Bank Zachodni WBK
Grupa Santander

POST-MPC COMMENT

15 April 2015

No (even a verbal) action from the MPC

After March's MPC meeting, which concluded the easing cycle with a 50 bp rate cut, we wrote about the MPC as the last action heroes. It looks like nothing has changed. The MPC reiterated that chance for continuation or re-opening of the cycle are minimal, saying at the same time that any tightening is very distant at the moment. The official statement and the press conference did not bring any revelations. While journalists tried, similarly as market participants in recent weeks, tried to focus on zloty appreciation and its possible effects on monetary policy, the NBP Governor tried to play this down and to avoid any unambiguous comments. The only question is if the zloty shows further appreciation, which (in a deflationary environment) could be problematic from the MPC (even if they do not confirm that). Suggestions of no actions (interventions, if needed) aiming at limiting excessive zloty appreciation in the world of the so-called "currency war" might simply invite capital flows.

As expected, Poland's Monetary Policy Council left NBP's rates unchanged at its April's meeting. The reference rate is still at 1.50%.

The official communiqué noticed a slight acceleration of global economic growth, in particular rebound in the business cycle in the euro zone. The MPC highlighted a solid growth in Poland's economic activity and estimated that GDP growth in 1Q 2015 was slightly higher than in 4Q 2014 (our forecast assumes stabilisation of growth in 1Q15). The Council also noted that the main driver of Poland's GDP growth was domestic demand, while external demand, even though accelerating, remains low and limits economic activity. In the MPC's opinion there is no demand pressure in Poland's economy – low increase in wages, commodity prices, inflation expectations.

In the last, most important, paragraph of the statement the MPC said that "in the coming quarters price growth will remain negative, mainly due to the previously observed sharp fall in commodity prices". So, the Council paid attention mostly to falling prices of commodities, disregarding the fact that core inflation is also very low, and at the same time we are facing the strengthening of the zloty that may lengthen the deflation period. The Council referred to zloty appreciation only by saying that the fact that major central banks are keeping interest rates close to zero and the ECB has launched government bond purchases contributed to "some strengthening of the zloty".

During the press conference journalists' questions focused on the situation in the FX market and the likely impact of the zloty's appreciation on the monetary policy. This should not surprise, given the fact that the market has started to price in odds for more easing due to the deflationary effect of the Polish currency strengthening. NBP governor Marek Belka tried to play this down and to avoid any unambiguous comments. The only question is if the zloty shows further appreciation, which (in a deflationary environment) could be problematic from the MPC (even if they do not confirm that). Suggestions of no actions aiming at limiting excessive zloty appreciation in the world of the so-called "currency war" might simply invite capital flows. Let's hope this will not happen and there will be no excessive zloty's appreciation that could make the life more difficult to the central bankers but also weigh on the economy.

The concluding paragraph of the MPC statement says "that the adjustment of monetary policy in March – with continuing stable economic growth, an expected recovery in the euro area and good situation in the domestic labour market – reduce the risk of inflation remaining below the target in the medium term. Therefore, the Council decided to keep NBP interest rates unchanged". Governor Belka stressed very clearly that the MPC sustains the statement from the past month saying that the easing cycle has been concluded. He added also that the economic situation has not changed to the extent to meet the condition for more policy adjustment outlined in the minutes. Recall, that according to the minutes from the March meeting, the adjustment in the monetary policy would be possible in the case of the unexpected shocks in Poland or its surroundings. Today Belka specified that only sharp deceleration of the economic growth in Poland could be such a trigger. In our view, such situation should not take place in the coming months or even quarters so the NBP rates are likely to remain unchanged.

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Fragments of the MPC statement (indication of changes as compared to March statement)

Growth of global economic activity remains moderate, ~~although the situation varies across countries~~ **with a slight acceleration expected in 2015**. In the euro area economic growth remains slow ~~despite a slight acceleration in 2014 Q4~~ **compared to other developed economies, although incoming information signals gradual improvement of economic conditions**. In the United States, ~~economic growth is significantly higher than in the euro area, though it slowed down somewhat in 2014 Q4~~ **despite the recent deterioration of some indicators, recovery is expected to continue**. ~~In the largest emerging market economies, including China, GDP growth remains low as for these countries, and in Russia it has probably slid below zero~~. **In turn, economic outlook for Poland's eastern trading partners, i.e. Russia and Ukraine, remains unfavourable.**

~~Since the previous Council meeting, oil prices have increased slightly, but remained far lower than in previous years. At the same time, the prices for other commodities, including agricultural products, continued to decrease. The fall in commodity prices amid moderate global economic growth has been adding to a deceleration in price growth in many countries, and has been deepening deflation in most European countries. At the same time, the fall in commodity prices is supporting economic growth in countries that are net commodity importers. Major central banks have kept their interest rates at historical lows. The European Central Bank is starting to purchase government bonds, while the majority of non-euro area central banks have eased their monetary policies, also by lowering interest rates.~~ **After a sharp and long-lasting fall, global commodity prices have stabilised recently. This has weakened disinflationary forces in many countries. However, global price growth remains very low, and in the majority of European economies it is negative. In these conditions, major central banks are keeping interest rates close to zero and the ECB has launched government bond purchases. This has contributed to some strengthening of the zloty.**

In Poland, ~~the pace of economic growth in 2014 Q4 slowed down slightly, but stayed close to 3%~~. **economic activity remains stable, with GDP growth in 2015 Q1 probably slightly higher than in 2014 Q4.** ~~GDP growth remained stable due to further rise in consumer demand and still high, despite some deceleration, investment growth. Meanwhile, lending growth was stable and labour market conditions continued to improve. The seasonally-adjusted unemployment rate has been declining driven to a large extent by rising employment~~. **Rising domestic demand fuelled by improving labour market situation, good financial condition of enterprises and stable expansion in lending, remains the main driver of economic growth.** ~~At the same time, the uncertainty about demand outlook continues to~~ **In turn, the relatively low, although accelerating, growth in demand on the part of Poland's main trading partners and the continued uncertainty about the prospects for demand are factors** limit economic activity in Poland.

~~Despite improving labour market, wage growth in the economy remains moderate which indicates low wage pressure. Moderate wage growth, the fall in global commodity prices and no demand pressure, all contribute to deepening deflation, both in terms of consumer and producer prices.~~ **Amid moderate growth in demand and gradual improvement in labour market conditions, there is no demand pressure in the economy, and nominal wage growth remains moderate. Combined with low commodity prices, this is contributing to continuing deflation, both in terms of consumer and producer prices.** Alongside that, inflation expectations continue to be very low.

~~The Council became acquainted with the projection of inflation and GDP prepared by the Economic Institute, which is one of the inputs to the Council's decisions on NBP interest rates. In line with the March projection based on the NECMOD model – prepared under the assumption of unchanged NBP interest rates and taking into account data available until 17 February 2015 (projection cut-off date) – there is a 50-percent probability that the annual price growth will be in the range of -1.0÷0.0% in 2015 (as compared to 0.4÷1.7% in the November 2014 projection), -0.1÷1.8% in 2016 (as compared with 0.6÷2.3%) and 0.1÷2.2% in 2017. At the same time, the annual GDP growth rate – in line with this projection – will be with a 50-percent probability in the range of 2.7÷4.2% in 2015 (as compared with 2.0÷3.7% in the November 2014 projection), 2.2÷4.4% in 2016 (as compared with 1.9÷4.2%) and 2.4÷4.6% in 2017.~~

~~Taking into account prolonging deflation and a significant increase in risk of inflation remaining below the target in the medium term, as indicated by the March projection, the Council decided to decrease NBP interest rates. Decision to lower the interest rates at the current meeting concludes the monetary easing cycle.~~ **In the opinion of the Council, in the coming quarters price growth will remain negative, mainly due to the previously observed sharp fall in commodity prices. At the same time, the adjustment of monetary policy in March – with continuing stable economic growth, an expected recovery in the euro area and good situation in the domestic labour market – reduce the risk of inflation remaining below the target in the medium term. Therefore, the Council decided to keep NBP interest rates unchanged.**

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