POST-MPC COMMENT

8 November 2017

New projection is not enough

The Monetary Policy Council kept the main interest rates unchanged, with the reference rate at 1.5%. At the same time, the MPC decided to cut the required reserve ratio on funds with maturity of at least two-years to 0% (from current 3.5%) – the decision will be effective since March 2018.

The NBP projection showed CPI path with mid-point higher than the previous one by c.0.25pp in 2018-19 and GDP growth higher by 0.15pp in 2017-18. Interestingly, higher mid-points resulted from increases in the lower end of the predicted inflation bands. In the crucial fragment of the official statement, the MPC dropped earlier claim that the risk of exceeding the inflation target in the medium term is limited and wrote it expects inflation to fluctuate near the target in the coming years. The statement said also that core inflation rose and is moderate, while in previous months they wrote that it remains low. Still, the MPC repeated the assessment that the current level of interest rates "is conducive to keeping the Polish economy on the sustainable growth path and maintaining macroeconomic stability".

During the post-meeting press conference, the NBP President Adam Glapiński repeated he still believes that keeping interest rates stable until the end of 2018 would be the most appropriate, assuming that everything would go in line with the NBP projection. In his view, the increase in CPI forecast was minor and he would not worry about it, as he sees risks for economic growth in future. He also mentioned disciplined state budget and PLN appreciation as factors that limit the need for monetary tightening. Glapiński was accompanied at the conference by dovish Jerzy Żyżyński and hawkish Łukasz Hardt. Interestingly, the latter did not raise too many hawkish arguments, saying that the MPC should wait until early 2018 before making any decision. He said he would not rule out that rate hikes would be necessary if inflationary pressure intensifies, however it is not a done deal. He also added the progress in ECB policy normalisation will be important for him and a delay in this area would make a rate cut in Poland difficult. Żyżyński did not surprise at all, saying that higher inflation was not a reason for higher rates as long as there is no excessive credit growth.

The decision to cut the reserve requirement for long-term deposits was explained as a step to eliminate the discrimination of domestic depositors, as the reserve for non-residents' deposits with maturity >2Y was already zero. We think the move could be an attempt to ease the impact of negative real interest rates on households' savings.

In sum, a bit more hawkish MPC statement was offset by a dovish tone of the press conference. It seems that the NBP Governor Glapiński still holds a firm majority. Despite the hawkish comments of several MPC members in recent weeks, which boosted market expectations that the new NBP projection could be a game-changer, it did not happen, which was in line with our view. We think a change of balance of views in the rate-setting panel would require more evidence from the economic data of building wage and inflationary pressures. We expect that the data will provide such evidence but it will take at least a few months. Therefore, after a short-time relief on the market after more dovish than expected press conference, the expectations for rate hikes could start building again at the start of 2018.

Inflation and GDP projections

	GDP growth				CPI inflation			
	Nov 16	Mar 17	Jul 17	Nov 17	Nov 16	Mar 17	Jul 17	Nov 17
2016	2.3÷3.4	-	-	-	-0.7 ÷ -0.6	-	-	-
2017	2.6÷4.5	3.4÷4.0	3.4÷4.7	3.8÷4.6	0.5÷2.0	1.6÷2.5	1.6÷2.3	1.9÷2.0
2018	2.2÷4.4	2.4÷4.5	2.5÷4.5	2.8÷4.5	0.3÷2.6	0.9÷2.9	1.1÷2.9	1.6÷2.9
2019	-	2.3÷4.4	2.3÷4.3	2.3÷4.3	-	1.2÷3.5	1.3÷3.6	1.7÷3.7

According to the NBP projections, the GDP and CPI growth will fall to within the ranges given above with probability of 50%.

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

Global economy continues to recover. ~~Available data indicate that GDP~~ **Economic** growth in the euro area ~~stabilised~~ remains higher than in ~~2017 Q3, after picking up in~~ **the** previous ~~quarters~~ **year, driven by an improvement in the labour market conditions, favourable sentiment of economic agents, and a recovery in international trade**. In the United States, ~~economic conditions are strong, although~~ **GDP growth in 2017 Q3 was close to that observed in the previous quarter, despite the negative impact of** adverse weather factors ~~could have had a negative impact~~ on economic activity ~~in recent months~~. In China, ~~monthly indicators suggest that GDP~~ **economic** growth ~~may slow~~ **in 2017 Q3 slowed** down slightly ~~in 2017 Q3~~.
Despite ongoing global recovery, inflation abroad remains moderate, on the back of persistently low domestic inflationary pressure in many countries. ~~Prices~~ **At the same time, prices** of ~~some~~ **certain** commodities, including oil, have risen somewhat of late.
The European Central Bank keeps interest rates close to zero, including the deposit rate below zero, ~~and continues its~~. **At the same time, the ECB has extended the duration of the** asset purchase programme. ~~At the same time, the~~ **at least until September 2018, cutting the amount of monthly purchases as of next year by half. The** US Federal Reserve ~~gradually tightens its monetary policy, embarking on a reduction of~~ **in turn, has started reducing** its balance sheet.
In Poland, ~~incoming~~ monthly data ~~confirm continued stable~~ **indicate that GDP** growth in ~~economic activity.~~ **2017 Q3 was probably higher than in the previous quarter.** Growth ~~is~~ **was** still driven primarily by consumer demand, supported by rising employment and wages, disbursement of benefits and very good consumer sentiment. At the same time, ~~a marked rise in~~ **faster** construction and assembly output growth **than in the first half of the year** points to a probable recovery in investment.
The annual growth in prices of consumer goods and services remains at a moderate level. ~~At the same time, while wage growth in the economy has picked up,~~ **All** core inflation ~~is~~ **measures have risen, though** still ~~low~~ **remain moderate.**
The Council became acquainted with the results of the November projection of inflation and GDP, prepared under the assumption of unchanged NBP interest rates. 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 1.9-2.0% in 2017 (against 1.6-2.3% in the July 2017 projection), 1.6-2.9% in 2018 (compared to 1.1-2.9%) and 1.7-3.7% in 2019 (compared to 1.3-3.6%). At the same time, the annual GDP growth – in line with this projection – will be with a 50-percent probability in the range of 3.8-4.6% in 2017 (against 3.4-4.7% in the July 2017 projection), 2.8-4.5% in 2018 (compared to 2.5-4.5%) and 2.3-4.3% in 2019 (compared to 2.3-4.3%).
Taking into account the present information, including the results of the November projection, the Council judges that in the coming years inflation will run close to the inflation target. As a result, the current level of interest rates is conducive to keeping the Polish economy on the sustainable growth path and maintaining macroeconomic ~~balance~~ **stability.**
The Council adopted a resolution on the required reserve ratios. In line with this resolution the required reserve ratio on funds received for at least a two-year period will stand at 0%. The resolution comes into force on 1 March 2018 and applies since the required reserve maintenance period starting on 30 April 2018.

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