



Weekly Briefing

Poland economy briefing:
Significant reduction in interest rates of the National Bank of Poland
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Significant reduction in interest rates of the National Bank of Poland

Summary

The Monetary Policy Council of the National Bank of Poland (NBP) decided in September to cut interest rates very sharply. The NBP's reference rates fell by 0.75 percent and now stand at 6 percent. Such a strong reduction came as a surprise to economists. NBP President Adam Glapinski said the time had come for rate cuts, since September inflation in Poland will most likely be in the single digits.

The government adopted a budget bill for 2024 in August. It assumes budget revenues of more than 151 billion euros and inflation of 6.6 percent. - This is a safe budget in difficult times, Prime Minister Mateusz Morawiecki said. He added that the draft is based on three pillars: security, social programs and health care.

Introduction

Inflation for September is likely to be slightly above 8.5 percent. And this means that today inflation is in single digits. So the conditions for rate cuts have been met," National Bank of Poland President Adam Glapinski said at a press conference.¹ The Monetary Policy Council (MPC) decided in September to cut NBP interest rates by 75 basis points. The reference rate fell to 6.00 percent. In July, the NBP President announced the end of the interest rate hike cycle.

The President of the NBP: we are watching the situation

From October 2021 to September 2022, the Monetary Policy Council (MPC) of the National Bank of Poland (NBP) raised the benchmark rate 11 consecutive times, by a total of 665 basis points to 6.75 percent, and until the 6th of September, kept it unchanged. This was the highest rate level since late 2002 and the fastest pace of rate hikes in Poland in the history of the MPC. During the COVID-19 pandemic in the spring of 2020, the MPC cut the main rate to a record low of 0.1 percent. Before the pandemic, the reference rate had been held at 1.50 percent for five years until March 2020.

The NBP President Adam Glapiński pointed out that the main interest rate at 6.75 percent (before the cut) with annual inflation of 18.4 percent that prevailed in February "is very

different" from 6.75 percent with inflation at 9.5 or 10.1 percent. - A rate of 6.75 percent with inflation at 9.5 percent means a much more restrictive monetary policy, he argued. - If we didn't change rates, they would soon become positive in real terms, he pointed out, justifying the Monetary Board's decision. - We are observing the situation, and we believe that this adjustment (75 bps cut in interest rates) was necessary. - he said. ⁱⁱ

The Head of the NBP referred to the question of decisions at the next meetings of the MPC. - I am not announcing anything. We observe the situation and make decisions according to the situation," he said. In his opinion, the 6% level of rates is very high, and a 75 basis point cut is an adjustment. - It's 75 basis points, it's an abrupt adjustment, because we went down to what it should be, and we continue to act according to our assessment of the situation. We'll see what happens, what the reactions to our decisions are, and we'll make the appropriate decisions," the NBP Head noted. Adam Glapiński also said that the NBP's goal is not to freeze the Polish economy by bringing inflation to 0 percent, noting record low unemployment, "perhaps underestimated in Poland." The NBP predicts that inflation will fall to 6-7 percent by the end of the year.

The Economists surprised by scale of rate cuts

Most economists at Poland's largest banks had expected a cut in interest rates, but on a smaller scale - by 25 basis points. According to critics, such a decisive reduction in rates may not be beneficial in the fight against high inflation. According to many economists, Adam Glapinski has once again made it clear that he is willing to tolerate longer inflation above the NBP target. They assessed that the president is paying a lot of attention to sustaining economic activity and keeping the cost of fighting inflation to the labor market as low as possible.

Experts expect further rate cuts, albeit at different rates and scales. According to many Polish bank economists, financial markets have gained an argument that inflation in Poland will be permanently higher than inflation in the Eurozone or the US, and this has had a bad effect on the zloty (Polish currency) and long-term bond prices. Economists warn that the outlook for inflation next year is not as optimistic as the president claims, and interest rates could rise if inflation does not follow the path Glapinski assumes today. First, however, they expect cuts. According to economists at Polish banks - PKO BP, Pekao or Santander - by the end of this year there will be two more cuts of 0.25 percentage points each, meaning the rate would fall to 5.50 percent in December. ⁱⁱⁱ

The government has approved the country's 2024 budget.

Funding for the army, social programs and health care are the three main pillars of the 2024 budget law, which the government has approved since late August. The first is security, which will be allocated 35 billion euros . The second is social programs, which will consume more than 30 billion euros. And the third is health care, where spending will jump to 42 billion euros.^{iv} State revenues are expected to reach more than 151 billion euros next year. That's nearly of 18 billion euros more than after the revision of this year's budget. ^v According to the adopted budget, inflation in 2024 is expected to be 6,6 perc. - This is a safe budget in difficult times, Prime Minister Mateusz Morawiecki said.

The Head of the Polish government also announced increases for the budget sector of 12.3 percent. Such an amount has been secured in the budget for salary increases for firefighters, police officers and teachers, among others. The general government deficit is expected to be 4.5 percent of GDP. The prime minister assured that “his government is managing public debt and public sector finances in a secure manner, that the government maintains access to the financial market and is able to finance borrowing needs”.

GDP is expected to grow by 3 percent in 2024

According to the assumptions of the draft budget adopted back in June, the economy is expected to recover in 2024, with GDP growth expected to reach 3 percent. - In 2023, GDP is growing at a slightly slower pace - we assume that growth will be around 0.9 percent. In 2024, it will accelerate to 3 percent, Finance Minister Magdalena Rzeczkowska conveyed. - The Polish economy grew by about 32 percent in real terms between 2016 and 2022. This growth was the highest, it was greater than in any major EU country, and despite the fact that we faced really serious challenges, Rzeczkowska assessed.

The government also assumes real wage growth in the economy, which is expected to be enabled by decelerating inflation. It is expected to fall from an average annual rate of 12 percent in 2023 to 6.6 percent next year. Employment in the national economy is expected to grow by 0.3 percent in 2023, but is expected to rise by 1.2 percent in the following year, 2024. As a result, unemployment is expected to be lower than in 2023.^{vi}

Conclusion

The NBP's decisive reduction in interest rates marks the end of a long cycle of hikes and sustained high interest rates. It will mean a small, but noticeable drop in mortgage installments. The NBP's action shows that the key to the Central Bank's policy is to maintain economic growth and slowly curb inflation, which is why the scale of the cuts has been met with criticism from many economists. Many see their connection with the upcoming parliamentary elections. Further rate cuts are expected.

The state budget for 2024 presented by the government foresees half the inflation and 3 times the GDP growth of 2023, as well as a deficit of 4.5 percent of GDP and increased budget revenues. The main spending pillars of the 2024 budget are: Defense, Social Affairs and Health. However, critics of the government's policy point out that this budget is unrealistic and it should be amendment. In opinion of many economists and business organizations, many of state expenditures are hidden in special purpose funds that are not included in the state budget, and warn of increasing real state debt. The emphasize that is not development and investment budget. It is worth noting that the 2024 budget will already be implemented by the new government that emerged after the October parliamentary elections.

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- i TVN Biznes TV Portal <https://tvn24.pl/biznes/pieniadze/stopy-procentowe-i-inflacja-prezes-nbp-adam-glapinski-zabiera-glos-7332923>
 - ii The Economic portal Money.pl <https://www.money.pl/gospodarka/ta-decyzja-przejdzie-do-historii-adam-glapinski-tlumaczy-ruch-rpp-6938952716581504a.html>
 - iii The Economic portal BusinessInsider.pl <https://businessinsider.com.pl/gospodarka/co-tak-naprawde-powiedzial-nam-prezes-glapinski-tak-zmienia-sie-stopy/7f5p0pb>
 - iv The Economic portal Money.pl <https://www.money.pl/gospodarka/premier-odkryl-karty-oto-budzet-na-2024-rok-6934003821337504a.html>
 - v The Economic portal BusinessInsider.pl <https://businessinsider.com.pl/gospodarka/rzad-przyjal-budzet-na-po-wyborach-zobacz-co-sie-w-nim-znalazlo/xq3nfew>
 - vi The Economic portal Bankier.pl <https://www.bankier.pl/wiadomosc/Patrzac-z-lotu-ptaka-na-caly-budzet-Premier-Morawiecki-o-projekcie-przyszlorocznego-budzetu-8599691.html>