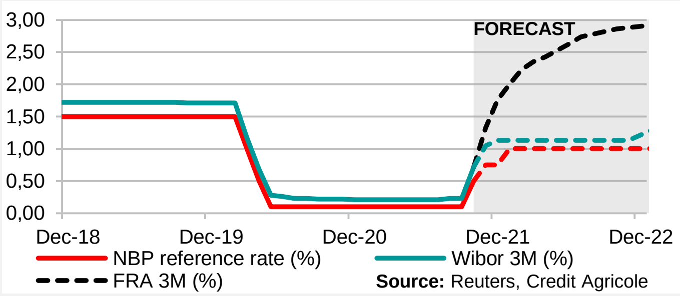
Polish manufacturing hindered by supply chain disruptions

This week

- **This week's most important event is the Monetary Policy Council meeting scheduled for Wednesday.** In our baseline scenario, we expect the MPC to lift interest rates by 25bps to 0.75%. The results of the newest inflation projection will be the main argument for a monetary policy tightening. We anticipate that the price growth path will be revised significantly upwards and will stay above the upper limit for deviations from the inflation target in Q4 2022. The FRA market is currently pricing in a much larger scale of hikes (see chart). Thus, the materialization of our forecast will be conducive to a slight weakening of the PLN a decline in yields on Polish bonds. However, we see a risk of an alternative scenario materializing whereby the MPC will raise interest rates by 50bps to 1.00% at this week's meeting. We believe that the content of the press release and the NBP President's speech at the post-meeting press conference will seek to tone down market expectations of further interest rate hikes, emphasizing the significant impact of supply shocks (which are beyond the influence of the domestic monetary policy) and the uncertain impact of the fourth wave of the COVID-19 pandemic on economic activity. We also revised our mid-term monetary policy scenario. We expect that if the MPC raises interest rates by 25bps this week, the next hike should be expected in January 2022.

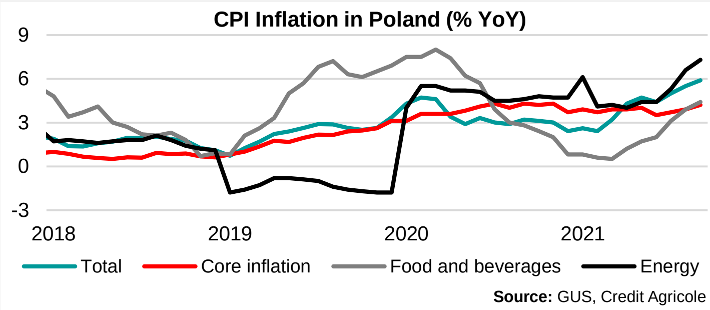


- **This week's highlight is the FOMC meeting scheduled for Wednesday.** We expect that, in line with earlier announcements, the Fed will decide to start tapering its asset purchase program this week. We believe that monthly purchases, currently amounting to USD 80bn in treasury bonds and USD 40bn in MBS (mortgage-backed securities), will be scaled down by USD 10bn and USD 5bn, respectively. This means that the quantitative easing program will be ended in mid-2022. In our baseline scenario, the first interest rate hike will not occur before 2023. The FOMC meeting will favor the increased volatility of the PLN exchange rate and yields on Polish bonds.
- **This week, important data from the US will be published.** The publication of labor market data is scheduled for Friday. We expect that non-farm payrolls rose to 475k in October compared with an increase of 194k in September with a parallel reduction of the unemployment rate to 4.7% vs. 4.8% in September. Before Friday's publication, additional information on the labor market will be provided by the ADP report on employment in the private sector (the market anticipates an increase of 400k in October vs. 568k in September). Yesterday also saw the release of the latest ISM index for manufacturing, which contracted to 60.8 pts in October, up from 61.1 pts in September, performing slightly above market expectations (60.5 pts). This drop followed from lower contributions from 2 out of its 5 components (for new orders and output), with higher contributions from suppliers' delivery times, inventories and employment having the opposite effect. The data points to a further increase in delivery times, reflecting the persistent supply bottlenecks in US manufacturing related to a shortage of certain raw materials and semi-products, which is driving up prices. We believe that the publication of labor market data will be neutral for the financial markets.
- **The last few days saw the release of data on the economic situation in Chinese manufacturing.** In October, the Caixin index for Chinese manufacturing rose to 50.6 pts compared with 50.0 pts in September, running above market expectations (50.0 pts). Thus, the index stood above the 50-point mark, which separates expansion from contraction, for the first time since July 2021. This trend resulted from higher contributions from 3 out of its 5 components (employment, new orders and suppliers' delivery times), with lower contributions from output and inventories

having the opposite effect. Particularly noteworthy in the data is the continued increase in the index for total new orders, with a simultaneous decline in the index for new export orders (for the third month running). This suggests that the improvement in Chinese manufacturing was driven by stronger domestic demand, while the slowdown in global trade activity, primarily related to supply bottlenecks, was deepening. The deterioration in economic conditions in Chinese manufacturing was signaled by the CFLP PMI index released last week as it fell to 49.2 pts in October, down from 49.6 pts in September, running below market expectations (49.8 pts). In the coming months, we believe that Chinese processing will be increasingly influenced by China's energy crisis (power supply issues), which may lead to a strong increase in manufacturing costs and, in extreme cases, to production being suspended in some plants (see MACROmap of 11/10/2021). This scenario is consistent with our forecast of China's economic growth (5.2% YoY in 2022 vs. 8.0% in 2021).

- **The PMI index for Polish manufacturing rose to 53.8 pts in October, up from 53.4 pts in September, exceeding both the market consensus (53.0 pts) and our forecast (53.2 pts)**. This trend resulted from higher contributions from 4 out of its 5 components (new orders, output, employment and inventories), with lower contributions from suppliers' delivery times having the opposite effect. The index shrank in October compared with the average value recorded in Q3 2021 (55.6 pts), which signals a slowdown in economic growth at the beginning of Q4 (see below).

Last week



- **According to the preliminary estimate, CPI inflation in Poland reached 6.8% YoY in October vs. 5.9% in September, exceeding both the market consensus (6.4%) and our forecast (6.5%).** GUS published partial data on the structure of inflation, including information on the pace of price growth in the "food and non-alcoholic beverages", "energy" and "fuel" categories. Inflation rose on the back of growing prices of food and non-alcoholic beverages (4.9% YoY in October vs. 4.4% in September), energy (10.2% vs. 7.3%), fuels (33.9% vs. 28.6%), as well as core inflation which, according to our estimates, increased to 4.6% YoY in October compared with 4.2% in September. October data poses an upside risk to our forecast according to which CPI inflation in Poland will climb to 4.9% YoY in 2021 from 3.4% in 2020, and to 5.5% in 2022.
- **Last week, vital data regarding the US economy was published.** In line with the first estimate, the annualized US GDP growth rate in Q3 contracted to 2.0% compared with 6.7% in Q2, running below market expectations (2.7%). The slowdown in GDP growth followed from diminished contributions from private consumption (1.08 pp in Q3 vs. 7.92 pp in Q2), net exports (-1.14 pp vs. -0.18 pp) and investments (-0.14 pp vs. 0.61 pp) with higher contributions from inventories (2.07 pp vs. -1.26 pp) and government spending (0.14 pp vs. -0.36 pp) having the opposite effect. Thus, in Q3 the main engine of US economic growth was inventories, while in Q4 it was chiefly spurred by private consumption. Such a growth structure reflects the recovery in inventories and the high base effect in private consumption related to the release of pent-up demand in Q2 reinforced by payouts under Joe Biden's stimulus package. Last week, data on PCE inflation was also published, which in September rose to 4.4% YoY vs. 4.2% in August on the back of an acceleration in the growth of food and energy prices. At the same time, core PCE inflation remained stable between September and August, standing at 3.6% YoY. Last week also saw the

release of preliminary data on durable goods orders, which fell by 0.4% MoM in September vs. a 1.3% increase in August (downward revision from 1.8%), exceeding market expectations (-1.0%). Excluding transportation, on a month-on-month basis durable goods orders were up by 0.4% in September vs. an increase of 0.3% in August. Thus, the volume of durable goods orders in the US in September was already 13.2% higher than in February 2020, i.e. the last month without a strong impact of the pandemic on orders. In turn, the volume of orders for civilian capital goods, excluding aircraft, was already 19.8% higher in September than in February 2020, signaling strong prospects for a continued significant recovery in US investments in the coming months. Last week, vital data from the US labor market was published. The number of new jobless claims dropped to 281k vs. 291k two weeks prior, running below market expectations (291k). In turn, the number of continued claims dropped from 2.5m to 2.2m. Directly prior to the outbreak of the pandemic, the number of continued jobless claims stood at 1.7 million. Thus, the data shows that the situation on the US labor market is gradually improving and is coming closer to equilibrium. Last week also saw the publication of data on new home sales (800k in September vs. 740k in August), which attested to continued high activity on the US housing market. A slight improvement in consumer sentiment was signaled by the Conference Board index, which expanded in October to 113.8 pts vs, 109.8 pts in September, running above market expectations (108.9 pts). The growth of the index was attributable to the increase in its components for both the assessment of the current situation and expectations. On the other hand, a slight deterioration in consumer sentiment was signaled by the final University of Michigan index, which fell to 71.7 pts in October vs. 72.8 pts in September and 71.4 pts in the preliminary reading The growth of the index was attributable to the increase in its components for both the perception of the present situation and expectations. Improvement in US households' sentiment is being held back by higher inflation and the waning effect of payouts under Joe Biden's stimulus package. Last week's data from the US economy poses a downside risk to our scenario, according to which throughout 2021 US GDP will expand by 6.1% vs. a decline of 3.5% in 2020, to grow by 4.0% in 2022.

- **Last week, a meeting of the European Central Bank was held.** In line with our expectations, ECB interest rates were kept unchanged (the deposit rate stands at -0.50%). The ECB reiterated its announcement that it would continue to buy assets under PEPP (Pandemic Emergency Purchase Program) while maintaining its envelope (EUR 1.850bn) and horizon (at least until March 2022). According to the statement, the EBC will continue APP (Asset Purchase Program) for EUR 20bn per month, as long as it is necessary to strengthen the mitigating effect of ECB's policy rates. The ECB also upheld its declaration that the program would end shortly before the ECB started raising interest rates. At the same time, the parameters of TLTRO (targeted longer-term refinancing operations) programs were kept unchanged. During the press conference following the meeting, ECB President Ch. Lagarde pointed out that the currently observed increase in inflation chiefly stems from higher prices of energy, supply bottlenecks and statistical effects related to the end of the VAT reduction in Germany, hence it is of a temporary nature. President Lagarde cautioned investors not to formulate any expectations about the future monetary policy of the ECB based on actions of other central banks. The dovish undertone of the ECB President's statement was aimed at lowering expectations of an interest rate hike in the Eurozone. However, it fell short of achieving the desired effect. Ch. Lagarde's statements support our scenario where the first interest rate hike in the Eurozone will not take place until 2026. We expect that this December the EBC will increase the envelope of PEPP by EUR 150bn to EUR 2,000bn and extend its time horizon to December 2022, thus facilitating its tapering. In addition, in our baseline scenario we assume that in January 2022 the ECB will increase the monthly scale of APP by EUR 10bn to EUR 30bn and maintain this scale until the program ends (we believe that its will run until December 2025). The easing of the monetary policy in the Eurozone we forecast follows from the fact that we share Ch. Lagarde's view that the currently observed uptick in inflation is only temporary. In our baseline scenario, we also expect a gradual increase in interest rates on loans granted to banks by the ECB under the TLTRO program.

- **According to the preliminary estimate, inflation in the Eurozone rose to 4.1% YoY in October vs. 3.4% in September, exceeding both the market consensus (3.7%) and our forecast (3.9%).** Inflation rose on the back of the growing prices of energy and services. Core inflation climbed from 1.9% YoY in September to 2.1% in October, its highest level since December 2002. The data poses an upside risk for our scenario whereby inflation in November will reach its local maximum of 4.4% YoY and in 2021 will amount to 2.5% YoY vs. 0.3% 2020.
- **Last week there was a publication of the preliminary GDP estimates for the Eurozone.** Quarterly GDP growth in the single currency area did not change between Q3 and Q2, standing at 2.2% (3.7% YoY in Q3 vs. 14.3% in Q2), exceeding market expectations (1.9% QoQ and 3.5% YoY, respectively) and running slightly below our forecast (2.3% QoQ). An increase in quarterly GDP growth was recorded, among others, in Germany (1.8% vs. 1.6%), France (3.0% vs. 1.3%) and Spain (2.0% vs. 1.1%), with Italy experiencing a drop (2.6% vs. 2.7%). The next GDP estimate in the Eurozone will be released on 16 November. We forecast that GDP in the Eurozone will rise by 5.4% in 2021, compared with a 6.4% decline in 2020, to expand by 4.4% in 2022.
- **The Ifo index, reflecting the sentiment of German businesses representing manufacturing, construction, trade and services sectors, climbed to 97.7 pts in October vs. 98.9 pts in August, i.e. just below the market consensus (97.8 pts).** The decline in the index was attributable to the decrease in its components for both the assessment of the current situation and expectations. On a sectoral basis, an economic slowdown was recorded in trade, manufacturing and services, while the situation in construction improved. We forecast that in 2021 German GDP will rise by 4.3% compared with a 4.6% decline in 2020.
- **Moody's did not publish a new report on Poland's rating last week, thus maintaining the long-term rating at A2 with a stable outlook.** The stabilization of the rating is neutral for the PLN exchange rate and bond yields.

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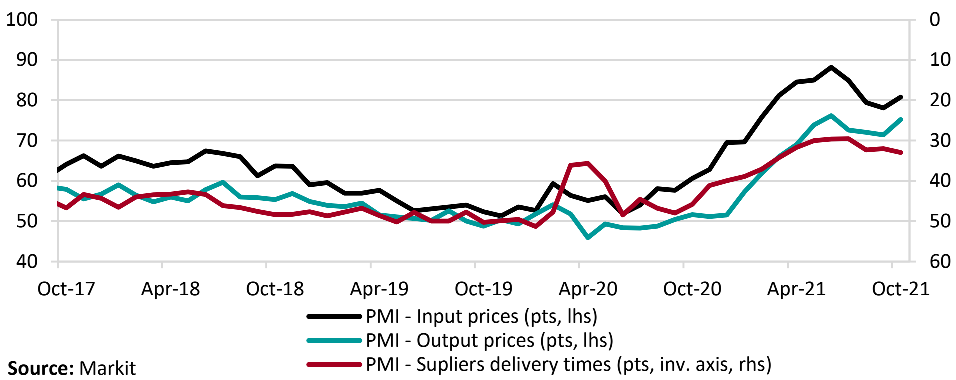
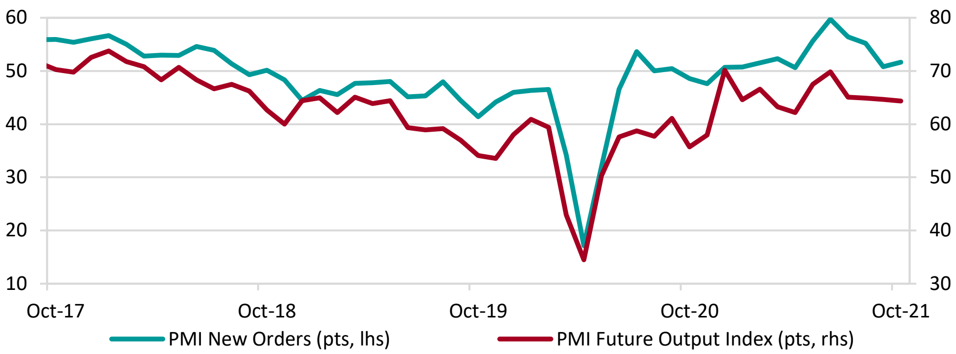
The PMI index for Polish manufacturing rose to 53.8 pts in October compared to 53.4 pts in September, exceeding the market consensus (53.0 pts) and our forecast (53.2 pts). This increase followed from higher contributions from 4 out of its 5 components (new orders, output, employment and inventories), with a lower contribution from suppliers' delivery times having the opposite effect. The index shrank in October compared to the average value recorded in Q3 2021 (55.6 pts), which signals a slowdown in economic growth at the beginning of Q4.



Source: Markit

Output increased in October at a slightly faster pace than in September. However, according to the press release, companies reported two factors that significantly hindered its growth. First, businesses saw weaker demand from abroad, which was reflected in the second consecutive month-on-month decline in new export orders. The second factor was disruptions in supply chains. Companies reported difficulties in purchasing production resources due to strong demand in global markets, accompanied by shortages of materials from suppliers and transportation issues. The direct effects of the growing supply bottlenecks in manufacturing were the extension of delivery times, a further increase in production backlogs and rising input and output prices. It is worth noting that at least 80% of manufacturing companies signaled a growth of the input prices in October and at least 75% increase in the output prices. Furthermore, companies reported a labor shortage in October, limiting opportunities to increase employment and production capacities.



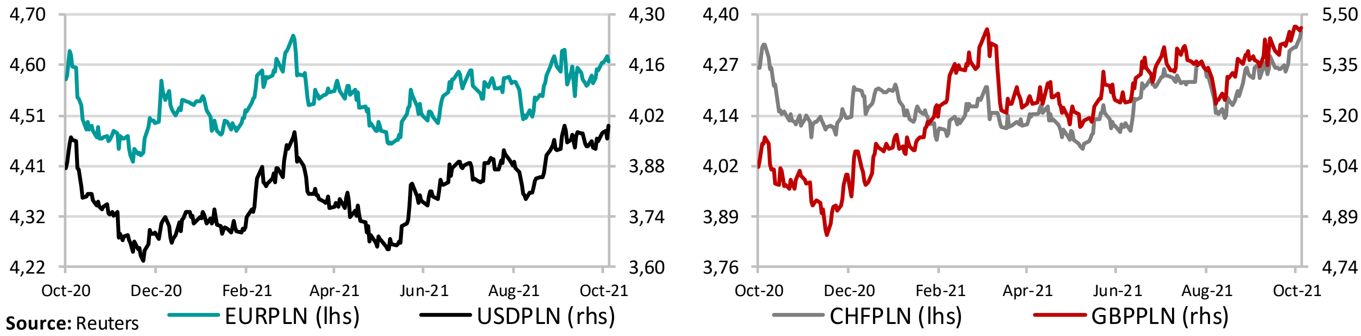
Source: Markit

Businesses also pointed to disruptions in supply chains and supply bottlenecks as a risk factor to a sustained recovery in manufacturing. This was reflected in a further 4-month decline in the expected output index over the next 12 months. However, it should be remembered that despite the aforementioned issues, activity in Polish manufacturing is supported by strong domestic demand, as attested by the acceleration in the total inflow of new orders. We stand by our scenario whereby the currently observed supply constraints are temporary, and as they ease off in the mid-term, activity in manufacturing should rebound.

In our opinion, today's data is slightly positive for the PLN exchange rate and yields on Polish bonds.

MPC meeting may weaken the PLN

FX rates



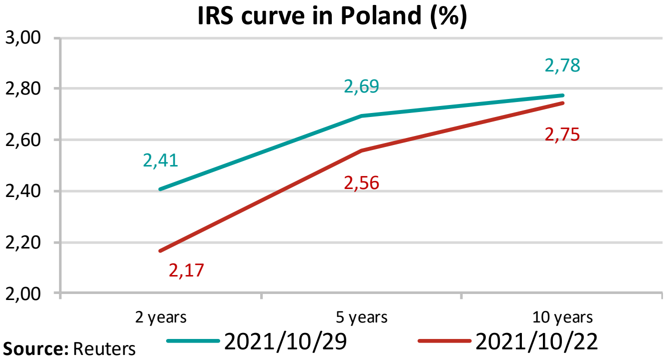
Source: Reuters

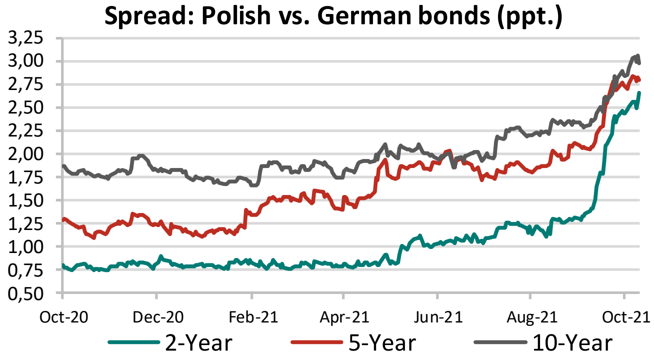
Last week, the EURPLN exchange rate climbed to 4.6106 (weakening of the PLN by 0.3%). The PLN was weakening through last week following an increase in global risk aversion reflected in the rise of the VIX index. The publication of higher-than-expected domestic inflation data strengthened investors' expectations of interest rate hikes in Poland, spurring a slight strengthening of the PLN on Friday.

In the case of the EURUSD rate, the highlight of last week was the ECB meeting. Despite presenting a dovish tone, Ch. Lagarde was unable to curb the expectation of an interest rates hikes in the Eurozone. Consequently, on Thursday the EUR strengthened against the USD. Also noteworthy is the weakening of the EUR against the CHF seen in recent weeks. The drop in the EURCHF rate is supported by higher global risk aversion, which is reflected in the increase of the VIX index. Consequently, the CHFPLN rate last week reached its highest level since the SNB abandoned the euro ceiling back in January 2015.

Today's publication of the PMI index for Polish manufacturing is, in our opinion, slightly positive for the PLN. This week, the key factor for the PLN will be the MPC meeting, which in our opinion may contribute to a slight weakening of the PLN. In turn, the Fed meeting may spur increased volatility of the EURPLN rate. Scheduled for Friday, the release of US non-farm payroll data will, in our opinion, not have a major bearing on the PLN exchange rate.

Fed meeting in the debt market's spotlight





Source: Reuters

Last week, 2-year IRS rates increased to 2.41 (up by 24 bps), 5-year to 2.69 (up by 13 bps), and 10-year to 2,78 (up by 3 bps). Last week saw a marked rise in IRS rates following the core markets (Germany, USA), particularly at the short end of the yield curve. Conducive to an increase in IRS rates are investors' expectations of monetary policy tightening by major central banks amid persistently high inflation. On Friday, a local factor driving up IRS rates was the publication of higher-than-expected domestic inflation data.

Today's publication of the PMI index for Polish manufacturing is, in our opinion, slightly positive for IRS rates. This week, the MPC meeting will be in the market's spotlight. We believe that it may contribute to a slight decline in IRS rates. The Fed meeting scheduled for Wednesday may spur increased volatility of IRS rates. We predict that the release of US non-farm payroll data will not have a major bearing on the curve.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-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	0,50	**0,75**
EURPLN*	4,60	4,47	4,55	4,52	4,52	4,63	4,56	4,48	4,52	4,56	4,52	4,60	4,62	**4,60**
USDPLN*	3,95	3,75	3,73	3,72	3,74	3,95	3,79	3,66	3,81	3,84	3,83	3,98	3,97	**3,93**
CHFPLN*	4,32	4,13	4,21	4,18	4,11	4,18	4,15	4,07	4,12	4,24	4,18	4,27	4,35	**4,31**
CPI inflation (% YoY)	3,1	3,0	2,4	2,6	2,4	3,2	4,3	4,7	4,4	5,0	5,5	5,9	**6,5**	
Core inflation (% YoY)	4,2	4,3	3,7	3,9	3,7	3,9	3,9	4,0	3,5	3,7	3,9	4,2	**4,3**	
Industrial production (% YoY)	1,0	5,4	11,1	0,7	2,5	18,6	44,2	29,6	18,1	9,6	13,1	8,9	**5,8**	
PPI inflation (% YoY)	-0,4	-0,2	0,1	1,0	2,2	4,2	5,5	6,6	7,2	8,4	9,6	10,2	**10,5**	
Retail sales (% YoY)	-2,1	-5,3	-0,8	-6,0	-2,7	17,1	25,7	19,1	13,0	8,9	10,7	11,1	**12,6**	
Corporate sector wages (% YoY)	4,7	4,9	6,6	4,8	4,5	8,0	9,9	10,1	9,8	8,7	9,5	8,7	**9,0**	
Employment (% YoY)	-1,0	-1,2	-1,0	-2,0	-1,7	-1,3	0,9	2,7	2,8	1,8	0,9	0,6	**0,4**	
Unemployment rate* (%)	6,1	6,1	6,3	6,5	6,6	6,4	6,3	6,1	6,0	5,9	5,8	5,6	**5,5**	
Current account (M EUR)	1550	1298	751	2034	652	71	1269	-531	-378	-1551	-1686	**-757**		
Exports (% YoY EUR)	5,8	12,4	17,0	1,0	5,6	27,7	68,6	40,5	22,7	13,1	19,4	**14,9**		
Imports (% YoY EUR)	-2,4	6,2	14,6	-3,7	6,0	23,6	58,3	52,4	34,7	21,5	32,9	**25,2**		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

Indicator		2021				2022				2020	2021	2022
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)		-0,8	11,2	4,8	4,8	4,5	4,8	4,5	4,8	-2,5	4,9	4,7
Private consumption (% YoY)		0,1	13,1	5,0	3,0	3,1	3,0	3,1	3,2	-3,0	5,1	3,1
Gross fixed capital formation (% YoY)		1,7	5,6	7,0	13,5	6,2	5,7	7,8	7,0	-9,0	7,9	6,8
Export - constant prices (% YoY)		7,3	29,2	16,3	7,9	7,0	7,5	7,3	7,5	0,1	14,1	7,3
Import - constant prices (% YoY)		10,3	34,5	20,0	9,8	8,1	7,9	8,0	8,0	-1,2	17,9	8,0
GDP growth contributions	Private consumption (pp)	0,1	7,4	3,0	1,5	1,9	1,7	1,8	1,5	-1,8	2,9	1,7
	Investments (pp)	0,2	0,8	1,1	2,9	0,8	0,8	1,3	1,6	-1,7	1,3	1,1
	Net exports (pp)	-1,9	-0,7	-0,8	-0,4	-0,2	0,2	0,1	0,2	0,7	-0,9	0,1
Current account (% of GDP)***		2,7	1,7	1,7	1,7	1,7	1,6	1,5	1,5	2,9	1,7	1,5
Unemployment rate (%)**		6,4	5,9	5,7	5,8	6,0	5,5	5,3	5,4	6,2	5,8	5,4
Non-agricultural employment (% YoY)		0,1	3,1	1,0	0,8	0,5	0,5	0,4	0,4	-0,5	1,2	0,5
Wages in national economy (% YoY)		6,6	9,6	8,1	7,5	7,0	6,5	7,0	6,3	5,3	7,9	6,7
CPI Inflation (% YoY)*		2,7	4,5	5,5	6,8	6,9	5,9	5,1	4,1	3,4	4,9	5,5
Wibor 3M (%)**		0,21	0,21	0,23	1,13	1,13	1,13	1,13	1,21	0,21	1,13	1,21
NBP reference rate (%)**		0,10	0,10	0,10	0,75	1,00	1,00	1,00	1,00	0,10	0,75	1,00
EURPLN**		4,63	4,52	4,60	4,60	4,57	4,50	4,45	4,40	4,55	4,60	4,40
USDPLN**		3,95	3,81	3,98	3,90	3,87	3,75	3,71	3,64	3,73	3,90	3,64

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST*	
					CA	CONSENSUS**
		Monday 11/01/2021				
2:45	China	Caixin Manufacturing PMI (pts)	Oct	50,2		50,0
14:45	USA	Flash Manufacturing PMI (pts)	Oct	59,2		
15:00	USA	ISM Manufacturing PMI (pts)	Oct	61,1	61,0	60,5
		Tuesday 11/02/2021				
9:00	**Poland**	**Manufacturing PMI (pts)**	**Oct**	**53,4**	**53,2**	**53,0**
9:55	Germany	Final Manufacturing PMI (pts)	Oct	58,2	58,2	58,2
10:00	Eurozone	Final Manufacturing PMI (pts)	Oct	58,5	58,5	58,5
		Wednesday 11/03/2021				
11:00	Eurozone	Unemployment rate (%)	Sep	7,5		7,4
13:15	USA	ADP employment report (k)	Oct	568		400
15:00	USA	Factory orders (% MoM)	Sep	1,2	0,1	0,0
16:00	USA	ISM Non-Manufacturing Index (pts)	Oct	61,9	62,5	62,0
19:00	USA	FOMC meeting (%)	Nov	0,25	0,25	0,25
	Poland	**NBP rate decision (%)**	**Nov**	**0,50**	**0,75**	**0,75**
		Thursday 11/04/2021				
8:00	Germany	New industrial orders (% MoM)	Sep	-7,7		2,0
10:00	Eurozone	Services PMI (pts)	Oct	54,7	54,7	54,7
10:00	Eurozone	Final Composite PMI (pts)	Oct	54,3	54,3	54,3
11:00	Eurozone	PPI (% YoY)	Sep	13,4		15,2
13:00	UK	BOE rate decision (%)	Nov	0,10	0,10	0,10
		Friday 11/05/2021				
8:00	Germany	Industrial production (% MoM)	Sep	-4,0		1,0
11:00	Eurozone	Retail sales (% MoM)	Sep	0,3		0,3
13:30	USA	Unemployment rate (%)	Oct	4,8	4,7	4,7
13:30	USA	Non-farm payrolls (k MoM)	Oct	194	475	450

*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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