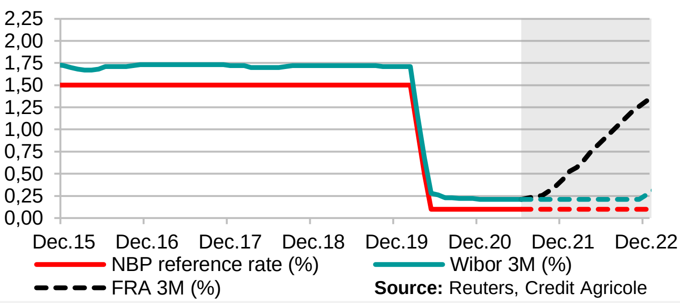
What scenario will the July NBP projection outline?

This week

- **The most important event this week will be the MPC meeting planned for Thursday.** We expect that the MPC will not change interest rates or modify the use of non-standard monetary policy tools (see below). The latest inflation projections will also be released. We expect the inflation and economic growth paths to be revised up vs. the March projection scenario. We believe that the MPC meeting will have a slightly negative impact on the PLN and yields on bonds.



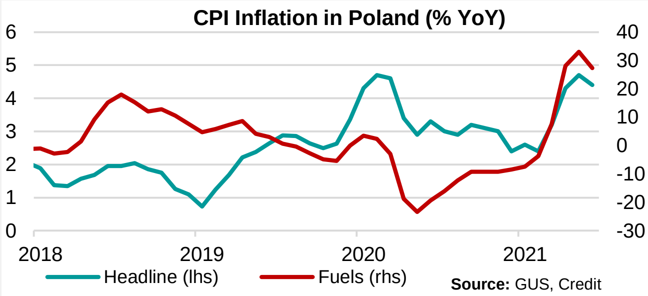
- **On Wednesday, Minutes of the last FOMC meeting will be published.** The Minutes will include a reiteration that the Fed sees its 2% inflation target as an average long-term inflation target. In other words, after a period of below-target inflation, the Fed allows inflation to temporarily exceed the 2% level. I will also be emphasized that the Fed is going to continue its expansive monetary policy for quite some time. An interesting item in the Minutes will be information about the expectations of individual Fed members regarding the pace of monetary policy tightening. In June, the median of FOMC members' expectations of the interest rates level at the end of 2023 rose to 0.50%, while in March it indicated that interest rates are expected to remain stable at the current levels at least until the end of 2023 (see MACROmap of 21/06/2021). The Minutes may also include comments about the start date of the tapering of quantitative easing programme. At the conference following the June meeting, the Fed Chairman J. Powell stated that it had been a meeting which started *"talking about talking about"* tapering of the said programme. We do not expect any market reaction to the publication of the Minutes.
- **The ZEW index, reflecting sentiment of analysts and institutional investors regarding the economic situation in Germany, will be published on Tuesday.** In accordance with the consensus, the index will drop to 75.4 pts in July from 79.8 pts in June. We believe that the publication of the index will be neutral for financial markets.

Last week

- **Given recent real economy data, the trends signalled by business surveys, and information about the course of the COVID-19 pandemic, we have revised our macroeconomic forecasts.** Our annual-average-economic-growth forecasts for 2021 (5.3%) and 2022 (4.9%) have remained unchanged, however, we have revised the quarterly profile of GDP growth. Due to the stronger-than-expected growth in activity seen currently in manufacturing and in household purchases, we have revised up our consumption, exports, and GDP forecasts for Q2. At the same time we have revised down our private consumption and GDP growth forecasts for Q4 due to the risk that the adverse impact of the forth wave of the pandemic on business activity may be stronger than earlier expected due to a slow progress in vaccinating population in Poland.
- **The PMI for Poland's manufacturing rose to 59.4 pts in June from 57.2 pts in May.** The PMI thus broke the record set a month ago, setting a new all-time high. The increase in the index resulted from higher contributions of all its components (new orders, current output, inventories, delivery times and employment). Particularly worth noting about the data are the marked increases in the sub-indices for new orders (the highest level since February 2014) and for current output (the highest level since January 2017). At the same time, there was a further increase in delivery times (a new record) and an increase in the production backlogs (a new record), which was

reflected both in higher prices of semi-finished products and components (a new record) and in output prices (a new record). Such a breakdown of data indicates a strong overheating in Poland's manufacturing (see MACROpulse of 02/07/2021). The average PMI for Poland's manufacturing rose to 56.8 pts in Q2 from 53.2 pts in Q1. Thus, data supports our revised forecast for Poland's GDP (see above).

- **In accordance with the flash estimate, CPI inflation in Poland dropped to 4.4% YoY in June from 4.7% in May, running below the market consensus (4.6%) and in line with our forecast.** GUS published partial data on the inflation breakdown, which contains information about the pace of price rises in the following categories: 'food and non-alcoholic beverages', 'energy', and 'fuels'. Inflation was driven down by slower rises in fuel prices (27.3% YoY in June vs. 33.0% in May) and by a drop in core inflation, which, according to our estimates, dropped to 3.4% YoY in June from 4.0% in May. At the same time, inflation was driven up by faster rises in the prices of food and non-alcoholic beverages (2.0% vs. 1.7%), while the pace of rises in energy prices did not change in June compared to May (4.4%). Last week's data supports our scenario that inflation hit its local high in May and will be declining in the coming months, but will stay at an elevated level (at an average level of 4.5% YoY in H2 2021).



Source: GUS, Credit

- **In accordance with the flash estimate, inflation in the Eurozone dropped to 1.9% YoY in June from 2.0% in May, running in line with the market consensus and above our forecast (1.8%).** The drop in inflation was mainly accounted for by slower rises in services and energy prices. We expect inflation to rise in H2, driven to a large extent by higher core inflation. In consequence, we forecast that inflation will hit its local high, exceeding 3% YoY, in Q4, and the annual average inflation rate for 2021 will rise to 2.1% YoY from 0.3% in 2020.
- **The Caixin PMI for China's manufacturing dropped to 51.3 pts in June from 52.0 pts in May, running below market expectations (51.8 pts).** The index was driven down by lower contributions of the new orders, current output, and delivery times components, while at the same time being driven up by higher contributions of the employment and inventories components. It is worth noting that the breakdown of data shows strong drops in the current output and new order components, which signals a weakening of domestic demand in China's economy. The PMI index for Chinese manufacturing, just like the flash PMI index for German manufacturing released two weeks ago (see MACROmap of 28/06/2021), also shows drops in the indices for production backlogs and the prices of semi-finished products and components, as well as smaller increases in delivery times compared to a month ago. This may suggest that supply barriers are slowly beginning to weaken, although they remain very high, limiting the scale of recovery in global manufacturing. This is consistent with our assessment that the coming months will bring greater availability of materials and unblocking of global supply chains, which will support further recovery in manufacturing and lower pressure on output prices. The Caixin PMI for services has been released today, too. The index dropped to 50.3 pts from 55.1 pts, running well below market expectations (54.8 pts). In our opinion, the significant drop in the index is mainly accounted for by a strong slowdown in the China's real-estate market. Last week's business survey results for China entail a downward risk to our forecast that China's GDP will grow by 8.5% in 2021 compared to an increase by 2.3% in 2020.
- **Last week, some important data on the US economy was released.** The number of new jobless claims dropped to 364k from 415k two weeks ago (upward revision from 411k), running slightly below market expectations (385k). This is also the lowest number of new jobless claims since March 2020. Despite the marked decline, it is still at almost double the pre-pandemic level, though. In turn, the number of continued claims rose to 3.5m vs. 3.4m. Last week also saw the

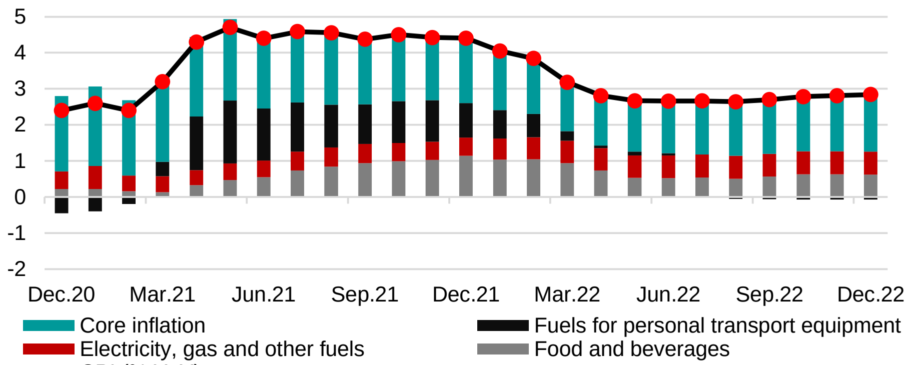
publication of data on non-farm payrolls, which rose by 850k in June vs. an increase by 583k in May (an upward revision from 559k), running clearly above market expectations (up by 700k). The strongest increase in employment was in tourism and recreation (+343k), the sector that suffered the largest decline in employment during the pandemic. This indicates a recovery of activity in this sector with the gradual fading of the pandemic in the US due to the increasing number of people vaccinated (see COVID Dashboard). The unemployment rate rose to 5.9% in June from 5.8% in May, running above market expectations (5.7%). The increase in the unemployment rate with simultaneous strong increase in employment can be explained by the fact that these variables are calculated on the basis of two different surveys, which sometimes, in the short term, leads to discrepancies between these data. At the same time, the labour force participation rate was unchanged in June compared to May, at 61.6%, still clearly below the levels observed before the outbreak of the pandemic (around 63.3%). The data on non-farm payrolls in the US combined with the data on the number of jobless claims indicate that the US labour market is still far from its equilibrium despite the ongoing improvement. Last week the ISM manufacturing index was published, which dropped in June to 60.6 pts vs. 61.2 pts in May, running slightly below market expectations (61.0 pts). The index was driven down by lower contributions of 2 out of its 5 components (delivery times, new orders and employment), with an opposite impact coming from higher contributions of current output and inventories components. Similar to the manufacturing PMIs for Germany and China, the ISM index indicated a decline in the indexes for manufacturing backlogs, as well as a smaller extension of delivery times than a month ago. This may suggest that supply barriers are slowly beginning to weaken, although they remain very high, limiting the scale of the recovery in global manufacturing (see above). Last week the Conference Board index was also published, which increased in June to 127.3 pts vs. 120.0 pts in May (revision upwards from 117.2 pts), running clearly above market expectations (119.0 pts). The increase in the index was due to an increase in its components for both the assessment of the current situation and expectations. Last week's data from the US economy do not change our scenario, according to which the annualised GDP growth rate will reach its local maximum in Q2 this year at 10.2% and will be on a downward trend from Q3 onwards. Consequently, US GDP will expand by 6.5% in 2021, compared with a decline of 3.5% in 2020, and will grow by 4.0% in 2022.

What scenario will the July NBP projection outline?

A meeting of the Monetary Policy Council is scheduled for Thursday. The MPC's press release after the June meeting was maintained in a dovish tone (see MACROpulse of 9/6/2021). First of all, when emphasising the supply-related nature of inflation rise in Poland, the Council quoted a passage of the Monetary Policy Guidelines for 2021, which reads that “due to the macroeconomic and financial shocks, inflation may temporarily deviate from the target and even run outside the band for deviations from the target” and “the response of monetary policy to the shocks is flexible and depends on their causes and the assessment of persistence of their effects, including their impact on inflation developments.” In our opinion, that this passage was quoted is clearly indicative of the Council’s reluctance to raise the rates in response to the significant inflation rise seen over the last couple of months. Secondly, the Council put a passage removed from the previous month’s press release back in the present release, the passage reading that the NBP’s monetary policy “stabilises inflation at the level consistent with the NBP’s inflation target in the medium term.” In our opinion, this means that the Council expects the inflation to return close to the target set by the MPC in the mid-term perspective, and that it is not necessary to tighten the monetary policy at the moment. Thirdly, the continuation of structural open-market operations announced in the June press release suggests that in the Council’s opinion even a

small adjustment to the unconventional monetary policy (preceding a potential raising of interest rates) would be unjustified at the moment.

This week we are going to learn the results of the latest, July NBP macroeconomic projection. In our opinion, the expected economic growth rate (4.1% YoY) will be raised compared to the March projection due to better-than-expected Q1 performance (particularly in the case of investments) and data coming in the last months, which signal a higher GDP growth rate also in Q2. It is difficult to say precisely to what extent the presented growth path will reflect the risk of a fourth pandemic wave in Poland in the fourth quarter of this year. The scenario of an economic growth rate close to 5% in 2022-2023 is likely to be maintained in the newest macroeconomic projection.



Source: GUS, Credit Agricole

We believe that the path of projected inflation will also be revised upwards vs. the March projection. According to the March document, the NBP expected inflation to reach 3.4% YoY in Q2, while it actually was 4.5%. The error was due to the underestimation of all three components of inflation (food, fuel and energy prices and core inflation). This error has the effect of raising the path in subsequent quarters as well. In our forecast, we assume that with the gradual fading of supply shocks and low base effects driving up inflation, annual total price dynamics will again be within the band of acceptable deviations from the inflation target (2.5±1%) starting from March 2022 (see chart). We expect the July projection to signal a similar inflation scenario in the coming quarters.

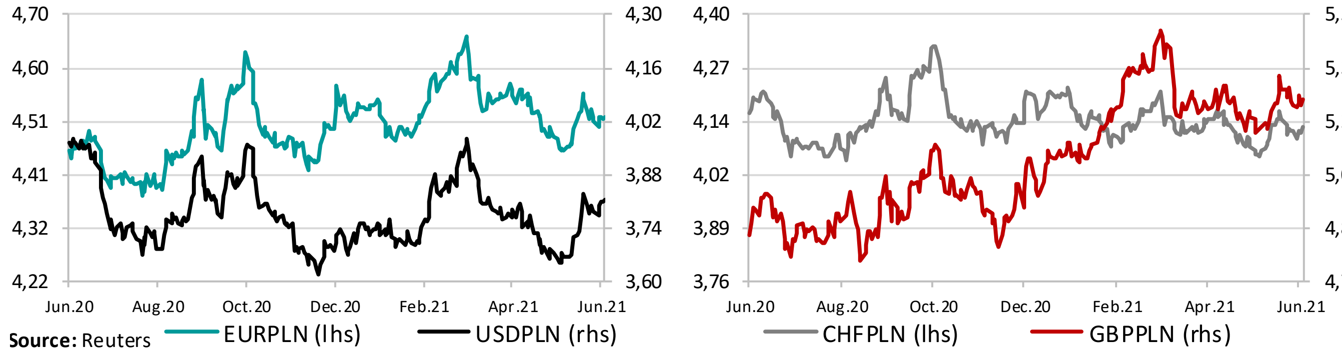
We expect the RPP to maintain the status quo on its monetary policy this week. In his speech after the June MPC meeting, NBP President A. Glapiński ruled out the possibility of a one-off, "warning" rate hike. We expect that the reduction in inflation recorded in June and its projected further slight decline forecast in the July projection over a horizon of several months will be an important argument for some MPC members to keep monetary policy parameters unchanged at this week's meeting. This scenario is supported by last week's statement by A. Glapiński, according to which ‘hasty decisions’ in the monetary policy could ‘spoil the prospects of recovery’.

Given the slow progress of the vaccination process in the population, the risk of another wave of the coronavirus pandemic remains an important argument for keeping interest rates unchanged in the coming months. According to the description of the discussion at the MPC meeting in May, the majority of the Council members believe that ‘if uncertainty regarding the course of the pandemic and, consequently, the future economic situation persists, and an increase in inflation above the target is due to factors beyond the control of monetary policy, it will be advisable to keep interest rates unchanged also in the coming months’. Moreover, the majority of the Council members emphasised that an increase in interest rates ‘would be justified only after the end of the pandemic’, mentioning also ‘the consolidation of the economic recovery and the emergence of risk of excessive inflation growth generated by demand factors’ as necessary conditions for tightening the monetary policy.

We maintain our scenario, in which the MPC will not change interest rates until the end of 2022. We believe that if, in line with our scenario, inflation falls to just above the NBP inflation target (2.5%) in Q2 2022, Council members will be reluctant to tighten monetary policy. This argument is relevant in the context of a change in the composition of the MPC after the end of its current term (early 2022). Even in the case of a potential change to a more hawkish MPC, inflation close to the target will be an argument for interest rate stabilization. We expect the reference rate to be raised for the first time in Q1 2023 (from 0.10% to 0.25%). In accordance with that scenario, the MPC will be tolerating potential upward deviations of inflation from the target in 2021-2022 as it will want to avoid a strong appreciation of the PLN as a result of the interest rate differential between Poland and the Eurozone.

MPC meeting may weaken the PLN

FX rates



Source: Reuters

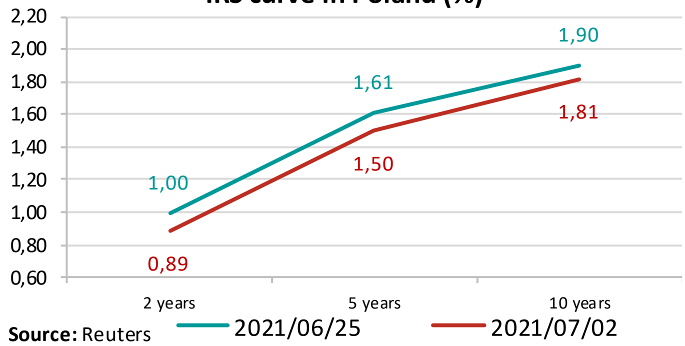
Last week, the EURPLN rate increased to 4.5165 (the PLN weakened by 0.2%). The EURPLN exchange rate was characterised by relatively low volatility last week. The publication of domestic inflation data and business survey results in Polish manufacturing did not have a significant impact on the PLN.

Last week saw a strengthening of the USD against the EUR. Thus, the EURUSD exchange rate returned to the downward trend initiated by the hawkish tone of the June FOMC meeting (see MACROmap of 21/6/2021), which increased investors' expectations for monetary policy tightening in the US. The publication of US non-farm payrolls data had a limited impact on the market.

This week the MPC meeting planned for Thursday will be crucial for the PLN. We believe, that it may lead to the weakening of the Polish currency. Wednesday's publication of the Minutes of the June FOMC meeting will be neutral for the PLN.

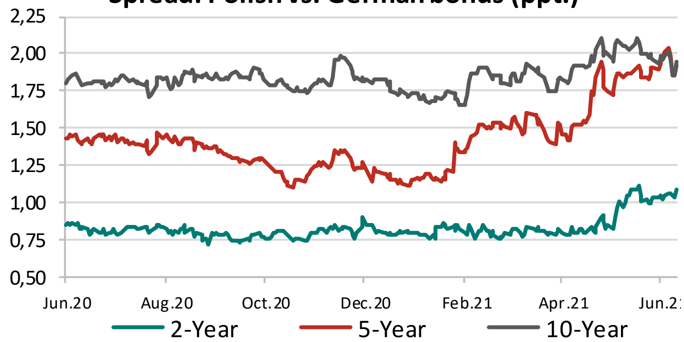
MPC meeting in the spotlight

IRS curve in Poland (%)



Source: Reuters

Spread: Polish vs. German bonds (ppt.)



Last week the 2-year IRS rates decreased to 0.89 (down by 12bp), 5-year rates to 1.50 (down by 11bp), and 10-year rates to 1.81 (down by 9bp). In the first part of the week, we saw a rise in IRS rates visible especially at the short end of the curve, as the market awaited domestic inflation data. The data turned out to be clearly below expectations, which led to a significant correction. IRS rates were stable later in the week.

This week the MPC Thursday meeting is going to be in the spotlight. In our view, it can lead to a drop in IRS rates. The publication of the Minutes of the June FOMC meeting scheduled for Wednesday is likely to be neutral for the curve.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Jun.20	Jul.20	Aug.20	Sep.20	Oct.20	Nov.20	Dec.20	Jan.21	Feb.21	Mar.21	Apr.21	May.21	Jun.21	Jul.21
NBP reference rate (%)	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	**0,10**
EURPLN*	4,44	4,41	4,40	4,53	4,60	4,47	4,55	4,52	4,52	4,63	4,56	4,48	4,52	**4,52**
USDPLN*	3,95	3,74	3,68	3,86	3,95	3,75	3,73	3,72	3,74	3,95	3,79	3,66	3,81	**3,80**
CHFPLN*	4,17	4,10	4,07	4,21	4,32	4,13	4,21	4,18	4,11	4,18	4,15	4,07	4,12	**4,12**
CPI inflation (% YoY)	3,3	3,0	2,9	3,2	3,1	3,0	2,4	2,6	2,4	3,2	4,3	4,7	**4,5**	
Core inflation (% YoY)	4,1	4,3	4,0	4,3	4,2	4,3	3,7	3,9	3,7	3,9	3,9	4,0	**3,4**	
Industrial production (% YoY)	0,5	1,1	1,5	5,7	1,0	5,4	11,1	0,7	2,5	18,6	44,2	29,7	**21,1**	
PPI inflation (% YoY)	-0,8	-0,6	-1,3	-1,4	-0,4	-0,2	0,1	1,0	2,2	4,2	5,5	6,5	**7,0**	
Retail sales (% YoY)	-1,9	2,7	0,4	2,7	-2,1	-5,3	-0,8	-6,0	-2,7	17,1	25,7	19,1	**9,5**	
Corporate sector wages (% YoY)	3,6	3,8	4,1	5,6	4,7	4,9	6,6	4,8	4,5	8,0	9,9	10,1	**9,6**	
Employment (% YoY)	-3,3	-2,3	-1,5	-1,2	-1,0	-1,2	-1,0	-2,0	-1,7	-1,3	0,9	2,7	**2,7**	
Unemployment rate* (%)	6,1	6,1	6,1	6,1	6,1	6,1	6,2	6,5	6,5	6,4	6,3	6,1	**5,9**	
Current account (M EUR)	3333	650	1273	1330	2307	1956	477	3341	1585	938	1740	**860**		
Exports (% YoY EUR)	4,3	2,2	2,4	6,6	3,7	10,0	14,6	-0,9	5,9	27,7	69,2	**39,9**		
Imports (% YoY EUR)	-7,4	-3,6	-4,0	2,1	-4,2	4,1	12,4	-4,0	6,2	24,6	59,8	**49,1**		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

Indicator	2020				2021				2020	2021	2022
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)	2,0	-8,3	-1,7	-2,7	-0,9	12,0	4,9	5,5	-2,7	5,3	4,9
Private consumption (% YoY)	1,2	-10,8	0,4	-3,2	0,2	12,3	3,8	3,5	-3,0	4,7	4,5
Gross fixed capital formation (% YoY)	1,7	-9,8	-8,2	-15,4	1,3	7,7	6,1	11,8	-9,6	7,6	8,4
Export - constant prices (% YoY)	2,7	-13,7	2,3	7,6	5,7	14,9	8,5	9,3	-0,2	9,4	8,3
Import - constant prices (% YoY)	0,8	-16,6	-0,3	8,2	10,0	9,6	6,7	8,0	-1,9	8,5	8,9
GDP growth contributions: Private consumption (pp)	0,7	-6,2	0,2	-1,7	0,1	6,8	2,2	1,7	-1,7	2,6	2,5
GDP growth contributions: Investments (pp)	0,2	-1,6	-1,4	-3,9	0,2	1,2	1,0	2,5	-1,8	1,3	1,4
GDP growth contributions: Net exports (pp)	1,1	0,8	1,4	0,1	-1,9	3,5	1,5	1,3	0,8	1,1	0,0
Current account (% of GDP)***	1,1	2,2	2,9	3,5	3,7	3,5	3,2	3,1	3,5	3,1	2,5
Unemployment rate (%)**	5,4	6,1	6,1	6,2	6,4	5,9	5,7	5,6	6,2	5,6	5,1
Non-agricultural employment (% YoY)	0,7	-1,8	-0,7	0,0	0,0	1,8	0,9	0,7	-0,5	0,9	0,4
Wages in national economy (% YoY)	7,7	3,8	4,8	5,0	6,6	7,0	6,5	6,3	5,3	6,6	5,8
CPI Inflation (% YoY)*	4,5	3,2	3,0	2,8	2,7	4,5	4,5	4,5	3,4	4,1	3,0
Wibor 3M (%)**	1,17	0,26	0,22	0,21	0,21	0,21	0,21	0,21	0,21	0,21	0,26
NBP reference rate (%)**	1,00	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,10
EURPLN**	4,55	4,44	4,53	4,55	4,63	4,52	4,45	4,45	4,55	4,45	4,30
USDPLN**	4,13	3,95	3,86	3,73	3,95	3,81	3,71	3,71	3,73	3,71	3,47

* quarterly average
** end of period
***cumulative for the last 4 quarters

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST*	
					CA	CONSENSUS**
		Monday 07/05/2021				
10:00	Eurozone	Services PMI (pts)	Jun	58,0	58,0	58,0
10:00	Eurozone	Final Composite PMI (pts)	Jun	59,2	59,2	59,2
10:30	Eurozone	Sentix Index (pts)	Jul	28,1		30,0
		Tuesday 07/06/2021				
8:00	Germany	New industrial orders (% MoM)	May	-0,2		1,3
11:00	Eurozone	Retail sales (% MoM)	May	-3,1		4,1
11:00	Germany	ZEW Economic Sentiment (pts)	Jul	79,8		75,4
16:00	USA	ISM Non-Manufacturing Index (pts)	Jun	64,0	63,0	63,5
		Wednesday 07/07/2021				
8:00	Germany	Industrial production (% MoM)	May	-1,0		0,5
20:00	USA	FOMC Minutes	Jun			
		Thursday 07/08/2021				
8:00	Germany	Trade balance (bn EUR)	May	15,9		15,9
14:30	USA	Initial jobless claims (k)	w/e	411		355
	Poland	**NBP rate decision (%)**	**Jul**	**0,10**	**0,10**	**0,10**
		Friday 07/09/2021				
3:30	China	PPI (% YoY)	Jun	9,0		8,8
3:30	China	CPI (% YoY)	Jun	1,3		1,4
14:00	**Poland**	**MPC Minutes**	**Jul**			
16:00	USA	Wholesale inventories (% MoM)	May	1,1		
16:00	USA	Wholesale sales (% MoM)	May	0,8		

*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

MACRO MAP

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