Polish MPC looks away from structural causes of CPI surge

The Monetary Policy Council maintains its narrative that the recent CPI spike is caused by external factors that are outside its influence. The National Bank of Poland governor reiterated that rates should remain unchanged for at least the next two years. Despite disagreement within the MPC, we believe that this scenario will hold

More than the usual grain of salt needed

In our opinion, the MPC statement and the conference call lacked a critical assessment of the causes of inflation and perspectives of economic activity in Poland. Current dynamics of prices was called moderate despite the fact that core inflation reached 3.1% year on year. This indicator already exceeds the center of the NBP inflation target and it will increase even further in the coming months in our opinion. Non-core inflation (food and energy) is on the rise as well, which should result in CPI exceeding 4.0% YoY for a few months - well above the upper bound of the NBP target (3.5%).

Most questions at the conference call concerned the sources of the inflation spike in December (to 3.4% YoY). Last month, Governor A.Glapiński attributed it to temporary factors (regulatory prices, eg, for waste collection) and disregarded structural causes, such as fiscal expansion and sharp rise of the minimum wage. However, the second reading two weeks ago showed that the CPI surge was demand-driven as core CPI accelerated to 3.1% YoY. Despite this fact the NBP governor did not change his position. He did not comment on the rise of core inflation, on labour costs and fiscal easing. Instead, he reiterated the opinion that the CPI rise was caused by external factors (not demand-related) outside of the influence of the NBP. These factors are:

- Drought and progression of swine fever causing food prices to surge.
- Rising prices of commodities (oil and gas) due to international conflicts.
- Rising electricity prices due to the climate policy of the European Union.

Without disregarding these factors, we think that the December CPI spike has structural causes that will last longer than the MPC expects. The record high increase in the minimum wage this year (by 15%) and introduction of occupational pension pillar are raising labour costs. It is hard to believe that these factors do not impact inflation. Hawkish members of the MPC, represented by K.Zubelewicz during the conference call, seem to agree with us, but they are outnumbered in the MPC.

Structural factors of the economic slowdown omitted

The economic slowdown in Poland is caused solely by external factors - according to the NBP governor. This opinion seems, however, inconsistent with his other comments at the same conference call in which he drew attention to stable exports of Polish enterprises.

In our view, the slowdown of the Polish economy is being caused by the inhibition of internal demand. The impact of social transfers is lower than expected by policymakers, because people have lowered their propensity to consume and save more. Simultaneusly, companies are reluctant to invest due to regulatory uncertainty and negative sentiment. The spike of investment in 4Q19 should be short-lived as it was to a large extent caused by a one-off factor - completion of power plant Jaworzno. Similarly, in 2020 public investments will fall, which is indicated by a strong slowdown in construction production or payments of EU funds (their pace has fallen from +67% to 0% YoY between 2018 and the second half 2019). Therefore, in our opinion, the GDP rate in 2020 will amount to 3.0% YoY, and thus will be lower than the NBP expected in the previous projection.

> The MPC's tolerant approach to further CPI growth or downplaying structural causes of inflation and economic slowdown reinforces our belief that rates will not change at least until the end of 2021.

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