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Economic Comment

It ain't over till it's over

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Polish Monetary Policy Council decided to hike main interest rates by 50bp (the reference rate up to 2.25%), in line with analysts' expectations.

The post-meeting statement was very similar to the one in December, the key fragments remained unchanged. The MPC repeated the sentence that its next decisions will be aimed at lowering inflation to the level consistent with the NBP target in the medium run, at the same time supporting balanced economic growth, and that the total size of monetary adjustment will depend on the incoming data. The door to next interest rate hikes remains wide open, it seems. However, the answer to the question about the precise timing of next moves is not easy. In February the MPC may be tempted to stay on hold, waiting for the next NBP projections (due in March) and the first effects of the government's anti-inflation shield (there will be no flash CPI release for January, as usual). So, a pause in February is possible, in our view, but not certain, as it will be dependent also on other incoming data and information (economic activity, pandemic situation, FX behaviour). We think the target NBP rate in this cycle will be at 3.5% at least (the market is pricing in even more, around 4% in mid-year).

The NBP governor's press conference is scheduled on Wednesday at 15:00 CET. And on Friday at 10:00 the flash CPI for December will be released (our forecast and market consensus at 8.3% y/y). Both may be important for expectations about the next MPC moves.

Changes versus December statement

The activity in global economy continues to recover, yet economic conditions are under a negative impact of supply-side constraints in some markets, high commodity prices and re-escalation of the pandemic in certain countries, including the euro area. Latest forecasts indicate that global GDP growth in 2022 will ~~remain~~be relatively robust, although lower than in 2021. The ~~emergence~~spread of a new variant of coronavirus ~~contributed to higher~~ remains an uncertainty ~~regarding~~factor for further course of the global epidemic and economic developments~~, and hence to some deterioration of sentiment in the global financial markets and an increase in risk aversion~~.

~~Commodity~~Energy commodity prices – in particular prices of natural gas, oil~~,~~ and coal~~,~~ – as well as prices of some agricultural commodities ~~– remain~~run at markedly higher levels than a year ago. ~~Together with continued~~At the same time, global supply chain disruptions continue and ~~still high~~ international shipping costs~~, and amid~~ are still elevated. Together with a strong recovery in demand, this contributes to a marked rise in inflation globally, which in many countries has reached highest levels in decades. Moreover, also inflation forecasts for the coming quarters have been revised up, which points to the risk of longer than previously judged impact of pandemic shock on inflationary processes.

~~Against this background some~~Amidst strong increase in current and expected inflation many central banks are withdrawing monetary accommodation, however, decisions of monetary authorities are not homogenous and take into account conditions for conducting monetary policy in particular economies. Central banks in the Central-Eastern Europe region have been increasing interest rates. The ECB~~, despite inflation being the highest in the euro area history,~~ keeps negative interest rates ~~and continues big~~, but it announced a reduction in the scale of asset purchases. ~~In turn, the~~The US Federal Reserve ~~keeps~~has increased the pace of reduction in monthly asset purchases while keeping interest rates close to zero~~, but at the same time signals the possibility of a more rapid deceleration of asset purchases, which together with an increase in risk aversion leads to an appreciation pressures on the US dollar in global markets~~.

In Poland, ~~economic activity continues to recover,~~ despite another wave of increase in infections~~. Robust economic conditions are reflected in preliminary estimate of GDP, according to which annual GDP growth in 2021 Q3 stood at 5.3%, accompanied by a significant acceleration in investment. Data~~, economic activity continues to recover, as indicated by monthly data on industrial production, retail sales and construction and assembly output ~~for October 2021 point to a solid increase in economic activity also in 2021 Q4.~~. The situation in the labour market ~~likewise~~ continues to improve, ~~as indicated by~~ which is reflected in decreasing unemployment, rising employment and a marked increase in average ~~wage~~wages. In the coming quarters economic conditions are expected to remain favourable. However, there are uncertainty factors related to the impact of the pandemic on global and domestic economic conditions, as well as to the effects of supply-side constraints and high energy commodity prices on the economy.

Inflation in Poland~~, according to the Statistics Poland flash estimate for~~ in November 2021~~,~~ increased to 7.~~7~~8% in annual terms, and in monthly terms it amounted to 1.0%. ~~The elevated~~ A

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significant contribution to an increase in inflation ~~resulted, to a great extent, from external factors beyond the control of domestic monetary policy, such as higher than a year ago global prices of energy and agricultural~~ was made by the rise in global prices of commodities~~, –~~ – including energy and agricultural commodities – observed in the second half of 2021, record high increase in prices of CO_2 emission allowances, rising prices of goods whose supply has been constrained by global pandemic disruptions as well as earlier increase in electricity prices and in waste disposal charges~~, as well as rising prices of goods, whose supply has been constrained by global pandemic disruptions. The ongoing~~. Ongoing economic recovery, including demand driven by rising household income, has also added to ~~the price growth.~~

~~The rise in global prices of both energy and agricultural commodities observed this year, record high increase in prices of CO_2 emission allowances, as well as continued global supply chain disruptions have led to significant~~ an increase in inflation. These factors, together with a rise in ~~inflation in Poland, which is going to remain~~regulated tariffs on electricity, natural gas and thermal energy will contribute to inflation remaining at an elevated level also in ~~the coming period. The~~ 2022. In turn, a reduction in some tax rates as part of the so-called Anti-inflationary Shield ~~announced by the government~~ will have a curbing impact on inflation.

In a longer perspective, inflation will decrease, which will be supported by expected fading of some global shocks currently boosting price growth, as well as by an increase in the NBP interest rates. At the same time, amidst further economic recovery and expected continuation of favourable labour market conditions, as well as probably more lasting impact of external shocks on price dynamics, there persists a risk of inflation running above the NBP inflation target in the monetary policy transmission horizon. In order to reduce this risk, i.e. striving to decrease inflation to the NBP target in the medium term, the Council decided to increase NBP interest rates again. The increase of the NBP interest rates will also curb inflation expectations.

Decisions of the Council in the coming months will continue to be aimed at reducing inflation to a level consistent with the NBP inflation target in the medium term, while taking into account economic conditions, so as to ensure medium-term price stability and at the same time support sustainable economic growth after the global pandemic shock. The Council's assessment regarding the total scale of monetary tightening necessary for achieving these goals will consider incoming information on perspectives for inflation and economic growth, including situation in the labour market.

NBP may still intervene in the foreign exchange market and use other instruments envisaged in the Monetary Policy Guidelines. The timing and scale of the measures taken by NBP will depend on the market conditions.

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