Monthly Pulse Check
Economy. FI. FX

November 15th 2021

mBank Research

For contact details and classification of the report see the last page.

Our view in a nutshell (≥1Y horizon) & major forecasts

Macro

- The presence of new Sars-Cov-2 variants poses some risk for the global economy and for populations below herd immunity thresholds. Subsequent waves will come but they seem much more manageable now with minimal economic and health damage. The picture among countries is mixed, though. Ongoing supply and price shocks, coupled with higher interest rates pose a more significant risk to growth now than Covid-19.
- Polish economy enters soft patch that will last 2-3 quarters. We do not expect the cycle to be derailed but risks are tilted to the downside now. Overall, due to disbursement of the new EU funds, Polish cycle is seen as longer and possibly stronger than in the U.S. and euro zone. It will also be more inflationary since labor market survived 2020 very well. Monetary policy normalization is set to continue.

Monetary policy: Fed. ECB. NBP

- Fed: Attention shifts to exit strategy. First rate hikes in H2 2022.
- ECB: Risks balanced. Market pressure for rate hikes in 2022 that are unlikely to be delivered.
- NBP: Normalization of rates has just begun. Given the shape of inflation projection, there is no need to deep rate hikes. The MPC narrative suggests, however, that central bank will react to upcoming surprises in inflation. It means rates are set to reach 2.5% fast. It will be enough to stabilize inflation little above 2.5% (i. e. mostly at NBP target) in 2023. Contrary to market pricing, we think that interest rate risks are tilted to the downside.

FX Market

- Weak zloty with risks tilted to the downside in the very near term. Tensions with the EU, tensions on eastern border, NBP not seeing the value in stronger zloty. Additionally, local currency lost its shield from C/A. However, as the year-end passes and investors get used to other factors, wide interest rate differential (terminal NBP rate expected >3%) may be enough to bring at least some appreciation of local currency vs the euro.

		2021 Q1 F	2021 Q2 F	2021 Q3 F	2021 Q4 F	2022 Q1 F	2022 Q2 F	2022 Q3 F	2022 Q4 F	2020 Q1-Q4	2021 Q1-Q4	2022 Q1-Q4
GDP y/y	%	-0,9	11,1	5,1	5,8	5,2	4,3	4,6	5,1	-2,7	5,2	4,8
Individual consumption y/y	%	0,2	13,3	3,6	8,8	8,2	6,4	4,0	4,5	-3,0	6,5	5,8
Investment y/y	%	1,3	5,0	4,2	7,7	-4,0	11,0	12,0	12,5	-8,4	4,6	7,9
Inflation rate (eop)	%	3,2	4,4	5,9	7,4	7,4	7,2	5,9	4,4	2,4	7,4	4,4
Unemployment rate (eop)	%	6,5	5,9	5,6	5,6	5,6	5,1	4,9	5,0	6,2	5,6	5,1
NBP repo rate (eop)	%	0,1	0,10	0,10	1,50	2,25	2,50	2,50	2,50	0,10	1,50	2,50
EUR/PLN (eop)	%	4,63	4,52	4,61	4,65	4,60	4,50	4,45	4,40	4,56	4,65	4,40
USD/PLN (eop)	%	3,95	3,81	3,98	4,04	4,11	4,09	4,05	3,93	3,73	4,04	3,93

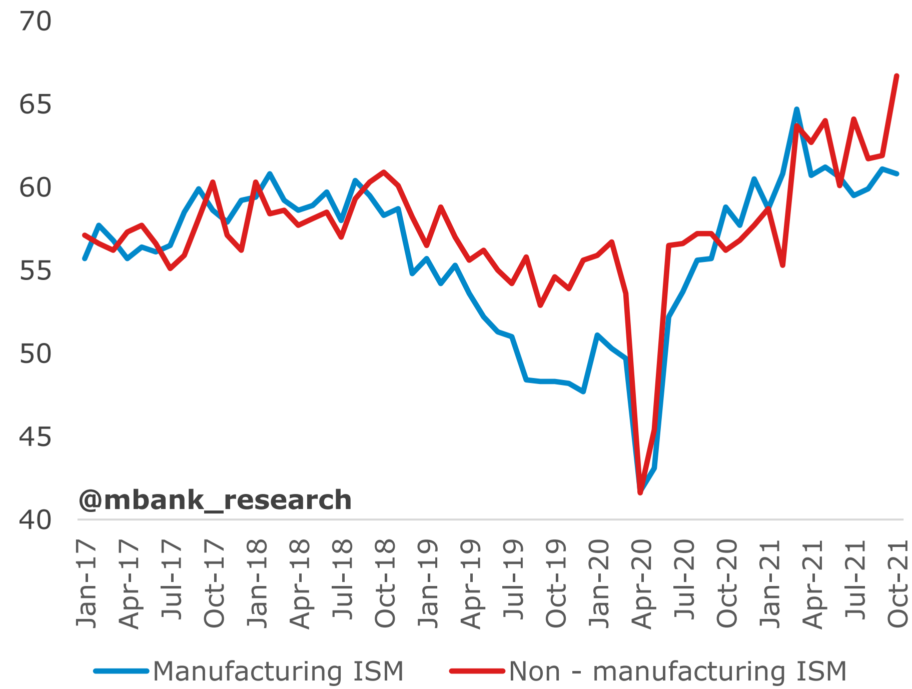
F - forecast

Highlights

- The fourth wave of covid-19 cases has arrived. No restrictions were introduced yet, but the next few weeks may bring some local changes as the number of cases is increasing. We are still convinced that possible restrictions will have minimal economic toll. At this very moment we globally consider Covid-19 more as a supply than demand shock. For monitor see here.
- Global picture did not change. High prices, petering out pent-up demand, supply bottlenecks and local Covid-19 outbreaks brew a consistent story of risks. Recently, new ones were added originating form high energy prices and next round of global food price increases. Inflation risk stays elevated and market pressure on central bank is mounting. Fed announced tapering and the case for raising rates will be strong enough in H2 2022 (see here). ECB decided to recalibrate PEPP program lately (moderately lower pace of PEPP than in previous two quarters) but emphasizes that it is not tapering. High inflation poses risks for expectations on monetary policy in the near term (20pb deposit rate hike in 2022 is priced in). So far, the narrative is consistent and ECB steers away from the need for monetary policy tightening. Ultimately, we think that low rates for longer scenario is still valid, but we start to think about rate hikes in euro zone in 2024 (EBC: see here).
- Polish economy looked good in Q3 (+5.1% y/y GDP growth, +2.1% q/q) but it is for sure the peak of sequential growth. Mobility and expenditures stay high (see here and here) but we see some fatigue, especially in the latter. It is also worth to note that we track nominal expenditures that overstate the condition of consumer demand (it can be easily seen while confronting nominal and retail sales). Supply constraints, high prices and later start of EU-sponsored investment cycle pose risk to the economy. The momentum is sufficient to deliver 5+ growth in 2021 but the outlook for 2022 is cloudy. Our current forecast of 4.8% is subject to downside risk. Inflation is at the highest level for more than 20 years (6.8 y/y, see here and here). Further acceleration is in the pipeline as electricity and gas increases will be introduced in early 2022. We aim for 7-8% inflation in Q1. Risks are clearly tilted to the upside.
- MPC decided to surprise the market with 40bp rate hike in October and 75bp in November. The recent inflation projection (see here and here) suggests that it is possible to bring inflation down to below 3.5% in 2023 without dramatic rate hikes. Yet, projection is understated near term and MPC members are ready to react to surprises. Therefore, we think that short-term inflation surprises will mostly determine terminal NBP rate. We opt for 2.5% in March and another 25-50bp hike in December. In our opinion risks are tilted to the downside.
- NBP’s asset purchase programme has come to an end since the value of purchases is negligible. However, NBP fails to admit that it is going to close the program but mostly treats it as ended… (see here and here).

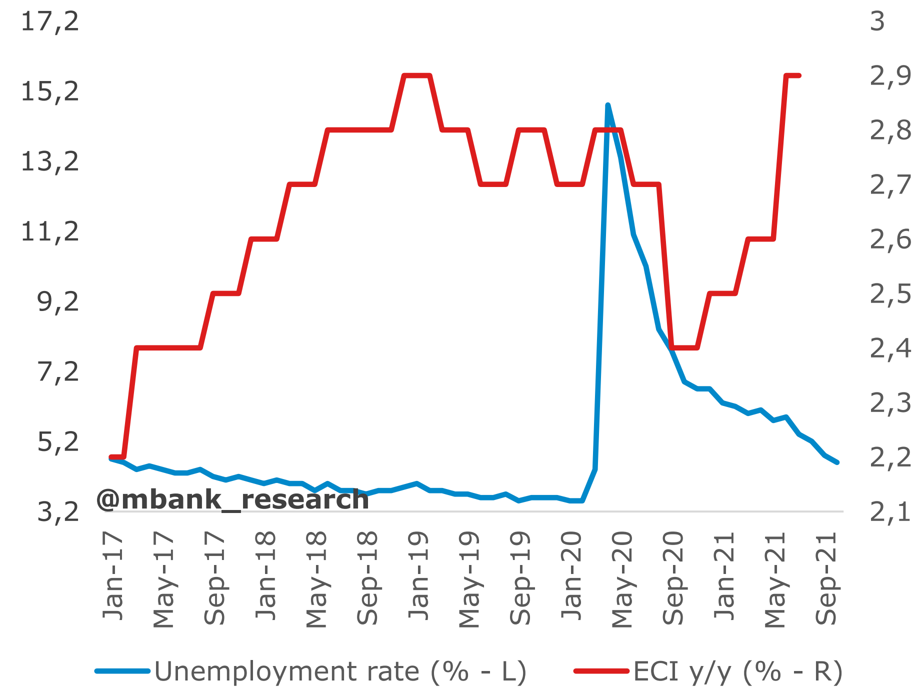
U.S. economy health check

ISM PMI: manufacturing & non-manufacturing



Source: ISM

Labor market: wages & unemployment rate

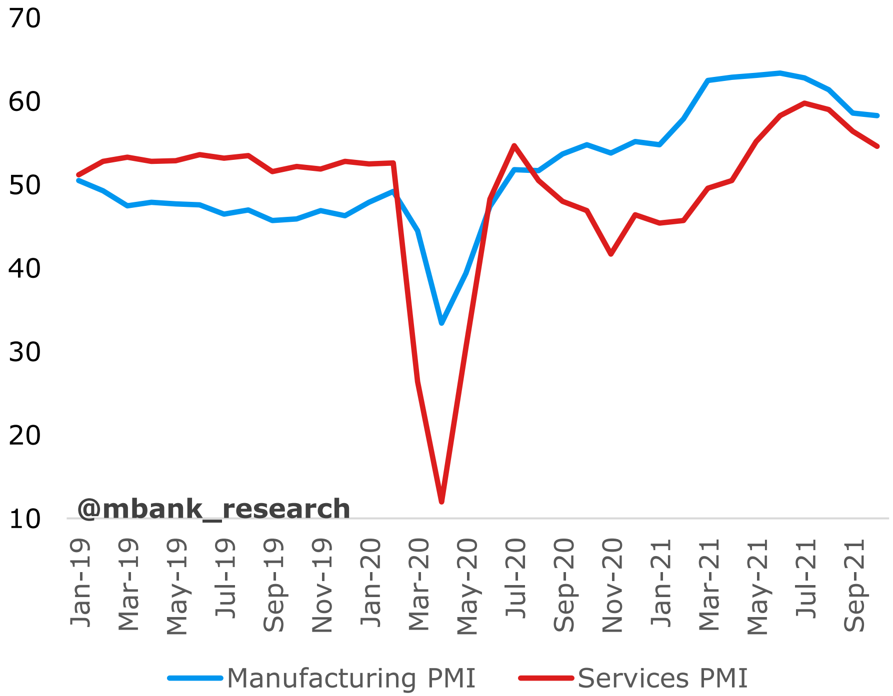


Source: FRED

- The labor market is moving towards the Fed target, but it will take a few more quarters to get there (goals regarding employment and unemployment rate will be probably fulfilled in the second half of next year). The overall condition of the economy is good (or even very good) – there are still supply problems, but the demand remains very strong. Perspectives for next quarters are also optimistic. Firms' sentiment (especially ISM in services) is very high.
- Fed has limited its bond purchases (tapering). Communication is carried out carefully and in advance. There are no signs of "taper tantrum". Tightening the monetary policy is much more cautious than after the financial crisis of 2007-2009.
- Fulfilling labor market targets and possibly not so temporary (as previously expected) inflation will result in earlier (than we previously expected) interest rate hikes. We think that monetary policy tightening by interest rates will commence in the second half of 2022. Given inflation dynamics, the risks are skewed towards more pronounced or even earlier move.

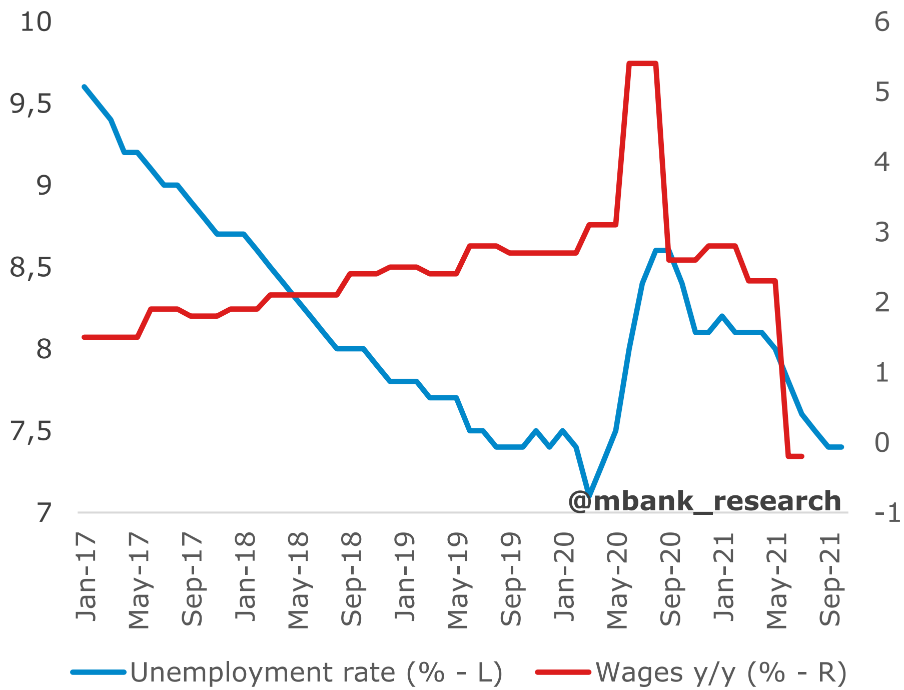
Euro area economy health check

Markit PMI: manufacturing & services



Source: Markit

Labor market: wages & unemployment rate

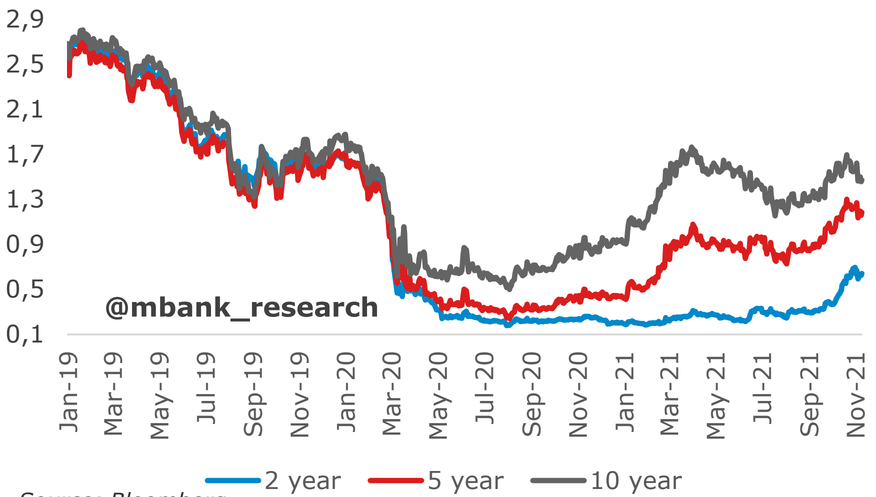


Source: Eurostat

- Firms' sentiment is not as high as in the US. The main difference is the epidemic situation (supply problems are common in both economies). In addition, demand weakened in sectors with previous high post-pandemic catching up effect.
- The ECB tries to convince market participants that it will not react to higher inflation. ECB claims that inflation is temporary and temporary means that current prints does not affect medium-term inflation.
- Temporarily increased PEPP purchases have returned to normal. The discussion about what can replace this program after its expiration at the beginning of 2022 is ahead of us (in December we will know much more). ECB will want to avoid a sharp expiry of asset purchases (the risk of fragmentation of the eurozone), hence the base option is to develop another, transitional or permanent program that will smooth the path of bond purchases, at least in 2022.

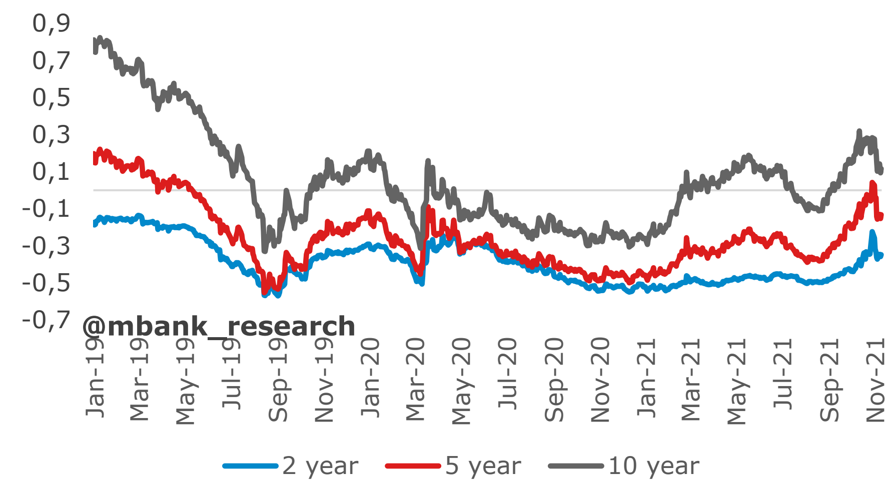
Global rates

US swap rates (%)



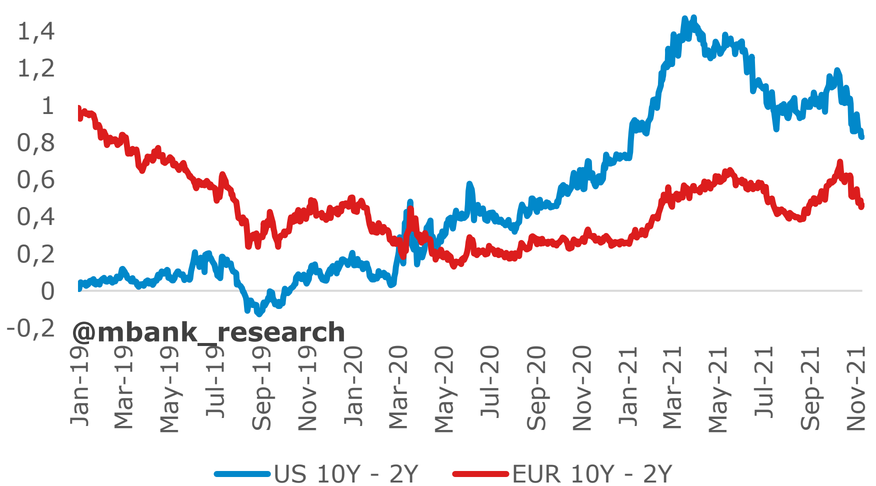
Source: Bloomberg

EU swap rates (%)



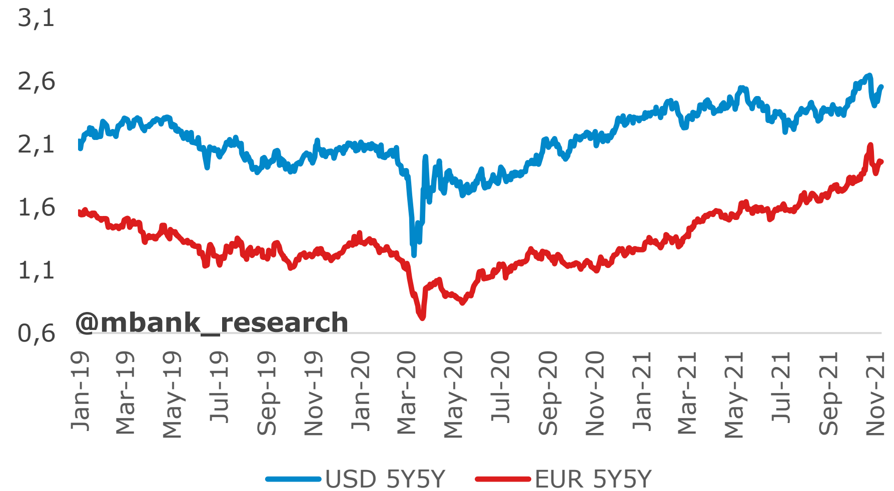
Source: Bloomberg

Swap spreads (10Y-2Y. p.p.)



Source: Bloomberg

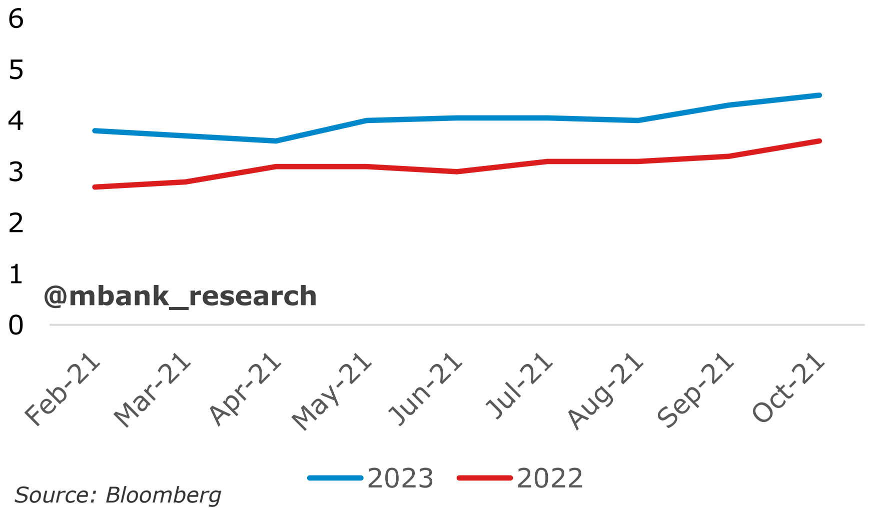
US and EZ inflation expectations (%)



Source: Bloomberg

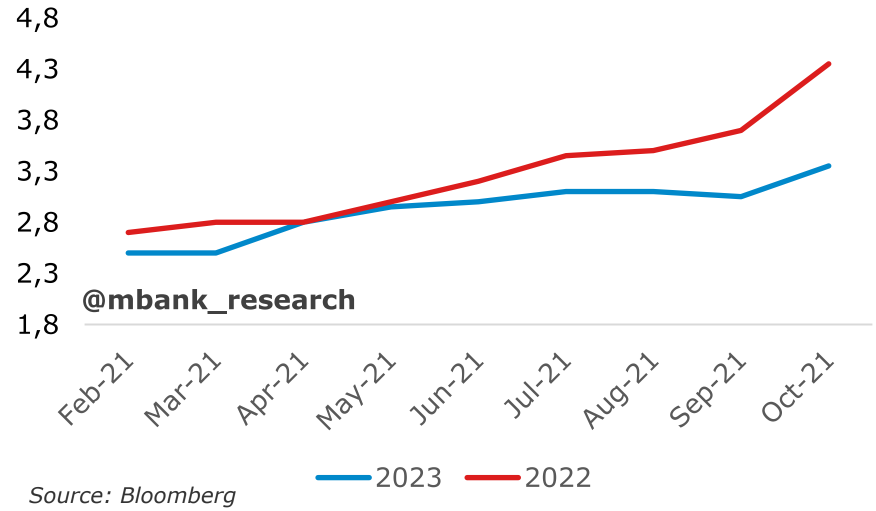
Consensus: what is expected in Poland?

Consensus tracker: GDP growth (% y/y. annual avg)



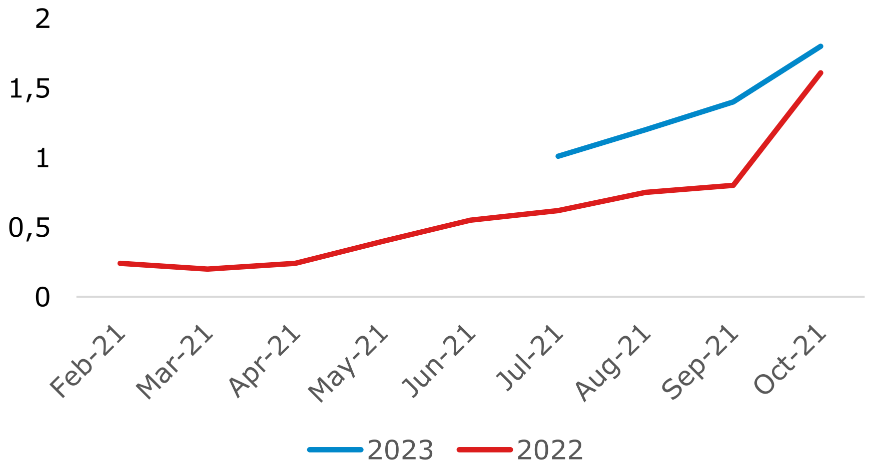
Source: Bloomberg

Consensus tracker: CPI inflation (% y/y. annual avg)



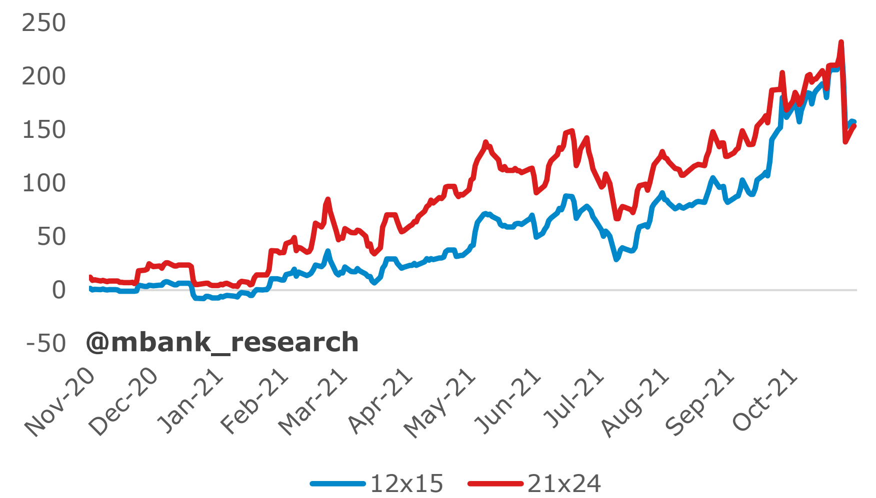
Source: Bloomberg

Consensus tracker: NBP ref. rate (% end of period)



Source: Bloomberg

Rate changes priced in by FRA (bps)



Source: Bloomberg

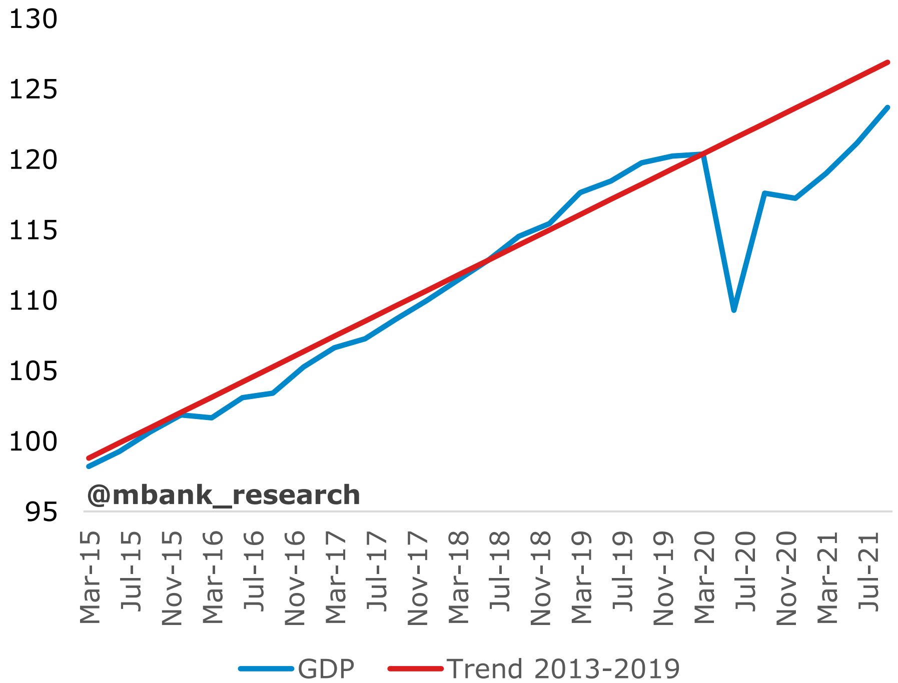
Upcoming Polish macro releases: November 2021

Publication	Date	Period	mBank	Consensus	Actual	Prior
CPI y/y (%)	29.10[1] 15.11[2]	Oct	6,7%	6,5%	6,8% 6,8%	5,9%
PMI (pts.)	02.11	Oct	51,6	53,0	53,8	53,4
Unemployment rate (%)	05.11[3] 25.11[4]	Oct	5,5%	5,5%	5,5%	5,6%
GDP (%)	12.11[1] 30.11[5]	3Q	4,8%	4,8%	5,1%	11,2%
Current account (m EUR)	15.11	Sep	-2300	-1300		-1686
Employment y/y (%)	19.11	Oct	0,6%	0,5%		0,6%
Wages y/y (%)	19.11	Oct	8,3%	8,8%		8,7%
Industrial output y/y (%)	22.11	Oct	5,3%	5,4%		8,8%
PPI y/y (%)	22.11	Oct	11,0%	10,8%		10,2%
Construction output y/y (%)	23.11	Oct	2,2%	3,3%		4,3%
Retail sales y/y (%)	23.11	Oct	6,5%	6,3%		5,1%
M3 y/y (%)	24.11	Oct	8,3%	8,3%		8,6%

[1] Flash estimate
[2] Final reading
[3] Ministry of Economic Development, Labour and Technology estimate
[4] Statistics Poland final reading
[5] Preliminary estimate

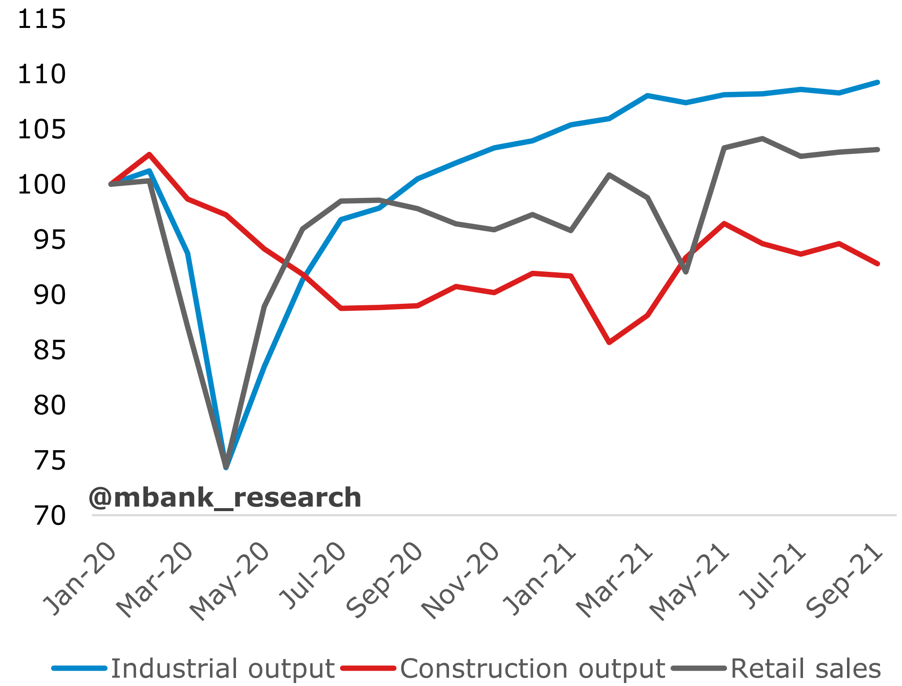
Poland: Fast catching up behind us

GDP (index 2015 = 100, seasonally adjusted)



Source: mBank, Statistics Poland

Seasonally adjusted, index 2015 = 100

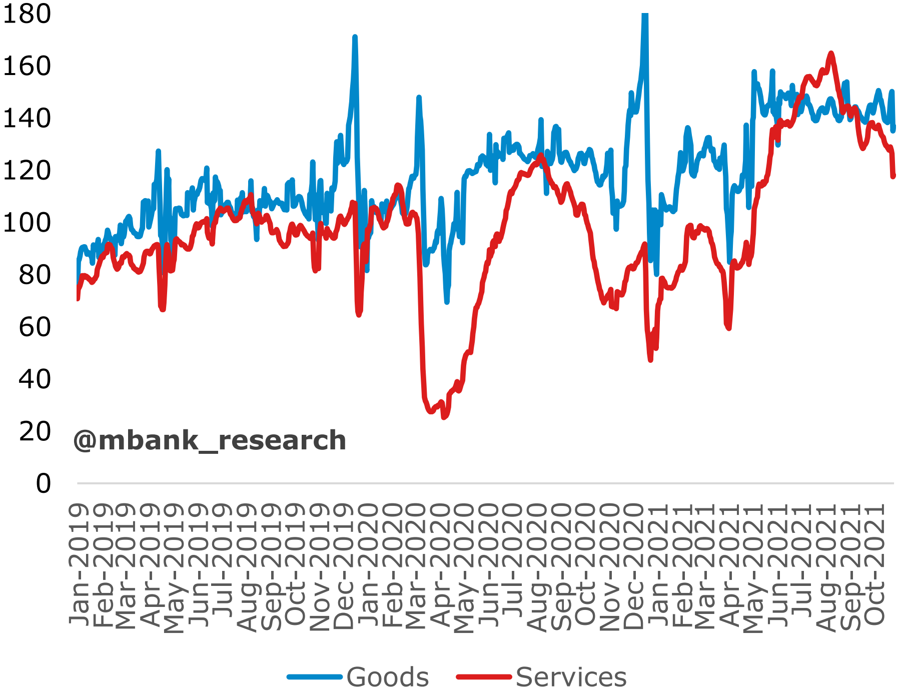


Source: mBank, Statistics Poland

- Momentum slows and we think there is more deceleration to come before economic activity re-accelerates again in 2022. There is sufficient momentum left to generate >5% GDP growth in 2021. The outlook for subsequent years darkens. Major risks near term consist of supply chain problems, high inflation, late start of EU-sponsored investment outlays. We are also running the risk of demand fatigue. It applies both to consumer demand for goods regardless of issues related to disposable income (preference shock?) and demand for running stock that may appear too high in the end.
- So far, there is no significant and drastic slowdown in industrial production, despite weak condition of automotive industry (here the effect of supply problems are the most significant). But in the next few months, signals from sentiments surveys (lack of materials, high prices, weakening demand) will translate into real data. Construction activity fails to accelerate reflecting possibly many factors but later start of EU-spending cycle should be regarded as baseline now.
- Retail sales is also relatively weak due to prices. Much of the consumer purchasing power disappeared because of inflation (nominal expenditures are above the pre-pandemic trend, but the real one is still far from it).

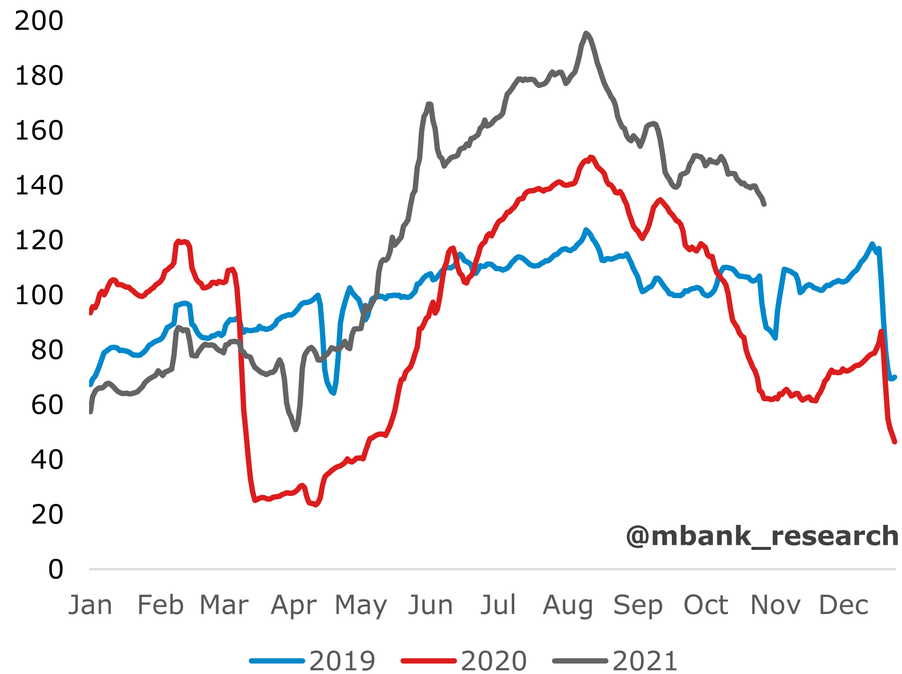
Poland: Card expenditures, #1

Card expenditures weekly, Jan20 = 100



Source: mBank transaction data. Own elaboration.

Restaurants, card expenditures weekly, Jan20 = 100

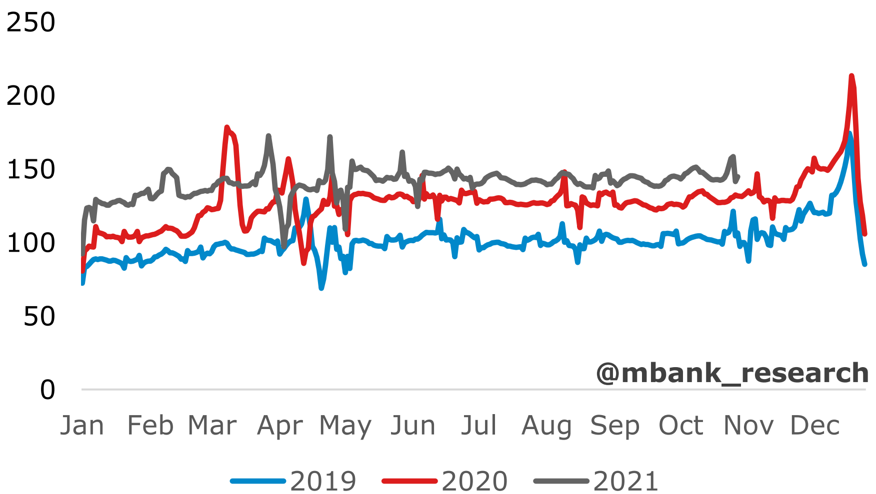


Source: mBank transaction data. Own elaboration.

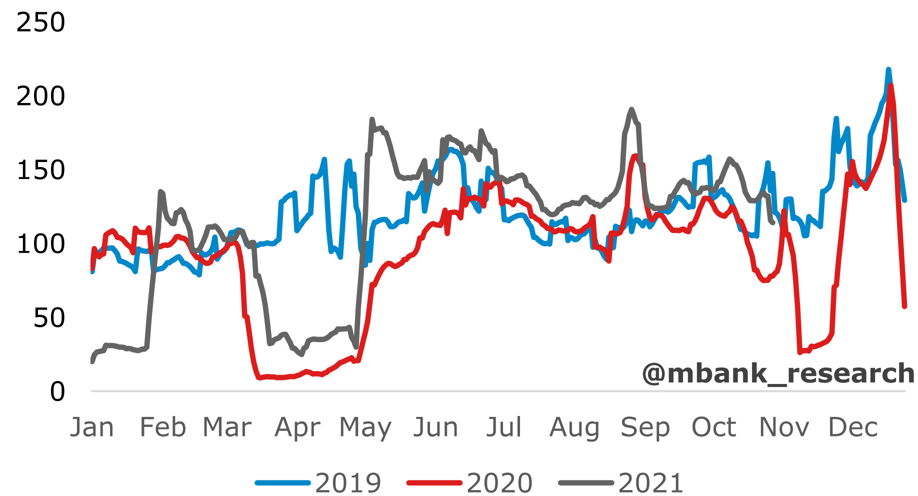
- After realizing the pent-up demand in previous months, card expenditures in services slowed down. But the scale of the slowdown is much smaller compared to previous year (and compared to other covid19 waves). Goods expenditures remain stable.
- The overall view on consumption (through the lens of card expenditures) remains positive. Levels of expenditures are either above (gastronomy) or close (tourism) to the ones observed before the pandemic. Expenditures in transport returned to old patterns (which can indicate the return of previous consumers behavior).
- But card expenditures data are nominal, so they can exaggerate the condition of the consumption. We know from the retail sales data that differences between nominal and real values now are much more significant and affect consumers choices (see previous slide).

Poland: Card expenditures #2, 7-day average

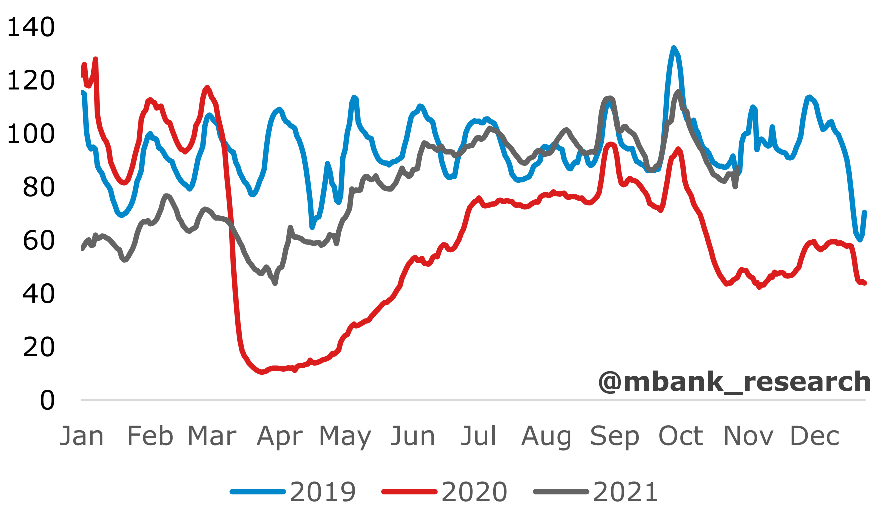
Food, beverages and non-specialized stores, Jan20 = 100



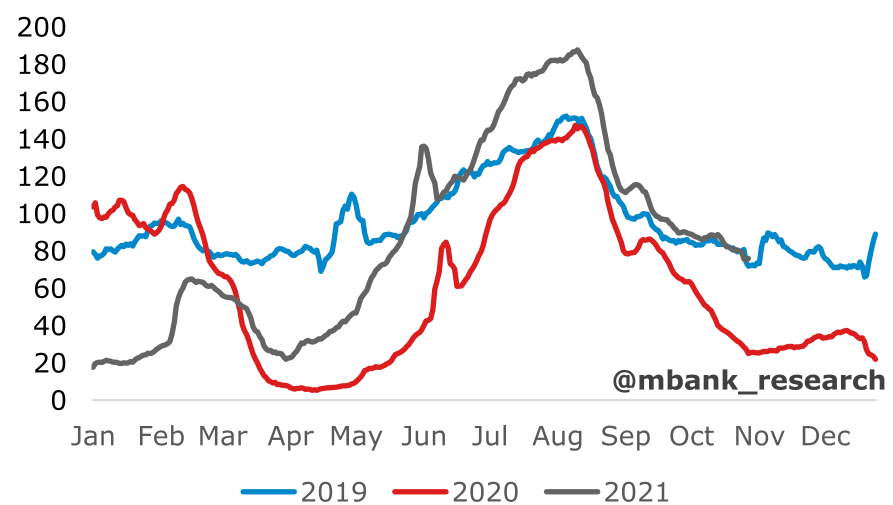
Clothing, footwear, Jan20 = 100



Transport, Jan20 = 100



Tourism, Jan20 = 100



Source: mBank transaction data. Own elaboration.

Poland: Google mobility, 7-day average

Retail & recreation (% change from Jan20)

Residentials (% change from Jan20)

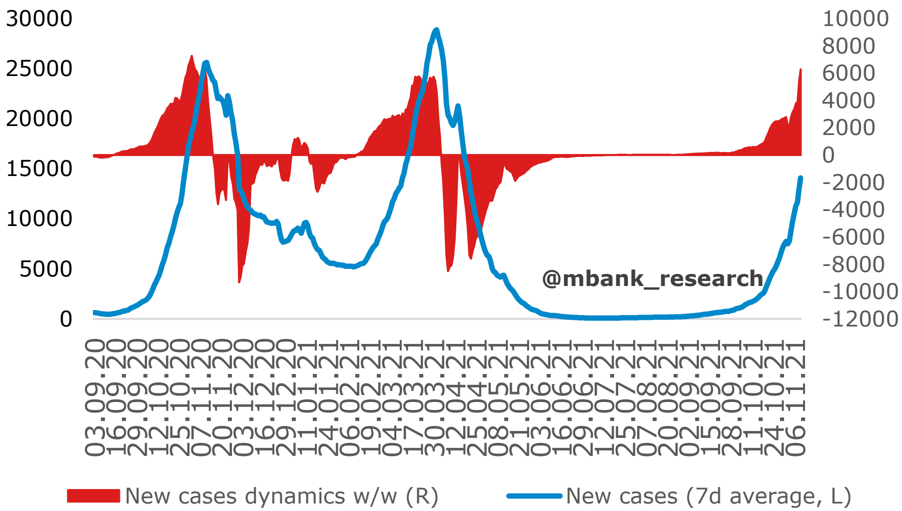
Workplaces (% change from Jan20)

Transit stations (% change from Jan20)

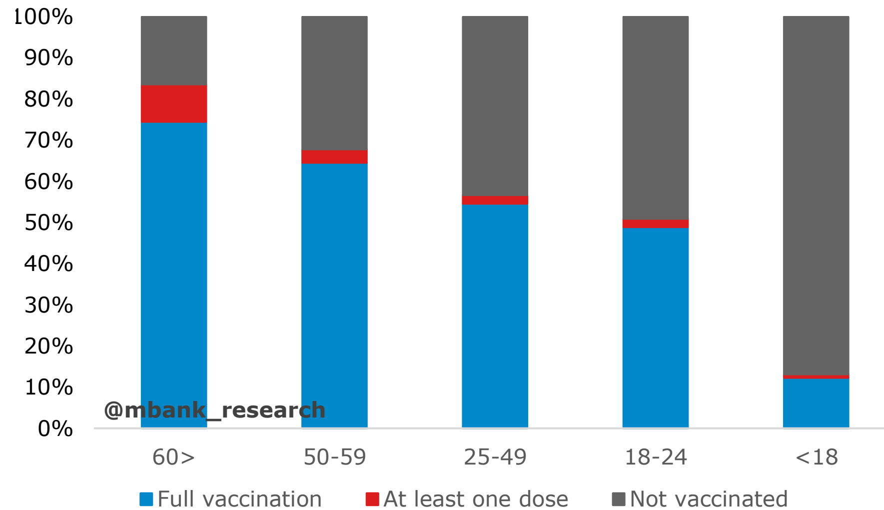
Source: Google mobility data. Insights in these reports are created with aggregated, anonymized sets of data from users who have turned on the Location History The baseline is the median value, for the corresponding day of the week, during the 5-week period Jan 3–Feb 6, 2020

Poland: COVID-19 situation

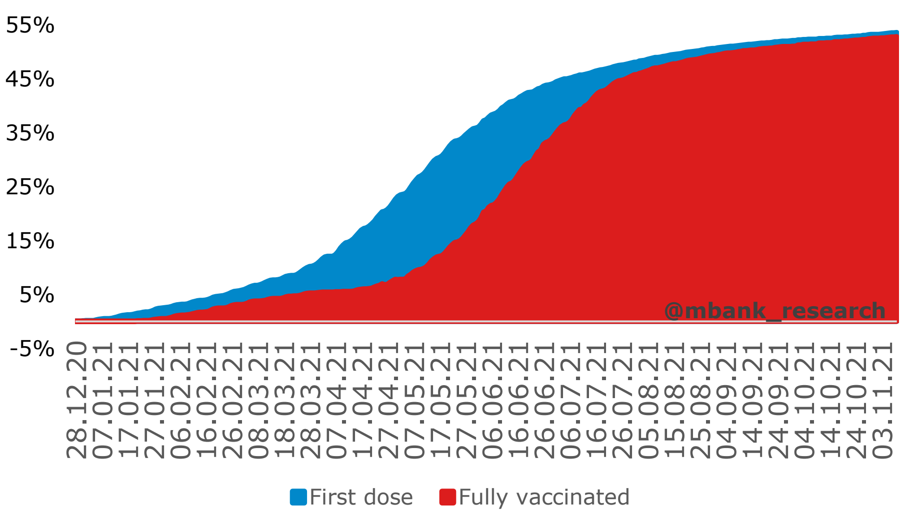
Daily new cases (7day average)



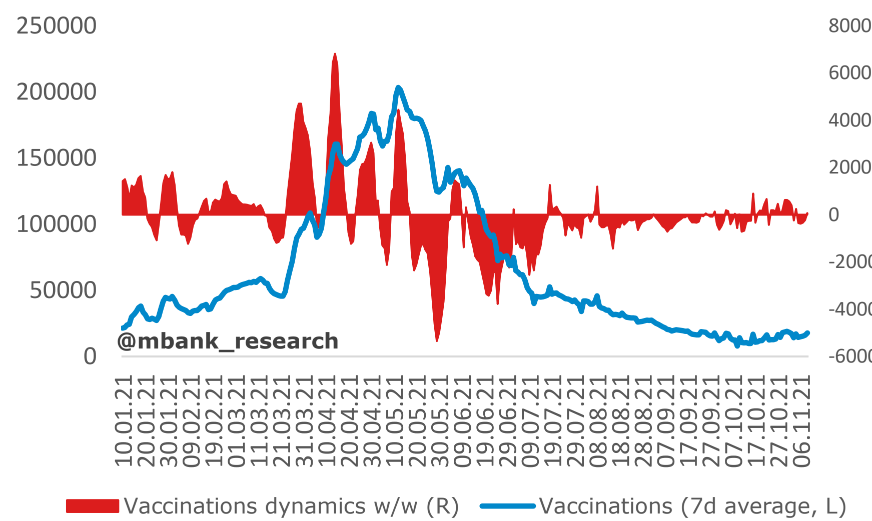
Cumulative uptake (%) of vaccinations by age



Cumulative uptake (%) of vaccinations



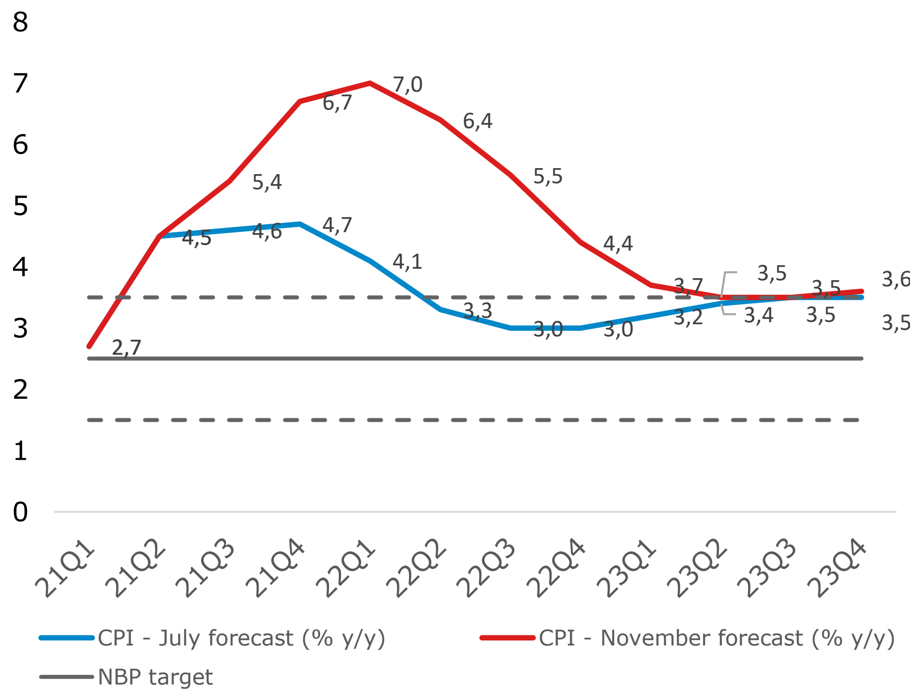
Vaccinations (first doses)



Source: Our World In Data, Covid-19 excel sheet by Michal Rogalski, gov.pl

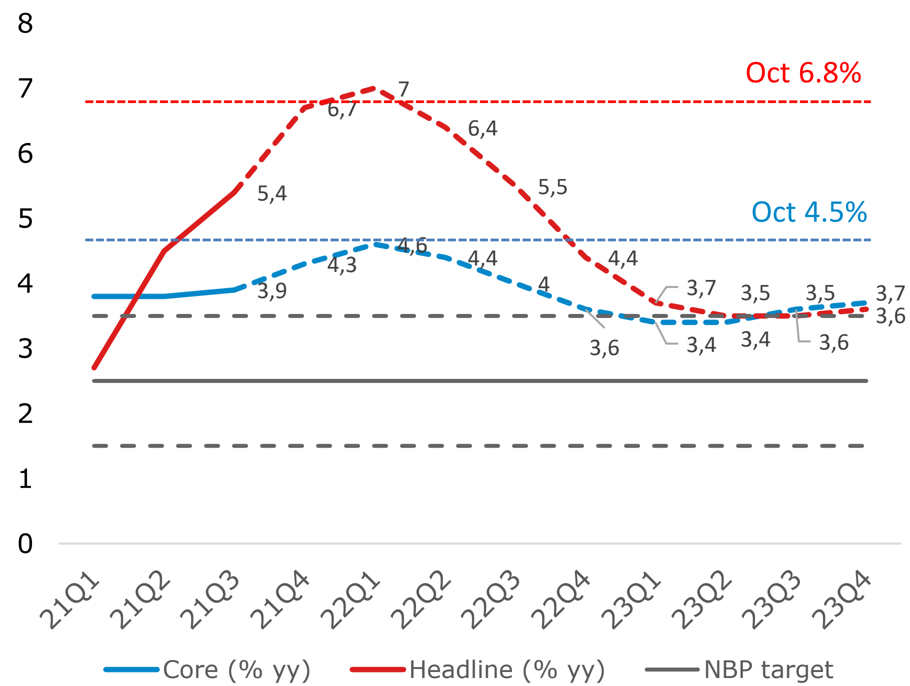
Poland: NBP new forecasts #1

CPI forecast (% y/y)



Source: NBP, own elaboration

Core and headline NBP forecasts (% y/y)

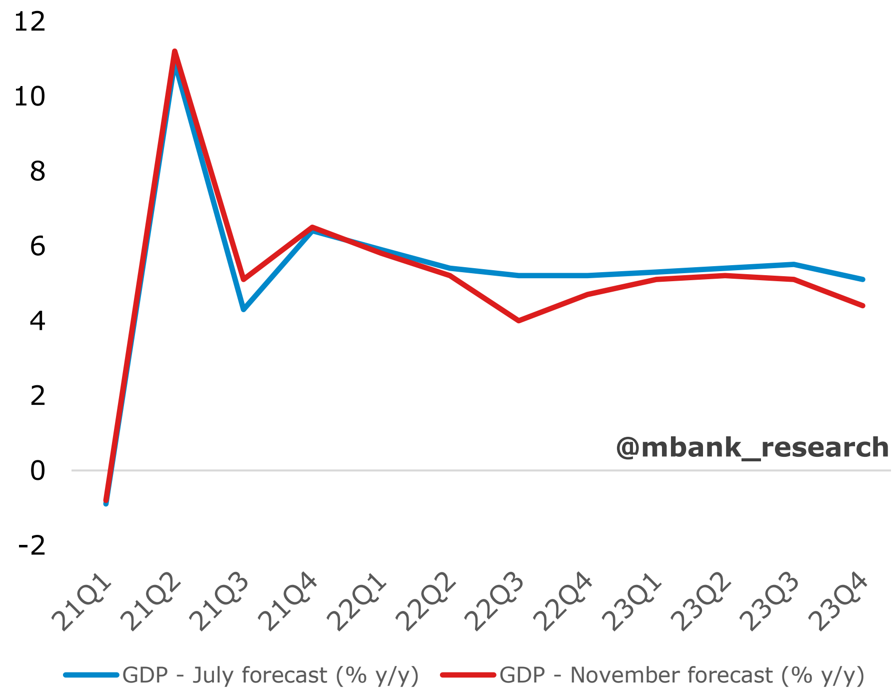


Source: NBP, own elaboration

- At the moment of publication, new NBP projection was already out of date. It was based on interest rates at the level of 0.5%. Thus, the effects of the recent rate hike are not included (contrary to projections in Czechia and Hungary, there is one simple, model rule regarding interest rate: constant rate determined at cut-off date).
- NBP revised upwards its inflation forecast for this and the coming years, mostly due to energy prices (they will add 1.5pp to CPI next year). NBP estimates that inflation will be at 6.7% y/y in 4Q2021, reach the peak in 1Q2022 (quarterly at 7% y/y) and gradually decline to 3.6% y/y in the end of forecast horizon (4Q2023). But if last interest rate hikes were included (+75bp) it would bring inflation below 3.5% in 4Q2023 (judging from public IRF graphs).
- However, in our opinion CPI will be running faster than projected in the near term. Consequently, the peak will be higher. We think that NBP underestimates the longevity and magnitude of food-price shock and adjustment of relative prices at the start of the year. These surprises will mostly determine the peak in interest rates (2.5%). We think there is only low probability of continuation of monetary policy tightening during the period of falling inflation.

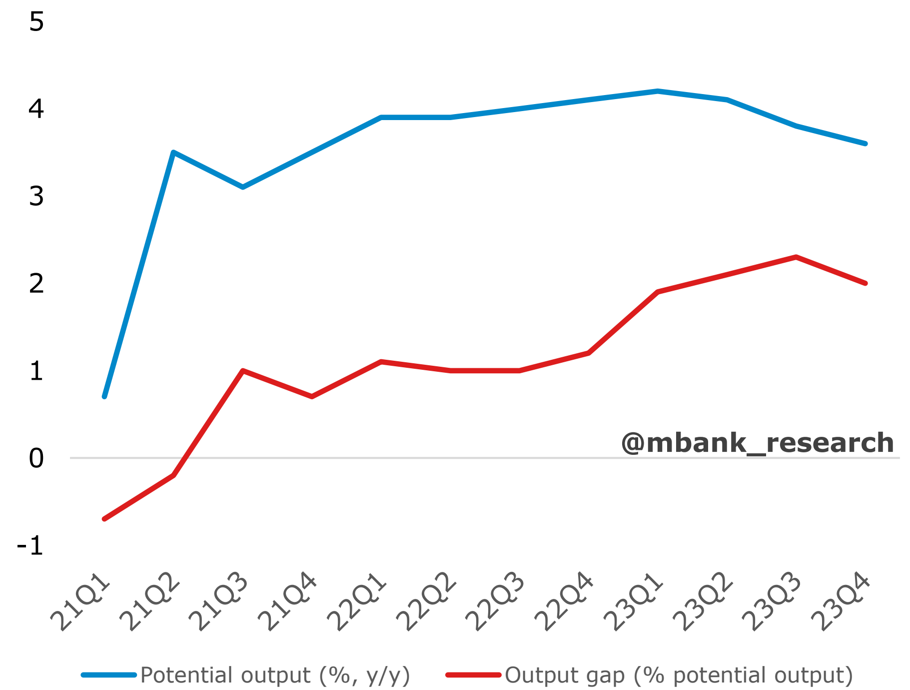
Poland: NBP new forecasts #2

GDP forecast (% y/y)



Source: NBP, own elaboration

Output gap forecast (% y/y)

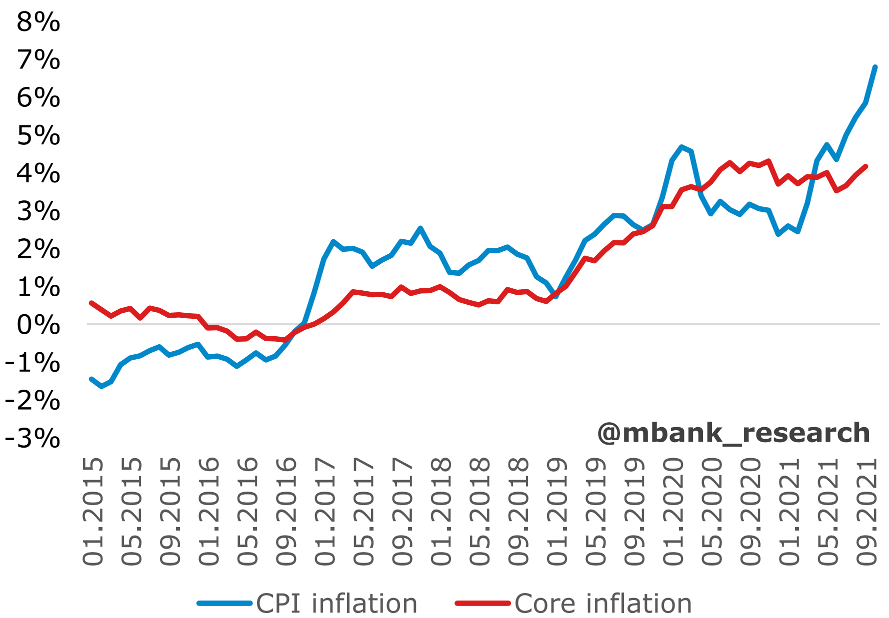


Source: NBP, own elaboration

- GDP growth is expected to stay strong and close to 5% bar in the coming years. As it was specified previously, the projection does not include recent rate hike. Since it is quite possible that we will see further rates hikes till next projection (March) it is also highly unlikely that growth rate will stay such high (it is not about level, it is about the pace). The same applies to inflation in 2023. It is highly likely that with rate hikes towards 2.5% in the next few months, CPI inflation will be 2.5-3.0% in 2023.
- It is worth to note that NBP projection exactly matches GDP figures for Q3 (5.1% y/y). It will not be a source of surprise for MPC members. It is then hard to argue that projection is too low with regard to inflation (actually, given expected and recent adjustment of rates it seems well ahead i. e. the demand-driven inflation may be portrayed on a high side).
- Thus, we think that December MPC meeting will bring a more moderate hike (25-50pb). The lower the pace of hikes, the higher the likelihood that the terminal rate in this cycle will be lower than market already expects (>3%) and below we are currently expecting (2.5%).

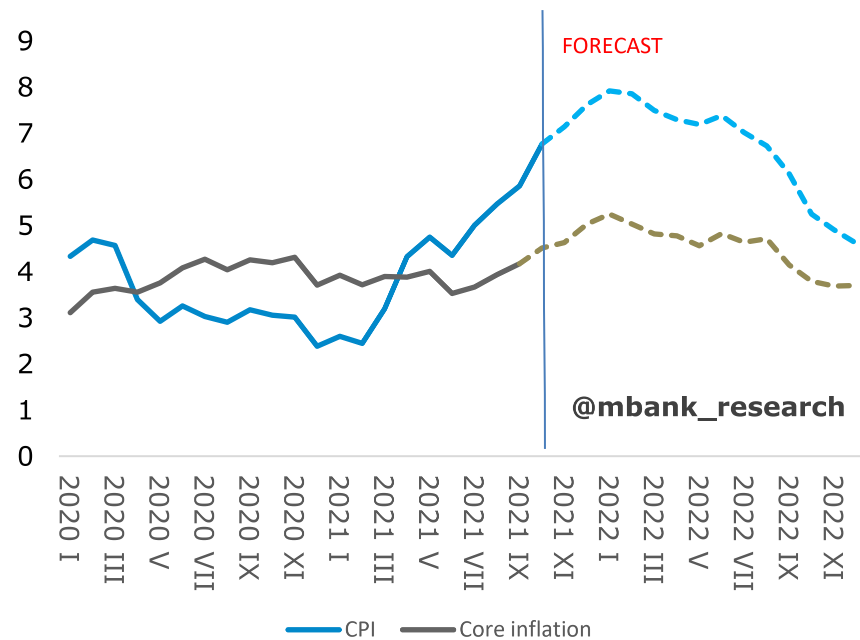
Poland: Inflation tracker #1

CPI and core inflation (% y/y)



Source: Statistics Poland, NBP, own elaboration

Core and headline inflation forecast

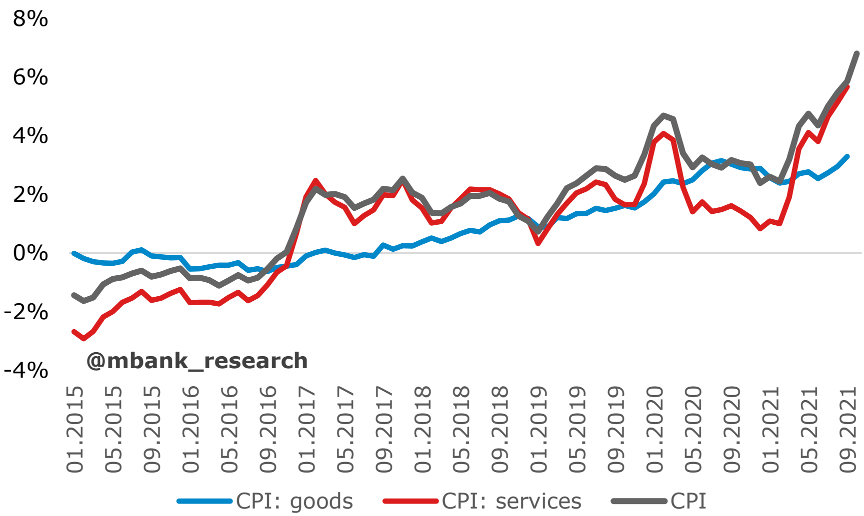


Source: Statistics Poland. own elaboration

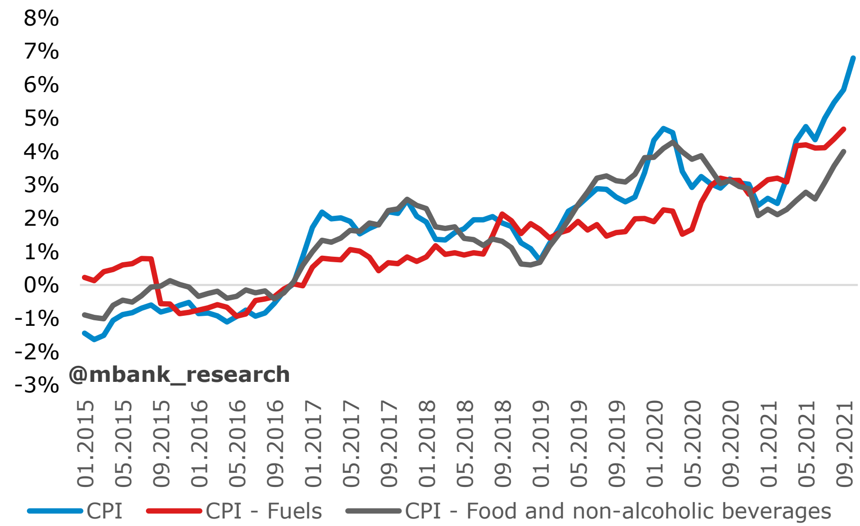
- October inflation surprised again (6.8% y/y, consensus: 6.5% y/y). The main reason for the last CPI increases was energy prices (+3% m/m, result not seen unless there were some regulatory changes). Food prices increased by +0.5% m/m, in line with last readings of faster price growth and we are still far from the end of this food prices series.
- Inflation should reach 7% next month. In the first quarter of 2022, we will test the range of 7-8%, but the risks are tilted to the upside, because of the unknown scale of secondary effects stemming from high inflation (with large increases in energy prices it can be significant). Inflation should stabilize in the 2Q2022 and slow down in the next ones. A scenario in which core inflation will significantly slow down in 2022 is unlikely. Rather, we will remain in the range of 4-5%.

Poland: Inflation tracker #2 (unorthodox, additional measures)

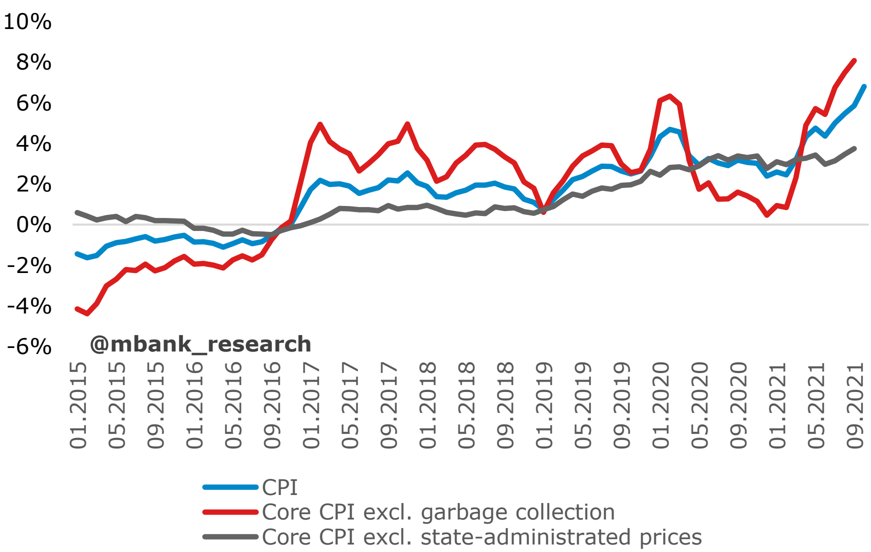
Goods and services prices (% y/y)



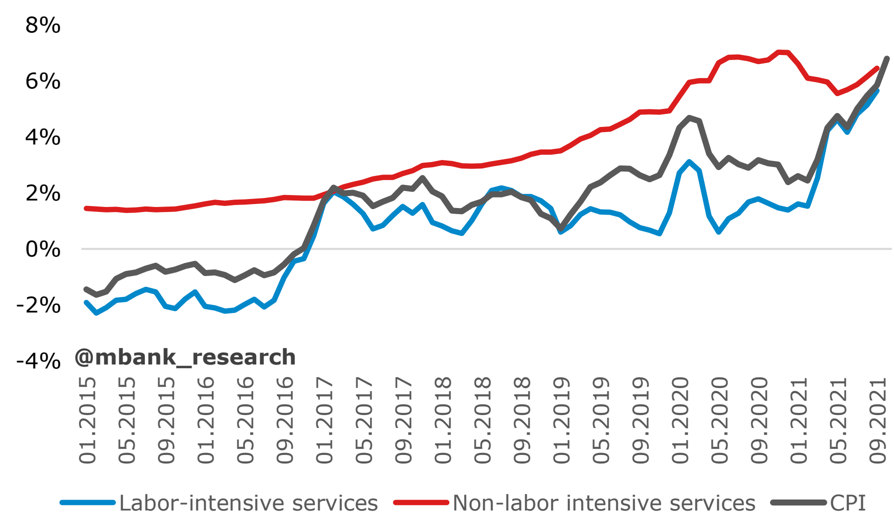
Food and fuel prices (% y/y)



Core inflation without garbage collection fees and without administrated prices (% y/y)



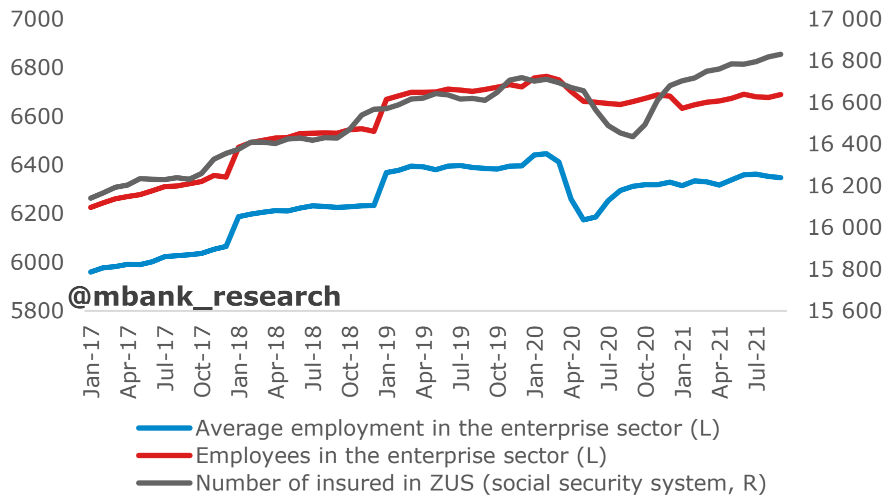
Services (% y/y)



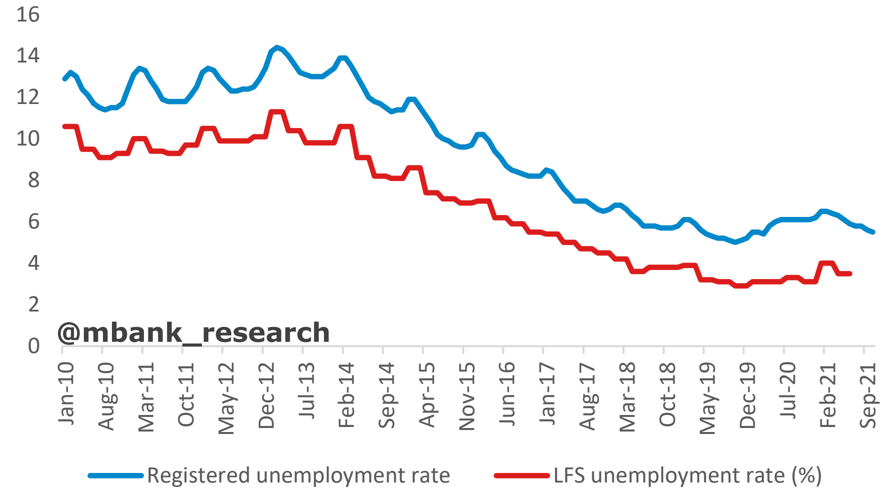
Source: Statistics Poland, own elaboration

Poland: Labor market tracker. Gradual improvement. Mind the low, starting level of unemployment rate.

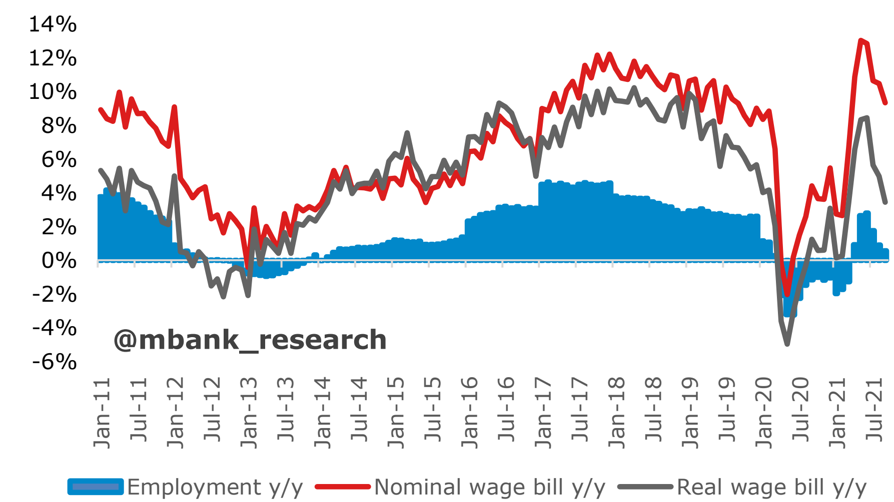
Employment



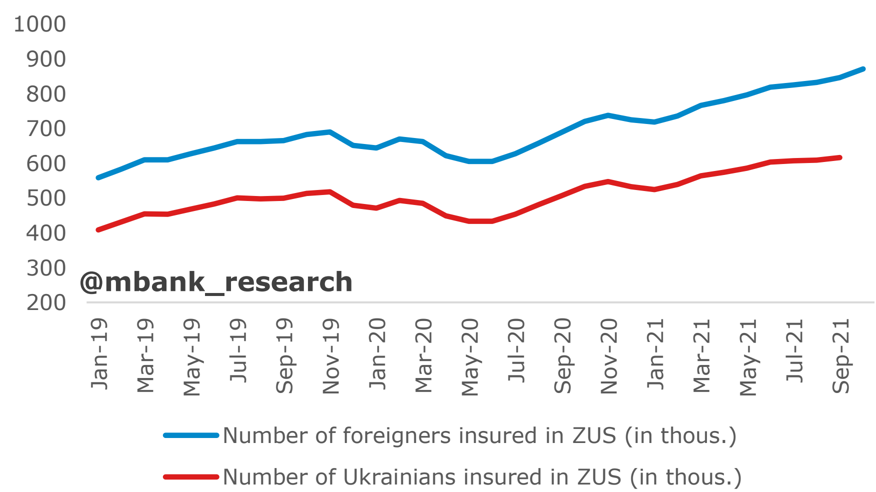
Unemployment rate



Wage bill



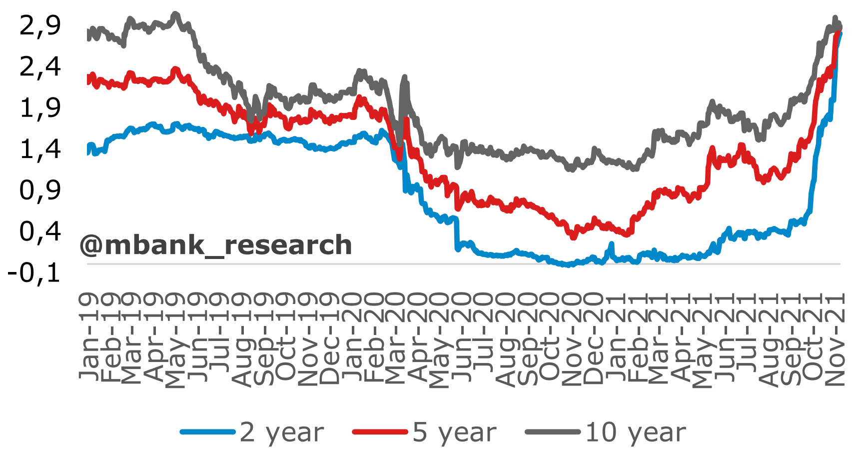
Immigration in the labor force



Source: Statistics Poland, ZUS Statistical Portal, own elaboration

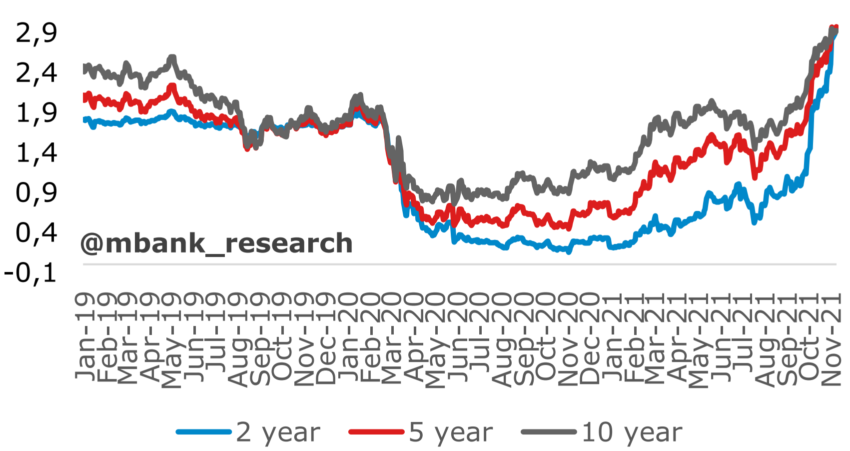
Polish rates, yields and spreads

POLGBs



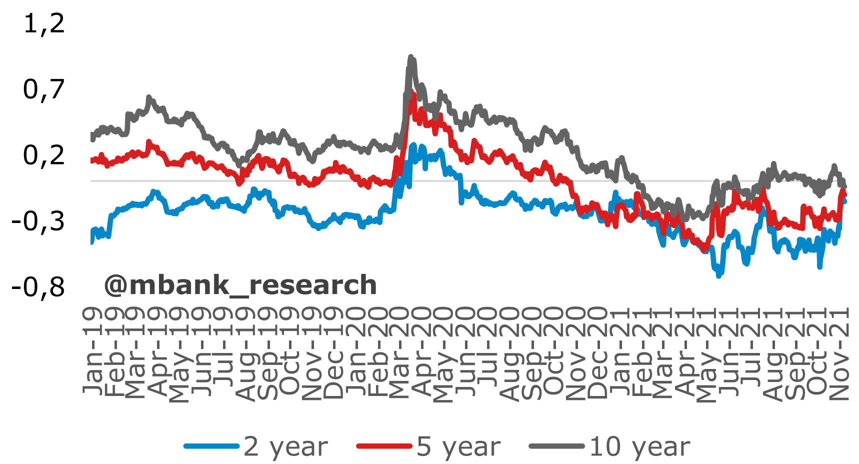
Source: Bloomberg

PL IRS



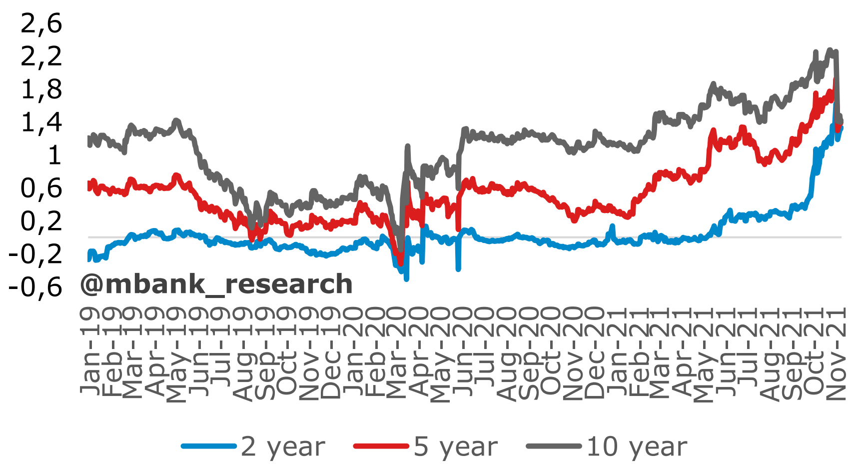
Source: Bloomberg

ASW spread



Source: Bloomberg

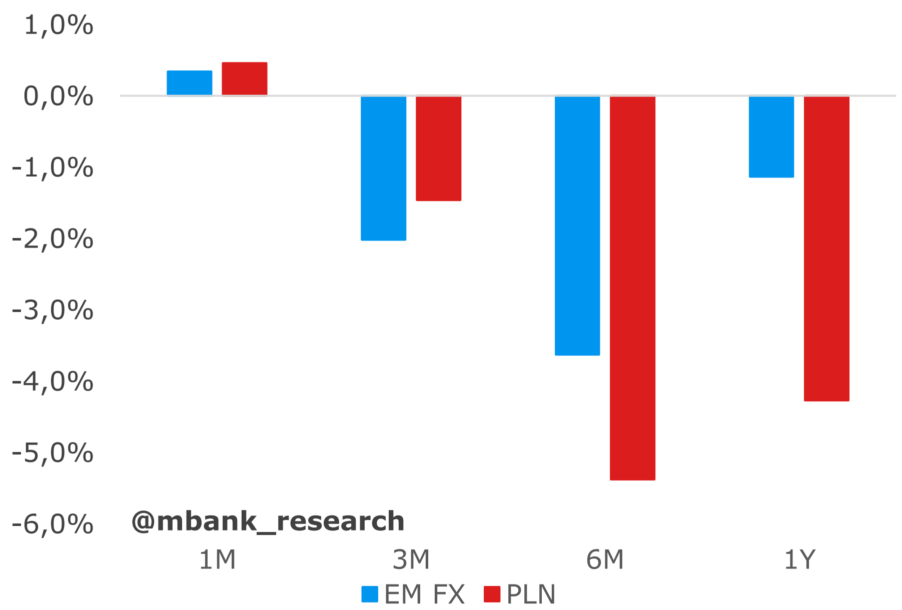
POLGB yield minus 3m WIBOR



Source: Bloomberg

EURPLN – waiting for appreciaton (not seen yet)

Still weak zloty



Note: Increase = appreciation to dolar. Decrease = depreciation to dolar

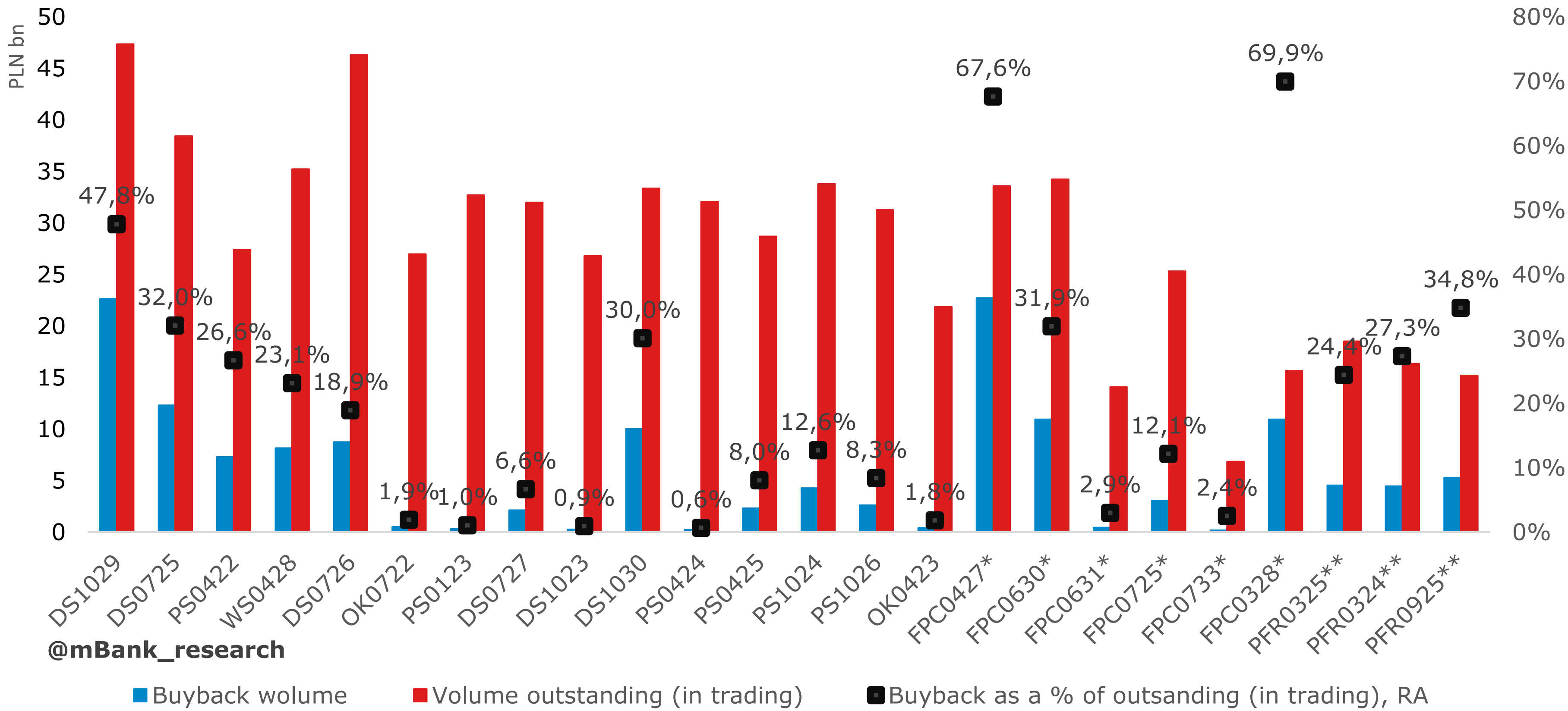
Source: Bloomberg

Real effective exchange rate

Source: BIS

- MPC moves did not affect much the EURPLN behavior. The main reason of relatively weak zloty is the general uncertainty about the coming quarters in the global economy - supply shocks and an attempt to guess their effects; slowly weakening faith of market participants in the continuation of a rapid recovery or growing certainty that the combination of supply shocks, high inflation and panic reaction of some central banks will sooner or later spoil the recovery. Conflict with EU regarding the rule of law is not resolved which can also affect EURPLN.
- There is also uncertainty about zloty’s behavior at the end of the year. It is not clear what exchange rate NBP will consider as optimal (investors still remember NBP actions at the end of 2020). If this risk passes, and the issues of relations with the EU and border problems go away, the zloty may start to strengthen since rate disparity is already higher than before pandemic.

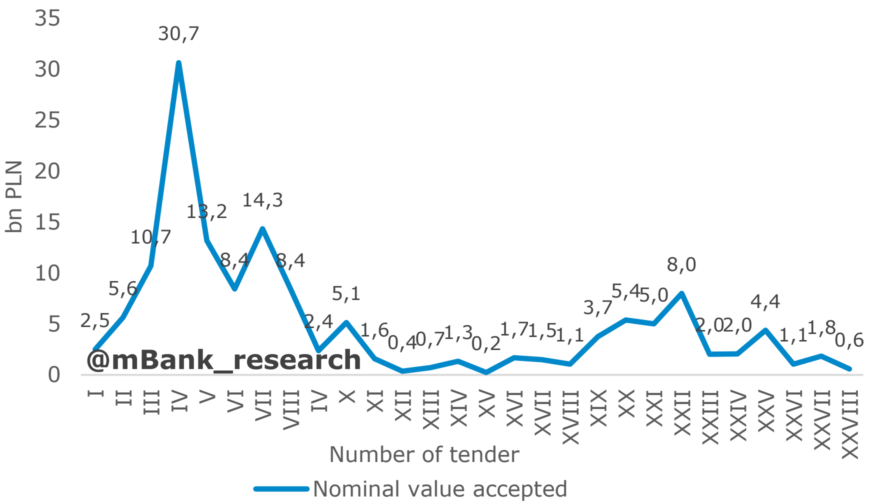
Appendix: NBP „structural" portfolio monitor

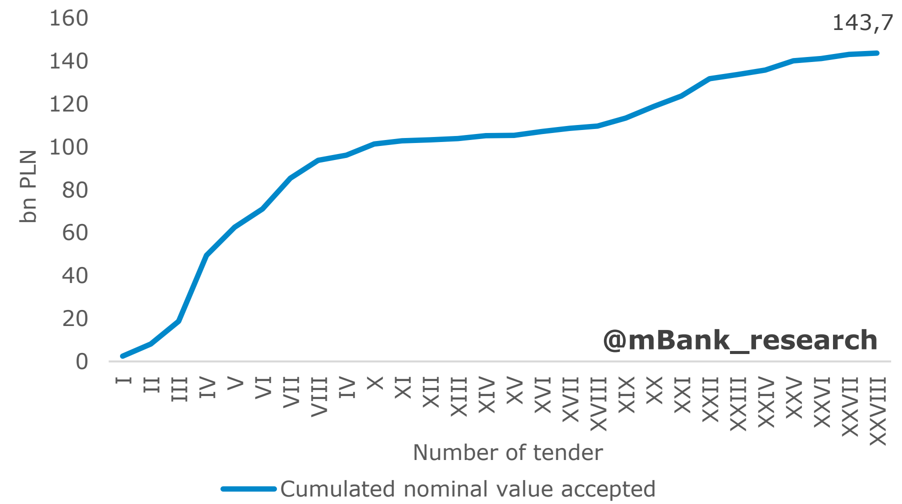


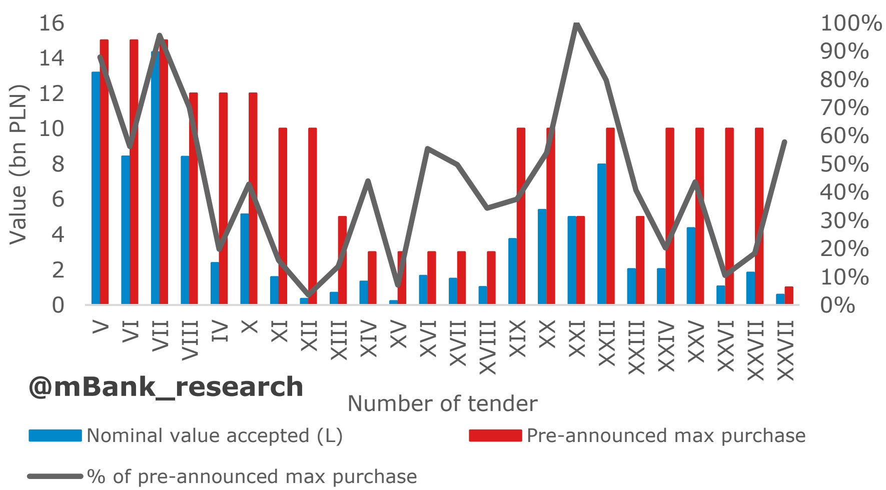
Source: Own elaboration on MF, NBP, NDS data.

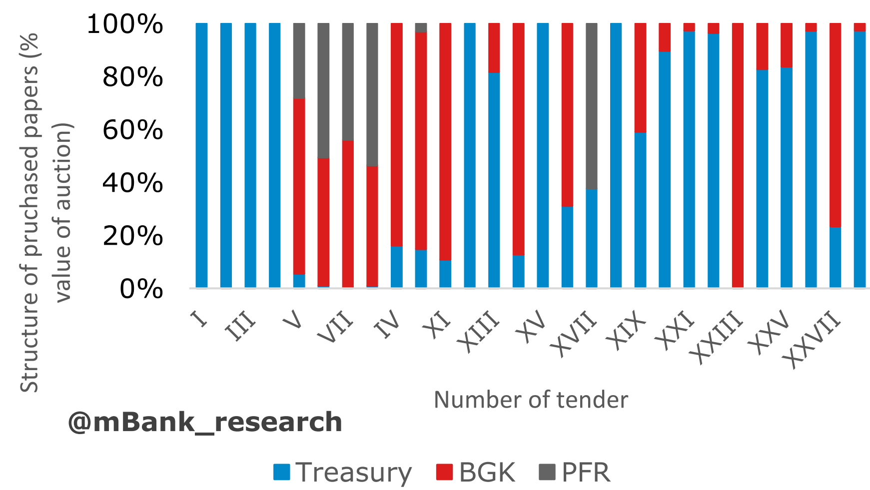
- The state for 15.11.2021. We present cumulative numbers.
- NBP launched structural open market operations in March 2020, and they constitute a purely new instrument introduced to fight the crisis.
- **Recent central bank's communication suggests that the regular program of purchases should be regarded as almost closed although NBP fails to admit that program actually ended.**

Appendix: NBP purchases, the timeline









❖ The state for 15.11.2021.

Source: Own elaboration on NBP data.

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