The rise in global food prices is gaining momentum

This week

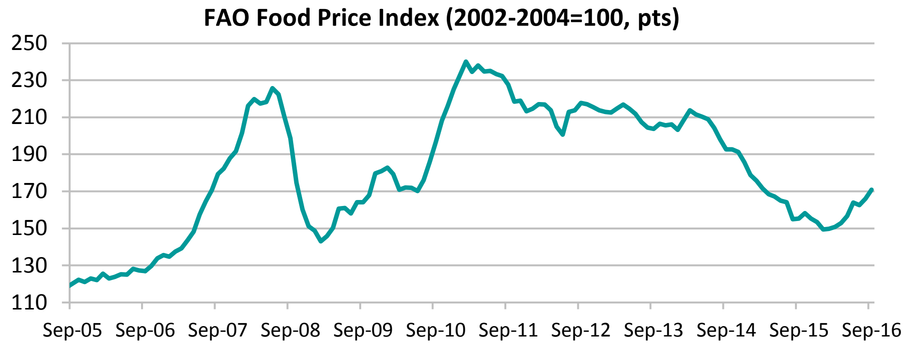
- **The most important event this week will be the Wednesday's reading of the September industrial production and retail sales in Poland.** We forecast that industrial production dynamics dropped to 2.8% YoY in September vs. 7.5% in August, due to the unfavourable difference in the number of working days effect. In turn, the nominal retail sales growth rate rose, in our view, to 6.7% YoY in September vs. 5.6% in August, due to higher expenditures related to the 500+ scheme, rise in retail prices, and improved consumer sentiment. We believe that if our forecasts materialize, the aggregate impact of the data will be slightly negative for PLN and yields on Polish bonds.
- **Important data from China will be released on Wednesday.** We expect that the economic growth rate has not changed in Q3 compared to Q2 and amounted to 1.8% QoQ (6.7% YoY both in Q3 and in Q2). In addition, other monthly data (industrial production, retail sales, and urban investments) will point, in total, to a similar pace of economic activity in September as in the month before. Our forecast of GDP dynamics is equal to the market consensus. Consequently, we expect that the aggregate impact of the above readings will be neutral for PLN.
- **The ECB meeting will be held on Thursday**. In our view, it will not bring any changes in the Eurozone monetary policy. At the press conference, M. Draghi is most likely to suggest that the ECB is working on changes in its monetary policy, making the further evolution of the ECB monetary policy conditional on the December macroeconomic projection. We believe that in December the ECB will decide to extend the asset purchase program by 6 months. During the conference after the ECB meeting, we may see increased volatility of PLN rate and prices of the Polish debt.
- **Significant hard data on US economy and business survey results will be released this week.** We forecast that industrial production increased by 0.2% MoM in September vs. a 0.4% decline in August, due to higher production growth in manufacturing. We expect the data on house starts (1174k in September vs. 1142k in August), building permits (1153k vs. 1152k), and existing home sales (5.31M vs. 5.33M) to confirm the continuation of the recovery in the US real estate market. Mixed results of business surveys for manufacturing will also be released this week. We forecast that the NY Empire State Index rose to 0.2 pts in October vs. -0.2 in September, while Philadelphia FED Index dropped to 4.0 pts in October vs. 12.8 pts in September. We believe that the aggregate impact of data on the US economy on the financial market will be limited.
- **The September data on average wages and employment in the corporate sector in Poland will be released on Tuesday**. We forecast that employment dynamics have not changed compared to August and amounted to 3.1% YoY. In turn, the average wage dynamics dropped to 4.4% YoY in September vs. 4.7% in August (high base effect from the year before). The release of data on corporate wages and employment will confirm the strong recovery in the labour market. The data will be neutral for PLN and the debt market, we believe.

Last week

- **The Minutes of the September FOMC meeting were released on Wednesday.** According to Minutes, most FED members agreed that there were growing numbers of arguments supporting interest rate hikes. Some believed that the interest rate hike should take place relatively soon if only the improvement in the labour market and higher economic activity continue. On the other hand, some FED members need more evidence that inflation will be getting closer to the target. The text of the Minutes supports our scenario in which we assume one increase of the target range for the Federal Reserve funds in 2016 by 25 bp in December to [0.50%; 0.75%].

- **Nominal retail sales dynamics in the US rose to 0.6% MoM in September from -0.2% in August.** Excluding car sales, they rose by 0.5% MoM in September vs. a 0.2% decline in August. The increase in retail sales in September resulted from higher sales dynamics in most of their categories. The preliminary University of Michigan Index was also released last week and dropped to 87.9 pts in October vs. 91.2 pts in September, suggesting a deterioration in consumer sentiment in the US. The index decline resulted from a decrease in its sub-index concerning expectations, while an increase in the sub-index concerning the assessment of the current situation had an opposite impact. The last week's data from the US economy do not change our forecast, in which the annualized GDP growth rate in the US will clearly accelerate to 3.9% in Q3 vs. 1.4% in Q2, running above the potential growth rate level.
- **According to the final data, CPI inflation in Poland rose to -0.5% YoY in September vs. -0.8% in August.** The increase in inflation was mainly due to higher dynamics of fuel and energy prices, which increased inflation by 0.5 pp in total. Slower price growth in the category "food and non-alcoholic beverages", which reduced inflation by 0.2 pp, had an opposite impact. Lower dynamics of food prices were largely due to high base effects from the year before, related to the last year's drought, visible especially in case of vegetables' prices (see MACROpulse of 11/10/2016). Core inflation has not changed in September compared to August and amounted to -0.4%. We forecast that deflation in Poland will continue until November 2016 and in the whole 2016 will run at a level of -0.6% YoY vs. -0.9% in 2015.
- **The deficit in the Polish current account rose to EUR 1047M in August from EUR 635M in July.** The decrease in the current account balance was due to lower balances on goods and services (lower from July by EUR 316M and EUR 187M, respectively). Higher balances of secondary and primary income (higher from July by EUR 47M and EUR 44M, respectively) had an opposite impact. Export dynamics rose to 8.0% YoY in August vs. -5.1% in July, and imports dynamics rose to 10.4% YoY vs. -6.8%. Higher exports and imports growth was largely due to a favourable difference in the number of working days. The data pose a downside risk to our forecast, in which the relation of cumulative current account balance for the last 4 quarters to GDP will increase to -0.4% in Q3 vs. -0.6% in Q2.
- **The surplus in the Chinese balance of trade dropped to USD 42.0bn in September vs. USD 52.1bn in August**. At the same time, export dynamics dropped to -10.0% YoY in September vs. -2.8% in August and import dynamics dropped to -1.9% YoY vs. 1.5%. Thus, the data suggest a clear deterioration in external demand for the Chinese exports in September. The last week's data do not alter our forecast, in which the GDP in China will increase by 6.7% in 2016 vs. a 6.5% increase in 2015. Thus, its growth rate will be in line with the GDP growth target set by the Chinese government for 2016 at a level of "6.5-7.0%".
- **ZEW index reflecting the sentiment among analysts and institutional investors regarding the economic situation in Germany rose to 6.2 pts in October vs. 0.5 pts in September**. According to the press release, the index increase resulted from better assessment of the current situation. Nevertheless, survey participants also pointed out the risks to the German economy, including the problems of the German banking sector, which may reduce further improvement in sentiment in the coming months. Data on the German balance of trade were also released last week and its surplus rose to EUR 22bn in August vs. 19.4bn in July. At the same time, export dynamics rose to 5.4% MoM in August vs. -2.6% in July and import dynamics rose to 3.0% MoM vs. -0.7%. The last week's data on the German economy do not change our forecast that the GDP growth rate in Germany will not change in Q2 compared to Q3 and will amount to 0.4%.

The rise in global food prices is gaining momentum

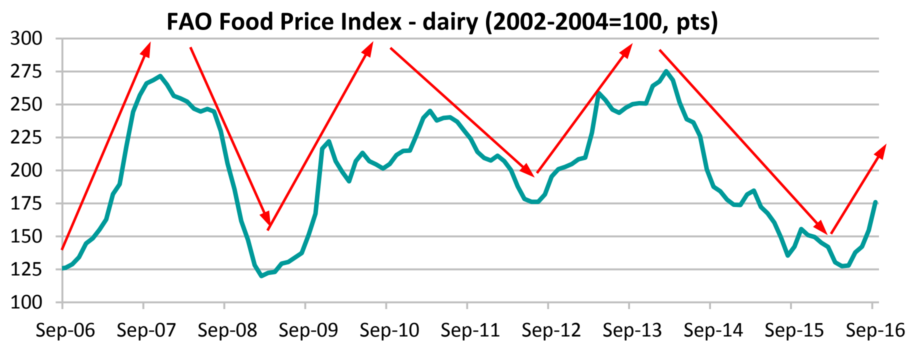


Source: FAO, Credit Agricole

The FAO Food Price Index rose to 170.9 pts in September vs. 166.0 pts in August (+2.9% MoM). At the same time, it has been the second month in a row when the FAO Food Price Index rose in annual terms (+10.0% YoY in September vs. +7.1% in August). The analysis below focuses on the assessment of the sustainability of the rise in global food prices and its impact on inflation in Poland.

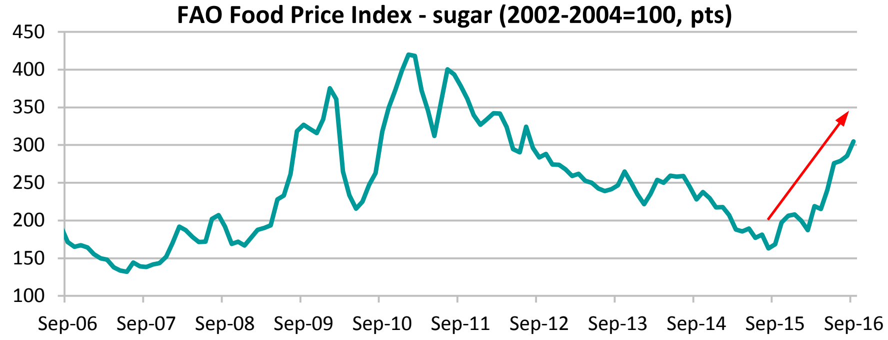
The FAO food price index illustrates the level of global food prices compared to their average level between 2002 and 2004. Thus, the current index value (170.9 pts) indicates that global food prices were higher by 70.9% in September 2016 than in the years 2002-2004. The index is a weighted average of five sub-indices of basic foods: meat, dairy products, cereals, vegetable oil, and sugar. The weights of the respective sub-indices reflect the share of the respective categories in the global food exports between 2002 and 2004.

The index increase in monthly terms resulted from higher prices of 4 out of its 5 sub-indices: dairy products (+13.8% MoM), sugar (+6.7% MoM), vegetable oil (+1.7% MoM), and meat (+0.2% MoM). The falling prices of cereals (-1.9% MoM) had an opposite impact. In annual terms, higher growth rate of global food prices resulted from higher dynamics of prices of sugar (81.0% YoY in September vs. 75.1% in August), dairy products (23.7% vs. 14.1%), vegetable oil (28.1% vs. 25.3%), and meat (-2.4% vs. -4.4%), while lower dynamics of cereals prices (-8.9% YoY vs. -7.4%) had an opposite impact.



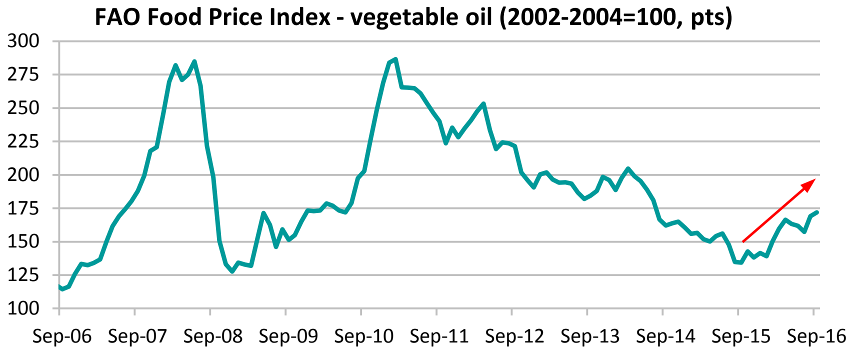
Source: FAO, Credit Agricole

The continued increase in the prices of dairy products is a consequence of the global milk market entering the upward phase of the cycle in Q2 2016. It results from lower dynamics of milk production amongst major exporters of dairy products and a simultaneous strong recovery of demand for dairy products in China. Due to low price elasticity of demand characteristic to the dairy industry, we expect that the rise in prices of dairy products will continue into subsequent quarters.



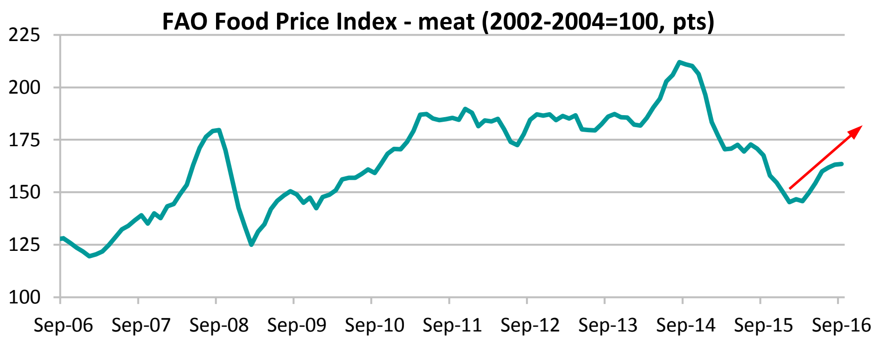
Source: FAO, Credit Agricole

The sharp increase in global sugar prices, which rose by 86.8% between August 2015 and September 2016, results from the decrease in its world stocks continuing since 2015. It is related to a lower, against historical background, production of sugar among major producers of sugar cane (i.a. India, China, and Thailand), given a simultaneous increase in the global consumption of sugar. In our view, the world sugar stocks are hardly likely to be replenished soon; therefore, we believe that the rise in its prices will be continued in the coming months.



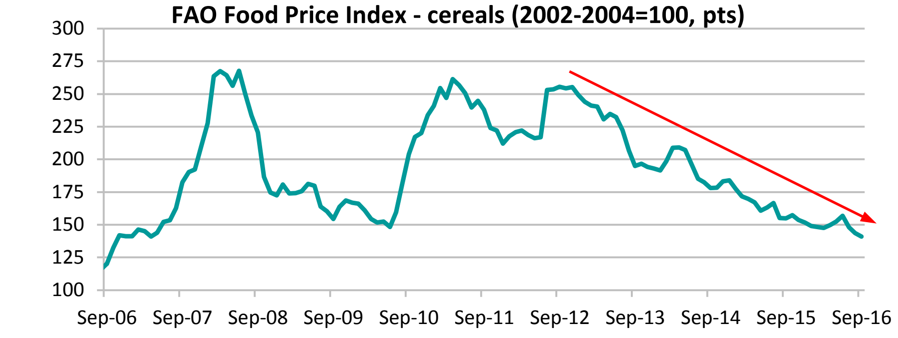
Source: FAO, Credit Agricole

The continuing upward trend in the prices of vegetable oil is the effect of the recently dwindling stocks of oilseeds. In accordance with USDA forecasts, the relation of ending stocks and consumption in the oilseeds market will decrease to 16.2% in the season 2016/2017, which will be its lowest level since the season 2014/2015. The reduction of stocks is a consequence of the higher consumption of oilseeds from their production, that has been continuing for two years now. We expect that in the coming months conducive to higher consumption of oilseeds and, consequently, to a rise in prices of vegetable oil will be the growing oil prices, which increase the relative price competitiveness of biofuels.



Source: FAO, Credit Agricole

A rise in meat prices has also been visible in recent months. It is especially visible for pork and poultry, which is due to a strong demand for these sorts of meat from the countries of South-East Asia. In the case of beef, the rise in prices continues to be limited by relatively low milk prices, which are conducive to a higher supply of this type of meat. We believe that the global prices of meat and of pork in particular can be expected to continue to rise in the next few months. In addition, the fact that the global milk market will enter an upward phase of the cycle will be conducive to a reduction of beef supply and, consequently, to an increase in its price.

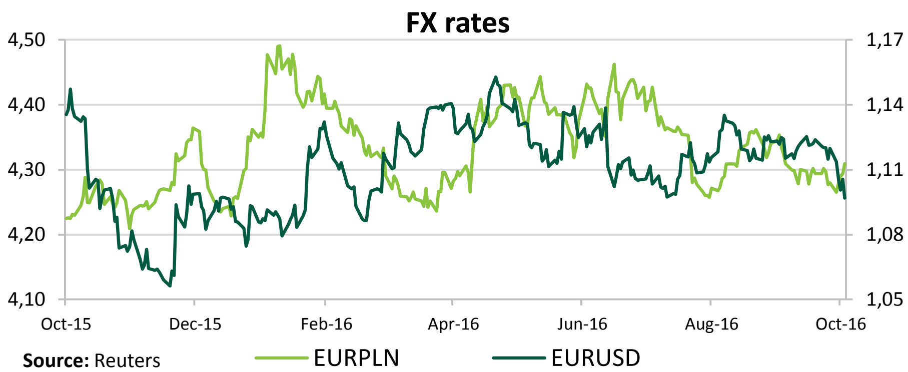


Source: FAO, Credit Agricole

A decrease continues in the prices of cereals, which in September 2016 hit the lowest level since October 2006. The falling cereal prices result from their growing oversupply in the global market. According to the data of the International Grain Council, the relation of ending stocks and consumption in the cereals market will rise to 24.1% in the season 2016/2017 vs. 23.8% in the season 2015/2016. Consequently, the likelihood of a significant rise in the prices of cereals in the coming months remains to be low.

The structure of global food price growth supports our view that the downward trend of global food prices has permanently reversed at the beginning of 2016. Due to the strong global integration of agricultural markets, the growing global food prices may be expected to be conducive to a rise in food prices in Poland. In Q4 2016 and in H1 2017, the rise in food prices will, in our view, be especially visible in the case of meat, dairy products, and sugar. Lower prices of fruit and vegetables will have an opposite impact on inflation, due to high base effects from the year before, related to the last year's drought. In addition, due to low base effects for the dynamics of fuel and energy prices (electricity and gas price cuts in January 2016), inflation will sharply increase to 1.8% YoY in Q1 2017. In H2 2017, we expect a slight decline in inflation. On the one hand, the closing of the output gap will be conducive to further increase in core inflation. On the other hand, the gradually abating low base effects for fuel prices will have an opposite impact. In addition, we expect the dynamics of food prices to decrease due to the high base effects from H2 2016. We expect that in 2017 the average yearly inflation will run at 1.8%. The main risks to our forecast are the evolution of the global fuel prices and changes in estimates concerning the global demand-supply situation for major agricultural products.

Data on domestic industrial production slightly negative for PLN

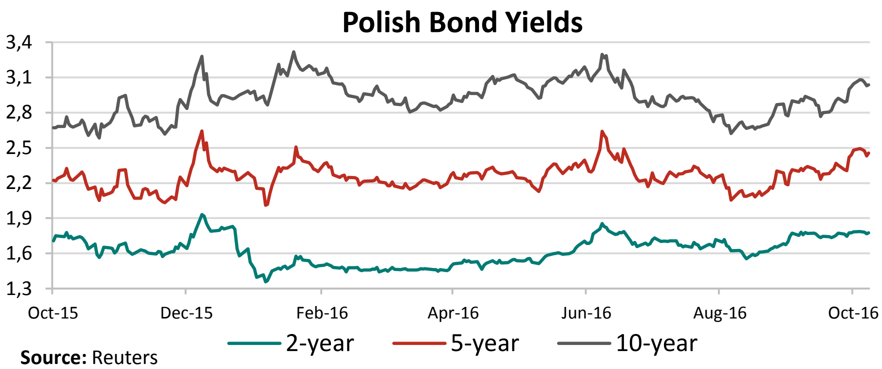


Source: Reuters

Last week EURPLN rate rose to 4.3092 (weakening by 0.7%). Monday saw appreciation of PLN and other emerging currencies together with a decrease in global risk aversion, reflected by a decrease in VIX index. Conducive to higher risk appetite may have been i.a. the presidential debate in the US, held on Sunday to Monday night, which the markets perceived as an increase in the likelihood of H. Clinton winning the elections. On Tuesday, PLN started depreciating and stayed within the downward trend until Thursday. Conducive to its depreciation was the increased uncertainty in the markets related to the anticipation of the Minutes of the September FOMC meeting as well as a clearly weaker from the market expectations data on the Chinese foreign trade, pointing to deterioration in demand in the global economy. Thursday afternoon saw a slight correction; nevertheless, from Friday morning, PLN was again depreciating, due to weaker-than-expected data on the Polish balance of payments.

The most important for PLN this week will be the Wednesday's data on industrial production and retail sales in Poland. If our forecasts materialize, the aggregate impact of the readings may be slightly negative for PLN. The Thursday's meeting of the ECB may contribute to increased volatility of PLN. Our forecasts concerning the data from China (GDP, retail sales, industrial production, and urban investments) and the USA (industrial production, house starts, building permits, existing home sales, NY Empire State Index, and Philadelphia FED Index) are close to the market consensus; therefore, we believe that their impact on PLN will be limited. Domestic data on corporate employment and average wages will also be neutral for PLN, we believe.

Polish debt market focuses on ECB meeting



Source: Reuters

Last week the yield of Polish 2-year benchmark bonds dropped to a level of 1.774 (down by 1 bp), of 5-year bonds to a level of 2.455 (down by 2 bp), and of 10-year bonds to a level of 3.038 (down by 1 bp). On Monday, the rise in yields on Polish bonds continued, following the core markets, which was related to increased market expectations of further normalization of the monetary policy in the US. On Tuesday, the trend reversed and decline in yields on Polish bonds continued until Thursday. It was most likely related to higher demand for the Polish debt, due to its relatively low prices. On Thursday Polish bonds opened higher than they closed on Wednesday, as the Minutes of the September's FOMC meeting fail to include information that would suggest a significant increase in the likelihood of a sooner than expected normalization of the US monetary policy. On Friday, the prices of the Polish debt were stable.

This week, the Polish debt market will focus on the Thursday's meeting of the ECB. We believe that during the conference after the meeting, we may see increased volatility of prices of Polish bonds. The aggregate impact of domestic data on industrial production and retail sales may be slightly positive for the prices of the Polish debt. Data from the US economy (industrial production, house starts, building permits, existing home sales, and NY Empire State and Philadelphia FED Indices) and domestic data on corporate employment and average wages will be neutral for the Polish debt market, we believe.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Sep-15	Oct-15	Nov-15	Dec-15	Jan-16	Feb-16	Mar-16	Apr-16	May-16	Jun-16	Jul-16	Aug-16	Sep-16	Oct-16
NBP reference rate (%)	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50	1,50
EURPLN*	4,25	4,25	4,27	4,26	4,42	4,35	4,24	4,37	4,38	4,38	4,35	4,36	4,29	**4,30**
USDPLN*	3,80	3,86	4,04	3,92	4,08	4,00	3,73	3,81	3,94	3,94	3,90	3,91	3,82	**3,86**
CHFPLN*	3,90	3,91	3,93	3,91	3,98	4,00	3,87	3,97	3,96	4,04	4,02	3,97	3,93	**3,97**
CPI inflation (% YoY)	-0,8	-0,7	-0,6	-0,5	-0,9	-0,8	-0,9	-1,1	-0,9	-0,8	-0,9	-0,8	-0,5	
Core inflation (% YoY)	0,2	0,3	0,2	0,2	-0,1	-0,1	-0,2	-0,4	-0,4	-0,2	-0,4	-0,4	-0,4	
Industrial production (% YoY)	4,0	2,4	7,8	6,7	1,4	6,8	0,7	5,9	3,2	6,0	-3,4	7,4	**2,8**	
PPI inflation (% YoY)	-2,8	-2,3	-1,8	-0,8	-1,2	-1,5	-1,9	-1,2	-0,4	-0,8	-0,5	-0,1	**0,1**	
Retail sales (% YoY)	0,1	0,8	3,3	4,9	0,9	3,9	0,8	3,2	2,2	4,6	2,0	5,6	**6,7**	
Corporate sector wages (% YoY)	4,1	3,3	4,0	3,1	4,0	3,9	3,3	4,6	4,1	5,3	4,8	4,7	**4,4**	
Employment (% YoY)	1,0	1,1	1,2	1,4	2,3	2,5	2,7	2,8	2,8	3,1	3,2	3,1	**3,1**	
Unemployment rate* (%)	9,7	9,6	9,6	9,8	10,3	10,3	10,0	9,5	9,1	8,8	8,6	8,5	**8,4**	
Current account (M EUR)	-550	-165	28	-846	679	-652	-217	492	389	113	-635	-1047		
Exports (% YoY EUR)	4,3	5,2	10,7	10,8	-1,3	5,4	0,0	4,1	0,0	5,7	-5,1	8,0		
Imports (% YoY EUR)	6,2	-1,0	6,3	4,4	0,3	7,4	0,9	0,3	1,5	0,4	-6,8	10,4		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

Indicator		2016				2017				2015	2016	2017
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)		3,0	3,1	2,8	2,9	3,3	3,5	3,3	3,9	3,6	2,9	3,5
Private consumption (% YoY)		3,2	3,3	4,0	4,0	4,0	3,7	3,0	3,1	3,1	3,6	3,4
Gross fixed capital formation (% YoY)		-1,8	-4,9	-3,4	-1,5	3,0	4,4	5,1	5,2	5,8	-2,7	4,7
Export - constant prices (% YoY)		6,9	10,9	6,6	6,6	7,2	7,0	6,1	7,0	6,8	7,7	6,8
Import - constant prices (% YoY)		9,3	9,9	6,0	6,1	6,9	6,3	6,6	7,3	6,3	7,8	6,8
GDP growth contributions	Private consumption (pp)	2,0	1,9	2,4	1,9	2,6	2,2	1,8	1,5	1,8	2,1	2,0
	Investments (pp)	-0,2	-0,9	-0,7	-0,4	0,4	0,7	0,9	1,4	1,1	-0,5	0,9
	Net exports (pp)	-0,9	0,8	0,4	0,4	0,4	0,6	-0,1	0,2	0,3	0,2	0,3
Current account***		-0,8	-0,6	-0,4	-0,5	-0,4	-0,5	-0,4	-0,6	-0,6	-0,5	-0,6
Unemployment rate (%)**		10,0	8,8	8,4	8,4	8,9	8,0	7,9	8,4	9,8	8,4	8,4
Non-agricultural employment (% YoY)		2,2	2,3	2,6	1,9	1,4	1,0	0,5	0,0	1,4	2,2	0,7
Wages in national economy (% YoY)		3,1	4,3	5,0	5,3	5,3	5,1	5,0	4,9	3,3	4,4	5,1
CPI Inflation (% YoY)*		-0,9	-0,9	-0,8	0,3	1,8	2,0	1,7	1,6	-0,9	-0,6	1,8
Wibor 3M (%)**		1,67	1,71	1,71	1,71	1,71	1,96	2,13	2,21	1,72	1,71	2,21
NBP reference rate (%)**		1,50	1,50	1,50	1,50	1,50	1,50	1,75	2,00	1,50	1,50	2,00
EURPLN**		4,24	4,38	4,29	4,30	4,30	4,20	4,20	4,15	4,26	4,30	4,15
USDPLN**		3,73	3,94	3,82	3,91	3,91	3,75	3,72	3,61	3,92	3,91	3,61

* quarterly average

** end of period

***cumulative for the last 4 quarters

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST* CA	FORECAST* CONSENSUS**
		Monday 10/17/2016				
11:00	Eurozone	HICP (% YoY)	Sep	0,4	0,4	0,4
14:30	USA	NY Fed Manufacturing Index (pts)	Oct	-2,0	0,2	1,0
15:15	USA	Industrial production (% MoM)	Sep	-0,4	0,2	0,2
15:15	USA	Capacity utilization (%)	Sep	75,5	75,6	75,6
		Tuesday 10/18/2016				
14:00	**Poland**	**Corporate sector wages (% YoY)**	**Sep**	**4,7**	**4,4**	**4,6**
14:00	**Poland**	**Employment (% YoY)**	**Sep**	**3,1**	**3,1**	**3,1**
14:30	USA	CPI (% MoM)	Sep	0,2	0,3	0,3
14:30	USA	Core CPI (% MoM)	Sep	0,3	0,1	0,2
		Wednesday 10/19/2016				
4:00	China	GDP (% YoY)	Q3	6,7	6,7	6,7
4:00	China	Retail sales (% YoY)	Sep	10,6	10,6	10,6
4:00	China	Industrial production (% YoY)	Sep	6,3	6,0	6,4
4:00	China	Urban investments (% YoY)	Sep	8,1	8,4	8,2
14:00	**Poland**	**Retail sales (% YoY)**	**Sep**	**5,6**	**6,7**	**6,1**
14:00	**Poland**	**PPI (% YoY)**	**Sep**	**-0,1**	**0,1**	**0,3**
14:00	**Poland**	**Industrial production (% YoY)**	**Sep**	**7,5**	**2,8**	**3,5**
14:30	USA	Housing starts (k MoM)	Sep	1142	1174	1175
14:30	USA	Building permits (k)	Sep	1152	1153	1164
		Thursday 10/20/2016				
10:00	Eurozone	Current account (bn EUR)	Aug	21,0		
13:45	Eurozone	EBC rate decision (%)	Oct	0,00	0,00	0,00
14:30	USA	Philadelphia Fed Index (pts)	Oct	12,8	4,0	5,8
16:00	USA	Existing home sales (M MoM)	Sep	5,33		5,35
		Friday 10/21/2016				
16:00	Eurozone	Consumer Confidence Index (pts)	Oct	-8,2		-7,9

*The forecasts of macroeconomic indicators for Poland were prepared by Credit Agricole Bank Polska S.A. The forecasts of foreign indicators were prepared by Crédit Agricole Corporate and Investment Bank
** Reuters

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