Rates unchanged in Poland; balance of risks skewed to earlier cuts

As expected, the Monetary Policy Council left interest rates unchanged. The reference rate remains at 6.75%. Recent comments suggest a slightly softer stance by the Bank chairman at tomorrow's press conference. Nonetheless, we see no room for rate cuts this year given persistent core inflation, but the risk is skewed to earlier cuts than we assumed

The commentary following the May meeting hardly changed. It underlined the deterioration of the domestic economic situation, including declines in retail sales, industrial production and construction output on an annual basis in March. The main changes in the post-meeting statement concern the update with new data on the external and the Polish economy, while the summary with policy guidance remained unchanged.

Attention now shifts to tomorrow's speech by National Bank of Poland (NBP) President Adam Glapiński. In recent weeks, some of the Council, including its chairman, have again begun to suggest interest rate cuts before the end of 2023. This may be a harbinger of a slightly more dovish tone from Glapiński, although still with some caution.

We hold the view that there will be no conditions for interest rate cuts before the end of this year. Although the disinflation process has begun, we believe it will remain at uncomfortably high levels for an extended period. In particular, core inflation remains persistently high, and this is despite a two-quarter-long decline in consumption. The NBP's March projection indicates that even with no change in interest rates, CPI inflation will not return to the NBP's target (2.5%, +/- 1 percentage point) before the end of 2025 (the latest in the CEE region). The possible start of a cycle of rate cuts as early as this year could delay inflation reaching its target. An upside risk to the CPI path could be a further increase in fiscal expansion.

We note, however, that the balance of risks for the rates scenario shifts toward an earlier rate cut than our scenario, which assumes the start of the monetary easing cycle in the second half of 2024. The arguments for an earlier start of easing than we assume are the following: the strengthening of the Polish zloty, the growing risk of recession in the US, the weakening economy in the eurozone and downside risks to the GDP rebound in Poland. Also, external supply shocks are unwinding quickly.

The NBP can use the changing sentiment of central banks in the region to change its stance in the coming months. Inflation projections of central banks in the region show an earlier return to a range around the target than in Poland. So Hungary has effectively started an easing cycle, Romania is not sterilising excess liquidity so there is easing without a change in the reference rate and the Czech Republic, where core inflation is improving the most in the region, may change its stance in the second half of 2023.

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