Rate hikes by the National Bank of Poland are far from over

CPI is set to remain elevated even after commodity shocks fade. A consumption-based GDP structure will only be galvanised by fiscal policy and refugee inflows. We see the National Bank of Poland pushing the reference rate to 6.5% in 2022 and 7.5% in 2023

We are keeping our 2022 GDP forecast at 3.2%, but signal upside risks. Early 2022 data has been very strong (particularly industrial production), calling for first quarter GDP growth of 7-8% year-on-year. The war in Ukraine will significantly affect trade (with a 50%+ drop in exports to both Ukraine and Russia). However, fiscal measures (3% of GDP announced so far) and the hosting of refugees (about 0.7-1.4% of GDP) should boost consumption, despite high CPI and confidence shocks.

Strong consumption should facilitate second-round effects, ie companies can pass higher costs (commodities, wages etc) on to CPI. The process remains underway, as pointed out by business surveys such as the PMI. Fiscal policy will only worsen long-term inflation risks. Given that, we have revised up our CPI forecast for 2022 to 10.5% on average (with upside risks) and 8.4% year-on-year in 2023.

Recent comments from the monetary policy committee (MPC), including from National Bank of Poland (NBP) Governor Adam Glapiński, suggest a shift towards a hawkish bias, targeting lower CPI and a stronger zloty. Our analysis indicates that rates should reach around 7.5%, with our GDP and CPI forecasts for 2022-23 based on if the MPC bias is similar to the Council in 2010-16 (it was more hawkish than the MPC over 2016-22, but moderate in historical terms). Our central forecast for NBP rates in 2022 is 6.5% and 7.5% in 2023. We look for a 50bp hike this week (with upside risk) and still hawkish rhetoric – given the above CPI backdrop, NBP willingness to strengthen the zloty amid hawkish regional rhetoric, and a suboptimal policy mix (substantial fiscal easing) which raises the risk of persistent CPI.

FX and money markets: We see substantial scope for zloty recovery in 2022. €/PLN should near 4.50 by year-end, or sooner. This reflects a shift in NBP policy. The central bank should not only considerably hike interest rates (more than priced in currently), conversion of external funding will now commence via the market. This will become a key factor supporting the zloty when Poland converts EU money on the market and potentially, access to the Recovery Fund will be partially resolved in the second quarter of the year.

Domestic debt and rates: We see scope for a further rise in Polish government bond (POLGBs) yields, particularly on the short end. A fiscal boost in 2022 and 2023 suggests that monetary easing next year, still priced by the market, is unlikely. Moreover, fiscal pledges from the government suggest elevated borrowing needs in the coming months. However, it is yet unclear how much of those will be financed via agency debt (PFR, or BGK) and how significant potential NBP bond purchases will be.

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