Poland leaves rates on hold

Poland's central bank left rates on hold but admits the odds of emergency monetary easing have grown

Poland's central bank left rates on hold, as expected.

We expect governor Adam Glapinski to reiterate that he was correct with his forward guidance in the recent months assuming flat rates until the end of the term. However, the next move is likely to be a cut, as, since the last meeting, the odds of emergency monetary easing have grown. As Covid-19 expands rapidly, emergency easing in the eurozone and CEE region will raise the odds of a National Bank of Poland rate cut too.

The central bank will present new projections this month, most likely showing substantially higher CPI and lower GDP paths. We expect the MPC to underline regulatory factors behind inflation overlooking demand-driven factors and the inflationary impact of the minimum wage hike which has disturbed the usual cyclical labour costs slowdown, supporting the neutral MPC stance.

We expect CPI estimates for 2020 to be revised upwards - from 2.8% to around 3.5% YoY. However, the projection will most likely point to inflation returning to the fluctuation band around the target this year. We forecast average CPI growth in 2020 will exceed 3.5%, and annual growth should touch 3.9% y / y.

At the same time, the Bank is likely to revise its GDP forecasts downwards emphasising that these forecasts are subject to high uncertainty due to the spread of the epidemic. We expect a decline in GDP from 3.6% to around 3% YoY in 2020.

Our last forecast of GDP growth in 2020 is 2.9% y / y, but if we see a materialisation of negative scenarios related to coronavirus, this may go down by 0.5-1 percentage points.

All internal demand proxies suggest 1Q20 GDP growth should be close to 4Q19 numbers. The stock building by households in the face of Covid-19 may cause some transitory consumption spike in 1Q20, but overall, we see GDP growth slowing to 2.9% YoY in 2020 due to weaker domestic demand.

Covid-19 is another downside risk. We estimate at least 0.5ppt (so far not included). Export-oriented industries were doing remarkably well, but we think Covid-19 is riskier than trade wars, given it may undermine eurozone and Polish domestic demand, both of which helped offset the impact of the German manufacturing recession.

The central bank may argue that the rate cut would be a blunt instrument to prevent the negative impact of Covid-19 on GDP. It is not only the cost of money but rather better access to liquidity which may be more effective in current circumstances. Deferred taxes or maybe a kind of non-standard measures (allowing banks to grant short term loans) should be a more effective instrument that would help companies to survive the Covid-19 outbreak and limit the negative impact of disruption in cash-flows on company liquidity and finally prevent defaults and second-round effects on the labour market.

Another argument against a rate cut (but less important now) is the elevated CPI, which should stay outside the range around the CPI target (2.5%+/-1%) for long.

> The coronavirus has caught markets off guard – widespread stop-losses pushed bonds yields downwards and swap rates to stretched levels, but three rate cuts priced within a year is a bit excessive in our opinion.
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> However, a substantial correction is unlikely as long as the coronavirus continues to spread.

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