

Poland: central bank slows tightening cycle

Today's press conference should be dovish, but we don't expect the governor to definitively end the tightening cycle given the CPI peak ahead (at close to 20% in Feb-23 in our view) and continued upside risk for inflation



Poland's central bank

The MPC raised interest rates by 25bp (the reference rate to 6.75%), in line with our view and consensus expectations. The switch to smaller 25bp increments in the tightening cycle (the previous hike was 50bp in July), reflects policymakers' growing concern about economic growth prospects. At the same time, however, inflationary pressures persist. In August, inflation rose to the highest level in decades at 16.1% year-on-year. Moreover, the inflation outlook remains highly uncertain, as the economy has yet to fully absorb the new energy shock. This process has already started and is one of the reasons why core inflation resumed its strong sequential rise in August, to around 10% YoY. Companies continue to pass on rising costs to the prices of their goods and services. In our view, the inflation peak is still ahead and we see CPI at about 20% YoY in February 2023.

The key changes in the communiqué suggest that the Council is strongly counting on the economic slowdown to reduce inflation. However, we are concerned that the GDP slowdown alone

will not materially accomplish this goal. The latest energy shock is so powerful that companies will continue to pass on costs to product prices, even in a weaker economy. We also expect a large fiscal expansion in 2023. European governments want to show that the gas war will not derail their economies. This is a reasonable approach but Poland already has a very expansionary policy mix. So the side effect of these energy programmes could be persistently high inflation, and this risk is quite high in the Polish economy.

In this environment, the MPC is likely to avoid explicit declarations about the imminent end of the hike cycle, leaving themselves wiggle room for further monetary tightening. In our view, interest rates could ultimately rise to 7.5% in the current cycle, and there will be no room for monetary easing in 2023, especially if there is further fiscal expansion as households and sensitive industries are protected from the consequences of rising energy prices in the forthcoming election year.

Key to shaping market expectations for the monetary policy outlook will be the tone of today's press conference by NBP President Adam Glapinski. We are concerned that the president will again strike a dovish tone, although in light of the uncertainty about the further course of the inflation path, he is unlikely to explicitly declare his readiness to end the cycle of rate hikes. Also, he can again announce that conditions for interest rate cuts may emerge at the end of 2023. The prime minister spoke about the approaching end of interest rate hikes on Tuesday.

The main changes in MPC press statement

1. unchanged paragraphs talking about future rates
2. counting on the GDP slowdown to lower CPI
3. no longer listing demand pressures among risks to CPI
4. noting high core inflation
5. noting strong labour market and wages.

A dovish statement from President Glapinski today would make the zloty exposed to a falling EUR/USD. Also, the National Bank of Poland's approach compared to the region suggests that the PLN should remain weak. The National Bank of Hungary is raising rates and communicating that it will tighten further. The Czech National Bank has stopped raising rates but is intervening to defend the koruna. The NBP says it will soon end the cycle of increases and may even start to cut rates from next year. But it is not intervening. So it is difficult to be optimistic about the zloty exchange rate.

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