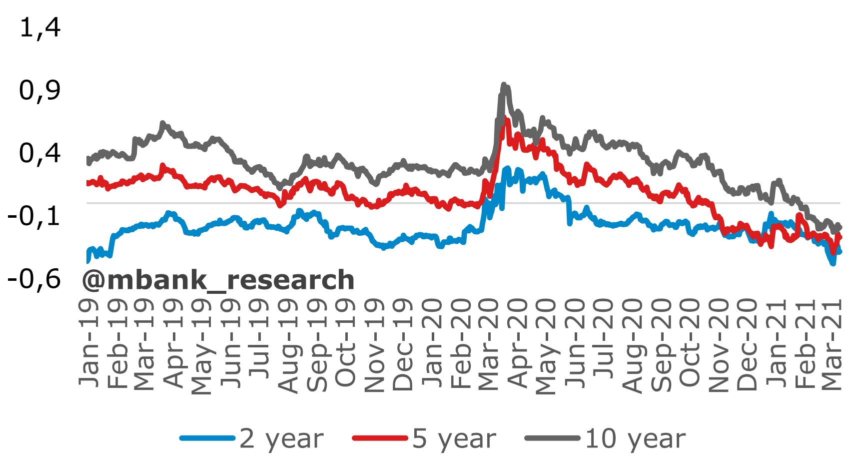
Source: Bloomberg

PL IRS



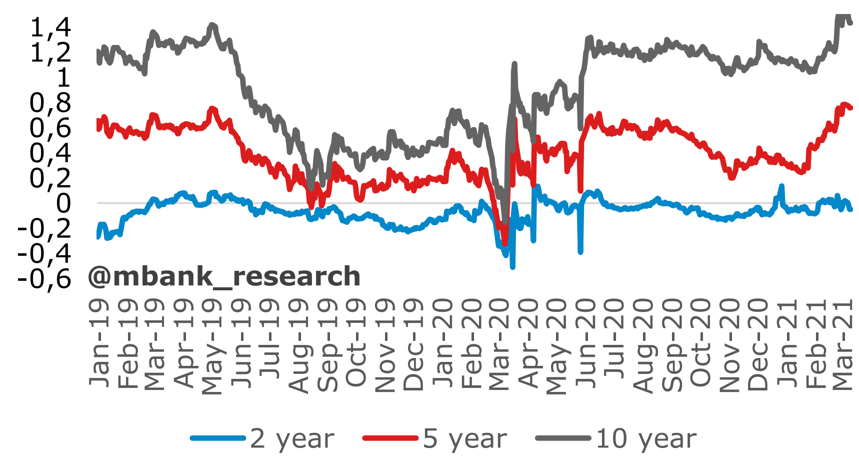
Source: Bloomberg

ASW spread



Source: Bloomberg

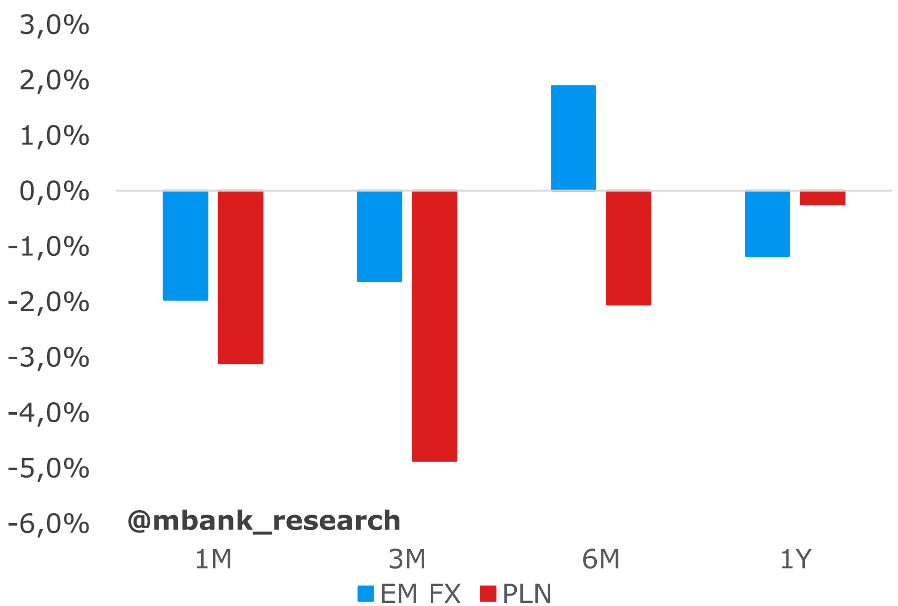
POLGB yield minus 3m WIBOR



Source: Bloomberg

PLN: weak until H2 2021 when some mild appreciation may kick in

Recently moving in the same direction as region



Note: Increase = appreciation to dolar. Decrease = depreciation to dolar

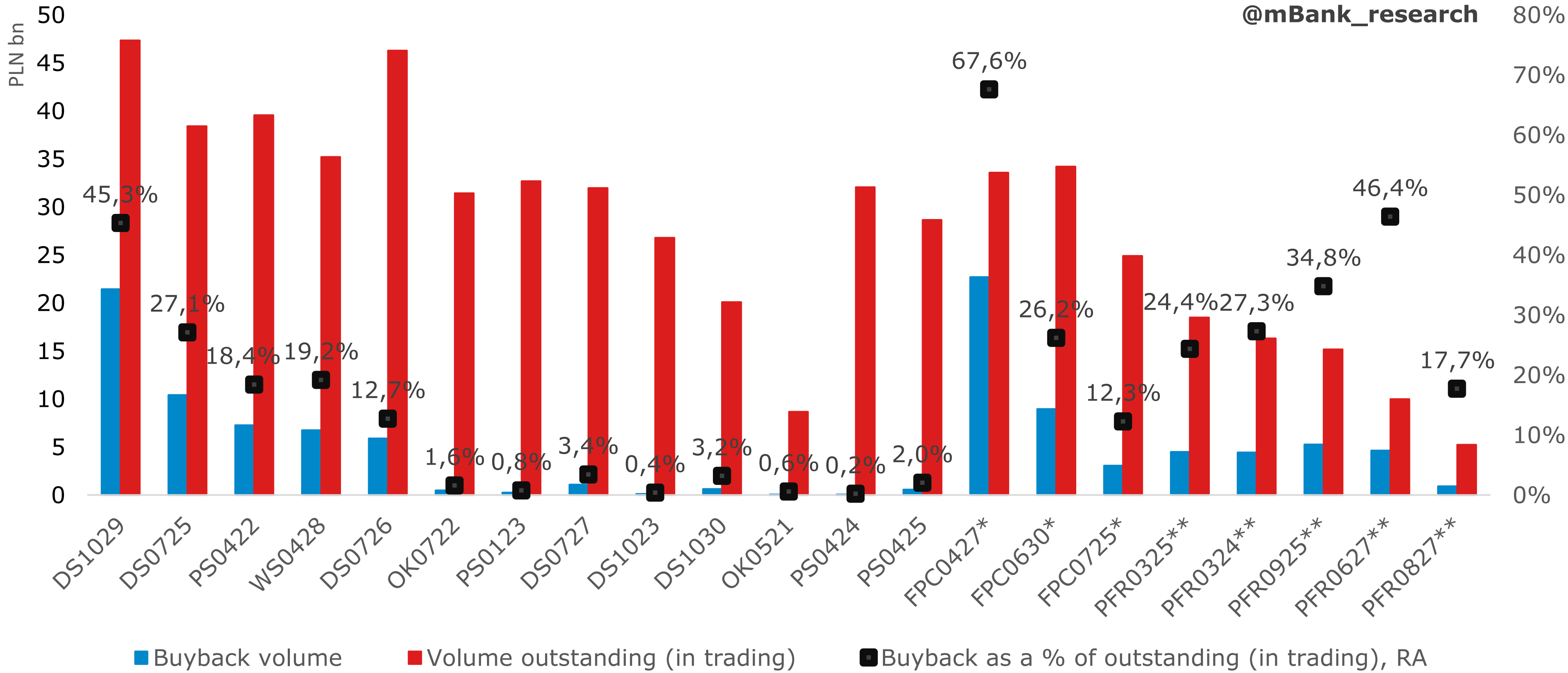
Source: Bloomberg

Real effective exchange rate

Source: BIS

- After the NBP intervention in late 2020, the zloty is moving more or less like the rest of the region.
- We think the zloty will stay weak in H1 2021, helped by strong dolar and very low real interest rates (with expectations for faster tightening acively combat by MPC's rhetoric).
- The return to modest appreciation is likely in H2 2021 as euro zone recovers, the drive for stronger dolar wanes and (cyclical) recovery trades kick in, helped by current account surplus. The most imporant risk here is – in our opinion – the MPC's attitude. Unless it changes a bit – by making the possibility of a start of policy normalization in 2022 a viable option - after the recovery takes hold, zloty will stay weak discounting low real rates and high inflation.

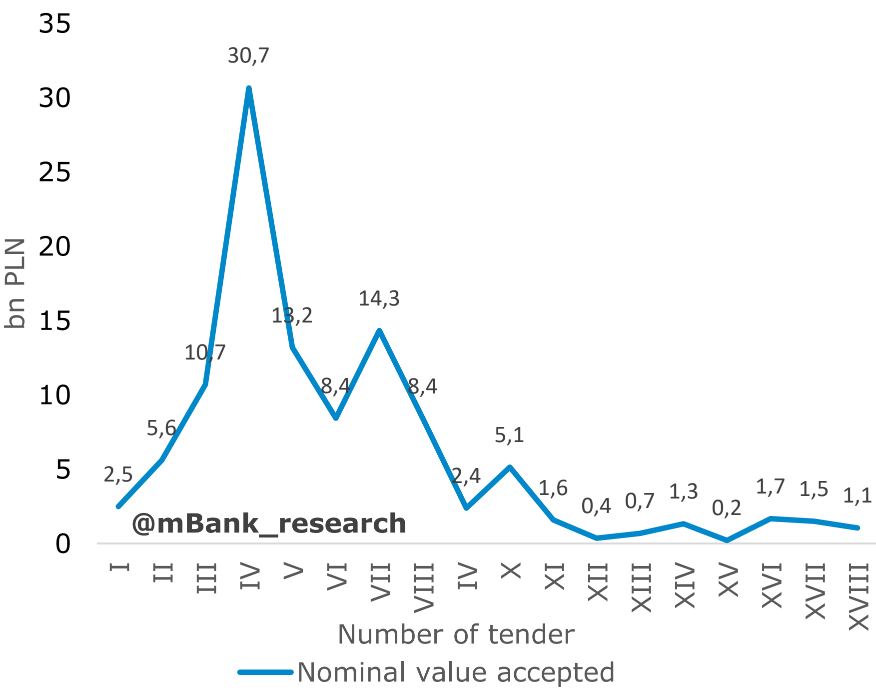
Appendix: NBP „structural" portfolio monitor

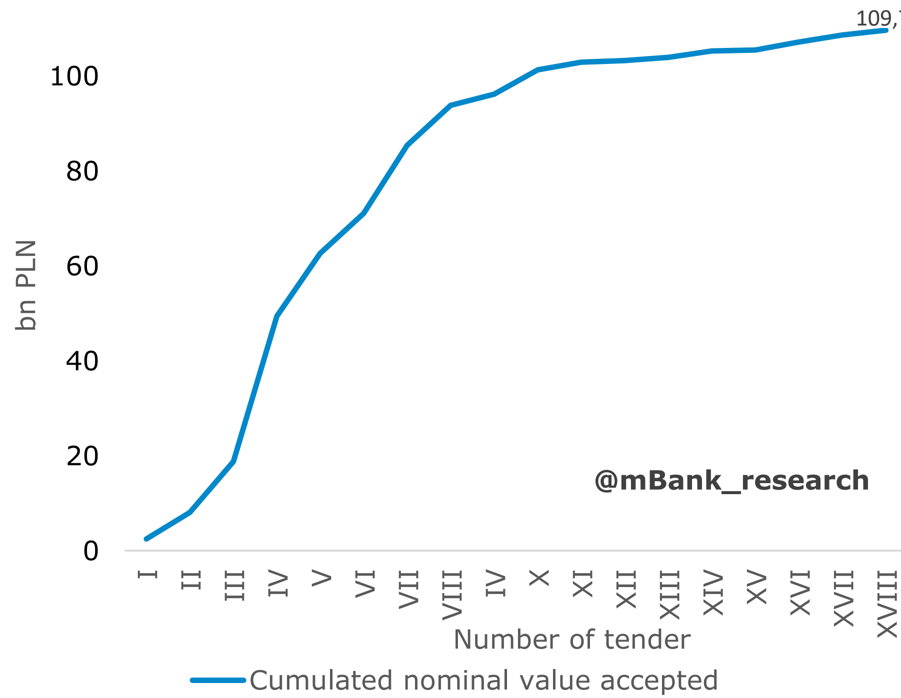


Source: Own elaboration on MF, NBP, NDS data.

- The state for 12.03.2021. We present cumulative numbers.
- NBP launched structural open market operations in March and they constitute a purely new instrument introduced to fight the crisis. **On March 11th NBP communicated that the schedule and elasticity of the operations may be enhanced to better meet current more challenging (higher) yield enovironment.**

Appendix: NBP purchases, the timeline





Source: Own elaboration on NBP data.

- The state for 12.03.2021.

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