

# Growth forecast remains unchanged

We keep our FY20 GDP growth unchanged at -3.7%. Despite introduction of lockdown in mid-March, economic growth remained solid in 1Q20. Zloty will follow global factors, while bond market participants will continue to digest last week's rate cut.

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## Watch this week

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### Forecast revision: GDP growth remains unchanged

After a careful overview of the available data and detailed GDP structure for 1Q20, we decided to keep our FY20 growth forecast unchanged at -3.7%. Despite the weaker than expected real economy data for April, the 1Q20 growth in annual terms proved to be stronger than we forecasted. However, the biggest hit is yet to come. Economic activity likely bottomed out in April (as evidenced by the double-digit drop in industry and retail sales growth) and the recovery will be gradual. We thus expect growth dynamics to plummet in 2Q20 by around 10% q/q.

The relaxation of measures since the beginning of May should support the recovery and economic activity should improve in the second half of the year, absent any second wave of the pandemic. Within the recovery plan recently proposed by the European Commission, Poland would be (tentatively) eligible for EUR 63.8bn (12.1% of GDP) in the form of grants and loans that could additionally boost investment growth. The situation on the labor market deteriorated in April and we expect the unemployment rate to increase further. Should the situation on the labor market deteriorate more severely, private consumption would remain subdued for a longer period of time.

The slowing economic growth and low oil prices will drag inflation down. We see CPI on average at 3.1% this year, due to particularly high inflation in the first quarter. The unexpected rate cut by the central bank moved Polish rates to the lowest level in the region and we believe they will stay there at least until the end of 2021. At this point, we do not see the central bank posting negative rates. The postponement of pension system reform cut PLN 13bn of budget revenues. Therefore, we see the budget deficit at 9.4% of GDP.

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## Last week's highlights

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- PMI index for May increased to 40.6.
- [Central bank cut target rate by 40bp to 0.1%](#). The decision was unexpected, as we believed that the central bank would wait for a new inflation and growth projection (due in July) for further easing. The weaker than expected real economy data for April, recent strengthening of the zloty and change in growth expectations of the MPC members were the main factors behind the easing.
- According to the NBP's statement, the volume of bonds bought within the QE program reached PLN 90.8bn.
- [1Q20 GDP growth was revised up](#) to 2.0% y/y (-0.4% q/q s.a.).
- [The flash inflation reading for May](#) came in at 2.9% y/y.
- The unemployment rate increased to 5.8% in April.

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Note: Past performance is not necessarily indicative of future results.

## Market developments

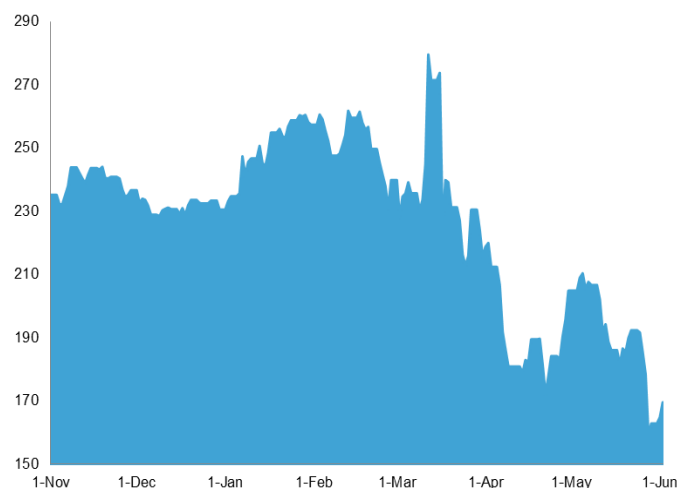
### Bond market drivers | Long end tumbles on rate cut

Ahead of the central bank meeting and subsequent rate cut, the 10Y yield remained broadly unchanged around 1.4%. The unexpected monetary easing by the NBP pushed the long end of the curve down below 1.2%. However, since then, we have seen a correction, as the 10Y yield moved towards 1.3%. The spread over the 10Y Bund narrowed and remains below 170bp. With no releases scheduled for this week, we expect markets to digest the last week's rate cut and a further increase along the curve cannot be ruled out. The QE operations are planned for June 10 and June 24.

### FX market drivers | Weaker US dollar supports zloty

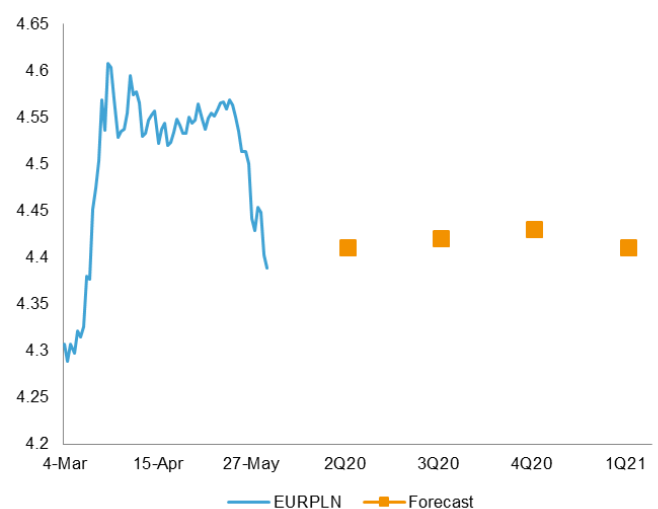
Over the course of the week, the zloty appreciated by almost 1.5% and broke the 4.50 mark vs. the EUR. Ahead of the central bank meeting, the zloty benefited from the weaker US dollar and global risk-on mood and moved towards 4.40 vs. the EUR. The unexpected rate cut by the central bank resulted in a weakening of the zloty, as it returned above 4.45 vs. the EUR at the end of the week. Yesterday's session brought further appreciation of the zloty and the EURPLN went below 4.40. Therefore, we see risks to our current forecast for the zloty, as further strengthening towards 4.35 cannot be ruled out. With an empty local calendar, the zloty will follow global news.

**Spread vs. German Bund (bp)**



Source: Bloomberg, Erste Group Research

**EURPLN**



Source: Bloomberg, Erste Group Research

## Upcoming in CEE

Date	Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Comment
02. Jun	9:00	CZ	GDP (q/q)	1Q P	-3.6%	<b>-3.6%</b>	-3.6%	GDP growth was affected mainly low decrease in exports and investment expenditures.
	9:00	CZ	GDP (y/y)	1Q P	-2.2%	<b>-2.2%</b>	-2.2%	As January and February were favorable, a slump in real economic activity was not so negative in 1Q.
	9:00	HU	PPI (y/y)	Apr			4.3%	
	9:00	HU	Trade Balance	Mar F			436.49	
03. Jun	8:00	RO	Unemployment Rate	Apr			2.88%	
	8:00	RO	PPI (y/y)	Apr			0.65%	
04. Jun	8:00	RO	Retail Sales (y/y)	Apr		<b>-7.2%</b>	4.1%	Retail sales to enter negative territory in April for the first time in almost seven years
	9:00	CZ	Wages (y/y)	1Q	1.9%	<b>2.60%</b>	3.6%	High inflation and slightly weaker nominal wage growth implied slower growth of real wages.
	9:00	HU	Retail Sales (y/y)	Apr	-15.00%	<b>-11.5%</b>	3.5%	Full force of the lockdown in April implies huge drop in retail sales, especially in the field of durable goods and fuel sales.
	9:00	SK	Retail Sales (y/y)	Apr		<b>-16.80%</b>	-3.6%	A significant decline in retail sales due to the measures associated with the pandemic is expected for April
05. Jun	9:00	CZ	Retail Sales (y/y)	Apr	-19.8%	<b>-12.50%</b>	-8.9%	Retail sales were negatively affected by the crisis as households postpone part of their purchases. On the other hand, demand for food increased in March and April, which in turn mitigated the slump.
	9:00	HU	Industrial Production (y/y)	Apr	-23.3%	<b>-21.60%</b>	-9.99%	Closure of decisive car-makers caused huge drop of industrial performance in April.
	9:00	SK	GDP (y/y)	1Q F			-3.9%	

Source: Bloomberg, Erste Group Research

## Market forecasts

### Government bond yields

	current	2020Q3	2020Q4	2021Q1	2021Q2
<b>Croatia 10Y</b>	0.9	1.0	1.0	1.0	-
spread (bps)	135	140	120	110	-
<b>Czechia 10Y</b>	0.7	1.4	1.4	1.4	1.4
spread (bps)	109	175	155	147	154
<b>Hungary 10Y</b>	1.9	2.1	2.2	2.4	2.5
spread (bps)	235	250	240	245	255
<b>Poland 10Y</b>	1.3	1.2	1.3	1.3	1.3
spread (bps)	168	160	145	140	140
<b>Romania 10Y</b>	4.0	3.8	3.7	3.5	3.6
spread (bps)	442	420	385	360	370
<b>Slovakia 10Y</b>	0.3	0.9	0.9	0.9	0.9
spread (bps)	68	130	110	100	102
<b>Slovenia 10Y</b>	0.51	0.60	0.60	0.60	0.60
spread (bps)	92	100	80	70	70
<b>Serbia 5Y</b>	2.6	2.3	2.4	2.2	2.1
spread (bps)	300	265	255	230	220
<b>DE10Y</b>	-0.4	-0.4	-0.2	-0.1	-0.1

### 3M Money Market Rate

	current	2020Q3	2020Q4	2021Q1	2021Q2
<b>Czechia</b>	0.34	0.36	0.36	0.35	0.43
<b>Hungary</b>	0.91	1.00	1.00	1.00	1.00
<b>Poland</b>	0.28	0.68	0.68	0.68	0.68
<b>Romania</b>	2.29	1.75	1.25	1.25	1.50
<b>Serbia</b>	1.17	0.99	0.91	0.91	0.91
<b>Eurozone</b>	-0.33	-0.40	-0.40	-0.40	-

### FX

	current	2020Q3	2020Q4	2021Q1	2021Q2
<b>EURHRK</b>	7.59	7.55	7.60	7.55	7.48
forwards		7.59	7.59	7.59	7.59
<b>EURCZK</b>	26.60	26.82	26.45	26.05	25.81
forwards		26.64	26.65	26.65	26.67
<b>EURHUF</b>	345.29	350.00	350.00	345.00	345.00
forwards		346.50	347.18	347.64	348.45
<b>EURPLN</b>	4.39	4.42	4.43	4.41	4.40
forwards		4.40	4.41	4.42	4.43
<b>EURRON</b>	4.84	4.88	4.90	4.92	4.94
forwards		4.90	4.94	4.99	5.03
<b>EURRSD</b>	117.65	117.50	117.70	117.50	117.40
forwards		-	-	-	-
<b>EURUSD</b>	1.12	1.10	1.10	1.12	-

### Key Interest Rate

	current	2020Q3	2020Q4	2021Q1	2021Q2
<b>Croatia</b>	0.30	0.05	0.05	0.05	0.05
<b>Czechia</b>	0.25	0.25	0.25	0.25	0.25
<b>Hungary</b>	0.90	0.90	0.90	0.90	0.90
<b>Poland</b>	0.10	0.10	0.10	0.10	0.10
<b>Romania</b>	1.75	1.50	1.50	1.50	1.50
<b>Serbia</b>	1.50	1.25	1.25	1.25	1.25
<b>Eurozone</b>	0.00	0.00	0.00	0.00	-

Source: Bloomberg, Erste Group Research

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