

## CEE: Central bank hesitations

Inflation continues to fall rapidly in the CEE region, while economic numbers are surprising on the negative side. At the same time, we see signs of a turnaround in the third quarter in some countries. Monetary policy is moving toward rate cuts, while fiscal policy tries in vain to tighten



Adam Glapiński,  
President of the  
National Bank of  
Poland

### Poland: The economy is bottoming

The third quarter of this year was likely a turning point for the Polish economy. The August set of monthly data presents a gradual improvement in construction and retail sales, while industrial activity remained subdued due to poor performance in manufacturing. We're revising up our third-quarter GDP estimate from -0.2 to 0% year-on-year and expect over 2% GDP growth in the third quarter of this year. Overall in 2023, economic growth is seen at a mere 0.4%. This should improve to 2.5% in 2024, thanks to a rebound in household consumption and a smaller drag from destocking.

CPI inflation for September decreased to 8.2% YoY from 10.1% YoY in August, below the latest projections from the National Bank of Poland (NBP) and the governor's expectations presented during the September press conference. Around half of the decline comes from one-offs i.e., sharply falling gasoline prices driving a drop in the market despite rising crude oil prices and PLN depreciation, the introduction of partially free medicine, cheaper tickets and the extension of

frozen electricity prices.

On top of that, food prices decreased for the fourth month in a row. Disinflation is expected to continue until mid-2024 but at a slower rate. After that point, we expect inflation to stabilise at around 5-6% YoY, with the NBP's target not yet sight over the medium term. Rising oil prices, monetary loosening, a weaker PLN and fiscal expansion will make it difficult to bring CPI to the central bank's target in 2024-25.

The NBP surprised markets with a bold 75bp rate cut in September, which triggered PLN weakening. In September, the bank switched to a 25bp cut. Both we and the market currently expect the easing cycle to be continued this year, albeit with smaller steps, to prevent further PLN weakening. We project another 25bp cut in November. In 2024, we see room for 75bp of policy easing, with rates reaching 4.75% by the end of the year.

We also see further PLN weakening by the end of the year, reaching around 4.72. The NBP's dovish bias remains in contrast to key central banks in the region and also encourages said weakening. Fundamentally, we expect Poland's current account improvement to slow, given soft economic prospects in the euro area. Moreover, opinion polls signal a rather uncertain political landscape following the general elections in October and a few scenarios which make access to RFF money uncertain. Long-end Polish government bonds remain at risk. The Ministry of Finance has already announced a relatively heavy issuance in the fourth quarter of this year (PLN9-20 billion). Bank Gospodarstwa Krajowego (BGK) will place bonds as well. Given the very limited interest of foreign investors in local debt, asset swap widening is very likely. Aggressive NBP policy easing and further fiscal pledges suggest that bringing CPI to the target is likely to take years. As such, local bond and swap curves are likely to steepen.

## Czech Republic: CNB ready to start cutting cycle

The Czech economy is still teetering on the edge of recession and even the third quarter figures do not show much sign of recovery. It seems that we will have to wait a little longer and the next steps will depend on the shape of neighbouring Germany, to which the economy is strongly linked. Inflation fell again to 8.5% YoY in August more or less as expected. More interestingly, core inflation is falling faster than expected, with the latest number at 6.0% YoY.

Looking ahead, we expect headline inflation to fall to 7.4% in September – although due to base effects caused by government measures from last year, it will once again jump into the 8-9% range in the fourth quarter. Still, for similar reasons and the re-pricing in energy, we expect January inflation to reach the 2-3% band, close to the central bank's target.

The government has approved a state budget for next year of CZK252bn, slightly more than initially expected but still within plans to consolidate public finances. The Chamber of Deputies is debating the consolidation package in its third reading and opposition blocking can be expected. However, we expect approval in the coming weeks. This year's state budget figures also show positive surprises. The public deficit should end at 3.2% this year and we expect 2.2% of GDP for next year.

The Czech National Bank confirmed in September its readiness to start discussing rate cuts and every other meeting is live. We expect the first rate cut in November with the central bank's new forecast. However, if inflation surprises to the upside or a weaker CZK in the interim, the cut may be delayed until the first quarter of next year.

## Hungary: Risks are accumulating

While high-frequency indicators show some improvement in Hungary's economic momentum, we can't say that the outlook is clearly brightening. The European Commission has asked nine questions to obtain more clarity on the implementation of judicial reforms. This stops the 90-day chess clock, which will start ticking again once Hungary answers, with only three weeks left. Now we see that the latest delay in the ongoing rule of law talks is only a minor one. We've already approached the issue from a technical perspective, but there is also an undeniable political side to it. As we see risks beginning to build around our base case, we have also put together a more pessimistic [alternative scenario](#) for 2024-25.

Returning to the short-term outlook, we see the technical recession ending in the third quarter of this year, but a full-year recession is likely to be unavoidable (-0.5% in 2023). Moreover, the outlook for next year is increasingly uncertain. Not only are internal (e.g., budgetary) risks mounting, but external ones too. The trade balance has improved markedly over the past six months, but the recent rally in energy prices could limit the upside. The labour market remains resilient, which bodes well for wage growth momentum. At the same time, this poses an upside risk to our 5.1% inflation outlook for 2024. Especially if the 10-15% raise in the minimum wage materialises next year.

This could throw a spanner in the works of the ongoing disinflation, which is mainly driven by large base effects for the rest of the year. Looking ahead to next year, we see several trigger points for reflation. That's why we see an extremely cautious and circumspect monetary policy going forward, aiming at a positive real interest rate environment (ex-post) as soon as possible. We maintain our view that the central bank will only cut policy rates by 25bp in October. While acknowledging the risks of a 50bp cut, we believe that the EUR/HUF level and volatility could lead the Monetary Council to opt for a less dovish easing, thus providing renewed support to the HUF.

## Romania: Fiscal adjustments set to reduce the deficit but weigh on the private sector

A second GDP reading confirmed the weaker-than-expected second quarter growth, which led to an average growth of 1.7% over the first half of 2023, down from 5.7% in the same period in 2022. Fixed investment stemming from EU-funded public infrastructure projects managed to keep the economy afloat, overtaking private consumption and accounting for the lion's share of growth contribution. Weaker public and private spending – as well as exports – took their toll on output. Our latest growth forecasts are 1.5% in 2023 and 2.8% in 2024.

From a monetary policy perspective, we think a first rate cut from the National Bank of Romania is now more likely to happen in the second quarter of 2024, rather than in the first quarter. This could likely happen due to a slight derailing of the disinflation path in August this year, significantly higher oil prices in the second half of 2023 and the likely upside pressures stemming from a higher fiscal burden in 2024. On one hand, higher wages and further EU-funded investment activity will support activity. On the other hand, a gloomy outlook for the German economy and our view that the eurozone will stagnate next year (and not accelerate slightly like the consensus believes) will weigh on Romania's external sector.

The government has recently assumed responsibility for the fiscal package, with the large bulk of the changes being enforced as of 1 January 2024. Meanwhile, the measures which should have

been enforced from 1 October 2023 – concerning the removal of fiscal facilities for the IT, construction and food industries – are currently postponed as two opposition parties challenged the package at the Constitutional Court. While it is uncertain how long this will extend the implementation of the package, anything between one and two weeks could be a starting point. Nevertheless, the fiscal burden on the private sector will increase and cost-push shocks are now a key upside risk to our 2024 inflation forecast. While the intra-year profile could edge slightly higher next year, we still hold on to our 4.0% inflation forecast for the end of 2024.

## Authors

### Rafal Benecki

Chief Economist, Poland

[rafal.benecki@ing.pl](mailto:rafal.benecki@ing.pl)

### Frantisek Taborsky

EMEA FX & FI Strategist

[frantisek.taborsky@ing.com](mailto:frantisek.taborsky@ing.com)

### Peter Virovacz

Senior Economist, Hungary

[peter.virovacz@ing.com](mailto:peter.virovacz@ing.com)

### Valentin Tataru

Chief Economist, Romania

[valentin.tataru@ing.com](mailto:valentin.tataru@ing.com)

### Stefan Posea

Economist, Romania

[tiberiu-stefan.posea@ing.com](mailto:tiberiu-stefan.posea@ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and

which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.