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Economic Comment

MPC clearly more dovish

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In line with expectations, the MPC left interest rates unchanged with the reference rate still at 1.50%. Governor Adam Glapiński visibly changed his tone to even more dovish and suggested that rates might remain intact even until the end of the MPC term (ie until 2022, earlier 2019 or 2020 were indicated as the horizon of interest rate stability). Later on, monetary easing is possible with use of non-conventional tools, as further rate cuts would be risky. Glapiński explained that after oil prices fell and energy price hike was averted, inflation does not exceed the target in the whole forecasting horizon. Moreover, after 2022 the inflow of EU funds will fall markedly, contributing to slower GDP growth.

We see the CPI inflation to be higher than the MPC expectations, but we believe that the inflation rebound will be too slow to change the MPC rhetoric in 2019, thus we think that rates will stay stable this year.

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The statement from the meeting did not change much compared to the previous ones though the Council underlined that the inflation will likely run below the path forecasted in the November's edition of the central bank report after oil prices fell and the government prevented the energy prices rise.

Governor Adam Glapiński visibly changed his tone to even more dovish during the press conference and suggested that rates might remain intact even until the end of the MPC term (ie until 2022). In the previous months Glapiński indicated 2019 or 2020 as the horizon of interest rate stability. What justifies his change of tone is the reduction of inflation forecasts and worries about slowdown of the economy. According to the NBP governor, inflation will not exceed the 2.5% y/y target in the whole horizon of the forecast (in the November projection, CPI approached 3.5% y/y already in 2019 and stayed above the 2.5% for the rest of the forecast horizon). Economic slowdown in 2019 is to be gentle (with GDP growth staying above 4% y/y), but in 2022 the EU funding will be reduced which can potentially create a need for monetary easing. Such easing would have to be based on unconventional measures (according to the governor, the MPC has a ready toolbox), as further rate cuts would be risky for smaller financial institutions. In the later part of the press conference, governor Glapiński said in turn that analyses were not conclusive about the detrimental effect of further cuts and that rates in Poland are high enough to allow some decrease if needed.

The remaining MPC members who attended the press conference (Jerzy Kropiwnicki and Jerzy Żyżyński) supported the governor's view. According to Żyżyński, interest rate hikes would be justified in the case of an excessive credit creation that is not currently observed. Rate cuts could be considered in the scenario of a further deceleration of the German economy. Kropiwnicki said he is not worried about any excessive wage rise demands as for years the salary growth did not keep the pace with the productivity now we may observe convergence.

We see the CPI inflation to be higher than the MPC expectations, but we believe that the inflation rebound will be too slow (with CPI and core inflation reaching 2.5% at the year end at the earlies) to change the MPC rhetoric in 2019, thus we think that rates will stay stable this year.

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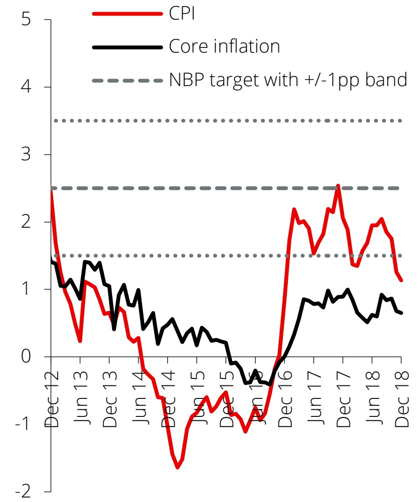
CPI and core inflation vs NBP target



Source: GUS, NBP, Santander

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

Global economic conditions remain favourable, although incoming data suggest a weakening in some economies. In the euro area, following a decline in GDP growth ~~declined~~ in 2018 Q3, ~~and incoming data indicate a gradual~~certain economic ~~slowdown.~~climate indicators deteriorated further. In the United States, ~~GDP data for 2018 Q3 confirmed that~~ economic conditions ~~in this country are still~~remained very strong~~. In turn,~~ in 2018 Q4, yet forecasts suggest lower growth in 2019. Also in China activity growth is gradually slowing down.

~~Heightened~~The continuously heightened uncertainty about the global economic outlook ~~persists, which has~~is having an adverse effect on the prices of some assets in the international financial markets. At the same time, global oil prices have fallen ~~sharply~~ in ~~the~~ recent ~~period~~months.

~~Inflation is still elevated~~A marked decline in commodity prices, notably the prices of oil, has contributed to lower inflation in many countries ~~due to the earlier increase in energy prices~~. At the same time, core inflation in the environment of the Polish economy, including the euro area, remains moderate.

The European Central Bank keeps interest rates close to zero, including the deposit rate below zero. At the same time, the ECB ~~continues to~~ has terminated the net purchase of financial assets, ~~although~~yet it ~~has announced the termination of~~ will continue to reinvest the ~~purchases by~~funds from the ~~end of the year.~~maturing securities. The US Federal Reserve ~~kept~~raised interest rates ~~unchanged~~ in ~~November, after another interest rate hike in September~~December 2018.

In Poland, ~~preliminary GDP~~incoming data ~~for 2018 Q3~~ point to ~~a strong~~ economic conditions~~.~~ remaining strong. GDP growth is still driven by rising – albeit at a slightly lower rate than in ~~the~~ previous quarters – consumption, that is fuelled by increasing employment and wages as well as very high consumer sentiment. ~~In 2018 Q3, this was~~This is accompanied by a ~~marked~~ rise in investment.~~ Amid relatively high growth of domestic demand and the weakening of economic conditions in Poland's external environment, net exports had a negative contribution to GDP growth~~.

Notwithstanding relatively high economic growth and wages rising faster than in the previous year, annual consumer price growth has declined in recent months and remains moderate. At the same time, inflation net of food and energy prices continues to be low.

In the Council's assessment, current information points to a relatively favourable outlook for economic conditions in Poland, although a gradual slowing in GDP growth is expected in the ~~years~~quarters ahead. ~~In 2019 inflation might be increased by rising energy prices, i.e. factor beyond~~At the ~~control of monetary policy. The scale of energy~~same time, according to current forecasts, the annual price growth ~~in 2019~~ will ~~probably be limited by the fall~~increase in the coming months, yet – due to the decline in oil prices ~~seen~~and the freeze on electricity prices – the scale of this increase will be smaller than anticipated in ~~recent months.~~the November projection. In the medium term~~, in turn~~, the expected slowdown in economic growth will have a dampening effect on inflation. Consequently, in the monetary policy transmission horizon inflation will remain close to the target.

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