Minutes of the Monetary Policy Council decision-making meeting held on 3 July 2024

During the discussion at the meeting of the Monetary Policy Council it was noted that the economic conditions in Poland's main trading partners was gradually improving, but remained markedly weakened. It was pointed out that in 2024 Q1 consumption growth in the euro area had been lower than households' real disposable income growth, which indicated that households may have used part of their income to increase savings. In 2024 Q2 GDP growth in this economy was probably low again, and, in particular, in Germany annual GDP growth may have been close to zero. It was underlined that activity in Europe's industrial sector was particularly weakened, while in services the situation is relatively better. It was mentioned that forecasts for the next quarters indicated a rather gradual economic recovery in the euro area. In turn, the economic situation in the United States was still markedly better than in the euro area and, according to available forecasts, it would remain so in the coming periods.

When discussing inflation processes abroad, the Council members noted that in many economies price growth continued to run slightly above the inflation targets of the central banks. At the same time, it was stressed that in the largest advanced economies core inflation was higher than headline inflation. This is due to the still elevated service price growth amid a strong disinflation of goods prices.

The Council members drew attention to the fact that the European Central Bank had cut interest rates in June 2024. Meanwhile, the Federal Reserve of the United States continued to keep interest rates unchanged.

While discussing economic activity in Poland, the Council members assessed that a gradual economic recovery was continuing, although recent data were mixed. It was pointed out that annual GDP growth in 2024 Q2 had probably been higher than in 2024 Q1. When analysing monthly data, it was observed that retail sales had risen by 5% in annual terms in May 2024. In turn, industrial as well as construction and assembly output in May were lower than a year ago. It was underlined that the poor condition of the industrial sector was also evidenced by sentiment indicators, including the PMI index, which was probably partly connected with the ongoing downturn in the German industry.

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With regard to the labour market conditions, it was noted that in May wage growth in the enterprise sector was slightly higher than in April, which amid only slightly higher inflation meant that real wage growth remained high. At the same time, employment in this sector declined once again, particularly in industrial enterprises.

During the discussion, attention was drawn to the rise in value of household consumption loans in the recent period, while noting that in the case of housing loans their monthly increases were declining. The weakening of lending in the housing loans segment was probably related to the closure of the applications acceptance for the "Safe Mortgage" programme. It was also pointed out that the so-called repayment holidays boosted disposable income of some households. While discussing the financial situation of consumers, certain Council members indicated that in recent years households' bank debt had fallen, particularly in real terms. The Council members highlighted that annual corporate credit growth remained low.

Referring to the economic activity outlook, the Council members pointed out that according to the July projection the economic recovery should continue in the coming quarters. Therefore, GDP growth would probably be higher in 2025 than in 2024 whereas, according to the projection, in the following year it may slow down slightly.

At the meeting it was noted that according to the Statistics Poland flash estimate, CPI inflation was 2.6% y/y in June 2024 (compared to 2.5% in May). It was underlined that for a second consecutive quarter price growth was in line with the NBP medium-term inflation target (2.5% +/- 1 p.p.). Annual growth in prices of food and non-alcoholic beverages rose in June 2024, while annual growth in energy prices declined. It was estimated that in June inflation net of food and energy prices had once again decreased, although it remained higher than the CPI inflation. This was a result, in particular, of the still elevated growth in services prices due to high wage growth, amid the relatively high share of wages in the costs of the service sector.

The Council members pointed out that the sharp annual fall in producer prices had continued recently, confirming the fading of most external supply shocks and cost pressure reduction. Together with the relatively low – despite some acceleration – economic activity growth, this was conducive to limiting inflation. It was judged that inflation was also curbed by the appreciation of the zloty exchange rate, which was consistent with the fundamentals of the Polish economy. The majority of the Council members indicated that the current level of interest rates was a factor which should limit inflationary pressure also in the medium term. Certain Council members were of the opinion that given the anticipated increase in inflation in the coming quarters and the related possible rise in inflation expectations, real interest rates would decrease.

When discussing the inflation outlook, the Council members noted that according to the July projection, inflation would probably increase in the subsequent quarters, running at a level markedly above the NBP inflation target. It was emphasised that this would take place amid the ongoing economic recovery and the strong rise in wages. It was pointed out that, in these circumstances, what mattered for the medium-term outlook was how the expected increase in inflation would affect inflation expectations and wage growth, and how households' propensity to consume and save would evolve. It was underlined that the acceleration of energy prices in the second half of 2024 should be seen as a supply shock which temporarily boosts inflation but also reduces households' disposable income. Certain Council members highlighted the fact that the July projection signalled also higher food price growth in the subsequent quarters stemming from the lagged effects of the VAT rate increase and the higher agricultural commodity prices. In this context, the Council members pointed out that in line with the *Monetary Policy Guidelines*, the medium-term nature of the inflation target means that due to macroeconomic and financial shocks, inflation may temporarily deviate from the target and even run outside the band for deviations from the target. It was emphasised that the response of monetary policy to shocks is flexible and depends on their causes and the assessment of persistence of their consequences, including the impact on inflation developments. At the same time, it was observed that according to the latest projection, prepared under the assumption of unchanged NBP interest rates, inflation would return to the NBP target in 2026. This suggests that there is no need for an interest rate rise in response to the anticipated increase in inflation in the coming quarters.

The Council members noted that fiscal policy remained a risk factor for the inflation outlook. It was stressed that so far some of the proposed fiscal measures had still not been implemented, such as the increase in the amount of social benefits or the introduction of new ones. At the same time, attention was drawn to the fact that Poland might become subject to the excessive deficit procedure, although at this stage it was difficult to assess what impact it would have on fiscal policy in the coming years. The persistence of other significant sources of uncertainty was also underlined, including the tense geopolitical situation, commodity price developments and the economic conditions in Poland's main trading partners.

The majority of Council members assessed that despite the observed economic recovery, demand and cost pressures in the Polish economy remained relatively low, which, amid weakened economic conditions and lower inflation pressure abroad, curbed domestic inflation pressure. However, demand pressure in the domestic economy is stimulated by a marked wage growth, stemming, i.a. from wage increases in the public sector. In the coming quarters, consumer price growth is likely to increase and will be running above the NBP inflation target, which will be driven by higher energy prices. When the impact of energy price increase fade – amid the current NBP interest rates level – inflation should return to the medium-term NBP target, although the impact of higher energy prices on the inflation expectations is an uncertainty factor. The inflation developments over the medium term will be also affected by the further fiscal and regulatory policy measures, the pace of economic recovery in Poland and the labour market conditions. Against this background, the Council decided to keep the NBP interest rates unchanged. The Council judged that the current level of the NBP interest rates was conducive to meeting the NBP inflation target in the medium term.

A view was expressed that given the forecast rise in inflation, as well as the recovery in consumer demand and high wage growth, the current level of NBP interest rates was too low to ensure the sustainable return of inflation to the target in the medium term.

The Council decided to keep the NBP interest rates unchanged: the reference rate at 5.75%, the lombard rate at 6.25%, the deposit rate at 5.25%, the rediscount rate at 5.80%, and the discount rate at 5.85%.

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

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