

Warsaw, 31 January 2006

INFORMATION FROM THE MEETING OF THE MONETARY POLICY COUNCIL

held on 30-31 January 2006

The Council decided to lower the NBP interest rates by 0.25 percentage point to the following levels:

- reference rate 4.25% on an annual basis;
- lombard rate 5.75% on an annual basis;
- deposit rate 2.75% on an annual basis;
- rediscount rate 4.50% on an annual basis.

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Since the Council's meeting in December 2005, no significant changes have been observed in the prospects for economic growth and inflation in the external environment of the Polish economy. In December the annual growth rate of consumer prices in the euro area decreased to 2.2% from 2.3% recorded in November, while in the United States it dropped from 3.5% to 3.4%. Since the December Council meeting, oil prices have risen (the Brent oil price has grown by USD 6.9 per barrel, i.e. by 12.4%). On the other hand, the forecast oil prices for 2006 have not changed significantly so far. Still, high uncertainty persists as to the effect of the high growth in oil prices on the economic growth rate and inflation.

Data published since the Council's previous meeting indicate the continuation of growth tendencies in the Polish economy, which have been observed since 2005 Q2. According to GUS estimates, the GDP growth rate in Poland in 2005 reached 3.2% and was slightly lower than the expectations of both the NBP and most market analysts. The recently published GUS estimates point to an increased role of domestic demand, investment in particular, in GDP growth in 2005.

Since mid-2005, the industrial output has been on a gradual increase. In December 2005 the growth rate of industrial output – for the third consecutive month – exceeded the expectations of both external forecasters and the NBP, and amounted to 9.2% y/y, (8.5% in November). In seasonally adjusted terms this growth was even higher and stood at 13.3%, as compared to 7.4% a month before. December also saw an acceleration of growth in construction. The annual growth in the construction and assembly output rose to 8.3% in December as compared to 5.9% in November, i.e. from 8.6% to 10.6% in seasonally adjusted terms. In the period May-November 2005 the moderate upward trend in retail sales was continued. The annual growth of retail sales in this period ranged between 5.0 and 8.0%.

The employment in the corporate sector has been growing since the beginning of 2005. In December 2005 employment in the enterprises was higher than a year before by 2.5% and recorded the highest annual growth rate recorded in 2005. Moreover, the BAEL survey (Labour Force Survey) in 2005 Q3 indicates an acceleration of the recovery in the labour market. In 2005 Q3, the growth rate of working persons in the economy increased (growth of 2.8% y/y as compared to 1.9% in 2005 Q2 and - excluding private farming - of 3.7% in comparison to 2.7% in 2005 Q2). Along

with that, unemployment continued to decrease (according to BAEL, the unemployment rate was at 17.4% in 2005 Q3, in comparison to 18.2% a year before, whereas according to the data from the labour offices – it reached 17.6% in December in comparison to 19.0% a year before). The recovery in the labour market is accompanied by a considerable increase in the labour supply. In 2005 Q3, the economically active figure stood at 17.4 million (growth of 1.7% y/y), which was the highest level recorded since the first BAEL survey in 1992.

December reported a lower growth of wages in the corporate sector (nominal growth of 1.5% y/y as compared to 6.9% y/y in December and 6.4% y/y in November). Growth in wages was much lower than in the previous months due to the shift in the payments of the annual bonus in the mining industry, which had increased the growth rate in the previous two months. In 2005 Q4 as a whole, the nominal growth of wages in the corporate sector stood at 4.8%, this being the highest rate in 2005. It means that increased growth in output was in this period accompanied by acceleration in the growth of wages. It should be emphasised that a necessary condition for a sustained acceleration in economic growth grounded in the rise of employment is that - in the longer run - the growth in real wages is not faster than the growth in labour productivity.

The annual growth in consumer prices in December declined to 0.7%. The decrease in the annual inflation mainly reflected the decline in the prices of food and fuels. The fall in food prices in December resulted, among other things, from their high supply, introduction of restrictions on Polish food exports to Russia and the decreased demand for poultry caused by the bird flu effect. The drop in fuel prices was mainly due to the reduction in distribution margins. The continuing appreciation of the zloty was an important factor favouring the decline in inflation. "Net" inflation stabilized at a low level and amounted to 1.1% in November and December. The remaining core inflation measures stayed in the range of -0.4%-1.0%. In January inflation expectations of households decreased to 0.9% against 1.5% in the previous month. This decline was mostly associated with the decrease in inflation in November 2005.

December 2005 saw a slight increase – for the first time since April 2005 – in producer prices in industry in annual terms (growth of 0.5% y/y; i.e. fall of 0.4% m/m). The low level of producer prices in industry resulted from a stronger than a year ago zloty exchange rate and a moderate growth in domestic demand.

The NBP inflation projection presented in the January *Inflation Report* was prepared on the basis of data available as of 2 January 2006 and so, among others, it does not account for the GUS estimates of GDP in 2005. The projection indicates that with a 50-percent probability the annual GDP growth should stay in the range of 3.8%-5.1% in 2006, 3.4%-5.2% in 2007 and 3.6%-5.5% in 2008, respectively.

The January inflation projection indicates that growth in prices in 2006 will be lower than expected in the August projection. In 2007 inflation will accelerate and at the end of the year should be close to the level from the projection presented in August 2005. Assuming unchanged interest rates, there is a 50-percent probability that inflation will stay within the range of 0.5%-2.3% in 2006 Q4 (compared to 1.0%-3.1% in the August *Report*) 1.1%-3.6% in 2007 Q4 (compared to 1.2%-4.1%) and 0.8%-3.9% in 2008 Q4.

It has to be emphasised that the inflation projection and the distribution of probabilities presented in the *Report* do not account for all sources of uncertainty related to the scale of future rise in employment, the impact of globalisation effects on price processes, the economic policy of the government in the years to come and the path of the exchange rate. Moreover, the projection does not allow for the latest developments which may have great bearing on the forecast growth of prices. On the one hand, oil prices in January 2006 were higher than accounted for in the projection. On the other, the zloty exchange rate in January was stronger and the data on national accounts indicate that the GDP growth in 2005 Q4 and the whole of 2005 was slightly lower, while the rise in investments was significantly higher, than assumed in the January projection.

NBP

The Council maintains its conviction that implementing an economic strategy focused on creating conditions which ensure the introduction of the euro at the earliest possible date would be most favourable for Poland and would contribute to higher long-term economic growth.

The next meeting of the Council will be held on 21-22 February 2006.