Widening divergence across the CEE region

Lately, we've seen divergence beginning to widen across Central and Eastern Europe. Poland remains the strongest economy, the Czech Republic has surprised to the upside, while Hungary and Romania are growing below expectations. We also see more divergence in the direction of inflation, as well as monetary and fiscal policy

Poland remains strong, the Czech Republic is surprising to the upside, and Hungary and Romania are growing below expectations

Poland: Policymakers ready to start monetary easing

Last month, we saw the hawkish bias from Poland's Monetary Policy Council (MPC) since December shift to a more dovish stance, as illustrated by the National Bank of Poland Governor Adam Glapiński. Lower-than-expected CPI inflation in the first quarter of the year, slowing core inflation, easing wage pressure and probably softer annual GDP growth than in last year's final quarter all bolster the argument for the adjustment. According to the flash estimate in April, CPI fell to 4.2% year-on-year and is broadly expected to be around 3% YoY in July amid a high reference base from July 2024, when energy prices were partially deregulated.

In such an environment, there's no need to maintain a restrictive monetary policy stance and a high real rate. What's more is that authorities decided to postpone the approval of new energy tariffs for households from mid-2025 into the year's fourth quarter. The hope is that this will allow for lower levels amid favourable developments of wholesale electricity prices on the energy stock exchange.

We expect policymakers to cut NBP rates by 50bp in May. Another important decision to be made is pinning down the policy easing strategy for the coming months. We think the Council could pause in June and resume rate cuts in July, after the next central bank staff projection.

We also see rate setters switching to a standard 25bp pace in response to upcoming data and high levels of uncertainty, including the impact of US tariffs on global price developments. We see room for 125bp of cuts in 2025 and an additional 75bp in 2026, bringing the main policy rate to 3.75% at the end of next year. Markets have priced aggressive and frontloaded cuts in – so a potential pause in June, alongside a less dovish tone than expected in May's post-meeting press release and conference, could trigger a rebound in PLN yields.

Czech Republic: Consumer rules, while industry is at a crossroads

The Czech economic rebound continues; consumers are still king, with their budgets benefiting from tamed inflation and nominal wage increases. There are even enough resources to propel the construction boom, with demand for residential properties outpacing supply and pushing up property prices. Private spending and reviving construction are also set to foster economic expansion throughout the coming quarters.

Meanwhile, industrial confidence tanked recently on the back of the trade war undermining the global growth outlook, with Germany – the dominant partner of Czech exporters – not being able to come up with a viable growth model and properly lift off. The price competition in manufacturing rules with an iron fist in conditions of a laggard demand, while declining prices pose a threat to profit margins. Czech fixed investment remains weak, which could weaken growth prospects in the not-so-distant future.

With inflation below target and low Brent crude prices putting a lid on future price increases, we believe that this is the right time to set monetary conditions in a way that Czech firms could not resist investing in. Under the current setup, we see the Czech National Bank's board reducing the policy rate to 3.25% by the summer to support the rebound of the Czech industrial base. Getting lower is likely not an option right now, as core inflation remains elevated and could gain traction as household budgets see some relief in the form of lower energy bills. The Czech economy is set to outperform the wider eurozone, which will contribute to a gradual appreciation of the koruna, along with the more potent rates differential vis-à-vis the European Central Bank.

Hungary: Another year when hopes for strong GDP growth are quickly dashed

This is the third consecutive year that we have had to adjust our economic outlook significantly to the downside due to negative surprises in economic activity. With a quarter-on-quarter drop in GDP in the first quarter, we are facing the prospect of yet another technical recession in Hungary. One might be a coincidence, two might be bad luck, but three in three years? This suggests structural problems in the economy. Investment activity remains in freefall due to shaky business confidence and a lack of budgetary firepower.

While consumption remains a silver lining, this comes with an increased need for imports, especially given the trade war, which has probably resulted in front-loaded import activity. Conversely, external demand remains depleted, keeping industry and industrial exports on a downward trend. In this context, we are revising our 2025 GDP forecast from 1.9% to 1.2%, with a further downward revision possible.

The inflation outlook is improving in the short term, which is a blessing in disguise. This is partly due to weaker economic activity, which keeps demand-driven inflation in check. On the other hand, the government's price control measures are lowering food inflation, while falling oil prices are helping with fuel costs.

In summary, we have lowered our 2025 inflation outlook from 4.6% to 4.4% on average. Despite the dovish economic backdrop, as a baseline, we expect the central bank to keep interest rates unchanged throughout this year and anticipate the first rate cut at the start of next year. However, there are currently risks of further downside surprises in inflation due to hard-to-quantify government measures, as well as risks of downside surprises in economic growth driven by global developments. This would increase the chances of a rate cut at the end of this year.

Bearing this in mind, we maintain our bearish forecast for the Hungarian forint and expect EUR/HUF to move back into the 410–420 range in the second half of this year. This is not only due to rising expectations of monetary easing, but also to rising fiscal concerns and the elevated risk of negative credit rating actions.

Romania: Last minute fiscal improvements need to get around political uncertainties

After last weekend’s first round of Romania's presidential elections, all eyes are now on the near-term outcomes stemming from the complicated political situation. Our GDP growth base case remains that, while the Romanian economy is set for another challenging year, output could nevertheless see a slight pick up to 1.2% (2024: 0.8%) on the back of investments and a still-healthy private consumption outturn. Productivity improvements amid infrastructure upgrades and the Schengen ascension should also contribute positively. That said, the post-election environment brings heightened downside risks.

On the monetary policy front, the National Bank of Romania left rates on hold at its April meeting. Policymakers will likely continue with a cautious approach until they have a clearer view of the internal demand pressures and their impact on inflation, especially those stemming from the fiscal front. Moreover, we think that external risks need to moderate, too, before the NBR proceeds with more rate cuts. For 2025, we foresee a total of 50bp of rate cuts left for the second half of this year, taking the key rate to 6.00%. Upside risks are at play.

On the fiscal front, we continue to pencil in a fiscal deficit of 7.0% in 2025, following 2024’s whopping 8.6%. A reportedly more positive result in the April balances could bring more equilibrium to the picture if confirmed in late May. Prospects of more visible revenue collection improvements in the second half of the year are also an important factor. Risks to the outlook stem from scenarios of weaker-than-expected consumption and potentially tougher financing conditions. Renewed political negotiations also bring new risks for correction delays.

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