Minutes of the Monetary Policy Council decision-making meeting held on 6 July 2023

At the meeting it was pointed out that the economic conditions in the environment of the Polish economy remained subdued. In the euro area activity growth had been constrained in recent quarters. It was emphasised that the euro area economy was expected to rebound in the coming quarters; however, the scale of the recovery would be rather modest, and in Germany, according to forecasts, GDP would fall in 2023. In the United States the current economic conditions remained better than in the euro area, although forecasts indicated their possible weakening.

The Council members underlined that global inflation was declining, but continued to be elevated. CPI inflation in the United States had fallen to 4.0% in May, while HICP inflation in the euro area had fallen to 5.5% in June. In Central and Eastern European countries inflation had also declined. It was pointed out that in recent months core inflation had also begun to decline in many economies, although it remained elevated.

Forecasts signalled a further fall in global inflation in the coming quarters. This was supposed to result from both the fading of the earlier supply shocks and the significant global monetary tightening and the related weakening of economic activity. The continuation of the disinflation process is indicated by the significant fall in cost and price pressure, including a sharp decline in PPI inflation.

At the Council meeting it was pointed out that the central banks in the United States and the euro area forecasted that price growth would decline only gradually. As a result, inflation in these economies might still slightly exceed the inflation targets in 2025. It was underlined that the future pace of disinflation in the environment of the Polish economy would be determined in particular by the situation in the labour markets and enterprises' price policy. In this context, attention was drawn to the significant role of growth in corporate mark-ups and profits in shaping prices in recent quarters.

Amid subdued economic growth around the world, activity growth had also slowed down in Poland. The Council members stressed that May 2023 was the third month in a row in which retail sales had fallen sharply in annual terms. Consequently, it was pointed out that in 2023 Q2 the fall in household consumption had most likely deepened. Industrial as well as construction and assembly output had also declined in annual terms in May 2023. At the same time, it was highlighted that the situation in the labour market had not

Narodowy Bank Polski ul. Świętokrzyska 11/21 00-919 Warszawa, Poland phone +48 22 185 28 88 sekretariat.rpp@nbp.pl

changed significantly. It was observed that employment continued to rise in the services sector, while industry saw a fall in employment. This was accompanied by steady wage growth in the enterprise sector.

While discussing the economic activity outlook in Poland, the Council members indicated that in line with the NBP's July projection, GDP growth would be low in 2023. It was underlined that consumption growth might be negative throughout the whole of 2023, which would support the disinflation process. Although according to the July projection the coming quarters were to see some recovery in activity – amid a rise in real wages and the fading of the negative supply shocks – GDP growth was expected to remain moderate and the output gap negative over the projection horizon.

At the Council meeting it was underlined that – in line with earlier predictions – inflation declined significantly. According to the Statistics Poland flash estimate, CPI inflation fell to 11.5% y/y in June 2023. It was observed that in the last four months inflation had declined by about 7 percentage points, and that June was the second month in a row in which the overall consumer price level had remained unchanged from the previous month. Attention was drawn to a further drop in energy prices and a decline in food prices compared to the previous month.

Therefore, the majority of the Council members argued that the still high annual inflation rate was not resulting from current growth in the overall price level, but was reflecting past price changes in previous periods. It was pointed out that based on available data, it could be estimated that in June price growth of all the main groups included in the basket of consumer goods and services had declined, and that in particular core inflation had probably fallen markedly. The Council members also observed that PPI inflation had fallen rapidly in recent quarters and producer price growth in the manufacturing sector had already been negative in May 2023.

Certain Council members expressed the opinion that price-setting processes in Poland, like in other countries, were currently following a different pattern than in a low inflation period. In the view of these Council members, the decline in the annual CPI index mainly reflected the base effects and the fall in commodity prices, while inflation expectations – despite declining – continued to be high, and inflation both in Poland and aboard remained persistent. These Council members also underlined the improvement in the expected labour market situation envisaged in several previous NBP projections, which could support higher inflation.

However, while discussing the outlook for inflation in Poland, the majority of the Council members pointed out that in line with the July projection, in the coming quarters inflation would keep declining and in the second half of 2025 it would reach a level consistent with the NBP inflation target. This would be supported by the fading of the earlier shocks in commodity markets and the global supply chain disruptions, strong monetary policy tightening undertaken by NBP and the slowdown in aggregate demand growth. In the opinion of these Council members, the currently observed strong fall in PPI inflation, the reduction in value of loans to the non-financial sector and the declining inflation expectations of consumers and enterprises would also contribute to a fall in CPI inflation. It was judged that the disinflation process was also supported by the marked appreciation of the zloty observed in recent months.

Some Council members drew attention to the fact that relatively high wage growth could be a risk factor for the inflation outlook in Poland. However, the majority of the Council members judged that the weakening economic conditions would curb enterprises' ability to raise prices further and that firms would be able to absorb rising costs, including labour costs, by reducing their margins, which had been high in the previous quarters.

The majority of the Council members assessed that the weakening of the external economic conditions, together with lower commodity prices, would continue to curb global inflation, which would still contribute to lower price growth in Poland. The decline in domestic inflation would be supported by the weakening of domestic GDP growth, including the continued decline in consumption, amid a significant decrease in credit growth. The majority of the Council members assessed that the strong monetary policy tightening undertaken by NBP has been leading to a decline in inflation in Poland towards the NBP inflation target. At the same time, given the strength and persistence of the earlier shocks, which remained beyond the impact of domestic monetary policy, the return of inflation to the NBP inflation target would be gradual. Alongside that, it was underlined that the Council flexibly determined the desirable time necessary to bring inflation back to the target, as bringing inflation rapidly back to the target might entail significant costs to macroeconomic and financial stability. The Council members upheld the assessment that the decrease in inflation would be faster if supported by an appreciation of the zloty exchange rate, which, in the Council's assessment, would be consistent with the fundamentals of the Polish economy.

The majority of the Council members recognised that, taking into account the above conditions, and in particular the significant decline in inflation and its expected further gradual decline, as well as the weakening of the domestic economic conditions, including the consolidating fall in consumer demand, decline in inflation expectations, low growth in monetary and credit aggregates, and also the decline in inflationary pressure abroad combined with the risks to the global economic outlook, and taking into account the earlier strong monetary policy tightening, it was warranted to end the monetary policy tightening cycle. At the same time, certain Council members pointed out that the significant fall in inflation and declining inflation expectations amid unchanged interest rates were contributing to an increase in the restrictiveness of monetary policy. Under these circumstances, and also considering the prospect of a further fall in inflation and low economic activity growth, in the coming months it might be justified to consider lowering of the NBP interest rates.

The view was expressed that given the persistently high annual price growth and elevated inflationary expectations, the current level of the NBP interest rates was too low to ensure the return of inflation to the target in the medium term and to lower inflation expectations to levels consistent with the medium-term inflation target.

The Council decided to keep the NBP interest rates unchanged: the reference rate at 6.75%, the lombard rate at 7.25%, the deposit rate at 6.25%, the rediscount rate at 6.80%, and the discount rate at 6.85%.

The Council pointed out that further decisions of the Council would depend on incoming information regarding prospects for inflation and economic activity.

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