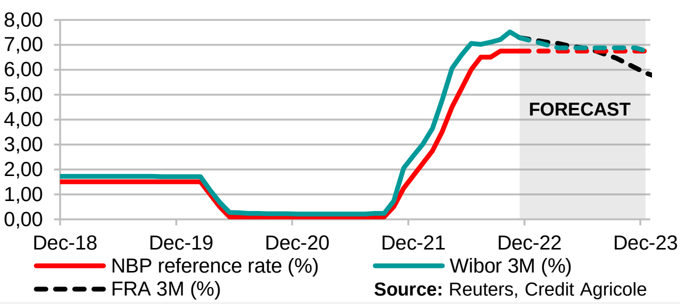
There is inflation, there will be disinflation

This week

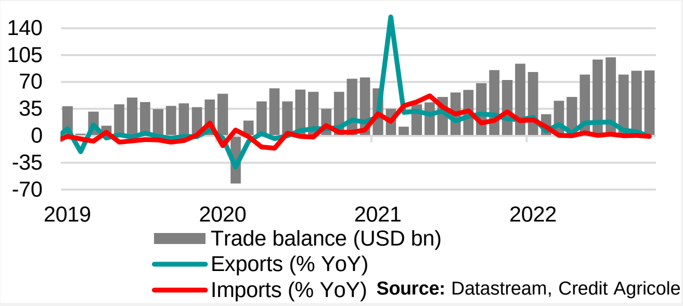
- **This week's most important event is the meeting of the Monetary Policy Council scheduled for Wednesday.** We expect the MPC to keep interest rates unchanged (NBP reference rate at 6.75%). November's second consecutive decision of the MPC to keep interest rates stable was consistent with the reluctance to keep tightening the monetary policy expressed in public statements by the NBP President and some MPC members despite the persistent and high inflation, and low probability of its return to the inflation target in the monetary policy transmission horizon. The decision to stabilise interest rates at this week's meeting will be consistent with the NBP president's comments at the November conference. At that time, A. Glapiński hinted that if inflation evolves in line with the NBP's November projection, further interest rate hikes should not be expected. A strong argument for the MPC in favour of maintaining the status quo in the monetary policy is the drop in CPI inflation recorded in November (see below). The decision to keep interest rates unchanged this week will be consistent with the market consensus, and thus it should be neutral for the PLN exchange rate and yields on Polish bonds. This week will also likely see the customary press conference with the NBP president, which will shed more light on the domestic monetary policy outlook.



Source: Reuters, Credit Agricole

- **Results of business surveys for the US will be published this week.** In our opinion, the non-manufacturing ISM index slipped to 53.3 pts in November, down from 54.4 pts in October. The deterioration of the situation in the services sector was driven by the weakening of consumer demand amid high inflation. Friday will see the release of the flash University of Michigan Index. We expect a further deterioration of household sentiment (56.0 pts in December vs. 56.8 pts in November). We believe that the combined impact of US data releases on the financial markets will be limited.

- **China's foreign trade figures are set to release on Wednesday.** According to the consensus, the Chinese trade balance shrank to USD 79.1bn in November from USD 85.2bn in October. The market expects exports growth to have slowed down in November to -3.5% YoY vs. -0.3% in October, with imports growth falling to -5.0% versus -0.7%. The data will most likely confirm the continued negative impact of the COVID-19 restrictions on Chinese domestic demand. In turn, exports data will signal a decline in global trade activity. We believe that the release of Chinese data will be neutral for the financial markets.



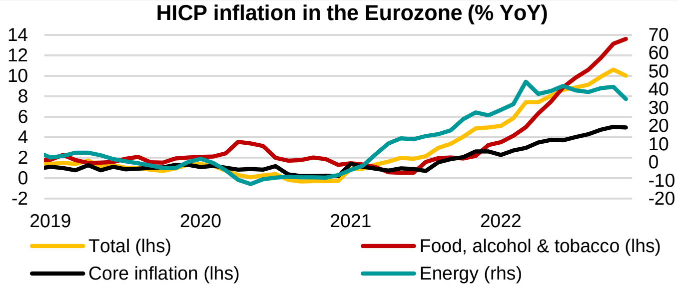
Source: Datastream, Credit Agricole

Last week

- **According to the flash estimate, CPI inflation in Poland fell to 17.4% YoY in November from 17.9% in October, running markedly below the market consensus (18.0%) and our forecast (17.9%).** This marks the first decline in inflation since February 2022. GUS published partial data on the inflation structure, including figures on the pace of price growth in the "food and non-alcoholic beverages", "energy" and "fuels" categories. Inflation was driven down by a slower price growth in such categories as "energy" (36.8% YoY in November vs. 41.6% in October) and "fuels" (15.5% vs. 19.5%), with faster price growth in the "food and non-alcoholic beverages" category (22.3% vs. 22.0%) as well as the rise in core inflation (up to 11.3% YoY in November vs. 11.0% in October in accordance with our estimations) having an opposite effect. The most surprising reading in the context of our forecast is the stronger-than-expected decline in price growth in the "energy" category (see MACROpulse of 30/11/2022). Thus, last week's data pose a downside risk to our scenario, according to which the annual average inflation in Poland will stand at 14.4% compared with 5.1% in 2021 and then fall to 11.8% in 2023.

- **According to the final estimate, GDP growth in Poland decreased to 3.6% YoY in Q3 from 5.8% in Q2, slightly above the flash estimate published earlier by the GUS (3.5%).** GDP growth between Q2 and Q3 was primarily driven down by the lower contribution of consumption caused by a decline in the real growth of the wage fund, as well as a strong deterioration in consumer sentiment. The lower contribution of investments also stifled GDP growth. We believe this trend was attributable to a sharp slowdown in housing demand reported by households, a slower increase in public investment, and diminishing investments in the micro and small enterprises sector. On the other hand, the higher contribution of inventories had the opposite effect, with the former serving as the main driver of GDP growth in Q3. However, in our opinion the increase in the contribution of inventories recorded in Q3 is only temporary, and their reduction in the coming quarters will slow down GDP growth. The most important factor adding to GDP growth between Q2 and Q3 was net exports. We believe that factors supporting exports in Q3 included the increased inflow of direct foreign investments to Poland, rebounding activity in the automotive industry, and the takeover of some supply chains from Ukraine. Moreover, the increased contribution from net exports to GDP growth was supported by a slowdown in consumer demand in Poland and the significant weakening of the PLN relative to main foreign currencies recorded in the previous months. We believe that in Q4, net exports will remain an important driver of GDP growth in Poland (see MACROpulse of 30/11/2022). Quarterly GDP growth adjusted for seasonal factors rose to 1.0% in Q3 (0.9% in the preliminary estimate) from -2.3% in Q2. This means that Poland managed to avoid a technical recession consisting in a decrease in GDP on a quarterly basis for at least two consecutive quarters. Thus, we are seeing a materialization of our "soft landing" scenario for the Polish economy. It assumes that although the growth of Polish GDP in 2023 will decrease substantially, it will remain positive (1.2% YoY vs. 4.5% in 2022 and 6.8% in 2021).
- **Poland's manufacturing PMI rose to 43.4 pts in November from 42.0 pts in October, running above the market consensus (42.4 pts) and slightly above our forecast (43.2 pkt.).** This marks the seventh consecutive month where the index remained below the 50-point threshold, which separates expansion from contraction of activity. The rise in the index is attributable to higher contributions from 4 out of its 5 components: inventories, production, employment, and total new orders. These rises were somewhat offset by a lower contribution of delivery times. In the data structure, the expected output in the horizon of 12 months deserves special attention as it increased in November to the highest level since last August, reading well above the 50-point mark that separates anticipated growth from contraction. This signals that the restructuring processes launched in many businesses to increase productivity and reduce energy consumption, as well as the reduction in supply constraints, led some companies to have a more optimistic view of their future activity, despite the continuing decline in orders and output (see MACROpulse 1/12/2022). The marked increase in the future output component supports our "soft landing" scenario for the Polish economy, according to which it will avoid recession in the coming quarters, with an economic growth of 1.2% for the whole of 2023.

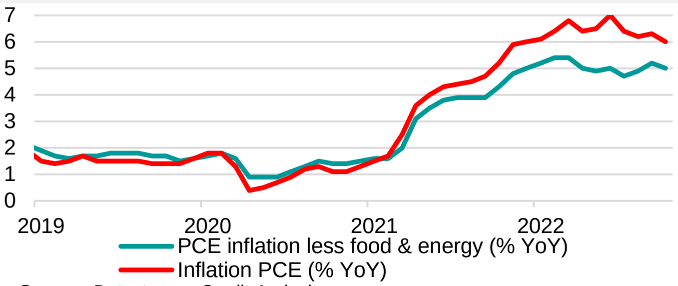
According to the flash estimate, inflation in the Eurozone fell to 10.0% YoY in November, down from 10.6% in October, well below the market consensus (10.4%). This marked the first drop in inflation since August 2021. Inflation declined on the back of lower price growth in the "energy" and "services" categories, with the higher price growth in the "food" category having the opposite effect. Core inflation remained stable between November and October at an all-time high of 5.0% YoY. We forecast that inflation in the Eurozone will reach its maximum in December, running slightly below 11% YoY. At the same time, we believe that it will remain above 8% at least until the end of H1 2023. The prospects for inflation remaining high over an extended period supports our upward revision of the Eurozone interest rate scenario, according to which the ECB will raise rates by 50bp in both December and February, followed by a 25bp move in March, thus concluding the hike cycle with the policy rate at 3.25% and the deposit rate at 2.75%.



Source: Datastream, Credit Agricole

In November, the Caixin PMI index for Chinese manufacturing climbed to 49.4 pts compared with 49.2 pts in October, outperforming market expectations (49.0 pts). Its increase was attributable to higher contributions from 2 out of 5 of its components (for new orders and delivery times), with lower contributions from current output, employment and inventories having the opposite effect. In the data, particularly noteworthy is the continued decline in both current output and new orders, including export orders. This is largely attributable to the negative impact of COVID restrictions on activity in Chinese manufacturing, as well as weakening global demand. We forecast that in the coming months, the Chinese government will intensify its economic policy measures aimed at stimulating economic growth. Nevertheless, we predict that China's GDP growth will slow down to 3.0% in 2022 from 8.1% in 2021.

Last week, some vital data regarding the US economy was published. Non-farm payroll grew by 263k in November compared with an increase of 284k in September (upward revision from 261k), running above market expectations of 200k. The most substantial expansion in employment was recorded in leisure and hospitality (+88.0k), education and health services (+82.0k) and the government sector (+42.0k). Standing at 3.7%, consistent with market expectations, the unemployment rate did not change in November compared to October. At the same time, the labour market participation rate slipped to 62.1% in November from 62.2% in October. Hourly wage growth in November rose to 5.1% YoY from 4.9% in October, indicating that the wage pressure in the US economy remains substantial. Last week also saw the release of data on PCE inflation, which in October dropped to 6.0% YoY vs. 6.3% in September. A decrease was also recorded in the case of core PCE inflation (5.0% vs. 5.2%), indicating weakening inflationary pressures in the US economy. Last week also saw the publication of consumer sentiment surveys results. The Conference Board index (100.2 pts in November vs. 102.2 pts in October) pointed to persistently poor consumer sentiment in the US. Moreover, last week the second estimate of US GDP was released, showing that the annualised rate of US GDP growth improved to 2.9% in Q3 compared with -0.6% in Q2 and 2.6% in the first estimate. Thus, in Q3 the USA pulled out of the technical recession it had entered in Q1 2022. The main drivers of GDP growth between Q2 and Q3 were higher contributions from net exports and inventories. Thus, in Q3 the main engine of US economic

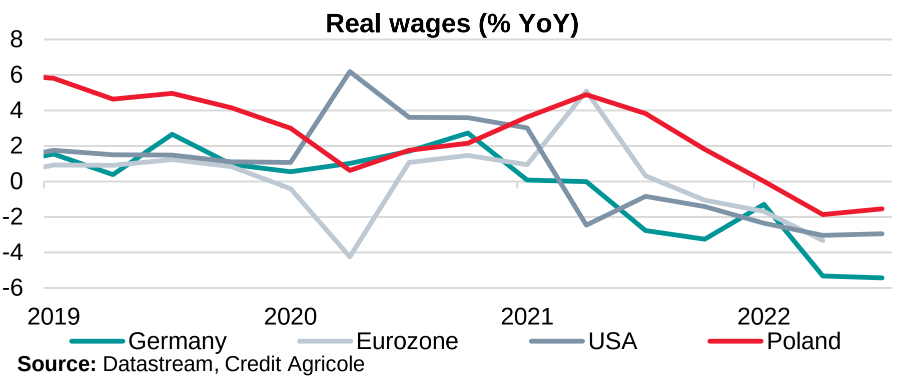


Source: Datastream, Credit Agricole

growth was net exports, while in Q2 it was chiefly spurred by private consumption. The ISM index signaled a deterioration in manufacturing as it fell to 49.0 pts in November from 50.2 pts in October, running below market expectations (49.8 pts). The index slipped on the back of higher contributions from 4 out of 5 of its components (new orders, output, employment and inventories), with the lower contribution from suppliers' delivery times having the opposite effect. In the structure of the data, particularly noteworthy is the continued decline in input prices (the component was well below the 50-point threshold), signaling waning cost pressure in US manufacturing. We see a downside risk to our scenario, according to which throughout 2022 US GDP will expand by 1.8% vs. a 5.7% growth in 2021, and increase by 0.5% in 2023.

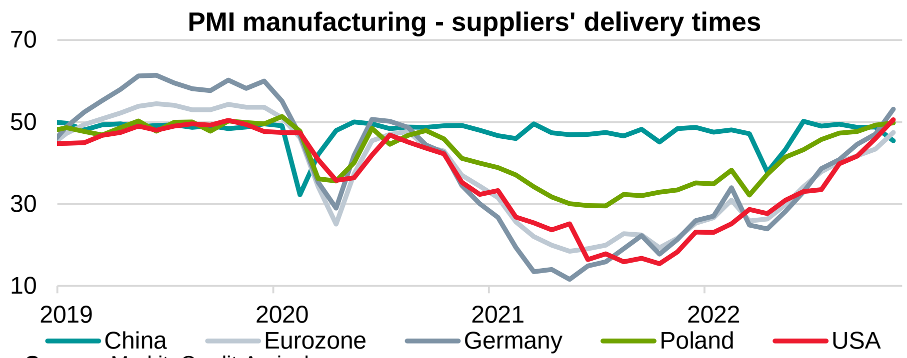
There is inflation, there will be disinflation

In accordance with the flash estimate published last week, CPI inflation in Poland went down to 17.4% YoY in November vs. 17.9% in October, running clearly below the market consensus (18.0%) and our forecast (17.9%). Inflation thus fell for the first time since June 2021 (disregarding its fall in February 2022 caused directly by the introduction of the Anti-Inflation Shield). We do not believe that this is the end of the rise in inflation in Poland. Nevertheless, we are noticing more and more signals in the global environment signalling disinflationary trends in the medium term.



Source: Datastream, Credit Agricole

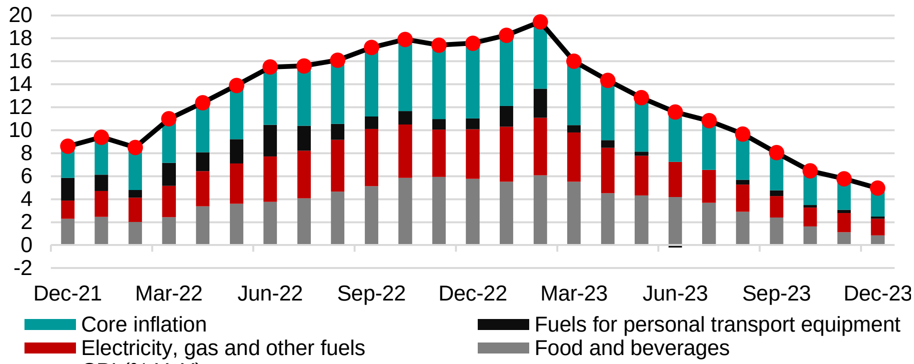
Among other factors, a fall in real wages will have a negative impact on inflationary pressures. Real wage growth rate has been on a downward trend since 2021, not only in Poland but also in other economies such as the US and the Eurozone, including Germany. In 2022, it reached negative values in all the economies mentioned. A reduction in the real purchasing power of households will drive down consumer demand.



Source: Markit, Credit Agricole

Declining supply constraints will be another factor supporting disinflation. The November PMI for Polish manufacturing saw an increase in the delivery times component to close to 50 pts. This means that the delivery times of intermediate goods used in production do not change. This is the first time we have encountered such a situation since late 2019 / early 2020, the period immediately preceding the outbreak of the pandemic. In the case of other countries (including Germany and the US), November even saw a reduction in delivery times. This signals that global and domestic constraints in terms of accessibility of intermediate goods caused by disruption in supply chains are diminishing (according to the manufacturing businesses surveyed in Poland, 'difficulties in sourcing materials and logistics have started to disappear'). Such trends contribute to a reduction in the price growth rate of these goods, as reflected in the reduction recorded in November in the PMI component for intermediate goods prices to its lowest level since October 2020. A reduction in inflationary pressures is already evident in PPI inflation in Poland. It reached a local maximum of 25.6% YoY in June and has been since on a downward trend. A slower increase in producer prices will have an impact - with some lag - on reducing consumer inflation in Poland and abroad.

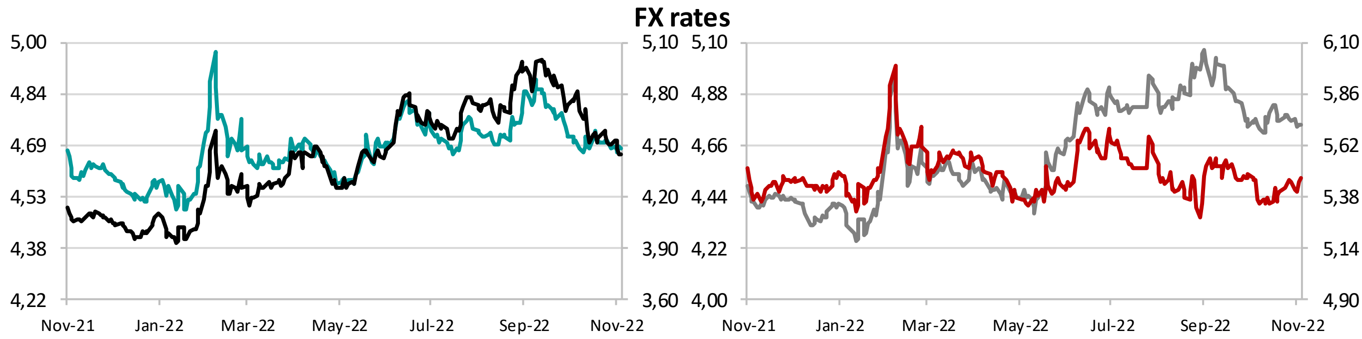
Given the trends outlined, we forecast that core inflation in the Eurozone will trend downwards in 2023. We expect it to decline from 5.0% YoY in November 2022 to a level close to 3.0% YoY towards the end of 2023. Given that the Eurozone is an important economic partner of Poland, domestic inflationary processes (especially in terms of core inflation) are correlated with trends observed in the common currency area. On the basis of our quarterly forecasting model, we estimate that a 1 pp drop in core inflation in the Eurozone has the effect of lowering core inflation in Poland by around 0.4-0.6 pp. Thus, the decline in core inflation that we expect in the Eurozone in 2023 will have the effect of lowering core inflation in Poland by around 1.0 pp.



Source: GUS, Credit Agricole

Also other external conditions will be pushing inflation down in Poland. The marked fall in the prices of most agricultural commodities on the world market visible in recent months will reduce the growth rate of prices of food and non-alcoholic beverages. The stabilisation of energy prices on global markets clearly below the local maxima observed in Q3 2022, in conditions of a slight appreciation of the PLN, will support disinflationary tendencies in Poland. Summarising the trends outlined above, we expect headline inflation to reach its local peak at slightly below 20% YoY in February 2023, before starting to ease back to around 5% by the end of 2023. We expect CPI inflation to reach 14.4% YoY in 2022 and 11.8% in 2023. There is a significant risk to our forecast due to the difficulty in estimating the resultant effect of the removal of the Anti-Inflation Shield and the introduction of a new mechanism to cap energy price increases in early 2023.

MPC meeting crucial for the PLN



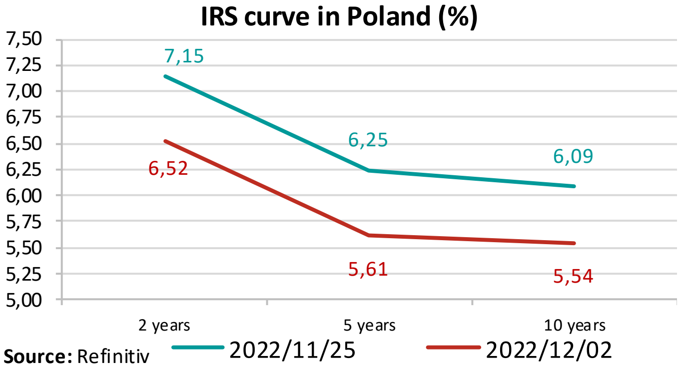
Source: Refinitiv

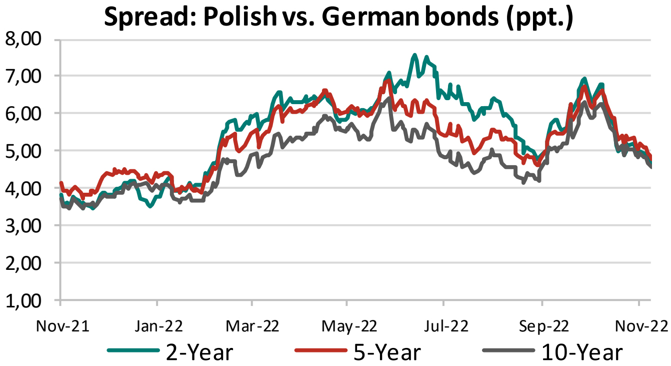
Last week the EURPLN exchange rate stood at 4.6785 (no change from the level two weeks ago). The beginning of last week saw low volatility in the EURPLN exchange rate, which was in a mild downward trend. The clearly lower-than-expected flash estimate of inflation in Poland published on Wednesday was slightly negative for the PLN, but it failed to reverse the trend. The correction and weakening of the PLN did not occur until Thursday, which was supported by the publication of PMI indices in the countries of Central and Eastern Europe indicating a continued decline in manufacturing activity. On the other hand, the publication of data signalling declining inflationary pressures in the US had the opposite effect.

Last week saw a marked weakening of the USD against the EUR. In the first part of the week it was supported by a statement from Federal Reserve chairman J. Powell, who said that he and other FOMC members did not want to tighten monetary policy too much. On Thursday, an additional factor acting to weaken the USD against the EUR was the publication of US inflation data, which dampened investors' expectations regarding the scale of further interest rate hikes by the Fed. The publication of US labour market data led to a correction and a strengthening of the USD against the EUR.

This week, the MPC's interest rate decision scheduled for Wednesday will be crucial for the PLN. In our view, the MPC will keep interest rates unchanged, which will be neutral for the PLN exchange rate. We believe that data releases from global economies planned for this week will not have a significant impact on the PLN. Information suggesting a possible change in the monetary policy stance of the Federal Reserve and the ECB, as well as information relating to the course of hostilities in Ukraine will remain an important factor determining the PLN exchange rate.

MPC meeting in the spotlight





Source: Refinitiv

Last week, 2-year IRS rates decreased to 6.52 (down by 63bp), 5-year rates to 5.61 (down by 64bp) and 10-year ones to 5.54 (down by 55bp). Last week saw a drop in IRS rates across the curve following the core markets. The drop in IRS rates in the core markets was supported by diminishing investors' expectations of interest rate cuts by the major central banks, linked to, among other things, the reported decline in inflation in both the US and the Eurozone, as well as the dovish statement by Federal Reserve chairman J. Powell (see above).

This week the MPC meeting scheduled for Wednesday will be crucial for the IRS rates. However, we believe it will be neutral for the curve. Other data releases from the global economy planned for this week will not have a significant impact on the IRS, in our opinion. Information suggesting a possible change in the monetary policy stance of the Federal Reserve and the ECB, as well as information relating to the course of hostilities in Ukraine will remain an important factor affecting the yield curve.

Forecasts of the monthly macroeconomic indicators

Main monthly macroeconomic indicators in Poland

Indicator	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22	Dec-22
NBP reference rate (%)	1,25	1,75	2,25	2,75	3,50	4,50	5,25	6,00	6,50	6,50	6,75	6,75	6,75	**6,75**
EURPLN*	4,65	4,58	4,58	4,69	4,64	4,67	4,58	4,70	4,73	4,72	4,85	4,71	4,67	**4,70**
USDPLN*	4,10	4,03	4,08	4,18	4,19	4,43	4,27	4,48	4,63	4,70	4,95	4,77	4,48	**4,85**
CHFPLN*	4,47	4,42	4,40	4,56	4,54	4,55	4,45	4,69	4,86	4,80	5,01	4,76	4,74	**4,95**
CPI inflation (% YoY)	7,8	8,6	9,4	8,5	11,0	12,4	13,9	15,5	15,6	16,1	17,2	17,9	**17,9**	
Core inflation (% YoY)	4,7	5,3	6,1	6,7	6,9	7,7	8,5	9,1	9,3	9,9	10,7	11,0	**11,4**	
Industrial production (% YoY)	14,9	16,3	18,0	17,3	15,4	12,3	14,9	10,4	7,1	10,9	9,8	6,8	**1,6**	
PPI inflation (% YoY)	13,6	14,4	16,1	16,1	21,9	24,1	24,7	25,6	25,5	25,5	24,6	22,9	**21,6**	
Retail sales (% YoY)	21,2	16,9	20,0	16,5	22,0	33,4	23,6	19,9	18,4	21,5	21,9	18,3	**14,0**	
Corporate sector wages (% YoY)	9,8	11,2	9,5	11,7	12,4	14,1	13,5	13,0	15,8	12,7	14,5	13,0	**12,4**	
Employment (% YoY)	0,7	0,5	2,3	2,2	2,4	2,8	2,4	2,2	2,3	2,4	2,3	2,4	**2,3**	
Unemployment rate* (%)	5,8	5,8	5,9	5,9	5,8	5,6	5,4	5,2	5,2	5,2	5,1	5,1	**5,1**	
Current account (M EUR)	-1483	-3883	-1091	-2032	-4206	-2844	-1340	-541	-1887	-3332	-1561	**-2060**		
Exports (% YoY EUR)	13,7	25,0	27,4	20,3	11,9	18,2	26,9	21,3	19,0	26,7	25,5	**22,6**		
Imports (% YoY EUR)	31,2	39,6	38,7	29,7	31,4	36,4	32,5	26,6	20,6	28,7	28,9	**23,0**		

*end of period

Forecasts of the quarterly macroeconomic indicators

Main macroeconomic indicators in Poland

Indicator	2022				2023				2021	2022	2023
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross Domestic Product (% YoY)	8,6	5,8	3,6	0,8	-1,0	0,1	2,6	3,2	6,8	4,5	1,2
Private consumption (% YoY)	6,7	6,4	0,9	0,5	0,2	0,4	0,5	0,5	6,3	3,5	0,4
Gross fixed capital formation (% YoY)	4,7	6,6	2,0	0,6	-1,4	0,2	1,9	2,4	2,1	3,0	1,1
Export - constant prices (% YoY)	4,2	5,2	6,9	3,3	1,6	0,5	2,9	4,5	12,5	4,9	2,3
Import - constant prices (% YoY)	9,4	6,9	6,0	0,9	0,7	-1,5	4,7	6,5	16,1	5,5	2,4
GDP growth contributions: Private consumption (pp)	4,0	3,6	0,5	0,2	0,1	0,2	0,3	0,2	3,5	2,0	0,2
GDP growth contributions: Investments (pp)	0,6	1,0	0,3	0,1	-0,2	0,0	0,3	0,5	0,4	0,5	0,2
GDP growth contributions: Net exports (pp)	-2,7	-0,7	0,6	1,4	0,6	1,3	-0,9	-1,0	-1,0	-0,2	0,0
Current account (% of GDP)***	-2,7	-3,5	-3,7	-4,5	-4,3	-4,2	-4,6	-4,7	-1,4	-4,5	-4,7
Unemployment rate (%)**	5,8	5,2	5,1	5,3	5,7	5,3	5,2	5,4	5,8	5,3	5,4
Non-agricultural employment (% YoY)	2,3	0,6	-0,9	-0,5	-0,5	-0,5	-0,5	-0,5	0,4	0,4	-0,5
Wages in national economy (% YoY)	9,7	11,8	14,6	14,0	14,5	13,2	11,4	9,9	8,9	12,5	12,3
CPI Inflation (% YoY)*	9,6	13,9	16,3	17,9	18,3	13,3	9,8	5,9	5,1	14,4	11,8
Wibor 3M (%)**	4,77	7,05	7,21	7,18	6,88	6,88	6,88	6,76	2,54	7,18	6,76
NBP reference rate (%)**	3,50	6,00	6,75	6,75	6,75	6,75	6,75	6,75	1,75	6,75	6,75
EURPLN**	4,64	4,70	4,85	4,70	4,78	4,73	4,70	4,65	4,58	4,70	4,65
USDPLN**	4,19	4,48	4,95	4,85	4,83	4,68	4,48	4,35	4,03	4,85	4,35

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

Calendar

TIME	COUNTRY	INDICATOR	PERIOD	PREV. VALUE	FORECAST* CA	FORECAST* CONSENSUS**
		Monday 12/05/2022				
10:00	Eurozone	Services PMI (pts)	Nov	48,6	48,6	48,6
10:00	Eurozone	Final Composite PMI (pts)	Nov	47,8	47,8	47,8
10:30	Eurozone	Sentix Index (pts)	Dec	-30,9		-27,5
11:00	Eurozone	Retail sales (% MoM)	Oct	0,4		-1,7
16:00	USA	Factory orders (% MoM)	Oct	0,3		0,6
16:00	USA	ISM Non-Manufacturing Index (pts)	Nov	54,4	53,3	53,1
		Tuesday 12/06/2022				
8:00	Germany	New industrial orders (% MoM)	Oct	-4,0		0,3
		Wednesday 12/07/2022				
8:00	Germany	Industrial production (% MoM)	Oct	0,6		-0,5
11:00	Eurozone	Final GDP (% YoY)	Q3	2,1	2,1	2,1
11:00	Eurozone	Revised GDP (% QoQ)	Q3	0,2	0,2	0,2
11:00	Eurozone	Employment (% YoY)	Q3	1,7		1,7
	China	Trade balance (bn USD)	Nov	85,2		79,1
	Poland	**NBP rate decision (%)**	**Dec**	**6,75**	**6,75**	**6,75**
		Thursday 12/08/2022				
14:30	USA	Initial jobless claims (k)	w/e	225		
		Friday 12/09/2022				
2:30	China	PPI (% YoY)	Nov	-1,3		
2:30	China	CPI (% YoY)	Nov	2,1		
14:00	**Poland**	**MPC Minutes**	**Dec**			
16:00	USA	Wholesale inventories (% MoM)	Oct	0,8		
16:00	USA	Wholesale sales (% MoM)	Oct	0,4		
16:00	USA	Initial U. of Michigan Sentiment Index (pts)	Dec	56,8	56,0	56,8

*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
** Refinitiv

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