Andriy Pyshnyy: National Bank of Ukraine press briefing - monetary policy decisions

Speech by Mr Andriy Pyshnyy, Governor of the National Bank of Ukraine, at a press briefing on monetary policy decisions, Kyiv, 12 December 2024.

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Dear colleagues,

The Board of the National Bank of Ukraine has decided to raise the key policy rate to 13.5% per annum. This decision is intended to preserve the sustainability of the FX market, keep inflation expectations in check, and gradually bring inflation down to the target of 5%.

In recent months, inflation has been rising faster than forecast by the NBU

In November, inflation accelerated to 11.2% yoy. On the one hand, consequences of limited food supply due to this year's weaker harvests were an important driver of price growth. The impact of this factor on inflation is expected to be neutralized next year as new harvests enter the market.

On the other hand, the inflationary surge is starting to look more and more fundamental, which is evidenced by further growth in core inflation. The latter is associated with increases in businesses' expenses on electricity and labor, as well as with exchange rate effects from the weakening of the hryvnia in previous periods.

Inflation expectations are relatively stable as of now. However, the risk that they might unanchor is increasing as households pay more attention to inflation processes.

Inflation is expected to slow in 2025 and move toward the 5% target further on

In the coming months, inflation is likely to continue to rise in annual terms due to the further impact of food supply factors, large budget expenditures, significant pace of wage growth, and wider energy shortages during the heating season.

However, going forward, inflation should decelerate as the situation in the energy sector improves and harvests increase.

This will also be facilitated by the NBU's monetary policy measures and an expected easing of external price pressures.

In 2025, volumes of international financial assistance will be sufficient for non-monetary financing of the budget deficit and maintaining the sustainability of the FX market

In recent months, the risks of international financing inflows being insufficient in 2025 have declined substantially thanks to the progress made in the implementation of the Ukraine Loan Cooperation Mechanism, which envisages non-repayable macrofinancial assistance, as well as in the allocation of funds under Extraordinary Revenue Acceleration Loans.

The NBU's forecast that next year Ukraine will receive more than USD 38 billion in international assistance remains relevant. This financing will enable the NBU to maintain an adequate level of international reserves to ensure the sustainability of the FX market.

The course of the war continues to be the key risk to inflation dynamics and economic development

The war continues and poses the risk of a further reduction in economic potential, in particular due to the loss of people, territories, and production facilities. The speed of the economy's return to normal functioning conditions will depend on the nature and duration of the war.

The main risks remain the same:

- the emergence of additional budget needs, mainly those to maintain defense capabilities
- the likelihood of an additional hike in taxes, which – depending on its parameters – might drive up pressures on prices
- further damage to infrastructure, especially energy and port infrastructure, which will restrain economic activity and put supply-side pressures on prices
- a deepening of adverse migration trends and a further widening of labor shortages on the domestic labor market.

At the same time, positive scenarios could also materialize, resulting, among other things, from the continued acceleration of European integration processes and recovery in the energy sector.

In order to maintain FX market sustainability, prevent expectations from becoming unanchored, and to gradually bring inflation back to its target, the NBU Board decided to raise the key policy rate from 13.0%, to 13.5%

The NBU sees a need to tighten its interest rate policy to reverse the inflation trend and bring back inflation to its 5% target on the policy horizon.

A higher key policy rate will help keep inflation expectations under control and support real yields on hryvnia instruments. This will fuel interest in hryvnia term deposits, and thus help reduce pressures on the exchange rate and prices, as temporary inflation drivers wear off.

Safeguarding the sustainability of the FX market will remain an important factor in bringing inflation back onto a downward trajectory. Given the sufficient amount of international assistance, the NBU's ability to compensate for the structural currency deficit in the private sector and smooth out excessive exchange rate fluctuations will remain strong.

The NBU will take further decisions to tighten its interest rate policy at upcoming meetings of the Board on monetary policy issues if there are persistent signs of unrelenting inflationary pressures and the threat that inflation expectations might become unanchored.

Thank you for your attention!