

Keep calm and don't expect too many cuts

TOP MACRO THEME(S):

- **Market expectations on interest rate cuts seem exaggerated (p.2):** Despite brighter inflation outlook and termination of the tightening cycle we see several arguments against overly optimistic market expectations on interest rate cuts.

WHAT ELSE CAUGHT OUR EYE:

- **The government estimates that in 2024 app. 3.6 million people will earn the minimum wage, app. 23% of those working in the national economy.** In recent years, the "scope" of the minimum wage has increased significantly. According to government's calculations from Jan 1st the minimum wage will be equal to 54.4% of the average wage in the national economy and from July 1st to 55.2%.
- **The number of foreigners insured in Social Security Fund at the end of June amounted to 1.094 million and was by 8.1% higher than a year ago.** For several months the number of insured Ukrainians has remained stable - it seems that the potential to employ them in Poland is running out. At the same time a significant increase in the number of insured foreigners from other countries was observed. In June, there were 346,000 of them, 22.2% more than a year ago.
- **CAB surplus in May turned out far better than expected reaching 1.4 bn EUR.** Higher than expected export growth (3.3% y/y) was the main source of surprise. In terms of 12m rolling sum, CAB deficit stands at -0.3% GDP against -0.7% GDP after April.

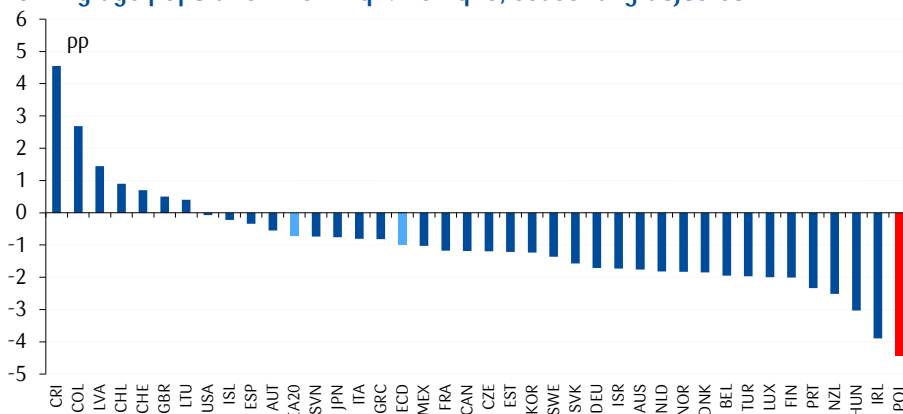
THE WEEK AHEAD:

- **The data to be released next week will likely confirm further disinflation** – both core CPI and PPI are set to decline in June.
- **Activity data for June will still be subdued,** as high inflation hinders domestic demand and external environment is still unsupportive. Consumer demand, however, is expected to rebound later in 2023, as real wage growth has likely turned positive in June, for the first time in a year.

NUMBER OF THE WEEK:

- **4.00** – USDPLN fell below 4.00 for the first time since Russia's invasion on Ukraine.

CHART OF THE WEEK: Percentage point change in inactivity rates among the working age population from 4q19 to 1q23, seasonally adjusted



Source: OECD, PKO Bank Polski.

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	2022	2023
Real GDP (%)	5.1	0.7
Industrial output (%)	10.5	-0.1
Unemployment rate# (%)	5.2	5.2
CPI inflation** (%)	14.4	12.0
Core inflation** (%)	9.1	10.6
Money supply M3 (%)	5.6	6.0
C/A balance (% GDP)	-3.0	0.8
Fiscal balance (% GDP)*	-3.7	-5.4
Public debt (% GDP)*	49.1	49.1
NBP reference rate## (%)	6.75	6.50^
EURPLN###	4.69	4.50

Source: GUS, NBP, MinFin, †PKO BP Market Strategy team forecasts; *ESA2010, **period averages; #registered unemployment rate at year-end; ##at year-end. ^under revision.

Market expectations on interest rate cuts seem exaggerated

- The inflation picture is getting brighter with a strong disinflation trend intact and its broadening nature. The official termination of the tightening cycle has boosted market expectations for interest rate cuts. In our opinion markets might be exaggerating expectations on the speed and strength of the upcoming loosening cycle.

The final CPI data for June confirmed that a strong disinflation trend remains intact. Inflation declined to 11.5% y/y (in line with the flash estimate), from 13.0% in June. Compared to its peak reached in February, the CPI inflation has already declined by 6.9pp. **The inflation picture is getting brighter** – (1) the decline of CPI inflation is driven by all of its main categories, including the core inflation; (2) June was the second month in a row in which the general price level has remained stable (no change in m/m terms); (3) even in the case of core inflation the decline in y/y terms mirrors not only a high statistical base, but also a weakening momentum (short-term trend, see chart).

Food prices declined in June (-0.3% m/m), for the first time since summer 2021. It seems that, slowly, we are getting back to the pre-pandemic seasonality pattern. For the short term we expect the food price disinflation to continue, from the current 17.8% y/y towards 8% y/y at the end of 2023. Nevertheless, in the mid-term, energy prices, high labour costs and the increasingly adverse effect of climate changes will likely keep food inflation at a relatively high level, above the CPI target.

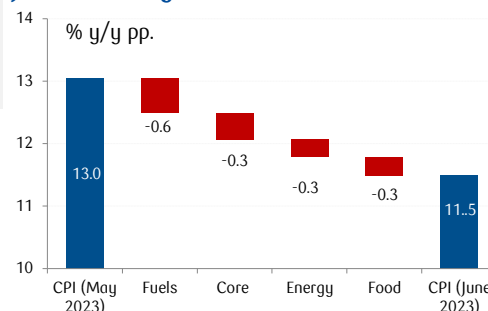
Energy prices continue normalizing, mainly in the case of solid fuels whose prices have turned negative in y/y terms for the first time since 2020. The y/y decline in fuel prices has deepened, to 18%, in line with the flash estimate.

Core inflation declined to 11.1% y/y (according to our estimates, the official data is to be published on July, 17th) compared to 11.5% y/y in May and 12.3% y/y in its peak in March. Its decline reflects statistical factors, the weakening second round effects of the energy shock and lower demand. We see growing number of categories for which the period of the strongest price increases has already passed. The momentum of core inflation (% m/m, sa) decreased in comparison to the peaks, but remains relatively high, implying core inflation at approx. 8% y/y after annualization.

In recent comments MPC members have underlined that prices have remained stable for the last 2 months and that the disinflationary trend has become more broad-based. They point at a single-digit inflation as a potential trigger for first interest rate cuts. According to our estimates the CPI inflation will turn single-digit in September, while in August it will be still slightly above the 10% y/y level.

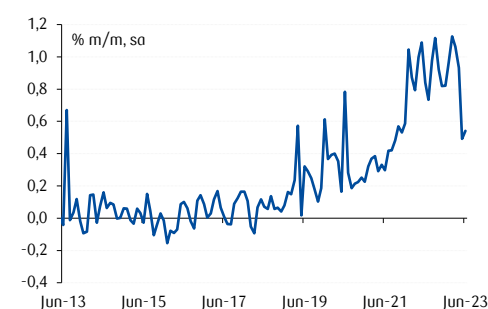
The official termination of the tightening cycle, recent MPC comments and the favourable current disinflationary trend have boosted market expectations regarding the potential for interest rate cuts. The FRA market suggests approx. 100bp cuts in 2023 and further 150bp in 2024. In our opinion, in both cases these expectations are exaggerated (unless we have a big positive inflation surprise).

Decomposition of CPI inflation between June and May 2023



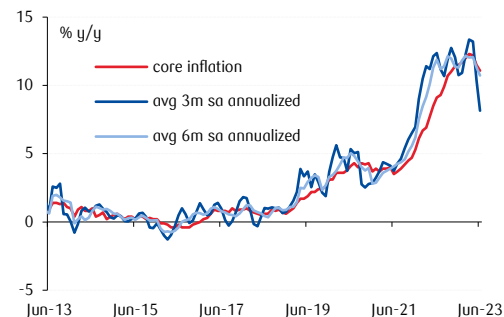
Source: Statistics Poland, PKO Bank Polski.

Core CPI inflation momentum



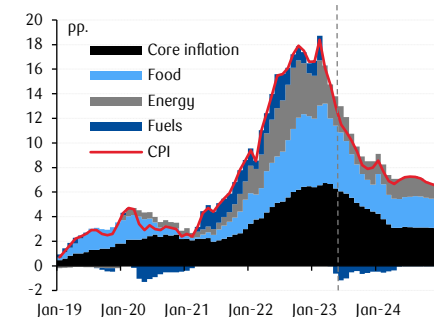
Source: Statistics Poland, PKO Bank Polski.

Core CPI inflation



Source: Statistics Poland, PKO Bank Polski.

CPI inflation forecast



Source: Statistics Poland, PKO Bank Polski.

(1) The current strong disinflationary trend will weaken in the coming months. In our opinion the headline inflation will decline by approx. 3.5pp in 2h23 (only half of the decline seen between February and June), towards around 8% y/y at the end of the year (our assumption is very close to the current NBP projection).

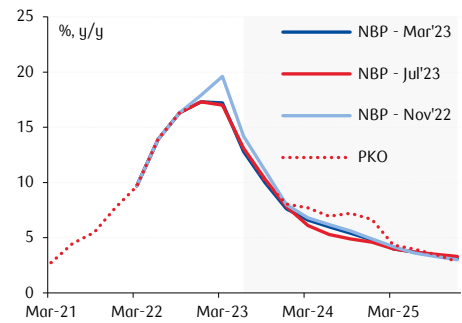
(2) In 2024 the disinflation trend will likely turn even weaker than in 2h23, due to (1) tax changes (return to higher VAT rate for food as early as in January), (2) unfreezing or at least a partly unfreezing of energy prices, (3) more flattish core inflation, which will mirror still strong labour market pressure (wages growing by around 10% y/y) and stronger demand (private consumption should turn positive in 4q23).

(3) According to the current NBP projection, the headline CPI inflation will decline towards 4.6% y/y in 4q24 and 3,3% in 4q25 compared to the NBP target defined as 2.5% (+/- 1pp). Thus, the current projection does not show much space for interest rate cuts, especially at the front end of the projection period.

(4) According to the NBP Governor, potential interest rate cuts will be gradual and cautious.

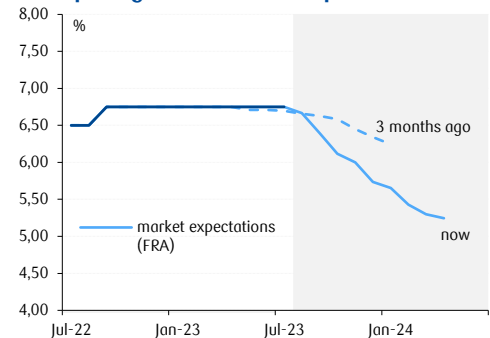
Considering our current CPI inflation assumptions, the NBP might start cutting interest rates in October. Should the cycle start then, we might see two (instead of one) 25 bp cuts this year. In our opinion in 2024 the loosening cycle will slow down (in line with the disinflation trend), resulting in approx. 100 bp cuts, towards 4.5-5.0%.

CPI projection (NBP) and PKO forecast



Source: NBP, Statistics Poland, PKO Bank Polski.

NBP policy rate market expectations



Source: Datastream, PKO Bank Polski.

Weekly economic calendar

Indicator	Time (UK)	Unit	Previous	Consensus*	PKO BP	Comment
Monday, 17 July						
CHN: GDP growth (2q)	3:00	% y/y	4.5	7.0	--	--
POL: Core inflation (Jun)	13:00	% y/y	11.5	11.1	11.1	Core inflation has likely declined for the third time in a row amid waning wage pressures.
Tuesday, 18 July						
USA: Retail sales (Jun)	13:30	% m/m	0.3	0.5	--	--
USA: Retail sales excl. autos (Jun)	13:30	% m/m	0.1	0.4	--	--
USA: Industrial production (Jun)	14:15	% m/m	-0.2	0.0	--	--
Wednesday, 19 July						
POL: Consumer Confidence (Jul)	9:00	pts.	-28.2	-27.1	-27.5	Deteriorating inflation and stable labour market have positive impact on consumer confidence.
EUR: HICP inflation (Jun, final)	10:00	% y/y	6.1	5.5	--	--
EUR: Core inflation (Jun, final)	10:00	% y/y	5.3	5.4	--	--
USA: Building Permits (Jun)	13:30	thous	1,491	1,488	--	--
USA: Housing starts (Jun)	13:30	thous	1,631	1,450	--	--
Thursday, 20 July						
GER: PPI inflation (Jun)	7:00	% y/y	1.0	--	--	--
POL: PPI inflation (Jun)	9:00	% y/y	3.1	0.7	0.7	Goods disinflation has likely continued, as prices in manufacturing were dragged down by stronger PLN, lower cost of commodities and unblocked supply chains.
POL: Industrial production (Jun)	9:00	% y/y	-3.2	-1.6	-1.6	IP was still under pressure from low demand and high statistical base.
POL: Wages (Jun)	9:00	% y/y	12.2	12.1	11.9	Employment remained stagnant as real wage growth has turned positive for the first time in a year.
POL: Employment (Jun)	9:00	% y/y	0.4	0.4	0.4	Construction dynamic was supported by low statistical base.
POL: Construction output (Jun)	9:00	% y/y	-0.7	1.8	1.0	
USA: Initial Jobless Claims (Jul)	13:30	thous	--	--	--	--
USA: Existing home sales (Jun)	15:00	million	4,3	4,21	--	--
EUR: Consumer Confidence (Jul, flash)	15:00	pts.	-16.1	--	--	--
Friday, 21 July						
POL: Retail sales (Jun)	9:00	% y/y	-6.8	-5.0	-5.0	Sales dynamics are not deteriorating any more.

Source: GUS, NBP, Parkiet, PAP, Bloomberg, Reuters, PKO Bank Polski. Parkiet for Poland, Bloomberg, Reuters for others.

Monetary policy monitor

MPC Members	Hawk-o-meter*	Recent policy indicative comments^
J. Tyrowicz	5.0	"For many months now the Council has been keeping rates at an unchanged level, a level I consider too low. (...) each current discussion about rate cuts currently harms the credibility of the monetary policy in Poland. Such talks also reduce efficiency of MPC actions, with 3M WIBOR now lower by ca. 0.8 pps than after the last rate hike. Let's not take this path because otherwise fight against inflation will take longer and will bear higher social costs" (12.06.2023, Parkiet, PAP)
L. Kotecki	4.8	"... it's simply too early for rate cut discussions in September or October. Maybe we'll see inflation below 10% by then, but if we are to discuss loosening of monetary policy we need at least several months of confirmation that single-digit inflation is a permanent phenomenon and not a one-time event, reached by low-base effect." (10.07.2023, Business Insider via Bloomberg)
P. Litwiniuk	3.7	"The government has to date declared a budget policy neutral for inflationary processes but it is changing. (...) The question is what will change and how many more ideas will be presented in the frame of the election campaign - this could have a negative impact on inflationary processes." (15.06.2023, TOK FM, PAP)
H. Wnorowski	2.7	"In September, inflation will certainly be clearly below 10%. But this is only one premise, although very important, maybe even weighing 50%. I am not set on any decision at a particular meeting. The information that will then be available will be important." (13.07.2023, Parkiet, PKO transl.)
A. Glapinski	2.4	"The MPC has decided that we are ending the cycle of rate hikes. Officially, we were in the tightening cycle, we were ready all the time to raise rates, now we are putting this weapon aside. No one expects something like this to happen anytime soon (...) Of course, if something happens, in the emergency mode, we can take that action, but we are no longer in that mode" (7.07.2023, NBPTv, PAP)
C. Kochalski	2.4	"In the light of the current data and information, a room for potential discussion of [rate] cuts may appear in some time, as we have already ended the hikes cycle. The very calendar indicates it could be after the summer vacation at the earliest. (...) We're still before a potential discussion on rate cuts, which sooner or later needs to happen." (13.07.2023, Interia.pl via Bloomberg).
W. Janczyk	2.0	"The current rates level seems adequate given the information we have today. (...) " in my opinion, in the course of the last few weeks, there has come no information that would prompt resumption of rate hikes in December. Currently, no premises can be seen that would prompt such steps." (2.12.2022, PAP).
I. Duda	2.3	"Good data may indeed encourage discussion on interest rate cuts, however, for the MPC to decide about the interest rate cut, the entire Council must see that the downward trend is permanent and that inflation is indeed quickly approaching the target. These are the conditions necessary to make such a decision" (31.05.2023, Biznes24, PAP, PKO transl.)"
G. Maslowska	2.1	"The process of disinflation will continue and perhaps in the last quarter of this year interest rate cuts will be possible, which will relieve indebted borrowers and support economic growth. However, this will be possible only when we will be sure that inflation has been brought under control and is falling towards the NBP's inflation target" (29.06.2023, PAP)
I. Dabrowski	1.9	"(...) I think that there is a high probability that interest rates will remain at their current level until the end of September. If the MPC was to consider a motion to cut interest rates, it would rather happen in October (...) Although if we saw a rapid decline of the index by another 5p. in the summer months, and we would find ourselves at clearly single-digit inflation levels, I cannot rule out that this will happen in September." (26.06.2023, PAP)

*the higher the indicator the more hawkish views. The positioning has been made based positively on PAP survey conducted among economists at banks in Poland (scale 1-5). ^Quotes in bold have been modified in this issue of Poland Macro Weekly.

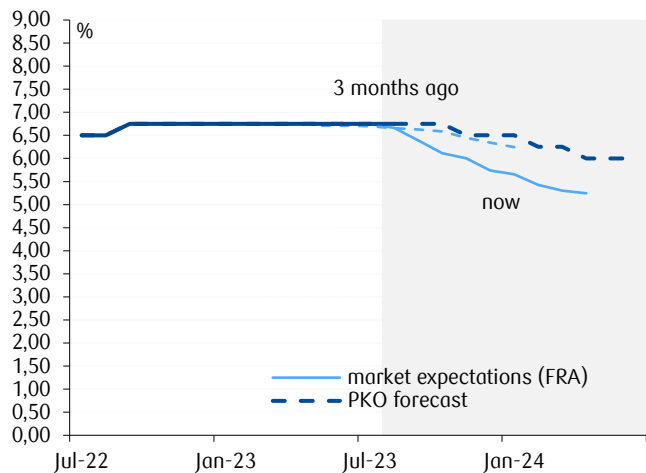
Interest rates – PKO BP forecasts vs. market expectations

		1M	2M	3M	4M	5M	6M	7M	8M	9M
Date	13-Jul	13-Aug	13-Sep	13-Oct	13-Nov	13-Dec	13-Jan	13-Feb	13-Mar	13-Apr
WIBOR 3M/FRA†	6,84	6,71	6,43	6,14	5,94	5,63	5,50	5,27	5,09	5,04
implied change (b. p.)		-0,14	-0,41	-0,71	-0,90	-1,21	-1,35	-1,57	-1,75	-1,81
MPC Meeting	6-Jul	-	6-Sep	4-Oct	8-Nov	6-Dec	-	-	-	-
PKO BP forecast*	6,75	6,75	6,75	6,75	6,50	6,50	6,50	6,25	6,25	6,00
market pricing^		6,62	6,34	6,05	5,95	5,69	5,61	5,38	5,20	5,15

WIBOR 3M from the last fixing, FRA transactions based on WIBOR 3M for subsequent periods, †in basis points, *PKO BP forecast of the NBP reference rate.

Poland macro chartbook

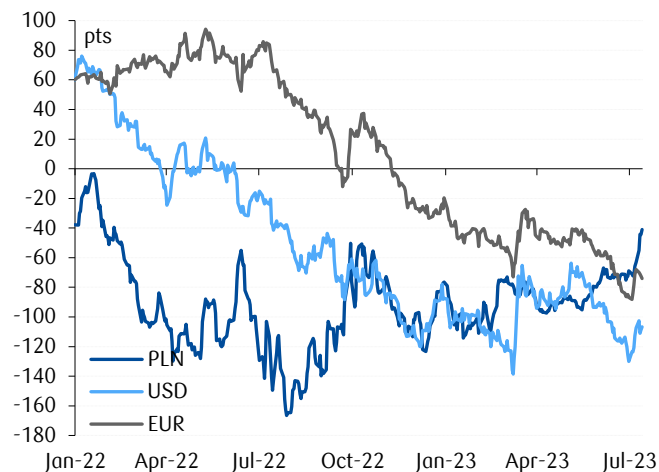
NBP policy rate: PKO BP forecast vs. market expectations



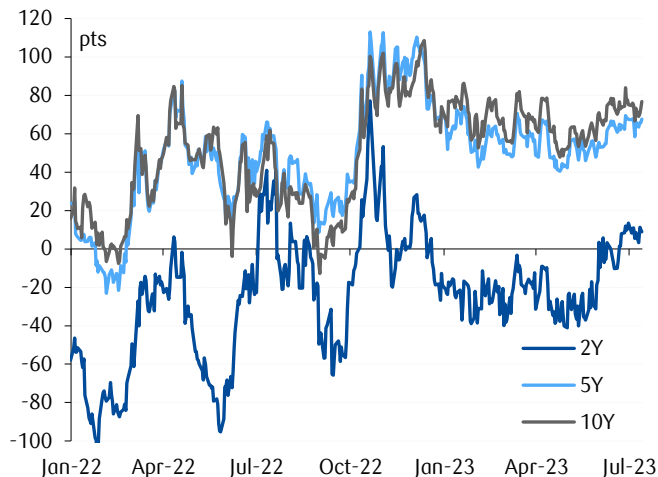
Short-term PLN interest rates



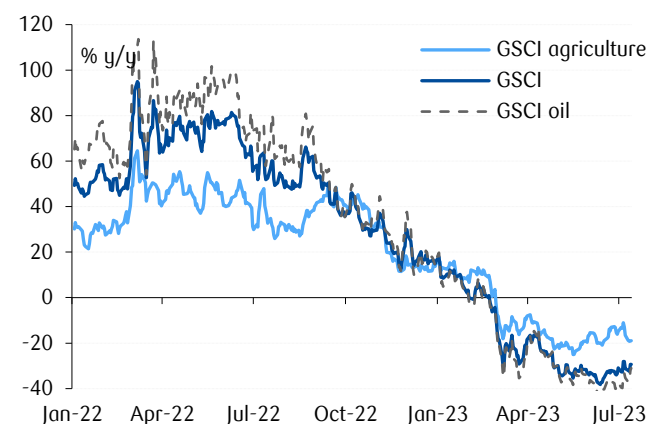
Slope of the swap curve (spread 10Y-2Y)*



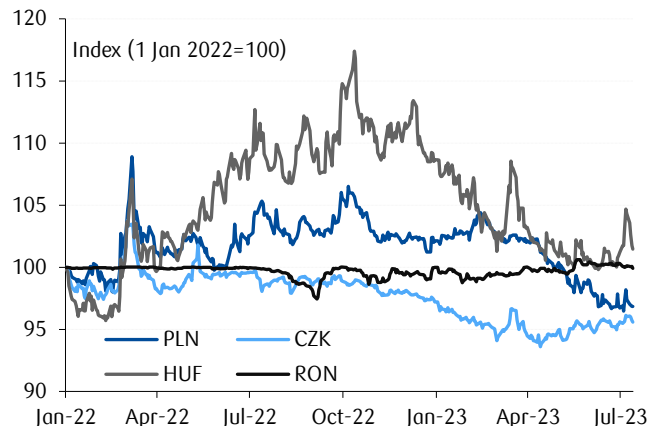
PLN asset swap spread



Global commodity prices (in PLN)

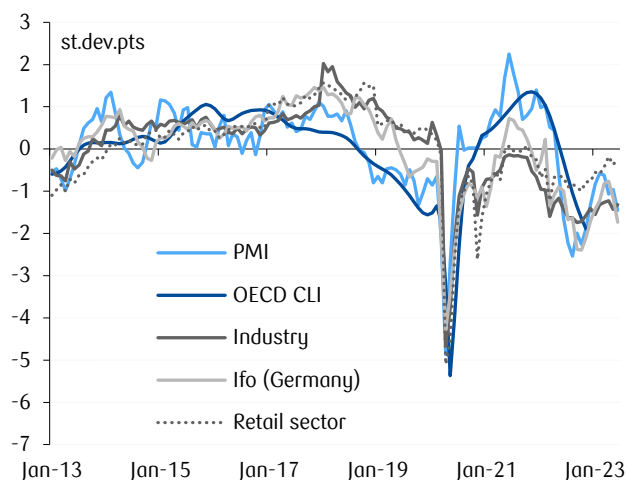


Selected CEE exchange rates against the EUR

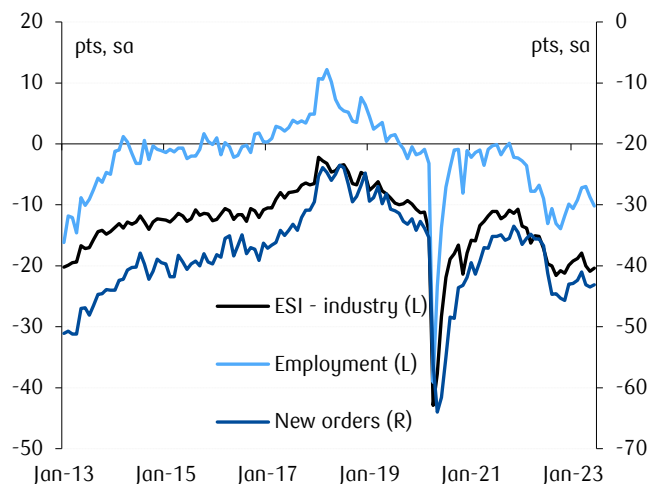


Source: Datastream, NBP, PKO Bank Polski. *for PLN, and EUR 6M, for USD 3M.

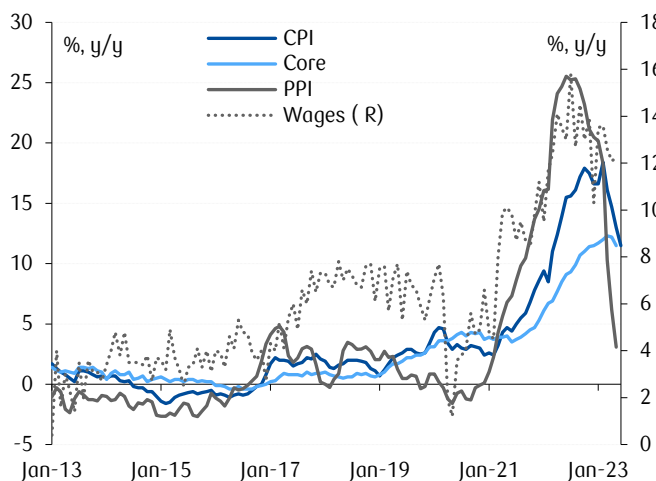
Economic sentiment indicators



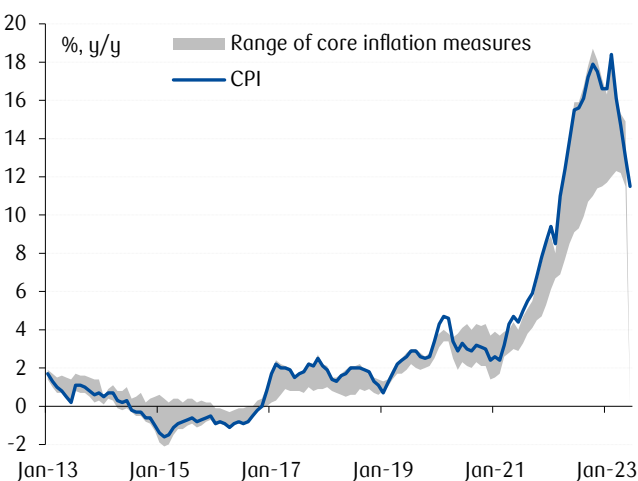
Poland ESI for industry and its components



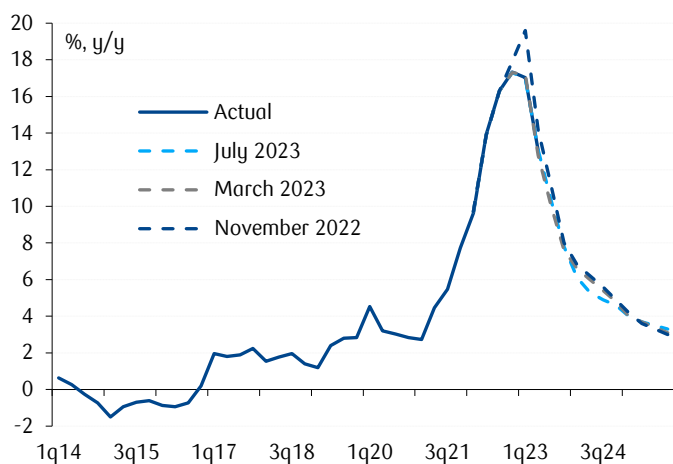
Broad inflation measures



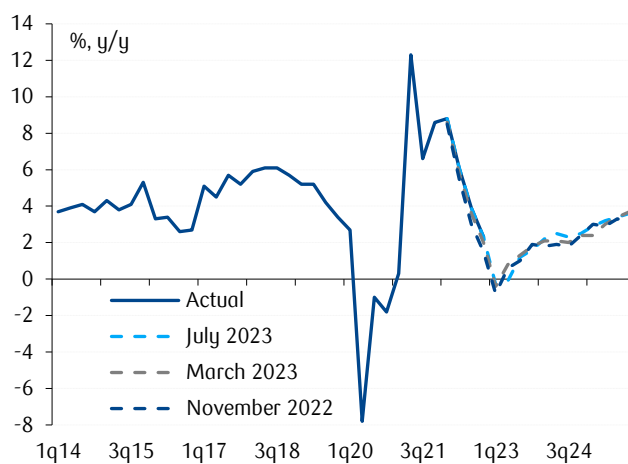
CPI and core inflation measures



CPI inflation - NBP projections vs. actual

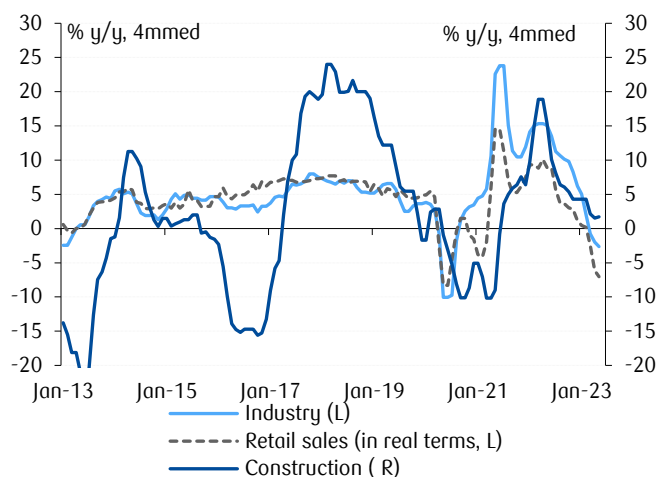


Real GDP growth - NBP projections vs. actual

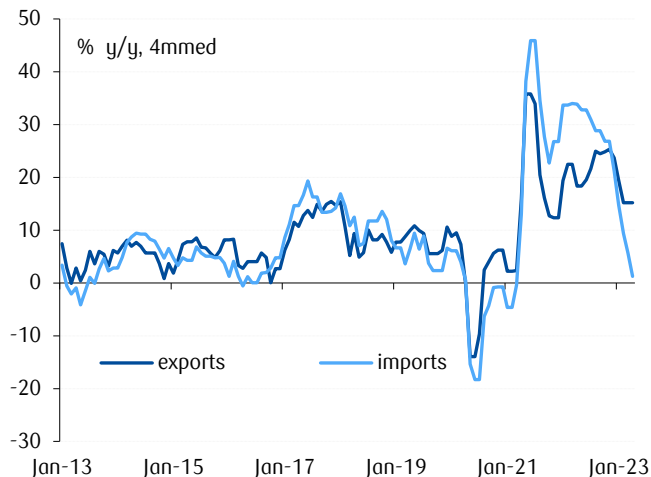


Source: Datastream, GUS, EC, NBP, PKO Bank Polski.

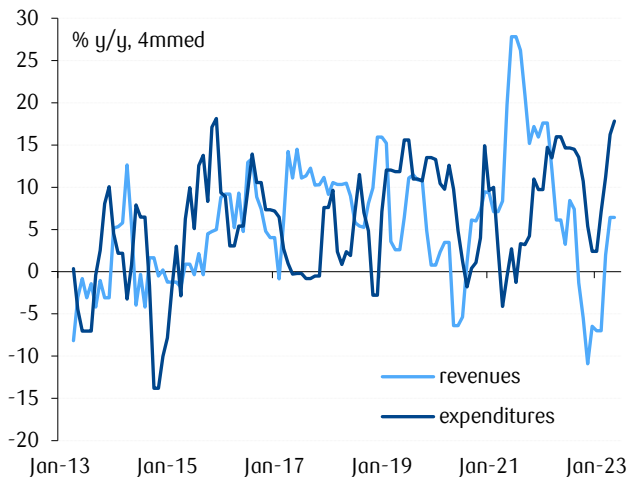
Economic activity indicators



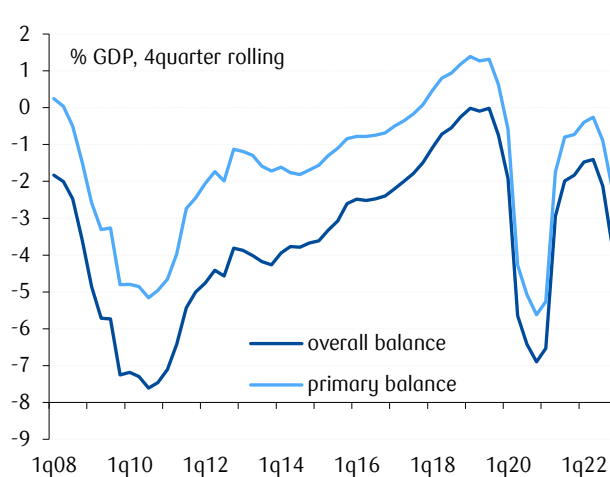
Merchandise trade (in EUR terms)



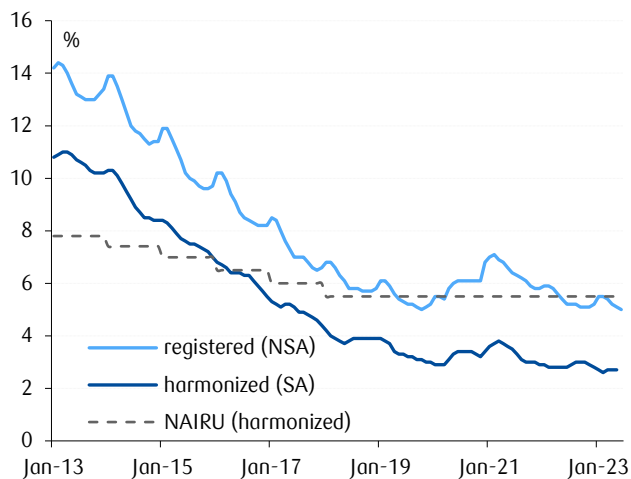
Central government revenues and expenditures*



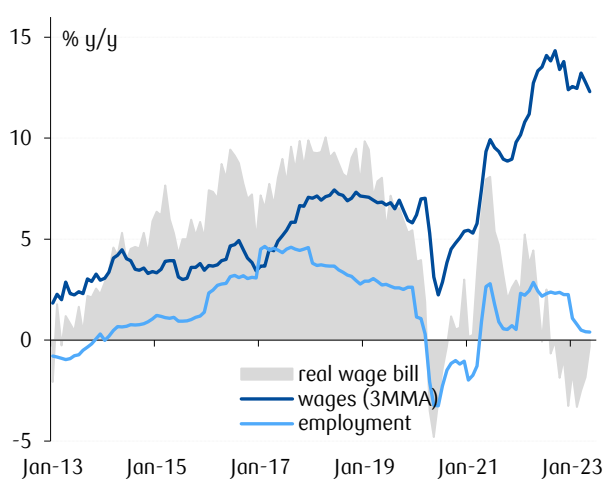
General government balance (ESA2010)



Unemployment rate

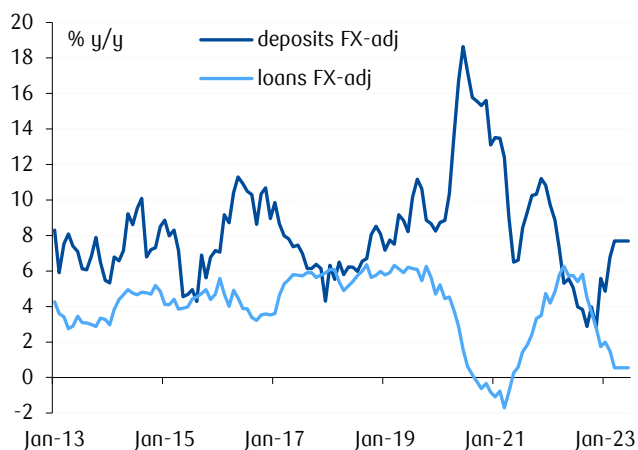


Employment and wages in the enterprise sector

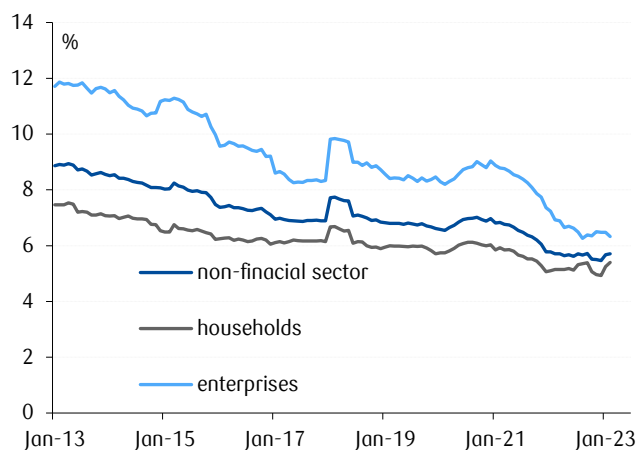


Source: NBP, Eurostat, GUS, MinFin, PKO Bank Polski. *break in series in 2010 due to methodological changes.

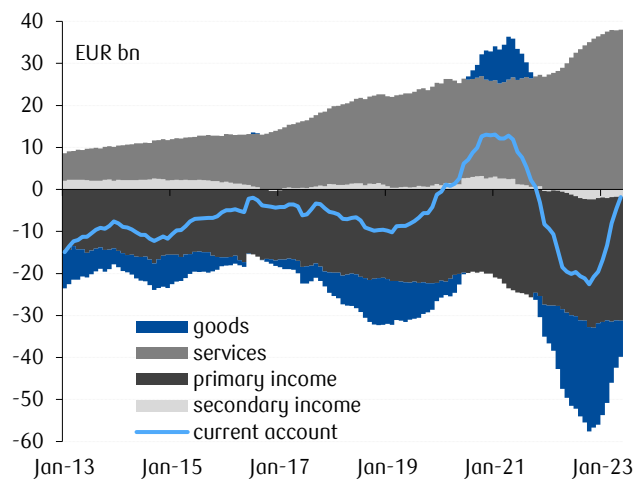
Loans and deposits



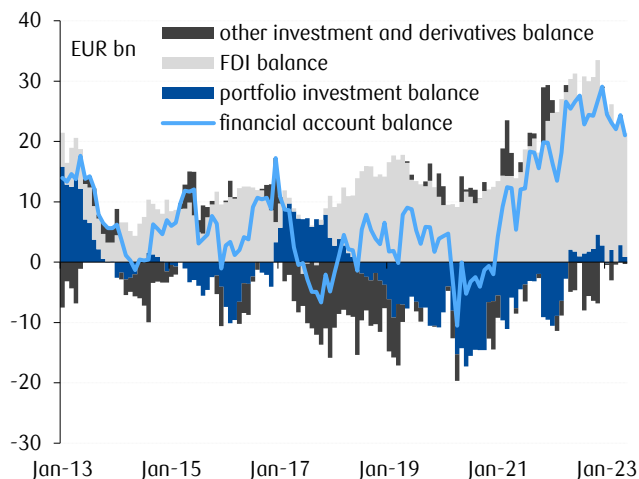
Non-performing loans (NPLs) - by sectors*



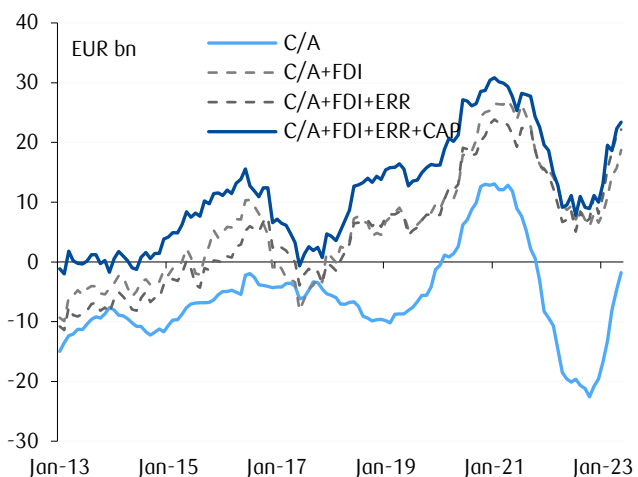
Current account balance



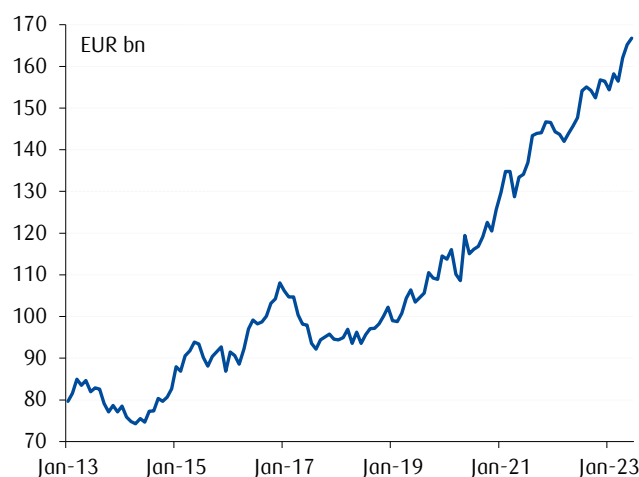
Financial account balance



External imbalance measures



NBP FX reserves (in EUR terms)



Source: NBP, PKO Bank Polski. *break in series in Jan2018 due to methodological changes.

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- [A soft landing scenario](#) (June 23, 2023)
- [External position rapidly improving](#) (June 16, 2023)
- [Exports shine, disinflation continues](#) (June 2, 2023)
- [No fireworks at the start of 2q](#) (May 26, 2023)
- [A surprisingly smooth start into 2023](#) (May 19, 2023)
- [MPC changes nothing](#) (May 12, 2023)
- [CPI keeps falling down](#) (Apr 28, 2023)
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- [Polish MPC still in a pause mode](#) (Apr 14, 2023)
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- [Corporate profits dwindle, margins narrow](#) (Mar 24, 2023)
- [Inflation never ceases to surprise](#) (Mar 17, 2023)
- [Spring is coming after all](#) (Mar 10 2023)
- [Consumers under pressure](#) (Mar 3 2023)
- [Bumpy road ahead](#) (Feb 24 2023)
- [Inflation peak not as scary as feared](#) (Feb 17 2023)
- [Nothing to see here](#) (Feb 10, 2023)
- [Growth less inflation-prone](#) (Feb 3, 2023)
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- [A soft patch](#) (Nov 18, 2022)
- [Monetary policy dilemmas \(again\)](#) (Nov 4, 2022)
- [Is Poland crisis resilient?](#) (Oct 28, 2022)
- [Not great, not terrible](#) (Oct 21, 2022)

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