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Economic Comment

Forecasts with no major changes, and so are MPC views

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In line with expectations, the MPC left interest rates unchanged and the statement did not differ significantly in the key points vs the previous one. The relatively slow economic growth abroad and uncertainty related to the future developments were stressed again.

At the same time the MPC – relying on the new NBP projections – still thinks that despite some expected economic slowdown in 2020 the pace of Poland GDP growth shall stay decent and inflation should not leave the range of allowed fluctuations around the target.

Adam Glapiński sustained his view that he sees high probability of the interest rates staying unchanged until the MPC's term. This view was shared by Rafał Sura who pointed to the downside risk to the inflation forecasts. Majority of the MPC members supports the wait-and-see approach and we do not expect any rate changes in 2019 and 2020.

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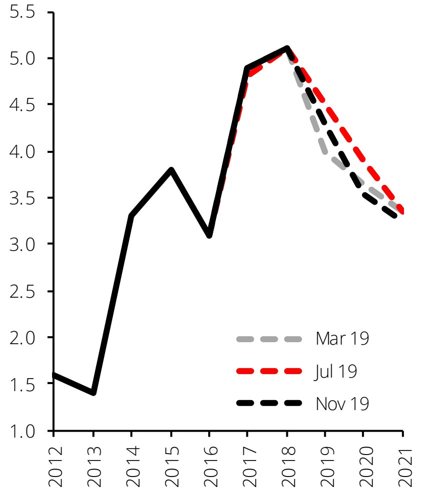
The new projection showed slightly lower GDP path with basically unchanged CPI path – the biggest difference concerned forecasts for 2019 (+0.3pp). In the Council's view, slight economic slowdown expected for 2020 amid inflation holding within the range of allowed deviation around the target supports the stable-rates scenario.

MPC decided to change the rules governing the creation of the reserves against FX risk. The law which worked so far obliged the NBP to create reserves from the whole surplus of incomes over costs. Adam Glapiński sustained his view that he sees a high likelihood of rates remaining unchanged toward the end of MPC's term (and if there were any rates changes at all then rather cuts than hikes). Rafal Sura confirmed the above, while pointed to downside risks to inflation forecasts (the increase in energy prices estimated at 8% y/y which would add 0.3pp to inflation, might not materialize). Łukasz Hardt underscored the existence of proinflationary factors: decent dynamic of wages, services and credit. Hard thinks that the optimal strategy for now is the „wait-and-see", however if the proinflationary factors were more significant than the economy's slowdown, and the inflation remained at around 3% y/y, he would consider small rates adjustments. However, the majority of MPC favors stable interest rates and in our opinion the rates will remain unchanged both in 2019 and in 2020.

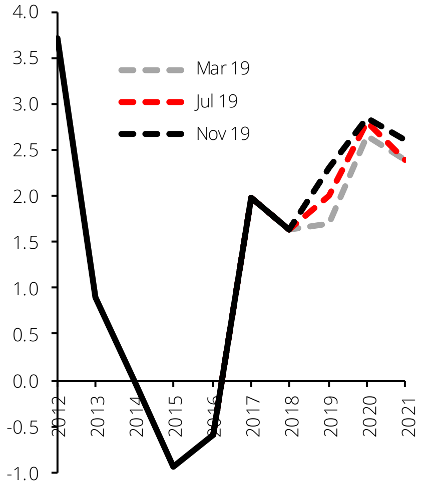
The new law allows for building reserves only from the positive exchange rate differences (at least this is what Adam Glapiński wrote in an article for "Rzeczpospolita" daily). What it means in practice is that the FX reserves (required level of PLN11.9 bn equals cumulative loss from the previous years; the reserve level at the end of 2018 stood at PLN3.9bn) are going to increase at a slower pace going forward, while NBP could possibly transfer its profit to the central budget (according to a law 95% of central bank's profit goes to the goverment) even if the reserve requirement is not met, which is already likely to happen in 2020. According to NBP governor the change will allow the central bank to increase the financial surplus, which will contribute to its credibility. We think that payout of profits before the FX reserves are rebuilt in full is negative for bank's credibility. It is difficult to find an argument for this kind of change in rules other than the need to pay in money into the central government in the years to come.

Central bank's GDP growth forecasts (central path)



Source: NBP, Santander Bank Polska

Central bank's CPI forecasts (central path)



Source: NBP, Santander Bank Polska

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Inflation and GDP projections in subsequent *Inflation reports*

	GDP growth			
	Nov 18	**Mar 19**	**Jul 19**	**Nov 19**
2018	4.8 (±0.4)	-	-	-
2019	3.55 (±0.85)	4.0 (±0.7)	4.5 (±0.6)	4.3 (±0.4)
2020	3.25 (±0.95)	3.65 (±0.95)	3.9 (±0.9)	(3.55±0.85)
2021	-	3.35 (±0.95)	3.35 (±0.95)	(3.25±0.95)
	CPI inflation			
2018	1.8 (±0.1)	-	-	-
2019	3.25 (±0.65)	1.7 (±0.5)	2.0 (±0.3)	2.3 (±0.1)
2020	2.9 (±1.0)	2.65 (±0.95)	2.8 (±0.9)	2.85 (±0.75)
2021	-	2.4 (±1.1)	2.4 (±1.1)	2.6 (±1.0)

Middle points of GDP and CPI growth paths and width of 50-percent probability ranges.

MPC statement (indication of changes as compared to October statement)

~~Incoming data suggest that global~~Global economic growth remains relatively low~~, with~~ and uncertainty about the global outlook ~~deteriorating further.~~persists. In the euro area, ~~economic~~annual GDP growth ~~remains low against~~in 2019 Q3 declined alongside the ~~backdrop of a~~ongoing downturn in industry. ~~Still favourable situation in the service sector is the factor mitigating the scale of the slowdown.~~ In the United States, economic conditions continue to be relatively strong, ~~even though economic indicators signal a weakening of~~ however, GDP growth in 2019 Q3 in the US economy also declined. At the same time, in China economic activity ~~in 2019 Q3. In China, incoming data point~~growth continues to ~~further weakening of GDP growth~~slow down.

In ~~September, global oil prices rose, yet remained below the level recorded a year ago. At the same time~~recent months, inflation declined in many countries ~~remains~~ and continues to run at a moderate level, supported by lower oil prices than a year ago. In particular, inflation is low in the euro area.

The European Central Bank ~~significantly loosened its monetary policy, lowering~~ is keeping the deposit rate unchanged, after lowering it further below zero ~~and announcing~~in September. At the ~~resumption of~~ same time it has resumed the asset purchase programme ~~as well as relaxing the terms of long-term refinancing operations. The ECB also~~ and signalled ~~that~~the maintenance of loose monetary policy in the ~~interest rates are likely to stay at the present or lower level in the subsequent~~coming quarters. The Federal Reserve ~~also loosened its monetary policy by cutting~~cut interest rates again in October.

In Poland, economic conditions remain good~~. At~~, although the ~~same time,~~ incoming data point to a possible decrease in the economic growth rate in 2019 Q3, ~~which is driven~~ mainly ~~by~~due to the economic downturn abroad. ~~Rising~~However, rising consumption, fuelled by ~~the~~ increasing employment and wages, very strong consumer confidence and social benefit payments, exerts a stabilising influence on GDP growth. ~~Investment in~~At the ~~economy also~~same time, the incoming data indicates that investment continues to rise, albeit at a slower pace.

Inflation in ~~September~~October 2019 – according to the GUS flash estimate – stood at 2.~~6~~5% y/y. ~~Higher~~Food price growth, despite a gradual slowdown, remains elevated and is ~~primarily driven by a previous marked increase in food prices, while~~contributing to higher inflation. On the other hand, lower energy prices than a year ago, including fuel prices, ~~have~~are having a curbing effect on price growth. At the same time, in the recent period core inflation has risen, but continues to run at moderate levels.

The Council became acquainted with the results of the November projection of inflation and GDP, prepared under the assumption of unchanged NBP interest rates. The November projection takes into account data and information published up to 18 October 2019. In line with the November projection based on the NECMOD model, there is a 50- percent probability that the annual price growth will be in the range of 2.2-2.4% in 2019 (against 1.7-2.3% in the July 2019 projection), 2.1-3.6% in 2020 (compared to 1.9-3.7%) and 1.6-3.6% in 2021 (compared to 1.3–3.5%). At the same time, the annual GDP growth – according to this projection – will be with a 50-percent probability in the range of 3.9-4.7% in 2019 (against 3.9-5.1% in the July 2019 projection), 2.7-4.4% in 2020 (compared to 3.0- 4.8%) and 2.3-4.2% in 2021 (compared to 2.4-4.3%).

In the Council's assessment, the outlook for economic conditions in Poland remains favourable, and GDP growth, despite the expected decline, will continue at a relatively high level in the coming ~~years. However,~~quarters. At the same time, there remains uncertainty about the scale and persistence of the slowdown abroad and its impact on domestic economic activity ~~has increased.~~. Inflation – after a temporary rise in 2020 Q1 – will stay close to the target in the monetary policy transmission horizon. Such an assessment is supported by the results of the November NBP projection of inflation and GDP.

The Council judges that the current level of interest rates is conducive to keeping the Polish economy on a sustainable growth path and maintaining macroeconomic stability.

The Council adopted the Inflation Report – November 2019 and the resolution on the principles for creating and releasing the provision against the foreign exchange rate risk of the złoty at Narodowy Bank Polski and amended the resolution on the NBP accounting principles.

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