

Strong recovery on the way

We revise our FY21 and FY22 GDP growth forecast upwards. Government presented new program that includes tax reforms, increased healthcare spending and extension of child benefits. 'Polish Deal' will boost private consumption in 2022.

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Watch this week

Upward revision of 2021 and 2022 growth forecast

We revised up our FY21 GDP growth forecast to 4.2% and FY22 forecast to 5.4%, reflecting recent developments and government announcements. Flash 1Q21 GDP growth arrived at -1.2% y/y (+0.9% q/q s.a.), proving the resilience of the Polish economy to COVID-19 restrictions, which affected the retail and services sectors and have been in place throughout 1Q21. The beginning of 2021 likely marked the last quarter with negative annual growth dynamics. The base effect and recovering economic activity will push 2Q12 GDP growth toward double-digit dynamics.

Pent-up demand and the relatively good situation on the labor market will boost household spending this year. We expect private consumption to be the main growth driver and increase by 4.1% in 2021. On the other hand, the still high degree of uncertainty will weigh on investment growth, which we see at only 1.7% this year. In 2022, funds available within the EU Recovery Plan will boost investments, while household spending will further accelerate, supported by the improving labor market and recently announced government program.

Over the weekend, the Polish government presented a new program, the 'Polish Deal', which includes tax reform, increased healthcare spending (to 6% of GDP in 2023) and expansion of child benefits. The government plans to increase the tax-free amount to PLN 30K (from the current PLN 8K) and raise the second PIT rate to PLN 120K (from the current PLN 85K). Moreover, the health contribution will be increased to 9% and will no longer be deductible from the PIT base. Furthermore, changes in civil employment contracts are planned as well. The increase of the tax-free amount is expected to cost the budget PLN 20-22bn annually, while increases in health contributions should bring PLN 14bn, with another PLN 2.5bn coming from changes in employment contracts. The government plans to introduce the announced tax reforms as of January 2022. All in all, the proposed changes will increase the disposable income of households and thus boost private demand, while further limiting the propensity to invest.

May 20 | Labor market statistics for April

We expect wage and employment growth for April to be strongly affected by the low base from last year, when restrictions and 'Kurzarbeit' schemes weighed on the labor market statistics. Double-digit wage growth cannot be ruled out, while employment dynamics likely returned to positive territory. Separately, the unemployment rate eased by 0.1pp to 6.3% in April.

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

Last week's highlights

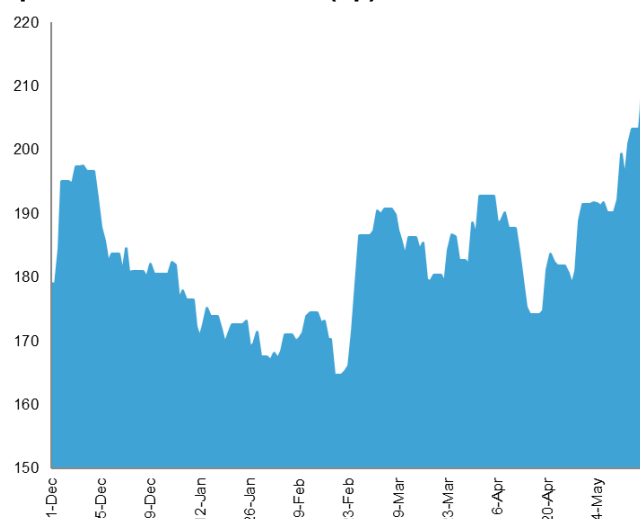
- Flash [1Q21 GDP](#) growth arrived at -1.2% y/y (+0.9% q/q s.a.). We revised our FY21 GDP growth forecast up to 4.2% (from 3.4%).
- Flash inflation for April has been confirmed at 4.3% y/y (0.8% m/m).
- Core inflation remained unchanged at 3.9% y/y in April.
- MPC members addressed recent surge in inflation. Rate setter Gatnar called for policy normalization as clear sign that central bank's focus shifted back to inflation. MPC member Zyzynski suggested 10-15bp hike in order to anchor inflation expectations. MPC member Hardt pointed to decrease benefits of loose monetary policy and growing costs of rising inflation.
- We published report on [CHF loans in Poland](#).

Market developments

Bond market drivers | 10Y yield surged toward 2%

Over the course of the week, the long end of the Polish LCY curve went sharply up by 20bp to 1.9%, following regional and core market developments. While the 10Y German Bund went up by 10bp during the week, the long end of the Romanian curved shifted up by 25bp and the Hungarian by 34bp. As a result, the spread over the 10Y Bund widened visibly to 210bp, which is the highest since the outbreak of the pandemic last year. Despite the increased purchases of the National Bank of Poland, the upward pressure on the curve persists. Last week, the NBP bought papers worth almost PLN 8bn and plans to hold another auction on May 26. This week, the MinFin will hold a regular bond auction and offer papers worth PLN 4-7bn. Given the recent strong increase of yields along the whole curve, we revised up our yield forecast and now expect the spread against the German Bund to widen toward 240bp by the end of the year.

Spread vs. German Bund (bp)



Source: Bloomberg, Erste Group Research

EURPLN



Source: Bloomberg, Erste Group Research

FX market drivers | Zloty followed regional peers

Surprisingly high inflation for April in Czechia and Hungary fueled market expectations for an earlier start to the monetary tightening cycle than was anticipated before. As a result, CEE currencies appreciated visibly, benefiting as well from a weaker US dollar. The zloty moved toward 4.53 vs. the EUR. We revised our EURPLN forecast and expect the zloty to appreciate marginally by the end of the year, conditionally on a stable monetary policy outlook. Recent comments from the Czech and Hungarian central banks suggest that the policy normalization in the CEE region might start earlier. If surging inflation and a strong economic recovery, coupled with policy normalization in Czechia and Hungary, force NBP to react, we could see stronger appreciation of the zloty. Moreover, market expectations for a weaker USD are positive for the zloty.

Upcoming in CEE

Date	Time	Country	Indicator	Period	Survey	Erste Est.	Prev.	Comment
18. May	8:00	RO	GDP (q/q)	1Q A		0.70%	4.82%	Mixed high frequency data vs. rather strong confidence indicators.
	8:00	RO	GDP (y/y)	1Q A	-1.80%	-1.80%	-1.4%	Past data revisions could lead to significant forecast changes.
	9:00	HU	GDP (q/q)	1Q P		-0.40%	1.30%	
	9:00	HU	GDP (y/y)	1Q P	-3.70%	-3.90%	-3.50%	Industrial exports probably contributed positively to GDP, while domestic demand might have remained subdued.
	9:00	SK	GDP (y/y)	1Q P		-3.10%	-2.70%	First quarter of 2021 hit harder due to stricter lockdown, with highly subdued household consumption and investment activity. On other hand, foreign demand assisted Slovak economy.
19. May		RS	Current Account Balance (monthly)	Mar			-49	
		SK	Unemployment Rate	Apr		7.98%	8.00%	We expect marginal decrease in unemployment rate, because of easing of restrictions in second half of April.
20. May	10:00	PL	Wages (y/y)	Apr	10.1%	11.50%	8.00%	Base effect to push wage growth into double-digit territory.
	11:00	HR	Unemployment Rate	Apr		8.90%	9.30%	Unemployment rate further down on monthly level in April.
	11:00	HR	Wages (y/y)	Mar			1.70%	
21. May	10:00	PL	PPI (y/y)	Apr	4.90%	5.10%	3.90%	Surging commodity prices to push PPI further up.
	10:30	SI	PPI (y/y)	Apr			2.00%	

Source: Bloomberg, Erste Group Research

Forecasts

Government bond yields

	current	2021Q2	2021Q3	2021Q4	2022Q1
Croatia 10Y	0.5	0.0	0.5	0.5	0.6
spread (bps)	62	23	68	66	68
Czechia 10Y	1.8	1.8	1.8	1.9	2.0
spread (bps)	187	198	198	203	203
Hungary 10Y	3.2	2.7	2.7	2.7	2.8
spread (bps)	330	288	286	289	292
Poland 10Y	2.0	2.00	2.20	2.20	2.25
spread (bps)	208	223	238	236	233
Romania10Y	3.3	2.9	2.8	2.8	2.9
spread (bps)	338	313	298	291	298
Slovakia 10Y	0.3	0.0	0.2	0.3	0.4
spread (bps)	41	23	33	46	43
Slovenia 10Y	0.29	0.10	0.10	0.10	0.20
spread (bps)	40	33	28	26	28
Serbia 5Y	2.4	2.2	2.2	2.2	2.1
spread (bps)	251	243	238	236	218
DE10Y*	-0.1	-0.2	-0.2	-0.2	-0.1

* Spreads based on Bloomberg consensus forecast

3M Money Market Rate

	current	2021Q2	2021Q3	2021Q4	2022Q1
Czechia	0.36	0.44	0.67	0.83	0.92
Hungary	0.85	0.78	0.78	0.79	0.80
Poland	0.21	0.21	0.21	0.21	0.21
Romania	1.54	1.55	1.50	1.40	1.50
Serbia	0.88	0.87	0.85	0.83	0.83
Eurozone	-0.55	-0.54	-0.54	-0.54	-0.54

Real GDP growth (%)

	2019	2020	2021f	2022f
Croatia	2.9	-8.0	4.5	4.0
Czechia	2.2	-5.6	3.3	4.3
Hungary	4.6	-5.0	4.4	4.7
Poland	4.7	-2.7	4.2	5.4
Romania	4.1	-3.9	4.2	4.5
Serbia	4.2	-1.0	6.0	4.0
Slovakia	2.5	-4.8	4.0	4.8
Slovenia	3.2	-5.5	4.4	4.1
CEE8 avg	3.9	-4.0	4.1	4.8

Public debt (% of GDP)

	2019	2020	2021f	2022f
Croatia	72.8	88.7	88.1	86.4
Czechia	31.2	38.4	45.0	48.1
Hungary	65.5	80.4	78.6	76.9
Poland	45.6	57.5	57.0	55.0
Romania	35.3	47.3	50.8	52.0
Serbia	52.1	57.4	59.5	57.8
Slovakia	48.2	60.3	63.5	63.5
Slovenia	65.6	80.8	79.5	77.1
CEE8 avg	45.9	57.4	58.7	58.2

FX

	current	2021Q2	2021Q3	2021Q4	2022Q1
EURHRK	7.52	7.53	7.53	7.53	7.53
EURCZK	25.45	25.62	25.54	25.36	25.08
EURHUF	352.41	360.00	360.00	360.00	360.00
EURPLN	4.54	4.55	4.52	4.50	4.50
EURRON	4.93	4.93	4.94	4.95	5.01
EURRSD	117.55	117.50	117.40	117.50	117.50
EURUSD	1.21	1.18	1.18	1.20	1.20

Key Interest Rate

	current	2021Q2	2021Q3	2021Q4	2022Q1
Croatia	0.05	0.05	0.05	0.05	0.05
Czechia	0.25	0.25	0.50	0.75	0.75
Hungary	0.60	0.60	0.60	0.60	0.75
Poland	0.10	0.10	0.10	0.10	0.10
Romania	1.25	1.25	1.25	1.25	1.25
Serbia	1.00	1.00	1.00	1.00	1.00
Eurozone	0.00	0.00	0.00	0.00	0.00

Average inflation (%)

	2019	2020	2021f	2022f
Croatia	0.8	0.1	1.2	1.5
Czechia	2.8	3.2	2.5	2.3
Hungary	3.4	3.3	4.2	3.2
Poland	2.3	3.4	4.0	3.5
Romania	3.8	2.7	3.2	2.4
Serbia	1.9	1.6	2.0	1.9
Slovakia	2.7	1.9	1.3	1.9
Slovenia	1.6	0.0	0.4	1.5
CEE8 avg	2.7	2.8	3.2	2.8

C/A (%GDP)

	2019	2020	2021f	2022f
Croatia	2.8	-0.8	0.5	0.4
Czechia	-0.3	3.2	0.2	0.3
Hungary	-0.5	0.1	-0.2	-0.3
Poland	0.5	3.5	2.1	1.2
Romania	-4.9	-5.2	-4.8	-4.2
Serbia	-6.9	-4.3	-3.6	-3.7
Slovakia	-2.7	-2.7	-1.6	-0.9
Slovenia	5.6	7.3	6.7	5.6
CEE8 avg	-0.8	0.9	0.1	-0.2

Unemployment (%)

	2019	2020	2021f	2022f
Croatia	6.6	7.5	8.0	6.9
Czechia	2.0	2.6	3.4	2.8
Hungary	3.4	4.2	4.5	3.8
Poland	5.4	5.9	6.2	5.9
Romania	3.9	4.9	5.9	6.1
Serbia	10.4	9.0	8.9	8.5
Slovakia	5.8	6.7	7.0	6.0
Slovenia	4.4	5.1	5.2	4.9
CEE8 avg	4.6	5.2	5.7	5.3

Budget Balance (%GDP)

	2019	2020	2021f	2022f
Croatia	0.3	-7.4	-4.2	-3.0
Czechia	0.3	-6.1	-7.0	-2.7
Hungary	-2.1	-8.1	-7.4	-5.0
Poland	-0.7	-7.0	-4.5	-3.2
Romania	-4.4	-9.2	-7.8	-5.4
Serbia	-0.2	-8.0	-6.5	-1.6
Slovakia	-1.3	-6.1	-6.0	-4.0
Slovenia	0.5	-8.4	-6.0	-4.0
CEE8 avg	-1.2	-7.4	-6.0	-3.7

Source: Bloomberg, Erste Group Research

Erste Group Research

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