National Bank of Poland press conference supports our non-consensus rates forecast

The Monetary Policy Council targets a lower CPI and stronger zloty, while concerns about GDP are less important now. We think strong fiscal expansion is another argument calling for further hikes. We see the terminal rate at 6.5% in 2022 with risks that 7.5% will be reached earlier than in 2023

The rationale behind the 100bp rate hike

The National Bank of Poland chair outlined the main reasons behind the 100 basis point rate hike in April:

- war in Ukraine and its impact on inflation,
- persistence of elevated inflation,
- fiscal expansion – the war requires new spending and it drives inflation higher, so the central bank should counteract it. Governor Glapiński did not mention that fiscal spending impacts growth and inflation immediately, while rate hikes with some delay.

- strong GDP – robust growth allows for substantial monetary policy tightening.

Inflation outlook

Adam Glapiński expects that inflation will continue to rise and may peak in June 2022 – in our opinion around 12% year-on-year. We stress that the price shock in 3 commodity markets (energy, metals, food), triggered by the war, have not yet fully fed into CPI.

The rising prices of fertilizers may lift food prices in the future. What is more, the war in Ukraine led to renewed intensifications of disruptions in global supply chains. Finally, fiscal spending is projected to increase on the back of rising costs due to the inflow of refuges and higher military expenditures.

What is worth pointing out is that the NBP chair admitted that 40-50% of current inflation is country specific and caused by internal factors. We have been flagging this for a long time as the consumption boom facilitates second-round effects, which is seen in core inflation.

The important long-term risk is that with this scale of inflation shock, the risk of deanchoring inflation expectations is growing rapidly. The governor's comments on that were vague, but the MPC statement already pointed out this risk.

Growth prospects

The NBP is very optimistic with respect to the GDP outlook. Policymakers point to the high starting point from 1Q22 and while seeing risks linked to the war, they also note positive factors (budget spending on refugees).

Chair Glapiński stressed strong fundamentals of the Polish economy and its resilience to external shocks (Lehman Brothers crisis, Covid-19 pandemic) and projects solid growth despite the uncertain impact of the conflict in Ukraine on businesses and households' behaviour.

MPC reaction function

We correctly recognized the shift in the MPC reaction function. Policymakers are currently focused on CPI and firming the zloty, with less importance attached to GDP prospects, even as compared with the previous policy setting.

MPC policy bias and further steps

MPC head Glapiński confirmed the very hawkish policy stance of the Council with many important statements. He noted that 4.5% is not a high interest rate and the April rate hike is not a pre-emptive move and does not rule out further adjustments. He noted CPI inflation is on an upward path and stressed that it cannot slide out of control. The 100bp rate hike is not a sign that the end of the tightening cycle is approaching. Inflation is still too high and the Council is determined to contain it.

In our view the Council will hike rates every month until CPI peaks. We see future moves at 75-100bps, with the latter more likely in the case of months with high surprises to the upside in CPI readings.

Quantitative tightening (QT), ie, balance sheet trimming

Despite the hawkish policy bias the NBP governor did not declare the start of actively trimming the central bank's balance sheet, but given the upcoming maturity of PLN7bn worth of bonds in the NBP assets, he did not rule out reinvestment.

Bottom line

Today's conference and comments from the NBP governor significantly support our forecast of target rates at 6.5% in 2022, with the risk that 7.5% may be reached earlier than in 2023.

Glapiński's press conference confirmed our assessment that a 100bp rate hike was mainly triggered by the high reading of March inflation and prospects of it increasing further on the back of upward pressure of commodity prices as well as fiscal expansion.

According to the NBP governor, rate cuts are possible at the end of 2023, and we assume that easing may rather start in 2024. At the beginning of 2023 – when the anti-inflation shields may be lifted, we see another CPI peak around 12%. In 2023 we still expect an expansionary fiscal policy from the national budget, maybe Recovery Plan. Also, 2023 is the last year of the old EU budget when spending usually mobilizes.

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