Rates unchanged in Poland despite rising inflation

The Monetary Policy Council kept National Bank of Poland rates unchanged, surprising investors. The Council rather prefers a longer period of disinflation and soft landing than a prompt return of CPI to 2.5%. Given the fast hikes in developed markets and a tense geopolitical environment, the zloty is at a risk of further weakening

ING and the consensus expected a 25bp rise in the main policy rate, while markets priced in a 25-50bp hike. In previous weeks, some Council members had explicitly declared a significant probability of ending the hiking cycle. The further sharp rise in inflation in September (especially core) did not change that opinion. This is surprising, since September's CPI negated the scenario of inflation peaking in the summer and trending downwards in the following months. In addition, major central banks entered a period of strong interest rate hikes, and the PLN weakened again. The decision to leave interest rates unchanged raises the risk of PLN depreciation, which will make it even more difficult to contain already high inflation. In the first reaction after the decision was announced, the PLN lost some 4gr against the EUR.

In the post-meeting statement, the MPC assessed that past rate hikes and the expected economic downturn will contribute to weakening demand and lowering inflation "toward the inflation target". In particular, the document notes that the MPC writes about lowering inflation "towards the target", not "to the target". In addition, it was noted that the return to the NBP target will be gradual, suggesting that the MPC is not determined to bring inflation down to 2.5% year-on-year quickly, and accepts a longer period of elevated CPI levels.

Markets will now focus on tomorrow's speech by NBP President Adam Glapinski, which may shed more light on the outlook for interest rates in the coming months. In our view, September's inflation data clearly point to another wave of price increases in response to earlier increases in costs, especially wholesale energy prices. Given the lag mechanism, the pass-through of higher costs to final prices will continue in the months ahead, even as demand softens. Inflation risks remain high, and in our view the peak in inflation is still ahead. At this stage we think the guidance that the tightening cycle is completed and discussion on possible rate cuts in 2023 to be risky. We see increasing chances of PLN weakening. The NBP's goals at the moment are rather to reverse the inflation trend and ensure a soft landing for the economy, than to bring inflation down to the target (2.5% YoY) as quickly as possible. Such a strategy raises the risk of a sustaining high inflation expectations and a prolonged period of elevated inflation.

While we expect CPI in 2023 will fall from 20% to below 10% YoY, in 2024, when the fiscal measures (mainly cuts in indirect taxes) are reverted, inflation will rebound. Also, our models present a persistently high CPI in 2023-24 even with a GDP slowdown from 4.1% on average in 2022 to 1.5% ion average in 2023. Therefore, in our opinion, we are facing policy tightening again in 2024, either rate hikes or fiscal tightening. The ultimate cost of fighting long-term high inflation will be higher than if the policy mix tightens now.

Author

Adam Antoniak
Senior Economist, Poland
adam.antoniak@ing.pl

Rafal Benecki
Chief Economist, Poland
rafal.benecki@ing.pl