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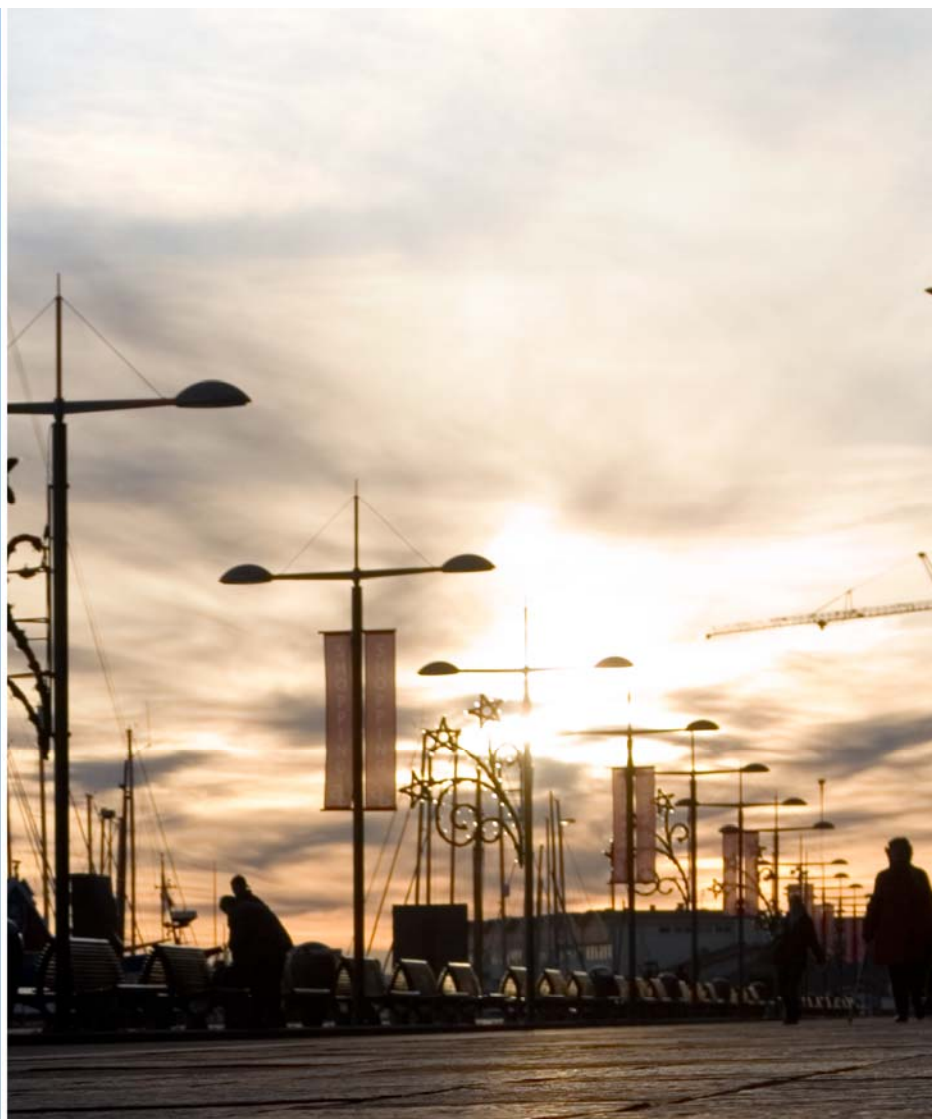
Poland Monthly

More rate cuts to come?

Economic outlook remains gloomy

National Bank has further to go

Weaker zloty, but downside capped



Macro Research | The world view from a Nordic perspective

POLAND

More rate cuts to come?

Against the backdrop of doubts surfacing over the outlook for China, a lack of confirmation in hard data that Germany is recovering and risk-off sentiment in global financial markets, Polish near-term prospects still look gloomy. In retrospect, the National Bank of Poland has been behind the curve in its assessment of the economy. It cut its policy rate again last week. Is that the final cut? Not quite yet is our view.

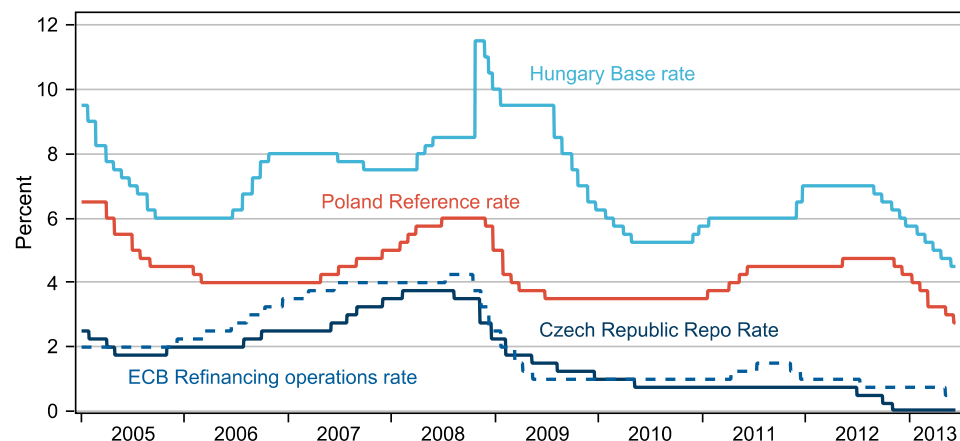
Low growth and low inflation

Polish growth turned out to be weaker than expected in Q1, with real GDP increasing by only 0.5 percent from the year before. The increase was entirely driven by net exports. At the same time, headline inflation has fallen continuously and was down to 0.8 percent in April. There was a slight uptick in core inflation that month, but the overall picture suggests that there is considerable slack in the economy. Clearly, inflation is significantly below the official target range and the risk of a rebound in the near future seems low.

Lacklustre external environment

The external environment also looks lacklustre. The data flow from China has not been overly encouraging so far this year. There are hopes that things will improve moving into the second half, but that is a forecast yet to be confirmed in hard data. The US seems to be on track to continue recovering and has made remarkable progress in mending its public finances. However, the flip side is that there is talk of the Federal Reserve starting to phase out its asset purchases. The latter has dominated sentiment in financial markets. It all adds up to rather gloomy conditions for Poland.

Policy rates



Source: Macrobond

The National Bank has cut rates more than it expected

With households and firms unwilling to spend, weak external demand, high unemployment and no inflationary pressures, it is not surprising that the National Bank has brought down its policy rate. Since November 2012, the policy rate has been cut by a total of 200bp. Is the cut last week also the final cut? We do not think so. There is still further room. Governor Belka has said that he wants to maintain a positive real rate. Based on current inflation, that would imply significant scope for additional easing. However, Belka most likely had in mind expected inflation, which is currently above 2 percent for 2014 and a notch higher for 2014. Against that background, we would suggest that the central bank is ready to cut its policy rate by another 25bp in July, after which it will most likely stay on hold.

Weaker zloty has potential to make a comeback

The weak state of the economy and the corresponding interest rate outlook has also made a mark in the FX market. After being traded in a range of 4-4.20 since last summer, the EURPLN has recently weakened, briefly moving above 4.30 before the National Bank stepped into the market. That tells us something about the National Bank's perspectives on the currency. It could be expected to buy the zloty if that level is approached again. Taking

a somewhat longer view, we think that the PLN, much like the SEK, has the potential to make a comeback. Despite the National Bank's easier monetary policy, Fundamentals are still attractive relative to those of the eurozone. Needless to say, both the interest rate and FX outlook could be impacted should the economy underperform again.

Financial forecasts

	12-Jun	<3mth	<6mth	<12mth
Policy interest rates				
Czech Republic	0.25	0.25	0.25	0.25
Hungary	4.50	4.25	4.00	4.00
Poland	2.75	2.50	2.50	2.50
EMU	0.50	0.25	0.25	0.25
USA	0.13	0.13	0.13	0.13
10-year bond yields				
Czech Republic	2.13	1.75	1.85	2.10
Hungary	6.38	5.30	5.15	5.10
Poland	3.93	3.55	3.40	3.85
Germany	1.59	1.30	1.40	1.60
USA	2.17	2.00	2.10	2.30
Exchange rates				
EUR/CZK	25.66	25.50	25.50	25.25
EUR/HUF	296	300	310	320
EUR/PLN	4.25	4.25	4.15	4.00
EUR/USD	1.33	1.27	1.23	1.10
EUR/SEK	8.68	8.70	8.30	8.20
SEK/PLN	0.49	0.49	0.50	0.49

Source: Handelsbanken Capital Markets

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