

Weekly Economic Update

Inflation gets lower, but is the target nearer?

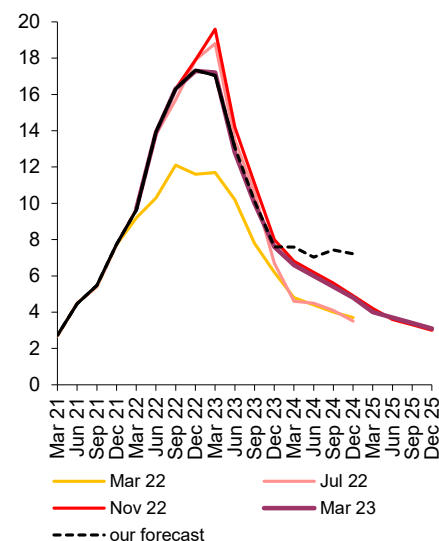
Economy next week

- The MPC meeting is the key event of the first week of July** – the decision is due on Thursday, the conference of the NBP president probably on Friday afternoon. Interest rates will again remain unchanged. As usual, market will focus on the tone of President Glapiński's communication. For several months now, some MPC members have been signalling that the descent of CPI inflation to single digits could open the door to a rate cut after the summer holidays. The flash inflation figure for June (11.5% y/y) was again lower than expected and heralds a single-digit inflation rate as early as September. Of course, it is not so much the fall in current inflation that should be crucial for the interest rate decision, but above all the prospect of its return to the 2.5% target. The results of the new NBP projection, which will be presented to the Council at its July meeting, will tell us much more about this mid-term outlook. The previous projection from March predicted that inflation might not approach the target until the very end of 2025, based on assumption that interest rates remain unchanged during this period. **In our view, the information that has appeared since March does not change the prospects for reaching the inflation target** - the starting point of the new projection is higher as regards CPI (2Q average actual at 13.1% vs. 12.8% in the projection) and core inflation (2Q average 11.6% vs. 11.1%), wage growth, GDP growth and lower in case of unemployment. On top of that, pro-inflationary effects of this year's budget amendment and the announced indexation of family benefits should be added. On the other hand, the zloty is stronger, which, according to a new NBP study on the monetary policy transmission mechanism, may influence the CPI more than previously thought (1% appreciation of the PLN may lead to a drop in prices by as much as 0.2% - which is about four times stronger than in earlier studies), and possibly bigger productivity gains may be assumed resulting from stronger investments. **If, as we believe, the results of the new projection do not bring the timing of inflation's return to target significantly closer, there will be no grounds for accelerating the discussion of rate cuts.** Nor will the discussion of reductions be helped by the international context - central banks in developed world are determined to continue fighting inflation and are likely to continue raising rates beyond the summer, as evidenced by signals from their recent meetings and the central banking forum in Sintra this week.
- The week will start with a market holiday in the US (Independence Day) and the publication of manufacturing PMIs for June. **We expect the PMI for Poland to fall slightly** (our forecast is 46.2 pts, median forecast 46.9 pts, compared to May reading of 47.0 pts), following indices for other countries that clearly signal a recession in European industry.
- In the following days the calendar includes PMIs for service sectors, industrial production and orders in several European countries and, at the end of the week, monthly US employment data. On Tuesday morning, there will be a decision by the Reserve Bank of Australia, which at its previous meeting surprised the market with a 25bp hike and now a similar move cannot be ruled out - analysts' expectations are spread almost equally, with a slight edge in expectations of no change.

Markets next week

- Despite a temporary correction in the middle of the week, the EURPLN returned to the previous Friday's levels despite a appreciating dollar against the euro, which theoretically should not favour the zloty. **We assume that the EURPLN will trade sideways in the coming weeks**, all the more so if there is no clear declaration of rate cuts after the MPC meeting after the summer. We still see potential for a correction, but recently we have also adjusted the forecasted EURPLN path slightly downwards - we assume that the scale of such a correction would not be large. We assume that the exchange rate will remain relatively close to the exports breakeven rate, low enough to support a drop in inflation, but high enough not to permanently impair the competitiveness of exports. In the event of a greater PLN weakening, BGK could be activate some more FX sale
- The market expectations for NBP rate cuts before the end of the year strengthened following lower-than-forecast inflation. This should remain unchanged for most of the week, while later the tone of the NBP President's conference and the results of the new projection will be key to further market reaction. If, as we suspect, the projection does not bring the timing of inflation's return to the target significantly closer, expectations of rate cuts may be adjusted somewhat. **In the baseline scenario, we still do not assume NBP rate cuts this year, which may bring periods of upward FRA and IRS adjustments and flattening of the IRS curve.** However, given the market positioning for future rate cuts and a slow but nonetheless further decline in inflation, we believe that this will not fundamentally change the downward trend in rates. Meanwhile, relatively high planned net issuance in Q3 may keep pressure on credit spreads over swaps.

CPI inflation according to subsequent NBP projection and our latest forecast, % y/y

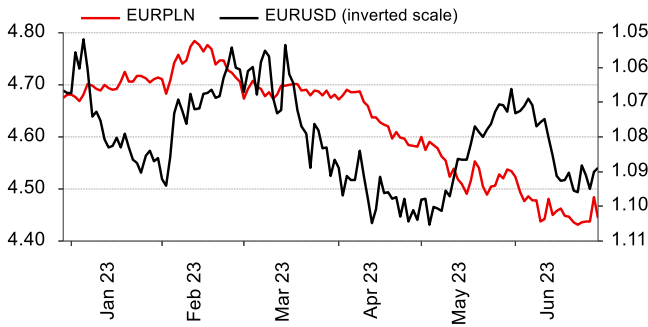


Source: NBP, Santander

Economic Analysis Department:

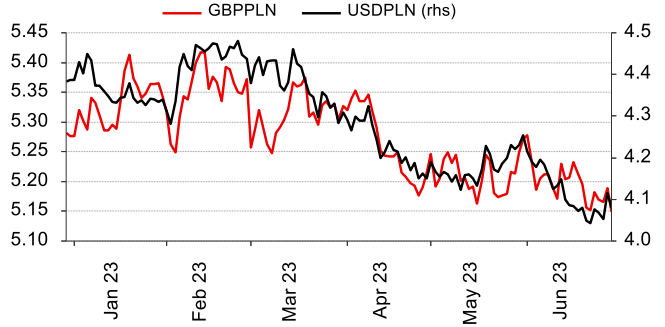
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EURPLN and EURUSD



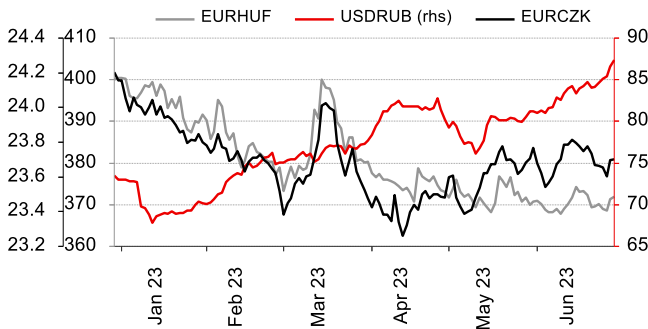
Source: Refinitiv Datastream, Santander

GBPPLN and USDPLN



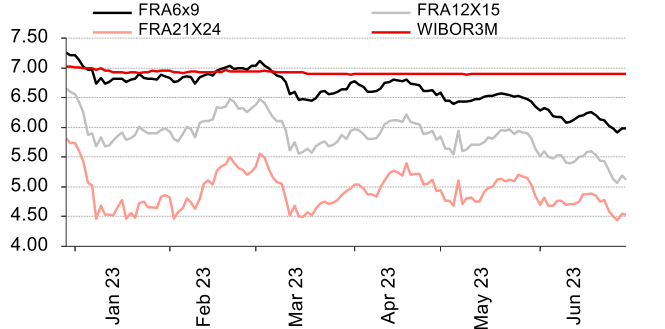
Source: Refinitiv Datastream, Santander Bank Polska

EURCZK, EURHUF and USDRUB



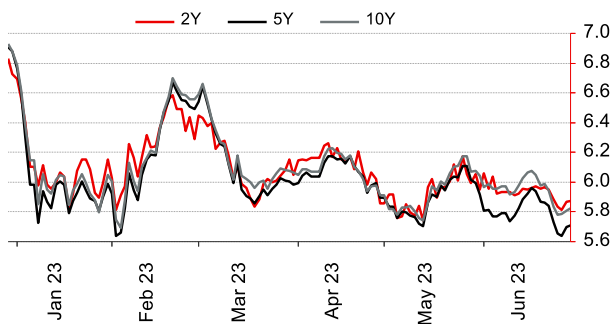
Source: Refinitiv Datastream, Santander Bank Polska

PLN FRA and WIBOR3M



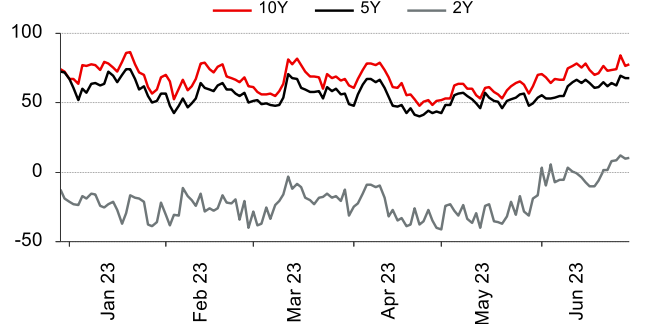
Source: Refinitiv Datastream, Santander Bank Polska

Polish bond yields



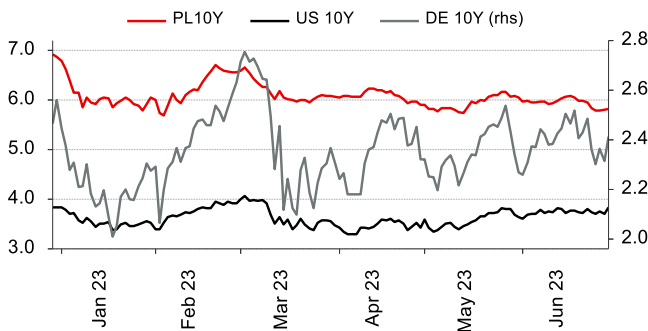
Source: Refinitiv Datastream, Santander Bank Polska

Asset swap spreads



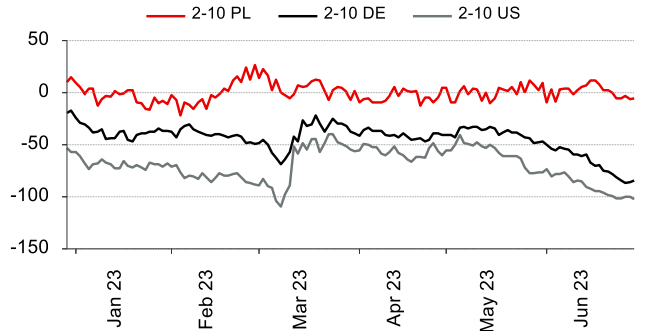
Source: Refinitiv Datastream, Santander Bank Polska

10Y bond yields



Source: Refinitiv Datastream, Santander

Steepness of yield curves



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	w/e	PERIOD	FORECAST		LAST VALUE	
				MARKET	SANTANDER		
MONDAY (3 July)							
09:00	PL	Poland Manufacturing PMI	Jun	pts	46.9	46.2	47.0
09:55	CN	China Manufacturing PMI	Jun	pts	50.0	-	50.9
09:55	DE	Germany Manufacturing PMI	Jun	pts	41.0	-	41.0
10:00	EZ	Eurozone Manufacturing PMI	Jun	pts	43.6	-	43.6
16:00	US	ISM manufacturing	Jun	pts	47.1	-	46.9
TUESDAY (4 July)							
08:00	DE	Exports SA	May	% m/m			1.4
WEDNESDAY (5 July)							
03:45	CN	Caixin China PMI Services	Jun	pts	56.2	-	57.1
09:55	DE	Markit Germany Services PMI	Jun	pts	54.1	-	57.2
10:00	EZ	Eurozone Services PMI	Jun	pts	52.4	-	55.1
16:00	US	Durable Goods Orders	May	% m/m		-	1.7
16:00	US	Factory Orders	May	% m/m	0.6	-	0.4
20:00	US	FOMC Meeting Minutes	Jun				
THURSDAY (6 July)							
	PL	MPC decision		%	6.75	6.75	6.75
08:00	DE	Factory Orders	May	% m/m	2.5	-	-0.4
08:30	HU	Industrial Production SA	May	% y/y		-	-5.8
11:00	EZ	Retail Sales	May	% m/m	0.2	-	0.0
14:15	US	ADP report	Jun	k	250	-	278
14:30	US	Initial Jobless Claims		k	265	-	239
16:00	US	ISM services	Jun	pts	51.2	-	50.3
FRIDAY (7 July)							
08:00	DE	Industrial Production SA	May	% m/m	-0.2	-	0.3
08:30	HU	CPI	Jun	% y/y	20.0	-	21.5
09:00	CZ	Industrial Production	May	% y/y	-3.0	-	-1.8
14:30	US	Change in Nonfarm Payrolls	Jun	k	200	-	339
14:30	US	Unemployment Rate	Jun	%	3.6	-	3.7

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

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