NARODOWY
BANK POLSKI

Monetary Policy Council

Monetary Policy Guidelines for 2025

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Warsaw, 2024

In setting the *Monetary Policy Guidelines for 2025*, the Monetary Policy Council, hereinafter the "Council", fulfils the requirements of Article 227 Section 6 of the Constitution of the Republic of Poland, which obligates it to formulate monetary policy guidelines and present them to the Sejm on an annual basis.

In the *Monetary Policy Guidelines for 2025* the Council has maintained the monetary policy strategy pursued by Narodowy Bank Polski, hereinafter "NBP", so far. Price stability remains the main statutory objective of monetary policy. At the same time, monetary policy will be conducted in a way that helps maintain sustainable economic growth and financial stability.

NBP will continue to pursue the strategy of a medium-term inflation target at 2.5%, with a symmetric band for deviations of +/-1 percentage point. NBP's interest rates will remain the principal instrument of monetary policy. Monetary policy will continue to be implemented under the floating exchange rate regime. However, NBP does not rule out interventions in the foreign exchange market. The scope, manner and scale of using monetary policy instruments by NBP will take into account in a flexible way the determinants of monetary policy implementation, including in particular market conditions as well as economic consequences of the severe global shocks of the recent years, including consequences of the COVID-19 pandemic and Russia's military aggression against Ukraine.

The *Monetary Policy Guidelines for 2025* is a translation of the publication of Narodowy Bank Polski entitled *Założenia polityki pieniężnej na rok 2025*. In case of discrepancies, the original prevails.

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Chapter 1. Monetary policy strategy

According to Article 227 Section 1 of the Constitution of the Republic of Poland (Journal of Laws of 1997, item 483; Journal of Laws of 2001, item 319; Journal of Laws of 2006, item 1471; Journal of Laws of 2009, item 946), "Narodowy Bank Polski shall be responsible for the value of Polish currency". The Act on Narodowy Bank Polski of 29 August 1997 (Journal of Laws of 2022, item 2025) states in Article 3 Section 1 that, "The basic objective of the activity of NBP shall be to maintain price stability, while supporting the economic policy of the Government, insofar as this does not constrain the pursuit of the basic objective of NBP."

Fulfilling the main obligations of NBP laid down in the Constitution of the Republic of Poland and in the Act on Narodowy Bank Polski, the Council strives to maintain price stability. At the same time, monetary policy is conducted in a way that helps maintain sustainable economic growth and financial stability.

The Council has been pursuing the price stability objective by using inflation targeting strategy. Under this strategy, since 2004 the monetary policy objective has been to keep inflation – understood as the annual change in the consumer price index – at 2.5% with a symmetric band for deviations of +/-1 percentage point in the medium term.

The medium-term nature of 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. 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. Each time inflation deviates from the target, the Council flexibly determines the desirable time necessary to bring it back to the target, as bringing inflation rapidly back to the target may entail significant costs to macroeconomic and financial stability. When deciding on the changes of monetary policy parameters, the Council takes into consideration price adjustments taking place in the economy, whose sources are beyond the impact of domestic monetary policy. In current conditions, these adjustments are mostly related to the severe global economic shocks of recent years caused by the COVID-19 pandemic and Russia's military aggression against Ukraine as well as to the effects of the structural changes taking place in the economy, including the energy transition, and to the process of Poland's convergence to the more advanced economies.

The monetary policy strategy pursued by the Council assumes flexibility of the instruments applied. This means that the range of instruments used by NBP can be adapted to the nature of disturbances observed in the economy and market conditions. The flexible use of monetary policy instruments is conducive to effective functioning of the transmission mechanism as well as macroeconomic and financial stability.

While taking monetary policy decisions, the Council considers the time lags in the transmission mechanism of monetary policy. The time lag between a decision on monetary policy parameters and its peak impact on real variables (such as output or employment) and on inflation takes several quarters and may change over time. Moreover, monetary policy is conducted under uncertainty, in particular about future economic developments.

Stabilising inflation at a low level is an important, yet insufficient condition to maintain balance in the economy, which, in turn, supports price stability in the long term. Imbalances in the financial sector may pose a threat to long-term price stability. Those imbalances should be counteracted mainly by macroprudential policy aimed at reducing systemic risk and in that manner supporting long-term, sustainable economic growth. This is important especially amid the free movement of capital and highly integrated financial markets. Monetary policy conducted by the Council supports macroprudential policy and in particular is conducive to financial system stability and mitigates the risk of imbalances building up in the economy by taking into account developments in asset prices (including real estate prices) and lending growth, insofar as this does not constrain the pursuit of the basic objective of NBP.

Besides monetary and macroprudential policy, fiscal policy plays an important role in maintaining macroeconomic stability. A fiscal policy which mitigates the impact of economic shocks, while ensuring long-term stability of public finance, is necessary to maintain macroeconomic stability.

The Council implements the inflation targeting strategy under the floating exchange rate regime. The floating exchange rate regime does not rule out interventions in the foreign exchange market whenever it is warranted by market conditions or conducive to ensuring the country's macroeconomic or financial stability.

Monetary policy communication is an important element of the Council's inflation targeting strategy. Thus, the Council's decisions together with their determinants are presented in the press releases (*Information from the meeting of the Monetary Policy Council*), as well as in the *Minutes of the Monetary Policy Council decision-making meetings*, *Inflation Reports*, *Monetary Policy Guidelines* and the *Report on Monetary Policy*. Furthermore, the Council's decisions and their determinants may be explained by the Governor of NBP at the press conferences and in the individual statements by the Governor of NBP or the members of the Council.

In line with the adopted strategy, in 2025 monetary policy parameters, including NBP interest rates, will be adjusted to the economic situation so as to ensure long-term price stability and, at the same time, support sustainable economic growth and financial stability.

Chapter 2. Monetary policy instruments in 2025

Determinants of monetary policy instruments

In 2025 the scope, manner and scale of use of monetary policy instruments by NBP will take into account the factors associated with its conduct. As in previous years, monetary policy instruments may be used in a flexible manner to account for the changing macroeconomic and market conditions.

The persistence of liquidity surplus in the domestic banking sector, expected by the central bank, will have a significant impact on the manner and scope of use of monetary policy instruments by NBP in 2025. For this reason, as in previous years, NBP's monetary policy instruments on a net basis will have a liquidity-absorbing nature. Banking sector liquidity in 2025 will be positively affected by the purchase of foreign currencies by NBP, mainly from the Ministry of Finance. The NBP sale of foreign currencies mainly to the European Commission, and a rise in currency in circulation, will have a curbing effect on the level of banking sector liquidity.

The operational target of NBP's monetary policy in 2025 will be to keep the POLONIA rate running close to the NBP reference rate. Depending on the market conditions, the level of the POLONIA rate may deviate from the NBP reference rate within the corridor set by the NBP deposit rate and lombard rate.

Interest rates

The key instrument of monetary policy in 2025 will be the NBP interest rates.

The NBP reference rate will determine the yield obtainable on the NBP main open market operations, while at the same time affecting the level of short-term market interest rates.

The NBP lombard rate will determine the interest on the lombard credit offered by NBP, allowing to obtain funds from the central bank on an overnight basis.

The NBP deposit rate will determine the interest rate on deposits, allowing to deposit funds with NBP on an overnight basis.

The discount rate will determine the interest on the bill discount credit.

Open market operations

The primary instrument which will be used to achieve the operational target of monetary policy will be the main open market operations. Through its main operations, NBP will affect liquidity conditions in the banking sector, and consequently the level of the POLONIA rate. These operations will normally be carried out on a regular basis, once a week, typically with a 7-day maturity. When conducting main operations, NBP will apply a fixed-rate tender procedure with the rate at the level of the NBP reference rate. Due to the expected further persistence of liquidity surplus in the banking sector in 2025, these operations will be carried out in the form of NBP bills issuance. The manner in which main operations are conducted may be modified if justified by a change in market conditions or parameters of NBP's monetary policy.

Fine-tuning operations will be an instrument supplementing main operations with regard to the achievement of the operational target of NBP monetary policy. Their use may be motivated by the need to provide liquidity to, or absorb liquidity from the banking sector. As part of liquidity-providing operations, NBP may offer repo transactions or redeem NBP bills before maturity. In the case of liquidity-absorbing operations, the central bank may issue NBP bills or offer reverse repo transactions. The maturity and the yield of these operations as well as the manner to conduct them will be aligned with the purpose of their application.

Structural operations may be conducted in order to change the liquidity structure in the banking sector in the long term, as well as to ensure the liquidity of the secondary market for debt securities or to strengthen the monetary transmission mechanism. As part of structural operations, NBP may purchase or sell debt securities in the secondary market, as well as issue NBP bonds.

Required reserve

The required reserve system will support the achievement of the operational target of NBP monetary policy, by stabilising the POLONIA rate. Averaged reserve requirement allows institutions subject to the reserve requirement the freedom to decide on the amount of funds held on the account with the central bank on particular days of the reserve maintenance period, provided that the average level of holdings at NBP accounts is maintained at a level not lower than the required reserve level. At the same time, the required reserve reduces the scale of NBP open market operations conducted to absorb liquidity surplus.

Changes in the required reserve ratios will depend on the conditions in which monetary policy will be pursued in 2025.

Standing facilities

Standing facilities offered by NBP are designed to limit the scale of the POLONIA rate fluctuations by stabilising liquidity conditions in the banking sector.

The lombard credit will enable banks to obtain overnight credit from NBP on each operating day. This credit is collateralised with assets accepted by the central bank, a list of which is published on the NBP website[1]. The interest rate on this credit, determining the marginal cost of obtaining funds from the central bank, in principle acts as a ceiling for the rates on the overnight interbank market transactions.

The deposit facility will allow banks to deposit their liquidity surpluses with the central bank on an overnight basis on each operating day. The interest on the overnight deposit in principle determines the floor for the rates on the overnight interbank market transactions.

The width of the corridor between the NBP deposit rate and lombard rate will be shaped in a way conducive to the effective transmission of monetary policy, taking into account the smooth functioning of the interbank short-term deposit market.

Bill discount credit

NBP may offer the bill discount credit aimed at refinancing loans granted to entrepreneurs by banks.

Foreign exchange swaps

NBP may carry out foreign exchange swaps. A foreign exchange swap is a transaction in which NBP purchases (or sells) the Polish zloty against a foreign currency in the spot market and, at the same time, resells (or repurchases) it under a forward contract at a specified date.

Foreign exchange interventions

NBP may intervene in the foreign exchange market.

[1] https://nbp.pl/en/statistic-and-financial-reporting/financial-markets/lombard-facility-repo

Chapter 3. Monetary policy determinants in 2025

External conditions

In the first half of 2024, the economic conditions in the external environment of the Polish economy remained subdued, despite some improvement. In the euro area, as well as in some of the Central and Eastern European countries, GDP growth stood below its long-term average. The consequences of previous years' supply shocks and the introduced monetary tightening were still negatively affecting economic growth. Meanwhile, economic activity growth in the United States in the first half of 2024 remained relatively high. Labour market condition in both Europe and the United States was favourable. Unemployment stood at low levels and wage growth remained rather high.

Inflation in the first half of 2024 – following a significant drop in 2023 – was somewhat above inflation targets in several economies, including the euro area and the United States. The factor contributing to lower inflation was waning of the severe supply shocks of previous years and the introduced tightening of monetary policy, as well as subsiding cost pressures translating into low annual growth in industrial producer prices. Core inflation in the first half of 2024 in the major advanced economies and the Central and Easter European countries was decreasing gradually, yet it remained higher than the headline inflation. Even though the growth in the prices of goods fell to a low level, services price growth remained relatively high, amid persistently elevated wage dynamics.

Available forecasts point to some acceleration of economic growth in the euro area in 2025, while the recovery in this economy will be gradual. In turn, economic growth in the United States – despite an expected weakening of GDP dynamics – will still be higher than in the euro area, according to forecasts. In both of these economies increasing private consumption will contribute to the economic growth, which will be supported by the favourable situation in the labour market and growth in real wages.

In line with the current forecasts, in 2025 inflation in the major economies will decrease slightly and may continue to marginally exceed inflation targets. Also core inflation will fall, which will be driven by waning of the previous supply shocks and their secondary effects on price processes and, in case of the euro area, the moderate scale of economic recovery. However, considering the relatively high growth in nominal wages, the disinflation process will be probably slowed down by the elevated dynamics of services prices and its only gradual decrease.

Domestic conditions

In the first half of 2024, economic activity growth in Poland accelerated, yet it was lower than its long-term average. GDP growth was supported by growing private consumption, amid a favourable situation in labour market, including low unemployment and high wage growth. As a consequence of weak economic conditions of Poland's trading partners, the contribution of net exports to GDP growth deteriorated significantly. Also dynamics of gross fixed capital formation outlays decreased, which was affected by the closure of their financing from the previous financial perspective of the European Union. In turn, a negative contribution of change in inventories was shallower than in 2023.

Growth in the consumer price index in the first half of 2024 decreased significantly compared to 2023. From February 2024, CPI stood at a level consistent with the NBP inflation target. The return of inflation to the target in this period was supported by waning of severe supply shocks of previous years, which translated into diminishing cost pressures and a fall in industrial producer price indices. Also the limited demand pressure, resulting partly from by the introduced tightening of the NBP monetary policy, contributed to lower inflation. Moreover, inflation was curbed by appreciation of the zloty.

Core inflation, likewise, fell significantly in the first half of 2024. Despite this – as in many other economies – it remained higher than the headline inflation, with a relatively high dynamics of services prices. Meanwhile, food price inflation, even though being considerably lower in the first half of 2024 than in 2023, increased since April 2024, due to reinstatement of VAT rate on staple food products from 0% to 5%. At the same time, energy prices, after decreasing in the first half of 2024 (in annual terms), since July 2024 rose markedly, which was caused by their partial unfreezing. In consequence, since July 2024 CPI inflation increased significantly and exceeded the NBP inflation target.

Available forecasts for 2025 point to an acceleration in GDP dynamics in Poland as compared to 2024. Private consumption will remain an important growth factor, but its dynamics will decrease, following a slower growth of household disposable income. In contrast, investment will pick up visibly in 2025, fuelled by an increased inflow of European Union's funds of the financial perspective 2021-2027. Amid a weak foreign demand, the contribution of net exports to GDP will be negative. According to forecasts, labour market situation will remain favourable, in particular unemployment rate will continue at a low level, however, nominal wage growth will decrease.

Inflation forecasts for 2025 predict that – after a strong rise in the second half of 2024 and the first quarter of 2025 – consumer price dynamics in Poland should gradually decrease towards the NBP inflation target. Apart from fading of factors boosting energy and food prices, the fall in inflation throughout 2025 will follow from the expected weakening of labour cost growth and the limited demand pressure, with the low inflation in the environment of the Polish economy. At the same time, forecasts point to core inflation being lower in 2025 than in 2024.

Main uncertainty factors

The outlined macroeconomic scenario is subject to uncertainty. Among the external factors, an important source of risk is geopolitical situation, in particular the further course of the ongoing military conflicts, including the military aggression of Russia against Ukraine.

Also the future developments in economic conditions worldwide are unclear, which is underlined by the recent increase in financial markets volatility. Another source of uncertainty is the shape of economic policies in major economies. This concerns both monetary and fiscal policies in major advanced economies, trade relations between the United States, the European Union and China, as well as economic policies in the European Union.

Fiscal policy in Poland is a further factor of uncertainty. On one hand, introduction of some of the considered fiscal actions would translate into higher public finance sector deficit. On the other hand, launching the Excessive Deficit Procedure against Poland may lead to a more restrictive fiscal policy.

Apart from fiscal measures, another source of uncertainty are the regulatory decisions concerning electricity and natural gas markets in Poland, changes in prices on global energy and food markets, as well as the impact of the European Union climate policy on prices of goods and services.

A significant uncertainty relates also to how higher energy prices would affect inflation expectations of households and wage dynamics. Moreover, it is unclear to what extent growth in wages and other sources of household disposable income would translate into private consumption and demand pressure, as well as how persistent services price inflation would be.

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