National Bank of Poland

Monetary Policy Council

Report on monetary policy implementation in 2012

Warsaw, May 2013

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In presenting the *Report on monetary policy implementation*, the Monetary Policy Council acts in accordance with Article 227 of the Constitution of the Republic of Poland, which imposes an obligation on the Council to present a report on the implementation of monetary policy guidelines within 5 months following the end of the fiscal year. In accordance with Article 53 of the Act on the National Bank of Poland, the *Report on monetary policy implementation* is published in the Official Gazette of the Republic of Poland, the *Monitor Polski.*

The Report presents the main elements of the implemented strategy of monetary policy, a description of macroeconomic conditions and decisions taken with respect to monetary policy in the reported year, as well as a description of the applied monetary policy tools.

The *Report* is accompanied by Appendices presenting the development of important macroeconomic variables, as well as by *Minutes of the Monetary Policy Council decision-making meetings* and the voting records of the Council's members on motions and resolutions.

An ex post assessment of the conduct of monetary policy should take into account, above all, that the decisions of monetary authorities affect the economy with considerable lags, with the strongest impact being observed after several quarters. Moreover, the economy is subject to macroeconomic shocks, which, while remaining in most cases outside the control of the domestic monetary policy, may to a large extent affect the economic situation and domestic inflationary processes in the short, and sometimes in the medium term.

This *Report on monetary policy implementation in 2012* is a translation of the National Bank of Poland's *Sprawozdanie z wykonania założeń polityki pieniężnej na rok 2012* in Polish. In case of discrepancies, the original prevails.

Chapter 1.

MONETARY POLICY STRATEGY IN 2012

In 2012, the Monetary Policy Council, henceforth "the Council", pursued monetary policy according to the principles included in *Monetary Policy Guidelines for 2012*, adopted on 23 August 2011, as quoted below.

The Monetary Policy Council decided to maintain the key elements of the NBP monetary policy strategy that had been presented in the *Monetary Policy Guidelines for 2011*.

According to Article 227 section 1 of the Constitution of the Republic of Poland “the National Bank of Poland shall be responsible for the value of Polish currency”. The Act on the National Bank of Poland of 29 August 1997 states in Article 3 section 1 that “the basic objective of NBP activity of shall be to maintain price stability, and it shall, at the same time, act in support of Government economic policies, insofar as this does not constrain the pursuit of the basic objective of the NBP”.

Nowadays central banks understand price stability as inflation so low as not to negatively affect decisions taken by economic agents, including investment and savings decisions. Ensuring price stability is a fundamental way in which the central bank contributes to high and sustainable economic growth. In pursuit of the task of maintaining price stability, central banks respond both to inflationary and deflationary threats.

Since 1998 the Monetary Policy Council, has based its monetary policy on inflation targeting (IT). Beginning 2004, the Council adopted a permanent inflation target of 2.5% with a symmetrical tolerance band for deviations of ± 1 percentage point. The Council pursues the strategy under a floating exchange rate regime. However, the floating exchange rate regime does not rule out foreign exchange interventions should they turn out necessary to ensure domestic macroeconomic and financial stability, which is conducive to meeting the inflation target in the medium term.

The experience of the National Bank of Poland, hereinafter “the NBP”, and other central banks shows that IT is an effective way to ensure price stability. The global financial crisis has shown that in order to ensure long-term price stability factors related to financial system stability should play a more pronounced role in monetary policy than to date. Therefore, monetary policy should aim at stabilising inflation at the target in the medium-term, while at the same time containing the risks of imbalances in the financial system. Inflation targeting enables the pursuit of such a policy while providing support for the regulatory and supervisory policies addressed to the financial sector.

In 2012, the Council pursued monetary policy guided by the following principles :

- First, the notion of *permanent* inflation target means that it refers to inflation measured as a year-on-year change in prices of consumer goods and services in each month compared to the corresponding period of the preceding year. While analysing inflation processes the use of quarterly and annual inflation indices is also justified, such as those applied in the NBP's inflation projection, in the state budget and in the statistics of the European Union, hereinafter "the EU", including the harmonized index of consumer prices – HICP. An important role in the assessment of inflationary pressure is also played by core inflation indices which make it easier to distinguish between temporary changes in the consumer price index from more sustained changes in inflation pressure. Moreover, core inflation indices make it easier to distinguish between impacts of supply or demand shocks on inflation.

- Second, monetary policy is unequivocally focused on maintaining inflation as close as possible to the target of 2.5% and not just within the tolerance band. This is to facilitate the anchoring of inflation expectations and thus to allow the central bank to change monetary policy parameters less frequently in response to potential shocks affecting current inflation. It may also lead to lower volatility of long-term interest rates.

- Third, the occurrence of shocks in the economy is inevitable. Depending on the strength and the direction of the shock and the degree of inertia of inflation expectations, the scale and the duration of inflation deviation from the adopted target may differ. In countries with sustained low inflation, the central bank usually does not respond to deviations from the inflation target if it deems them temporary, even when inflation leaves the tolerance band. When assessing the need for response, the Council will, however, take into account the fact that in Poland low inflation expectations have not been sufficiently anchored. The extent to which inflation expectations are anchored affects the scale and persistence of the impact of supply and demand shocks on inflation. In the case of shocks which, in the Council's opinion, may lead to a relatively permanent increase in inflation expectations and, as a result, to the rise in inflation due to the emergence of the so-called second-round effects, the central bank will adjust its monetary policy parameters accordingly.

- Fourth, the monetary policy response to shocks also depends on their causes and nature. In the case of demand shocks inflation and output move in the same direction. An interest rate increase weakens economic activity in the short term and, subsequently, inflationary pressure.
  In the case of supply shocks output and inflation move in opposite directions. The dilemmas of monetary policy in such a case are as follows:
  An attempt to neutralise the impact of a supply shock on inflation using monetary policy instruments may lead to even deeper plunge in output growth resulting from supply shock's negative impact on consumption and investment.
  On the other hand, an attempt to accommodate – by pursuing expansionary monetary policy – the real effects of a supply shock resulting in a rise in inflation and a decline in output growth usually leads to persistently higher inflation. This, in turn, requires far more restrictive monetary policy in subsequent periods. This leads to a stronger deceleration in economic growth than the monetary tightening that prevents inflation from being sustained at a heightened level.
  The response of the central bank to the shock should depend on the assessment of the persistence of the shock's effects, including the assessment of the risk of second-round effects.

- Fifth, because of the lags in the response of output and inflation to the monetary policy, the impact of monetary policy on the current inflation is limited. Current decisions of the monetary authorities affect price developments in the future just as the current inflation is influenced by interest rate changes made several quarters before. However, the time lag between an interest rate decision and its strongest impact on real variables (output, employment) and then on inflation is not constant. It depends, to a large extent, on structural and institutional changes in the economy. Those changes mean that central banks can only approximately assess this time lag. Turmoil in the domestic and international financial system may constitute an additional factor disrupting the monetary transmission mechanism.

- Sixth, monetary policy should take into account the need to maintain financial stability which is indispensable to ensure price stability in the longer term and which enables effective functioning of the monetary policy transmission mechanism. In this context, when assessing the balance of risks to future inflation and economic growth, asset price developments are of particular importance. Excessive interest rates cuts and the long-lasting maintaining lowered interest rates amidst low inflation and simultaneous fast economic growth may lead to a rapid asset price growth, thus increasing the risk of the so-called speculative bubbles. Rapid asset price growth is accompanied by the growing likelihood of asset price deviation from the levels justified by fundamentals, which increases the risk of an abrupt and significant decline in asset prices in the future. Rapid increase in asset prices, especially if it is accompanied by a fast rise in lending, poses a threat to the financial system stability, and consequently – in the longer term – to sustainable economic growth and price stability. Monetary policy supporting financial system stability is thus consistent, in the longer term, with the achievement of the basic objective of the central bank's activity i.e. ensuring price stability, although it may occasionally pose a risk of temporary deviation of inflation from the target. In order to maintain consistency between attempting to keep inflation at the target and supporting financial system stability, under certain conditions it may be necessary to lengthen the inflation target horizon.

- Seventh, in assessing the risk of turmoil in the financial system and the inflation outlook in the longer run, it is useful to analyse monetary and credit aggregates. A fast increase in these aggregates may lead to growing macroeconomic imbalances in the economy, including imbalances in the asset markets. Monetary policy decisions should take into account the risk connected with excessive increase in these aggregates. Regulatory and supervisory policies in the financial sector that have an impact on credit growth and its structure are an important factor influencing monetary policy.

- Eighth, in assessing the degree of monetary policy restrictiveness not only should the level of real interest rates be considered but also the level of the real exchange rate. Thus understood restrictiveness of monetary policy impacts, along with the implemented fiscal policy, the total restrictiveness of macroeconomic policy. Ensuring price stability amidst an overly expansionary fiscal policy may require a tight monetary policy, including keeping interest rates at a higher level.

- Ninth, monetary policy is pursued under uncertainty which excludes strict control of economic processes. This natural uncertainty means that while taking decisions related to monetary policy it is necessary to take into account all available information relevant for inflation developments, rather than the results of inflation projection only. Models used by central banks to forecast inflation may be imperfect in adequately reproducing behaviour of the economy if only because of its ongoing structural changes. In addition, it is not possible to adopt a simple policy rule which could be known *ex ante* to market participants.

- Tenth, an important input into the monetary policy decision-making process is the balance of factors affecting the probabilities of future inflation running above or below the target. This balance is based on the assessment of the actual economic developments, including the inflation projection. While assessing the factors affecting future inflation, the Council takes into consideration the past inflation developments since they have a bearing on the anchoring of inflation expectations at the inflation target. In particular, the Council takes into account the length of the period in which inflation remained close to the target and the length of the period in which it deviated from the target.

In the *Guidelines for 2012*, the Council announced that if a decision was taken on Poland joining the ERM II, the Council would make all necessary adjustments of the monetary policy strategy and – in consultation with the Council of Ministers – of the exchange rate policy to meet the convergence criteria required for the euro adoption. In the *Guidelines* the Council also stated that Poland's accession to ERM II and the euro area should take place at the earliest possible date after meeting all the required legal, economic and organizational conditions.

In the *Guidelines for 2012*, the Council underlined, that the situation of public finances would be an important factor affecting the monetary policy. In order to maintain macroeconomic stability, including price stability, it is necessary to conduct fiscal policy ensuring the long-term stability of public finances. Such a policy will also enable compliance with the euro adoption criteria.

Chapter 2.

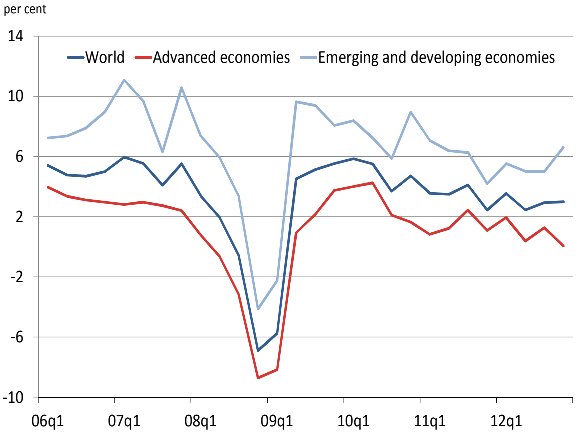
MONETARY POLICY AND MACROECONOMIC DEVELOPMENTS IN 2012

2.1. Macroeconomic developments in 2012

In 2012, the monetary policy of the NBP was conducted against the backdrop of unfavourable global economic conditions and periodically intensified tensions in the global financial markets, related, in particular, to the euro area debt crisis (Figure 2.1). In many countries, economic activity was dampened due to persistent uncertainty about future business conditions, further adjustments in the balance sheets of private and public sectors and continuously deteriorating labour market. In some countries, economic activity was additionally curbed by still relatively high commodity prices, coupled with – in the case of certain economies – large public sector debt.

Figure 2.1

Economic growth in the world (y/y)*.

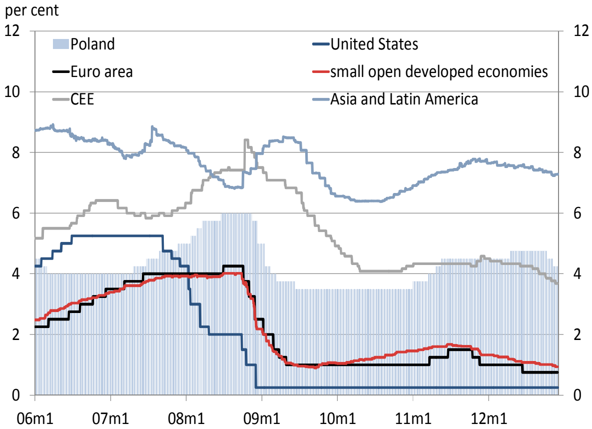


Source: IMF data.

*Aggregates based on: *World Economic Outlook Update*, January2012.

Figure 2.2

Central bank interest rates in the world*.



Source: Data of national central banks, Reuters Ecowin data, NBP calculations.

**Regional aggregates are arithmetic means including:*

- for the Asia and Latin America region: India, Indonesia, Malaysia, the Philippines, South Korea, Taiwan, Thailand, Brazil, Chile and Colombia

- for the small open developed economy group: Australia, Canada, Norway, Sweden and Switzerland.

As the above factors affected the individual countries and regions to a different degree, in 2012 – similarly as in the previous years – business conditions continued to differ across the world. In particular, growth in economic activity in the developed economies suffered a more significant downturn than in the emerging economies. Amongst the developed countries, GDP growth in the United States and Germany remained substantially higher than in those euro area countries that being most seriously affected by the competitiveness and debt crisis, remained in recession. Growth in the United States was supported by a relatively strong domestic demand, while in Germany it was fuelled by continuing robust external demand. As regards the largest emerging economies, the strongest rebound in GDP growth rate was recorded in China, where – like in many other economies of Asia and Latin America – growth was driven by revival of domestic demand.

In 2012, the main central banks increased the scale of their monetary expansion. The Federal Reserve Bank (Fed), the Bank of Japan (BoJ) and the Bank of England (BoE) kept their interest rates at a historically low level, whereas the European Central Bank (ECB) in the second half of 2012 cut its interest rates to the lowest level since the euro creation (Figure 2.2). At the same time, the main central banks expanded the scale of the existing quantitative easing programmes, and in the second half of the year – amidst deteriorating outlook for economic growth and the intensification of debt crisis in the euro area – they introduced new asset purchase and liquidity programmes[1].

In most developed countries, in 2012 further measures were taken to reduce their fiscal imbalances. These helped to reduce somewhat the general government deficits, however, in most cases, deficits remained high, adding to further public debt build-up.

In the first half of 2012, concerns about the macroeconomic stability in some euro area countries (in particular Greece and Spain) intensified again, driving up risk aversion in the financial markets. In the second half of the year, as some sources of uncertainty waned[2], further institutional reform in the euro area were announced and the ECB programme of Treasury bond purchase was introduced, the sentiment in the financial markets improved.

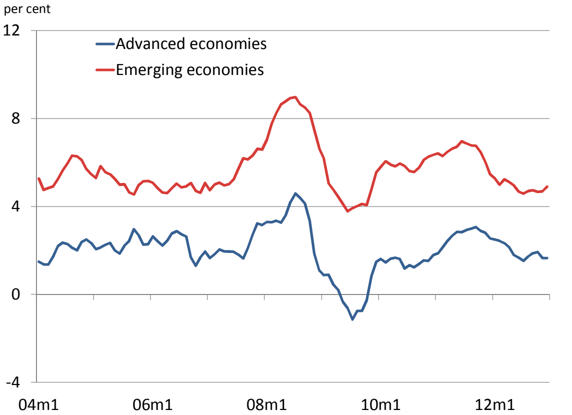
Weak demand in the global economy in 2012 contributed to a certain reduction in global inflation (both in the developed and in the emerging economies; Figure 2.3). Inflation decline was additionally supported by lower – as compared with the previous year – commodity prices (Figure 2.4). However, in some countries the extent of inflation decline was curtailed by hikes in indirect taxes and administered prices.

[1] In July 2012, the BoE announced its new liquidity programme *Funding for Lending*, designed to stimulate lending to enterprises and households. In September 2012, the Fed launched a new asset purchase programme involving the purchase of mortgage-based securities issued by government agencies (MBSs). Also in September 2012, ECB announced its OMT (*Outright Monetary Transactions*) programme, i.e. a programme of conditional, unlimited secondary-market purchase of Treasury bonds issued by countries most severely affected by the debt crisis. In October 2012 , the BoJ launched a new liquidity programme aimed at stimulating lending in the Japanese banking sector.

[2] In particular in Greece, parliamentary election was won by a party supporting the implementation of the austerity programme, while the euro area finance ministers decided to grant a credit line aimed at recapitalising the Spanish banking sector.

Figure 2.3

Global inflation*.

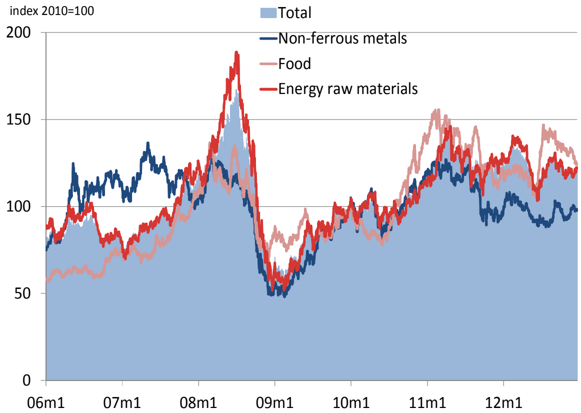


Source: Reuters Ecowin, IMF data, NBP calculations.

*Aggregates in accordance with the division adopted by the IMF (GDP-weighted). Weighted average inflation in the developed and the largest emerging economies (accounting for 80% of GDP in this group of countries in 2010).

Figure 2.4

Index of commodity prices in the global markets.

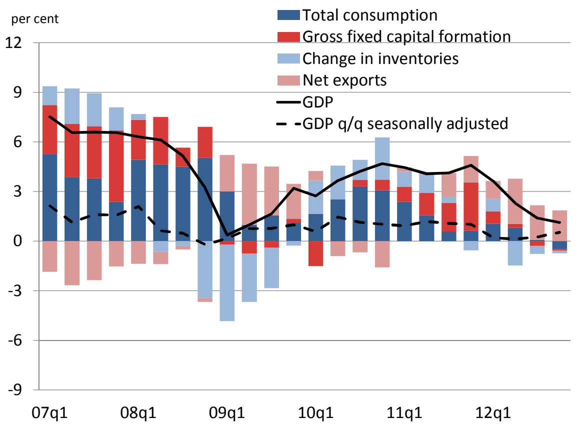


Source: Bloomberg data.

In Poland, amidst weakening external demand and heightened uncertainty about future economic conditions, growth gradually decelerated (Figure 2.5, Annex 1). The slowdown in consumption – especially pronounced in the second half of the year – was accompanied by falling investment. As a consequence, 2012 saw contraction in domestic demand. In turn, GDP growth was supported by a relatively large contribution of net exports, which, however, resulted from a stronger decline in imports growth than in exports growth.

Figure 2.5

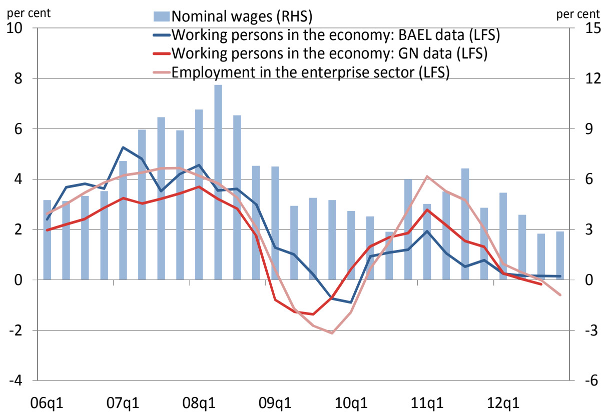
Contribution of aggregate demand components to GDP growth.



Source: GUS data, NBP calculations.

Figure 2.6

Annual growth in the number of persons working in the economy and in the corporate sector and the annual wage growth.



Source: GUS data.

Weaker consumer demand resulted, among others, from slow growth in household disposable income on the back of declining wage growth and stagnation in employment. Consumption growth was also adversely affected by stronger contraction in consumer loans and deteriorating household sentiment, in particular rising concerns about unemployment, which intensified in the second half of 2012. Slowing consumption growth in 2012 was accompanied by decreasing investment growth, which turned negative in the second half of the year. Weaker investment activity was primarily attributable to a decline in public investment related to finalizing some of the infrastructural investment projects launched before the European Football Championship, coupled with a deceleration in investment spending of local governments resulting from measures aimed at curbing the fiscal imbalance. At the same time, in the face of unfavourable outlook for domestic and external growth, the sentiment of economic agents deteriorated, and thus, corporate and household investment growth weakened.

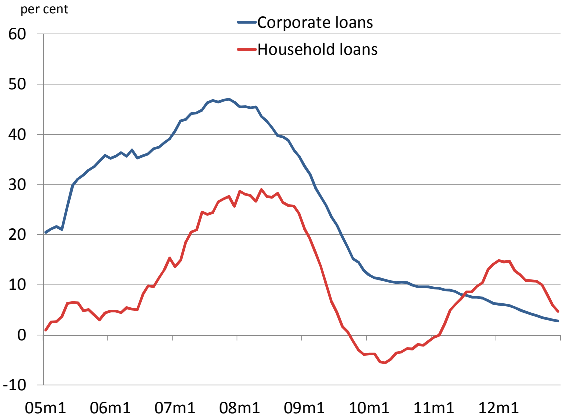
Slowing domestic demand was accompanied by a relatively large contribution of net exports to GDP, resulting from imports growth declining faster than exports (Annex 3).

As economic activity gradually lost momentum, employment in the economy came to a halt, while employment in the corporate sector decreased in the second half of the year (Figure 2.6). At the same time, the number of economically active persons continued to rise. As a result, the unemployment rate was on the rise in 2012, helping to curb wage pressure and bring down wage growth in the economy, and in particular in the corporate sector. Weaker wage growth helped to keep unit labour costs down despite a concurrent decrease in labour productivity growth.

In 2012 the process of reducing public finance imbalance continued. The general government sector deficit declined considerably for the second consecutive year (from 5.0% of the GDP in 2011 to 3.9% of the GDP in 2012 in ESA terms). This was achieved by limiting public investment projects financed with domestic funds (a simultaneous decline in public investment financed with EU funds had no effect on the size of the deficit). Moreover, the deficit narrowed due to measures launched already in 2011, such as the reduction of social security contribution transferred to the Open Pension Funds (OFE) enacted in March 2011, the application of the temporary expenditure rule and the wage freeze in the government sector.

Figure 2.7

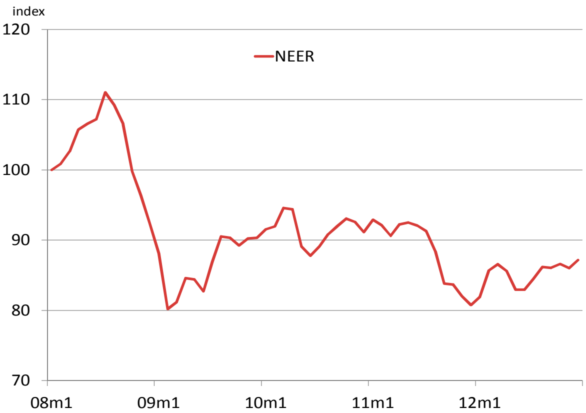
Annual growth in loans to the corporate and household sectors.



Source: NBP data.

Figure 2.8

Nominal effective zloty exchange rate (increase denotes appreciation).



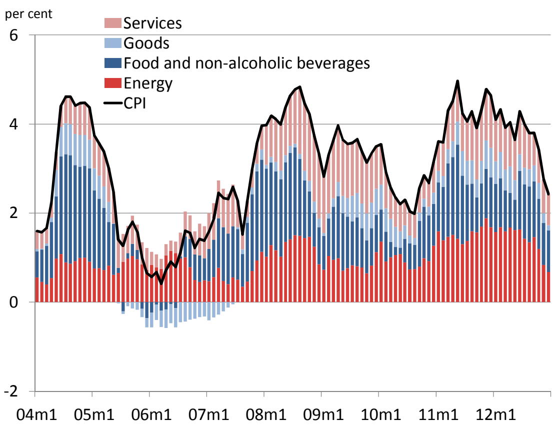
Source: Reuters Ecowin, OECD data, NBP calculations.

As economic growth slowed down, lending growth decelerated as well (Figure 2.70; Annex 4) Corporate credit growth declined, especially strongly in the second half of 2012, with substantial deceleration observed both in the current and investment loans. This could have been driven by weaker corporate investment demand amidst tighter lending conditions declared by banks. The year 2012 saw also an increasingly sluggish growth in lending to households. This was due to the combined effect of continued decline in consumer loans and slower growth in housing loans, resulting mostly from shrinking currency-denominated loans. Household credit expansion was constrained by the deteriorating economic situation of households as well as banks' more stringent lending policies, which – in the case of housing loans – was additionally aggravated by lowering price limits under the government-subsidised housing scheme "Family on its Own".

In 2012, the prices of domestic financial assets continued to be strongly affected by the sentiment prevailing in the global financial markets. Following a certain improvement in the global sentiment at the beginning of the year, the second quarter saw the return of heightened concerns about economic stability in the euro area, which fuelled risk aversion, and the resulting decline in the prices of some domestic assets, including equities. In the second half of 2012, the announcement of institutional reforms in the euro area and the expansion of the quantitative easing by the main central banks, including the ECB, had a positive impact on the sentiment in the global financial markets. Declining risk aversion attracted capital inflows to the emerging economies characterised by a high interest rate disparity vis-a-vis major advanced economies, including Poland. The inflow of capital contributed to higher prices of shares and Treasury securities and to strengthening of the exchange rates, including the zloty (Figure 2.8, Annex 3). The easing of the NBP monetary policy was also conducive to lower yields on Polish Treasury securities.

Figure 2.9

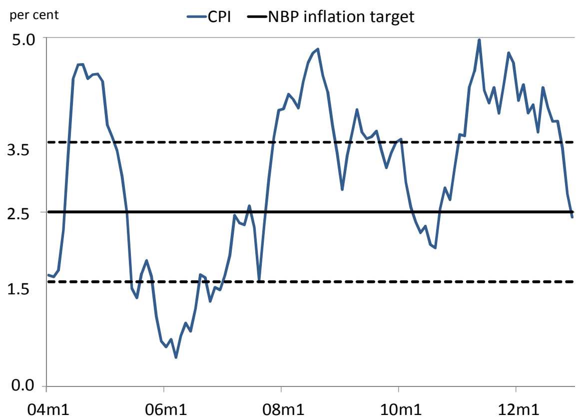
Annual price growth in the prices of consumer goods and services and contribution of main price categories to CPI.



Source: GUS data, NBP calculations.

Figure 2.10

Annual CPI and the inflation target.



Source: GUS data.

In 2012, the average annual CPI index (index of consumer goods and service prices) amounted to 3.7%.[3] While having declined on its 2011 figure, it continued to run at levels considerably higher than the NBP inflation target (Figure 2.9, Figure 2.10, Annex 2). In the course of the year, however, the CPI index declined substantially, and from October 2012 inflation dropped below the upper limit for deviations from the NBP inflation target, subsequently reaching the target level in December 2012.

Factors contributing to elevated inflation, particularly in the first half of 2012, involved the relatively sharp rise in administered prices (primarily those of energy carriers, related to a great extent to the 2011 and 2012 rises in electricity, gas and heating tariffs), as well as persistently heightened food price growth and the weaker, as compared to the previous year, zloty exchange rate. In turn, inflation decline, especially in the second half of the year, was related to a significant slowdown in demand and weaker wage growth, as well as to zloty appreciation recorded in that period. Moreover, lower inflation in 2012 was supported by the fading of the statistical base effect related to the rise in the VAT rates in January 2011.

[3] CPI - Consumer Price Index.

2.2. Monetary policy in 2012

Similarly to the previous years, in 2012 the monetary policy decisions of the Council were aimed at maintaining price stability, i.e. at stabilizing inflation at the 2.5% target in the medium term. At the same time, decisions of the Council were to support balanced economic growth. Bearing in mind the time lags in the monetary policy transmission mechanism, inflation and GDP in 2012 were influenced by the Council decisions taken in 2011.

In its 2012 decisions, the Council considered changing assessment of factors influencing inflationary processes over the monetary policy transmission horizon. This assessment relied on the information on economic developments available at the time of decision-making, including macroeconomic forecasts prepared by the NBP and external institutions.

After having increased the NBP interest rates on four occasions in 2011, at the beginning of 2012 the Council kept the NBP interest rates unchanged, while announcing the possibility of further monetary policy tightening. In May 2012, the Council assessed that the protracted period of inflation running above the upper limit for deviations from the target posed a risk that inflation might remain at an elevated level, particularly if inflationary expectations become persistently heightened. The data released at that time suggested that the scale of the anticipated economic downturn might be limited, which might prevent inflation from returning to the target in the medium term. Under such circumstances, the Council – aiming to maintain price stability in the medium term – increased the NBP interest rates by 0.25 percentage points; in particular it raised the reference rate from 4.50% to 4.75%.

At the beginning of the second half of 2012, the Council kept the interest rates unchanged. In 2012 Q4 the Council decided that a stronger than previously anticipated economic slowdown, combined with external factors, posed a risk of inflation falling below the target in the medium term. As a result, in November and December 2012 the Council cut the NBP interest rates by a total of 0.50 percentage points; the reference rate was lowered from 4.75% to 4.25%. At the same time, the Council announced that it would continue to ease monetary policy should the incoming information confirm a protracted economic slowdown, and should the risk of increase in inflationary pressure remain limited. In line with its announcements, in 2013 Q1 the Council further eased its monetary policy, cutting interest rates on three occasions by a total of 1 percentage point; the reference rate was down to 3.25%.

The 2012 decisions of the Council supported price stability in the medium term. These decisions are presented below in greater detail, along with the circumstances under which they were taken.

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The data available at the beginning of 2012 pointed to a slowdown in the world economic growth in 2011 Q4 and continuing weaker external economic activity in 2012 Q1. Yet, there were considerable differences across the regions. In the United States in 2011 Q4 economic growth gained momentum, however data released afterwards suggested that this acceleration might be a short-lived phenomenon. On the other hand, although in 2011 Q4 the euro area was in a mild recession, the incoming data suggested that in the subsequent quarters economic activity of this region might be expected to improve somewhat. In the emerging economies, especially the Asian ones, GDP growth in 2011 Q4 saw a temporary deceleration. At the same time, global inflation was on a downward trend, albeit remained elevated, especially in the emerging economies.

Main central banks continued to ease their monetary policy, maintaining interest rates at historically low levels. In February 2012, the Fed announced that interest rates in the United States should remain close to zero at least until the end of 2014. The ECB, on the other hand, at the end of December 2011 and in February 2012 conducted two 3-year Long Term Refinancing Operations providing liquidity to the euro area banking sector (in the amount of EUR 489 billion and EUR 530 billion respectively) to counteract the consequences the sovereign debt crisis in the euro area.

Concurrently with the actions undertaken by the ECB, the EU leaders at the end of 2011 decided on measures aimed at institutional reforms of the euro area (adopting of preliminary assumptions for the Fiscal Pact). This, combined with monetary policy easing, and, to some extent, also improved expectations on the global economic activity, especially in the emerging markets, strengthened sentiment in the financial markets and supported the appreciation of currencies of many emerging markets, including the zloty. The same factors, coupled with geopolitical tensions at the turn of 2011 and 2012 observed in the Middle East, translated into higher commodity prices which remained an important upward risk factor for inflation decline across the world.

The data released in 2012 Q1 pointed to a relatively robust economic growth in Poland. In 2011 Q4, GDP growth accelerated in particular due to higher investment growth (both public and private). Similarly to the previous quarters, there were signs of some weakening in household consumption, which was largely driven by falling growth in real disposable income. Despite worsening of some leading business indicators, the data available at the beginning of 2012, including, above all, data on continuously high growth in corporate lending and just a slight decline in industrial and construction/assembly output suggested that economic slowdown in the subsequent quarters might be limited.

Inflation – despite a decline in January 2012 (base effects, related, in particular, to the fading impact of the January 2011 increase of VAT rates) – continued to run close to the level of 4%, i.e. well above the target and above the upper limit for deviations from the target. Also inflation expectations of households and corporations remained above the upper limit for deviations from the target. In parallel, core inflation was above its long-term average. Moreover, the March inflation projection suggested that despite the expected gradual weakening of economic growth in the subsequent quarters, inflation was likely to remain above the upper limit for the deviations from the target until the end of the year and continue to exceed 2.5% also in the first half of 2013. High level of inflation was supposed to be continuously driven by external factors remaining beyond the direct impact of the domestic monetary policy. The persistence of those factors, influencing inflationary processes, translated into extending the period in which inflation was forecasted to run above the inflation target as compared to the previous projection. At the same time, inflation running at an elevated level since 2010 raised a risk of inflationary expectations becoming persistently heightened, which would increase the costs of maintaining price stability in the longer term.

Taking into consideration the above developments, in the period January – April 2012 the Council kept the NBP interest rates unchanged, pointing out that unless the outlook for inflation returning to the target improve and signs of considerable economic weakening in Poland appear, the Council might tighten its monetary policy in the subsequent months.

The data released in April and at the beginning of May 2012 pointed to renewed intensification of the sovereign debt crisis in the euro area. This led to a significant deterioration in the financial markets sentiment and depreciation of currencies of the emerging economies, including the zloty. Despite decline in commodity prices, in particular, in prices of energy commodities, their level remained high.

At the same time, the data concerning Poland pointed to weakening of GDP growth in 2012 Q1. On the one hand, data on the labour market, including slow employment growth and a merely moderate wage growth, combined with a steady decline in lending to households, confirmed that consumption growth was likely to continue on a downward tread. Also leading economic indicators suggested a certain weakening in economic activity in the subsequent quarters. On the other hand, in the analysed period, forecasts of economic growth for Poland in 2012 were revised slightly upwards. Also corporate lending continued to rise rapidly.

Inflation continued to run close to 4%, thus remaining above the upper limit for deviations from the target. Moreover, the subsequent months were supposed to see its further rise, which was suggested by short-term forecasts. Also inflation expectations of households and corporates, despite some downward trend, continued above the upper limit for deviations from the target. Core inflation remained at a heightened level.

At its May meeting, the Council assessed that the prolonged period of inflation running above the upper limit for deviations from the target posed a risk of inflation remaining at a heightened level despite the expected economic slowdown. In the Council opinion, although the anticipated economic slowdown would support inflation decline, since inflation will continue to be negatively affected by factors beyond the impact of domestic monetary policy, the scale of the slowdown might be limited, posing risk to inflation returning to the target in the medium term. The risk of inflation continuing at a heightened level was additionally increased by the persistence of elevated inflation expectations. Therefore, the Council decided to increase the NBP interest rates by 0.25 percentage point; the reference rate was raised from 4.50% to 4.75%. At the same time, in was emphasized that the incoming data would enable an assessment whether any further interest rate adjustments might be justified.

The data released between the May and July meeting of the Council pointed to deteriorating business conditions abroad. Economic activity in the United States in 2012 Q2 remained moderate. In the euro area, economic growth was close to zero. GDP growth weakened in Germany, Poland's main trading partner. Persisting weak economic conditions in developed economies constituted a factor undermining economic activity in many emerging economies. At the same time, forecasts of the global economic growth in the subsequent quarters continued to be revised downwards.

Economic conditions and outlook for economic growth were adversely affected by mounting concerns about the sovereign debt crisis in the euro area, translating into weak sentiment in the financial markets. In June 2012 sentiment in the global markets started to improve as the EU leaders agreed on measures to be taken to mitigate the sovereign debt crisis and support economic growth in the euro area. Expectations on further monetary policy easing by major central banks, including the Fed and the ECB, was another factor behind improved financial markets' sentiment, which, in turn, boosted global commodity prices. Overall, while the slowdown in the world economy helped to curb inflation, in many countries it remained elevated.

In Poland, the data on GDP in 2012 Q1 confirmed a gradual slowdown in economic activity, amidst weakening demand, both external and domestic. The released monthly data for 2012 Q2 pointed to low employment growth and still moderate wage growth, combined with a gradual decline in growth of industrial and construction/assembly output. Leading economic indicators and the results of the NBP July projection suggested that GDP growth might weaken substantially in the coming quarters.

Despite a gradual deceleration of economic activity, inflation continued above the upper limit for deviations from the target. Despite some decline, also core inflation and inflation expectations remained elevated. Yet, in line with the July projection, following a temporary rise in Q3, inflation was supposed to decline and return to the target within the projection horizon. Therefore, inflation was expected to return to the target sooner than indicated by the March projection.

Taking into account the incoming data, including weaker economic growth and inflation returning to the target within one year's horizon – as indicated by the projection, in June and July 2012 the Council decided to keep the NBP interest rates unchanged. In the opinion of the Council, the monetary policy tightening which had already taken place supported inflation decline, thus ensuring macroeconomic stability of the economy. At the same time, the Council did not rule out further monetary policy adjustments should the prospects of inflation returning to the target deteriorate.

In September 2012 – in response to worsening growth prospects in major developed economies – central banks of the United States and the euro area decided to increase the scale of their monetary expansion. The Fed extended the announced period of maintaining interest rates at their record low levels from the end of 2014 to mid-2015 and largely increased the scale of quantitative easing. The ECB, on the other hand, after lowering interest rates by 0.25 percentage points in July 2012 (in particular the refinancing rate was cut to 0.75% and the deposit rate to 0) announced the programme of purchasing Treasury bonds of euro area countries most severely hit by the debt crisis.

Measures undertaken by major central banks considerably strengthened sentiment in the financial markets, which, in turn, supported strong growth in global commodity prices observed from June to September 2012. Food price growth in Q3 was additionally enhanced by concerns about a heavy contraction in food supply as a result of drought in the United States and Eastern Europe.

In Poland, the data on GDP in 2012 Q2 pointed to stronger than expected economic slowdown. Both consumption and investment growth declined. Change in inventories accounted for a significantly negative contribution to GDP growth. Leading economic indicators continued on a downward trend. Also quarterly data on the labour market and monthly data on economic activity in 2012 Q3 suggested that economic activity continued to weaken. In particular, employment growth halted and household lending was significantly reduced, thus contributing to lower retail sales growth. At the same time, corporate lending weakened considerably, construction/assembly output fell – partly due to finalizing of some of infrastructural investment projects after the European Football Championship – and manufacturing output further decelerated.

At the same time, despite slightly lower core inflation, headline inflation remained elevated, as, in line with the expectations, growth in food prices accelerated. Inflation expectations of households remained relatively high.

In September and October 2012, the Council decided that the incoming data had altered the assessment of the situation in Polish economy, including the assessment of the risk of inflation remaining above the target in the medium term. In particular, amidst stronger than anticipated economic slowdown, inflation could be expected to return to the target faster than forecasted, although high prices of commodities, including food and energy, remained a risk factor to the decline of inflation. Given the above, although the Council decided to maintain the NBP interest rates unchanged, it also announced that should the incoming data confirm that economic slowdown would become protracted, while the risk of increase in inflationary pressure be limited, monetary policy might be eased. At the same time, the Council expressed an opinion that a more thorough assessment of medium-term prospects for economic growth and inflation would be possible after taking into account the results of the November inflation projection of the NBP.

The data released in the period from October to early December 2012 suggested that the global economic conditions had stabilized at a low level, with considerable differences in economic activity across the regions. In 2012 Q3, GDP growth in the United States picked up slightly, yet uncertainty about the scale of fiscal tightening in the American economy constituted an import risk factor for U.S. economic outlook in the subsequent quarters. At the same time, the euro area remained in recession. Economic slowdown was also observed in Germany, Poland's main trading partner. In the emerging economies, in 2012 Q3 economic growth leveled off at a relatively low, as for those countries, level.

In 2012 Q4 the financial markets continued to see positive sentiment, which was supported by further monetary policy easing by main central banks. However, in the analysed period, also temporary deterioration of sentiment were observed, which was partly driven by the uncertainty about the scale and consequences of the 2013 fiscal tightening in the United States. The previous quarter's growth in commodity prices was halted, yet prices remained high.

The data on the Polish economy confirmed a marked slowdown in economic activity. In particular in 2012 Q3, GDP growth declined considerably, mainly on the back of falling domestic demand, as consumption had come to a halt and investment expenditure had been reduced. This was accompanied by stagnating employment and further steep decline in lending to households and corporates. At the same time, the monthly data for Q4 indicated that manufacturing output and retail sales had come to a halt and construction/assembly output continued on a downward trend. This, together with the leading economic indicators, suggested that economic growth might be low also in the subsequent quarters. This was also suggested by the November projection of the NBP which assumed economic slowdown to be stronger than forecasted in the July projection.

Starting from Q3 inflation started to decline, and in October 2012 it lowered below the upper limit for deviations from the target. The decline in inflation was driven, apart from weaker growth in energy prices, by a drop in core inflation resulting from falling demand and cost pressures in the economy. It could have been expected that also in the subsequent months the same factors would continue to bring inflation down. Lower inflation was followed by a gradual decreasing inflation expectations. In line with the November projection, inflation was assumed to approach the target in mid-2013 and then to run below the target.

The Council assessed that given a marked economic slowdown in Poland, demand pressure in the economy would be limited in the subsequent quarters, which posed a risk for inflation declining below the inflation target in the medium term. Such an assessment was also supported by the November projection. The Council was of the opinion that a decrease in the NBP interest rates should support economic activity and thus reduces the risk of inflation falling below the target in the medium term. Therefore, in November and December 2012, the Council cut interest rates on two occasions, by the total of 0.50 percentage points; in particular the reference rate was lowered from 4.75% to 4.25%. At the same time, the Council noted in its press releases that it would further ease monetary policy should the incoming information confirm a protracted economic slowdown, and should the risk of increase in inflationary pressure remain limited.

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In 2012 – as in the previous years – communication with the public was an important element in conducting monetary policy based on the inflation targeting regime. It involved presenting the Council's decisions together with the assessment of economic developments that influenced the decisions. The most important instruments of communication in 2012 continued to include the following cyclical publications: *Inflation Reports, Information from the meeting of the Monetary Policy Council* (with accompanying press conferences held after the Council's meetings), *Minutes of the Monetary Policy Council decision-making meetings* (Appendix 5), as well as the annually published: *Report on Monetary Policy Implementation in 2011* and *the Monetary Policy Guidelines for 2013*[4].

[4] *The Minutes of the Monetary Policy Council decision-making meetings* (Annex 5) present a more detailed discussion of the problems and arguments which had a significant impact on the decisions taken by the Council in 2012.

Chapter 3.

MONETARY POLICY INSTRUMENTS IN 2012

In pursuing its monetary policy in 2012, the Council strived to attain such level of interest rates in the economy as would be supportive of achievement of the adopted inflation target in the medium term.

The monetary policy instrument directly affected by the Council was the NBP interest rates. The level of the reference rate determined the yields on open market operations. The deposit and lombard rate, in turn, bounded the rates on the standing facilities. The rediscount rate indirectly determined the interest rate on the required reserve holdings.

The 2012 set of policy instruments applied by the NBP did not differ substantially from the one used the year before. It was aligned with the adopted monetary policy strategy as well as with the persistent surplus liquidity in the banking sector. With the use of these monetary policy instruments, the Council was influencing the level of money market short-term interest rates.

The range of adopted monetary policy instruments entitled the NBP to introduce additional operations in 2012, different from those applied in 2011. However, as the situation in the domestic financial markets was relatively stable in this period, such additional operations were not called for.

Banking sector liquidity in 2012

In 2012, the NBP pursued its monetary policy amidst liquidity surplus prevailing in the banking sector[5]. The amount of the surplus averaged PLN 96 306 in the year 2012, i.e. PLN 378 million (0.4%) more than in 2011.[6]

In the first half of 2012, the level of the banking sector liquidity surplus was relatively stable, following a slight downward trend. In subsequent months of the year a steady rise in excess liquidity was observed. In December average level of the liquidity surplus reached PLN 116 040 million.

Average liquidity surplus in the required reserve maintenance period in December 2012 was PLN 25 961milion up on the corresponding 2011 figure. The increase in the banking sector liquidity surplus resulted from the influence of following factors: the higher amount of foreign currency purchases by the NBP over sale of those (by PLN 16 172 million), the disbursement of the part of the NBP profit to the State Budget; the disbursement of the discount on the NBP bills (PLN 4 458 million) and the

[5] The liquidity surplus in the banking sector is the surplus of funds retained by the banking sector in excess of the required reserve during the maintenance period. Liquidity surplus is measured by the total balance of the following NBP operations: open market operations, foreign exchange swaps and standing facility operations.

[6] The data on excess liquidity are averages for the required reserve maintenance period.

disbursement of interest on the required reserve (PLN 1 276 million). On the other hand, banking sector liquidity was stemmed by: the rise in the required reserve ratio (PLN 2 007 million) the increase in the volume of cash in circulation (PLN 1 622 milion), the repayment of refinanced loans (PLN 359 million) and the increase in the amount of public sector deposits held at the NBP (PLN 84 million).

NBP interest rates

An instrument of key significance to the conduct of monetary policy was the NBP reference rate. Changes in the level of this rate set the direction of the monetary policy pursued. By determining the yields on open market operations the level of this rate influenced the interest on short-term money market instruments, including unsecured interbank deposits. With regard to overnight deposits, average interest rate (weighted by the value of the transaction) should approximate the NBP reference rate. The band for interest rate fluctuations regarding these deposits was bounded by the NBP deposit and lombard rates. The rediscount rate, in turn, indirectly determined the interest on the required reserve holdings.

In 2012, the Council changed the NBP policy rates on three occasions. Until 9 May 2012, they were standing at the following levels: reference rate at 4.50%, lombard rate at 6.00%, deposit rate at 3.00%, and rediscount rate at 4.75%. The Council's decision of 10 May 2012 raised all NBP interest rates by 25 bp. This was followed by a decrease of 25 bp as a result of the Council's decision of 8 November. The last Council decision to be taken in this regard in 2012 was to decrease all the central bank interest rates by another 25 bp on 6 December. As a result of these changes, as at the end of 2012, the NBP interest rates were standing at the following levels: the reference rate at 4.25%, the lombard rate at 5.75%, the deposit rate at 2.75% and the rediscount rate at 4.50%.

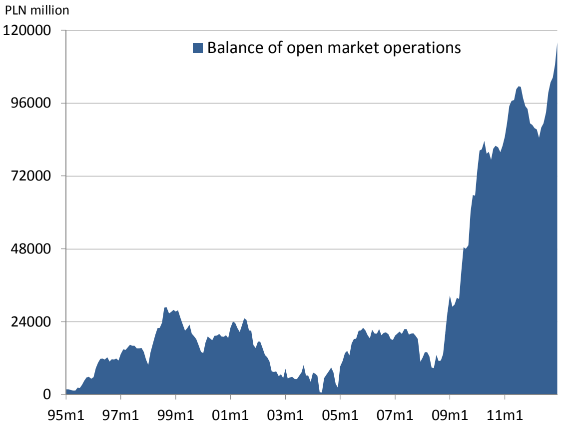
Open market operations

In 2012, the NBP used open market operations to manage the liquidity conditions in the banking sector. These were conducted on a scale sufficient to allow the POLONIA rate to to run close to the NBP reference rate[7]. Considering the persistent liquidity surplus in the banking sector, these operations were liquidity-absorbing and involved issuance of NBP bills.

[7] POLONIA (Polish Overnight Index Average) – average overnight rate weighted by the value of transactions on the unsecured interbank deposit market. The NBP publishes the levels of this rate on the Reuters information site (NBPS) every day at 5.00 p. m.

Figure 3.1

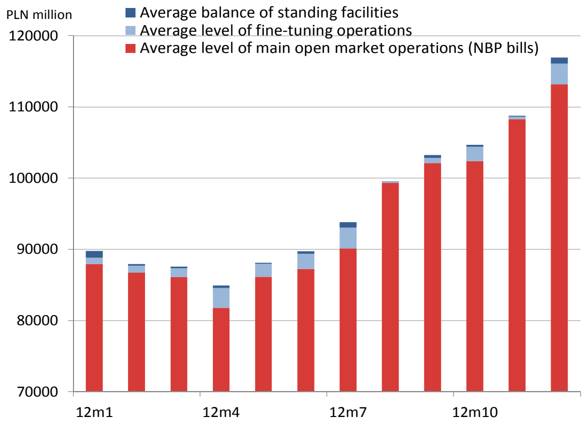
Average monthly balance of open market operations in 1995 - 2012.



Source: NBP data.

Figure 3.2

Liquidity absorbing instruments in the respective months of 2012.



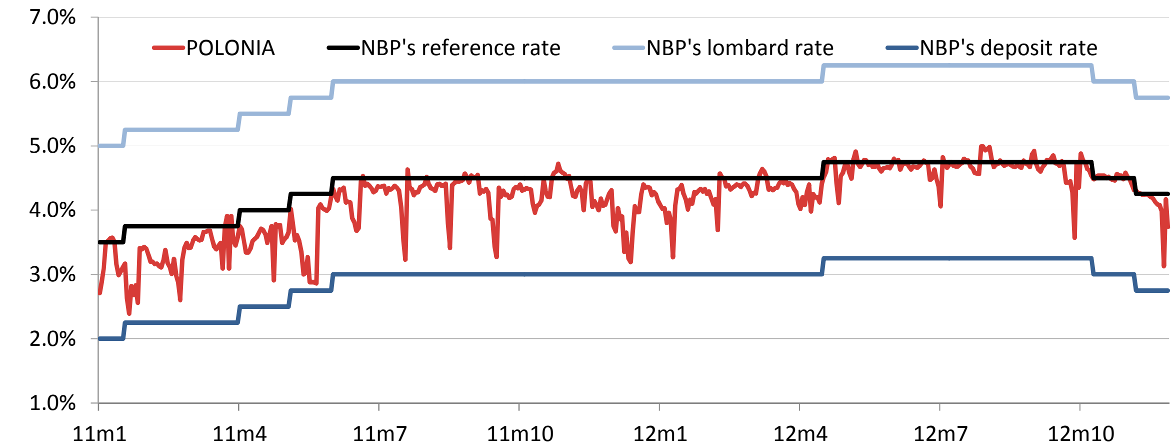
Source: NBP data.

The main open market operations were carried out on a regular basis, once a week, in the form of issue of NBP bills with 7-day maturity. The same yield was offered at all auctions and equal to the NBP reference rate. In 2012, the average daily volume of bill issued under main open market operations amounted to PLN 94 331, million and exceeded the 2011 level by PLN 567 million.

The Bank also issued the NBP bills as its fine-tuning operations. The maturity of these operations was shorter than the main open market operations. They were conducted on an ad-hoc basis during the required reserve maintenance periods, whenever liquidity conditions in the banking sector were substantially out of balance, and regularly on the last working day of the above mentioned periods. Twenty-three fine-tuning operations were altogether conducted in 2012, i.e. four less than in the previous year. All of them were liquidity-absorbing operations. The average daily issue of NBP bills under these operations amounted to PLN 1 582 million and exceeded the 2011 level by PLN 129 million.

Figure 3.3

The NBP interest rates and the POLONIA rate in 2011-2012.



Source: NBP data.

Despite tensions persisting in the global financial markets in 2012, which affected the banks' manner to manage their liquidity position, the POLONIA rate was running at levels markedly closer to the NBP reference rate than in the previous years.

Similarly to the previous year, in 2012 the fact that the POLONIA rate was tending towards the NBP reference rate resulted, to a great extent, from the continuation of fine-tuning operations conducted by the NBP in addition to the main open market operations. Such arrangement of open market operations helped to stabilise the expectations of the interbank market participants with regard to developments in the banking sector liquidity conditions. In managing their own liquidity positions, banks assumed that the central bank would be able to balance the liquidity conditions in the banking sector predominantly through open market operations. This diminished banks' propensity to invest their liquidity buffers in instruments yielding substantially lower than the NBP open market operations. This in particular referred to unsecured deposits carried out in the interbank market at a rate markedly below the NBP reference rate as well as overnight deposit offered by NBP on all working days.

The average deviation of the POLONIA rate from the NBP reference rate in 2012 was 21 basis points (bps)[8]. This is less than a half of the deviation seen in the previous year (43 bps) and one-third of the 2010 figure (69 bps). The volatility of the POLONIA index as measured by standard deviation was also smoothed out, amounting to 21 bps as against 34 bps in 2011 and 38 bps in 2010. In 2012, the average deviation of the POLONIA rate from the NBP reference rate - along with its volatility - came close to the domestic interbank market quotations seen before the onset of the crisis in the global financial markets.

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At the end of 2011, the National Bank of Poland launched activities designed to acquire information on the actual cost of money in the unsecured interbank deposit market. The arrangements were completed in March 2012, allowing for collection data on interbank transactions as of April 2012. The information is contained in the payment orders dispatched to the SORBNET system and relates to the maturities and yields on deposits made by domestic banks at other domestic banks. Based on these data, the NBP calculates the average rate on unsecured interbank market deposits with maturities quoted by the transactions on a given day, which helps assess the range of interest rate on the individual transactions with a given maturity. Additionally, the central bank is able to evaluate the diversification in the volume of transaction for the respective standard maturities.

The creation of the above-mentioned mechanism enabled the NBP, as one of very few central banks, to monitor the actual interest rate on the transactions concluded in the unsecured interbank deposit market and to compare it with the rates quoted by banks at the WIBID/WIBOR fixing.

The analysis carried out by the NBP shows that both the POLONIA rate, which includes only part of the *overnight* transactions in the discussed market, and the WIBID/WIBOR indices are in line with the actual rates on the unsecured deposits traded in the interbank market.

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[8] *Average deviation of POLONIA rate was calculated according to the uniform base of 365 days in the year.*

Reserve requirement

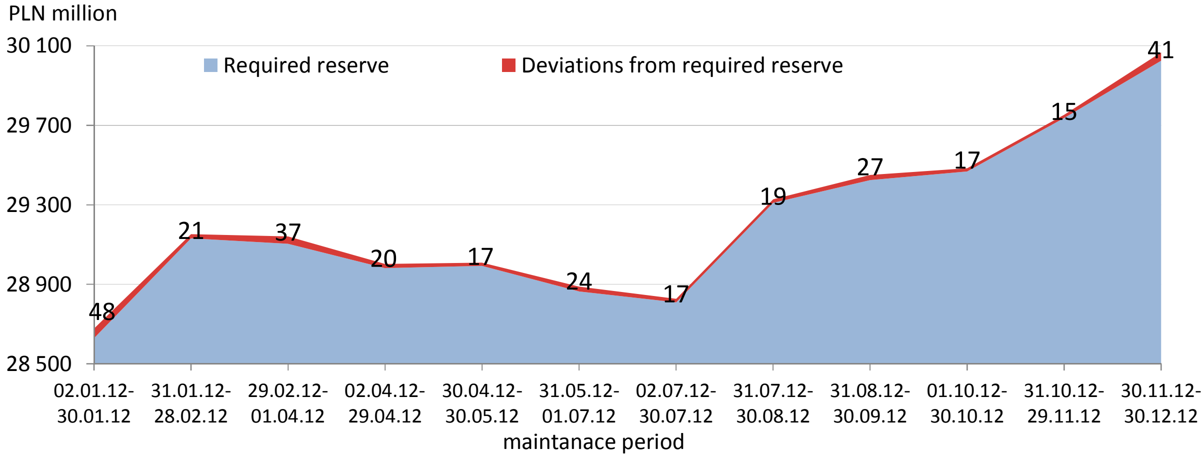
The system of required reserves has contributed to the stability of the short-term market interest rates. This resulted from its averaged basis, according to which the banks can freely determine the amount of holdings at the central bank during the maintenance period, provided that the average balances held at the NBP in the maintenance period are at least equal to the required reserve level.

Moreover, the obligation to maintain the required reserve limited the amount of surplus funds at the disposal of banks. Thus, under prevailing liquidity surplus, the reserve requirement system enabled the central bank to reduce the scale of its liquidity-absorbing open market operations.

The requirement to maintain a certain amount of reserves on accounts with the NBP applied to banks, branches of credit institutions and Polish subsidiaries of foreign banks. Required reserves were calculated on the basis of banks' collected deposits and funds coming from sale of securities. Excluded from reserve calculation were funds received from another domestic bank, funds acquired from foreign sources for the period of at least two years and those deposited in credit and savings accounts of building societies and in individual pension accounts. As of 29 February 2012, banks may also exclude from the reserve base the funds obtained under agreements for Individual Pension Insurance Accounts.

Figure 3.4

Changes in the required reserves level and deviations from the reserve requirement in 2012



Source: NBP data.

Required reserves were calculated and maintained in the Polish zloty. Banks reduced the amount of the calculated reserve requirement by the PLN equivalent of EUR 500 thousand. In 2012, the basic reserve requirement ratio amounted to 3.5% on all liabilities, except for funds received in respect of sale of securities in repo and sell-buy-back transactions, in which case the reserve requirement stood at 0.0%. The amount of required reserves as at 31 December 2012 stood at PLN 29 918 million, posting an increase of PLN 1 879 million on the corresponding figure recorded at 31 December 2011 (an increase of 6.7%).

The remuneration on the required reserve balances held by banks on accounts with the NBP was equivalent to 0.9% of the rediscount rate. The average interest on the required reserve funds in 2012 amounted to 4.37% as against 4.03% in 2011. The increase was the effect of the change in the rediscount rate, which rose from an average of 4.47% in 2011 to 4.86% in 2012.

In all reserve maintenance periods in 2012, average balances held by banks at the NBP remained slightly in excess of the required reserve. The surplus ranged from the low point of PLN 15.2 million observed in November to a peak value of PLN 47.8 million in January. The average excess reserves on banks' accounts amounted in 2012 to PLN 25.2 million, i.e. 0.09% of the average required reserve.

A factor conducive to minimising the difference between the reserve holdings and the required reserve in the respective periods was the availability of a range of instruments facilitating the management of funds on accounts with the NBP (open market operations, in particular the fine-tuning operations offered at the end of the maintenance period, overnight deposit, lombard credit) and the fact that remuneration on the reserve funds was not paid on amounts of the required reserve.

In 2012, one instance was recorded of failure to maintain the required reserve by a commercial bank. All the co-operative banks maintained the mandatory level of the required reserve in 2012.

Standing facilities

Standing facilities are designed to curb the scale of *overnight* market rate fluctuations. These operations were conducted at the initiative of banks, and were designed primarily to supplement the short term liquidity of the banking system and enable banks to place excess free funds with the NBP for the duration of one day. In this manner, the central bank was able to prevent excessive fluctuations in the interbank interest rates. The remuneration on lombard credit, which determines the price of money obtained from the NBP, set the upper bound of overnight rate fluctuations in the interbank market. The deposit rate, on the other hand, constituted the floor for their downward fluctuations.

In 2012, the banks' use of lombard credit was very limited. The total drawing on the lombard credit amounted to PLN 21 million, as compared with PLN 173 million in 2011. The average daily drawing on the lombard credit amounted to PLN 56 thousand.

In 2012, banks placed overnight deposits totalling PLN 143 billion at the NBP, i.e. 45.2% less than in the previous year. The average daily overnight deposit amounted to PLN 393 million, as against PLN 711 million in 2011.

Foreign exchange swaps

By using a foreign exchange swap or similar transaction, the NBP could purchase (or sell) zloty against foreign currency on the spot market, with a simultaneous sale (repurchase) in a fixed-date forward transaction.

In 2012, the central bank did not conclude such transactions.

Currency interventions

In 2012, the NBP did not intervene in the currency market.

Other operations

Intra-day credit helped banks to manage their liquidity position during the business day, while at the same time ensuring the liquidity of interbank settlements at the NBP. It is a non-interest bearing loan secured with debt instruments, incurred and repaid on the same business day. In 2012, daily provision of operating liquidity to the banks in the form of intra-day credit ranged from PLN 31.4 billion to PLN 57.0 billion. The drawing on intra-day credit increased by 34.5% on its 2011 level, which was related to the launch, at mid-2011, of the public finance consolidation process.

Intra-day credit in the euro is an instrument ensuring the liquidity of banks' settlements within the TARGET2-NBP system. The loan, incurred and repaid on the same business day was collateralised with Treasury securities previously accepted by the ECB. In 2012, the average daily euro liquidity provision to banks amounted to EUR 10 million. The drawing on this credit increased by 67.8% on its 2011 value.

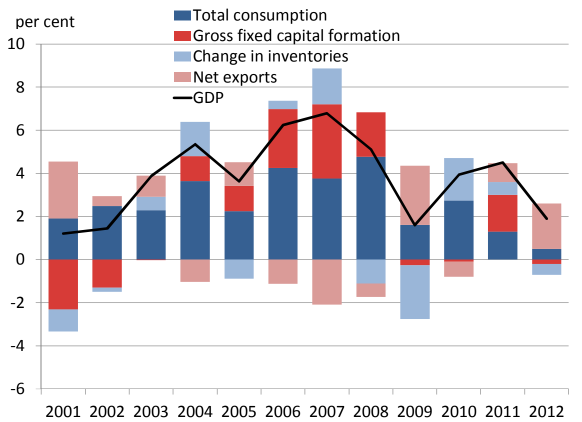
Appendix 1

GDP AND AGGREGATE DEMAND

In 2012, GDP growth slowed down and amounted to 1.9% y/y (as against 4.5% y/y in 2011). The decline in output growth – particularly pronounced in the second half of the year – was the effect of weaker consumption growth combined with a slight decline in investment. On the other hand, GDP growth was supported by a relatively high contribution of net exports, as imports decelerated faster than exports (Figure Z.1.1., Figure Z.1.2, Table Z.1.1). Slower exports growth was attributable to flagging external demand, which dragged on domestic demand through its adverse effect on investment, and, indirectly, also consumption.

Figure Z.1.1

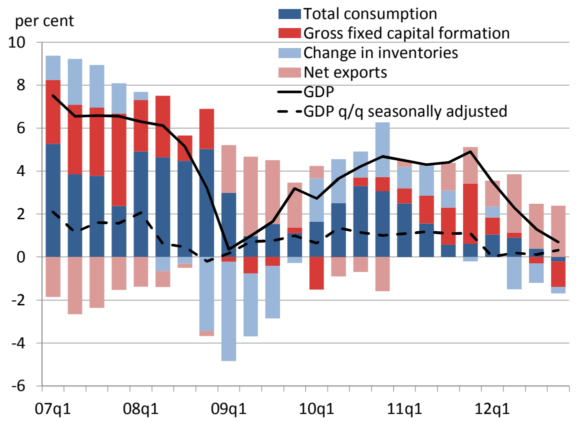
Contribution of aggregate demand components to GDP growth (annualized data).



Source: GUS data.

Figure Z.1.2

Contribution of aggregate demand components to GDP growth (quarterly data).



Source: GUS data, NBP calculations.

Private consumption growth, which in the first half of 2012 remained roughly at its 2011 Q4 level, slowed down considerably in the second half of 2012. Sluggish consumption demand was driven by a weak growth in households' disposable income, as wage growth declined amidst shrinking employment growth. Another factor curbing consumption was slower growth in lending to households, including a fall in consumer loans, and deteriorating sentiment of households – particularly on account of rising concerns about unemployment in the second half of 2012.

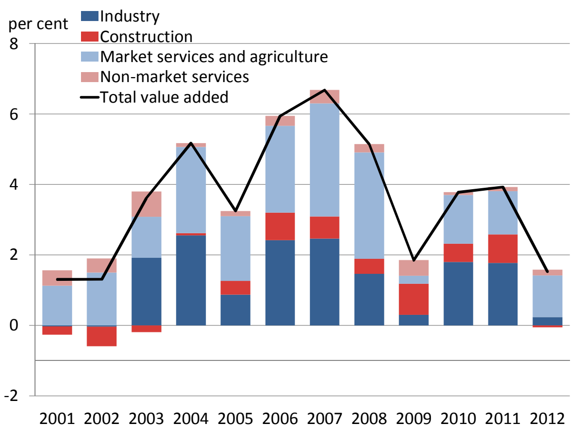
In 2012 gross fixed capital formation growth lost momentum, turning negative in the second half of the year. Investment growth was mostly dampened by a contraction in public investment, coupled with weaker household and corporate investment. Cuts in public investment were partly related to the completion of some infrastructural investment projects launched in the run-up to the European Football Championship, along with the effect of fiscal rules putting constraints on local governments' investment capacity. On the other hand, the subdued corporate investment activity can probably be ascribed to poor demand prospects amidst the anticipated domestic economic slowdown and rather weak external activity. This was compounded by a deterioration in enterprises' financial situation and tighter lending conditions imposed by banks on long-term corporate loans. Weaker corporate investment could additionally result from enterprises' limited needs to modernize their assets, as substantial expenditures to that end had already been incurred in the years 2010-2011[9]. Slower housing investment, in turn, was attributable to households' poorer economic situation, a substantial cuts in price limits under the government-subsidised housing scheme "Family on its Own" as well as the tightening of banks' credit policies in the mortgage loan segment. As gross fixed capital formation growth was sluggish and the contribution of change in inventories to GDP growth negative – a result of the pro-cyclical character of this category – accumulation in 2012 was lower than in 2011.

Public consumption in 2012 remained largely unchanged on its 2011 figure.[10] The stagnation in public consumption was related to government measures aimed at narrowing the public finance deficit, in particular to the implementation of the expenditure rule as well as fiscal rules in the local government units and to the wage freeze in the government sector.

In 2012, the largest contribution to GDP growth came from net exports (2.1 percentage points as opposed to 0.9 percentage points in 2011). The relatively large contribution of net exports resulted from continued exports growth amidst a substantial drop in imports demand related, on the one hand, to a slowdown in the import-intensive export production, and, on the other, to the flagging domestic demand.

Figure Z.1.3

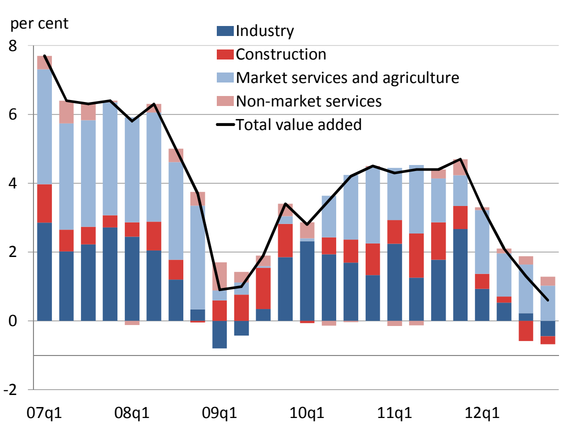
Contribution to gross value added growth (annual data).



Source: GUS data, NBP calculations.

Figure Z.1.4

Contribution to gross value added growth (quarterly data).



Source: GUS data, NBP calculations.

Gross value added rose in 2012 at a lower pace than in 2011 (1.8% versus 4.5%, respectively) due to a significantly slower value added growth in industry and its decline in construction. As a result, the largest contribution to value added growth came from market services and agriculture (1.2 percentage points), amidst a considerably lower contribution from industry and non-market services (0.2 percentage points each) and a slightly negative contribution of construction (-0.1 percentage points, Figure Z.1.3, Figure Z.1.4).

[9] This was reflected in a drop in newly launched replacement investment projects.

[10] The contribution of this category to GDP growth was nought.

Table Z.1.1

GDP and domestic demand.

	2004	2005	2006	2007	2008	2009	2010	2011	2012
Growth rate of GDP and its components at constant prices (%)									
GDP	5.3	3.6	6.2	6.8	5.1	1.6	3.9	4.5	1.9
Domestic demand	6.2	2.5	7.3	8.7	5.6	-1.1	4.6	3.6	-0.2
Consumption	4.3	2.7	5.2	4.6	6.1	2.0	3.4	1.6	0.6
Private consumption	4.7	2.1	5.0	4.9	5.8	2.1	3.2	2.6	0.8
Capital formation	14.7	1.4	16.1	24.3	3.9	-11.5	9.3	11.2	-3.3
Gross fixed capital formation	6.4	6.5	14.9	17.6	9.6	-1.2	-0.4	8.5	-0.8
Exports	14.0	8.0	14.6	9.1	7.1	-6.8	12.1	7.7	2.8
Imports	15.8	4.7	17.3	13.7	8.0	-12.4	13.9	5.5	-1.8
Contribution of net exports to GDP growth (percentage points)	-1.0	1.1	-1.1	-2.1	-0.6	2.7	-0.7	0.9	2.1
Structure of GDP at current prices (%)									
GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Domestic demand	102.4	100.7	101.8	102.9	104.0	99.9	101.2	101.2	99.7
Consumption	82.3	81.5	80.8	78.4	80.1	79.6	80.2	79.1	79.0
Private consumption	63.7	62.5	61.6	59.6	60.7	60.2	60.4	60.3	60.3
Capital formation	20.1	19.3	21.1	24.4	23.9	20.3	21.0	22.1	20.7
Gross fixed capital formation	18.1	18.2	19.7	21.6	22.3	21.2	19.9	20.2	19.4
Exports	37.5	37.1	40.4	40.8	39.9	39.4	42.2	45.1	46.2
Imports	39.8	37.8	42.2	43.6	43.9	39.4	43.4	46.2	45.8
Net exports	-2.4	-0.7	-1.8	-2.9	-4.0	0.1	-1.2	-1.2	0.3

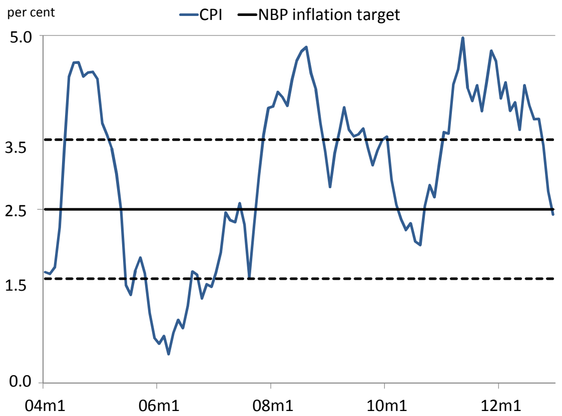
Source: GUS data, NBP calculations.

Appendix 2

PRICES OF CONSUMER GOODS AND SERVICES

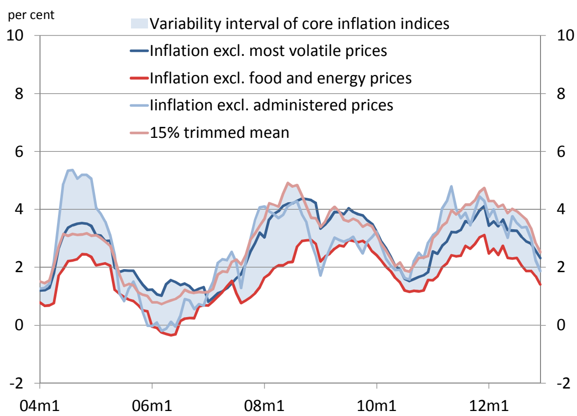
In 2012 the average annual index of consumer goods and services prices (CPI) stood at 3.7%, thus remaining above the NBP inflation target set at 2,5% ± 1 percentage point. Yet, inflation was lower than a year before, when it had run at 4.3%, and declined markedly during the year (from 4.1% in January to 2.4% in December 2012). As a result, at the end of 2012 inflation stood at the level consistent with the NBP inflation target (Figure Z.2.1, Table Z.2.1).

Figure Z.2.1
Annual CPI and the inflation target.



Source: GUS data.

Figure Z.2.2
Core inflation indices (y/y).



Source: NBP calculations based on GUS data.

Inflation running at a heightened level, especially in the first half of 2012, was primarily caused by a relatively sharp growth in administered prices – mainly those of energy carriers – driven largely by the 2011 and 2012 rises in electricity, gas and heating tariffs. This was combined with persistently steep growth in food prices and price effects of the weaker zloty as compared with the previous year. On the other hand, in particular in the second half of 2012, inflation was curbed by markedly lower demand and falling wage growth as well as zloty appreciation in that period. Moreover, inflation decline in 2012 was supported by the waning of the statistical base effects, including the impact of the January 2011 VAT rise.

2012 saw a decline in all core inflation measures, with the strongest drop observed in inflation net of administered prices (Figure Z.2.2).

The consumer price index reflects price developments in four main categories: energy, food and non-alcoholic beverages as well as goods and services (Figure Z.2.3, Figure Z.2.4). In 2012 price growth in all main categories of goods decreased, while remaining above the long-term average. Similarly to the previous year, energy and food and non-alcoholic beverages accounted for the largest contribution to inflation (Figure Z.2.4). In 2012, trends in price growth in individual categories were as follows (the order of categories reflects their contribution to the total CPI in 2012):

- Energy: Despite a fall in January 2012 (waning impact of VAT increases), in the first half of 2012 growth in energy prices remained relatively high on the back of rising tariffs on electricity, gas and heating, following the previously observed strong increases in energy commodity prices in the global markets. The second half of 2012, in turn, saw a gradual decline in energy price growth, particularly strong in Q4, partly driven by a fall in crude oil prices observed in this period (as compared to their strong rise in the corresponding period of 2011). Moreover, slower growth in energy prices at the end of 2012 was also supported by depreciation of the exchange rate of the zloty. In 2012, the average annual growth in energy prices stood at 7.9% (as compared to 9.1% in 2011).
- Food and non-alcoholic beverages: At the beginning of 2012 the average annual growth in prices of food and non-alcoholic beverages decelerated, in particular, as a result of increasing supply of cereals in the market. At the same time, the decline in the prices of the analysed aggregate was curbed by strongly rising prices of certain food articles[11]. In mid-2012 the annual growth in food prices accelerated due to stronger growth in prices of unprocessed food, largely driven by positive base effects and lower crops[12]. At the end of 2012, food price growth again declined slightly as supply of certain food items increased[13]. In 2012 the average annual growth in prices of food and non-alcoholic beverages reached 4.3% (as compared to 5.4% in 2011).
- Services: Slower growth in prices of services in 2012, similarly to the majority of other goods categories, was due to the waning impact of the 2011 VAT rises as well as weakening growth of demand. Following a decline in January 2012 (related to VAT) prices of services in the subsequent months of the first half of 2012 were relatively stable. In August 2012, service price growth sank due to the negative base effect of prices of urban transportation tickets and telephone subscription fees[14]. In the subsequent months, growth in prices of services remained relatively low. In 2012, the average annual growth in prices of services reached 3.0% (as compared to 3.3% in 2011).
- Goods: Despite the waning impact of VAT increases, as of January 2012, the growth in good prices remained relatively high in the first half of 2012. However, in the second half of 2012, amidst weakening demand, the growth of good prices started to decelerate. A particularly sharp fall in good price growth, observed in 2012 Q4, was partly caused by the base effect related to prices of medical and pharmaceutical products[15]. Comparatively high fluctuations in goods

[11] March 2012 saw a considerable rise in egg prices as a result of the implementation of EU regulations obliging chicken breeders to use larger chicken nesting boxes.

[12] In June 2012, there was a significant rise in vegetable prices. This rise was the result of a positive base effect connected with low growth in this food category in 2011 on account of reported cases of E. coli contamination.

[13] In particular, high supply of cereals in the domestic market was a factor behind falling prices in the group of bread and cereal products.

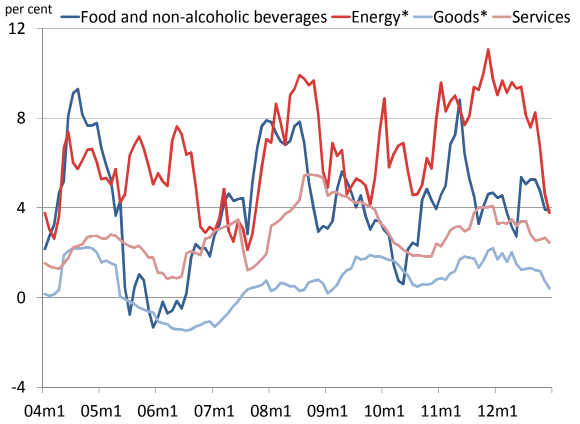
[14] August 2011 saw a strong rise in prices of urban transportation tickets and landline and mobile telephone subscription fees.

[15] Strong growth in prices of medical and pharmaceutical products in 2011 Q4, driven by the introduction of a new list of reimbursed drugs, considerably curbed growth in this price category at the end of 2012.

prices observed in 2012 were also the result of a different than a year before distribution of price changes in the tobacco product group following rises in the excise taxes. Moreover, earlier than in 2011 start of clothing and footwear sales also added to goods price volatility[16]. In 2012, the average annual growth in the prices of goods reached 1.3% (as compared to 1.5% in 2011).

Figure Z.2.3

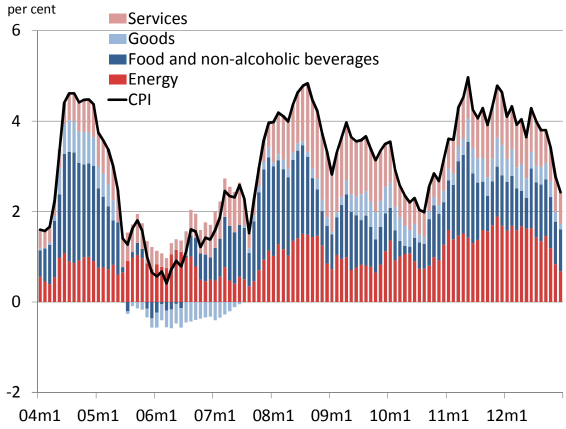
Annual price growth in the prices of food, energy, goods and services.



Source: NBP calculations based on GUS data.
*The category of *energy* includes energy products (electricity, gas, heating fuel).
***The category of goods is exclusive of food, non-alcoholic beverages and energy.*

Figure Z.2.4

Annual price growth in the prices of consumer goods and services and contribution of main price categories to CPI.



Source: NBP calculations based on GUS data.

[16] Due to a different distribution of price growth, resulting from the excise tax rise, in the first half of 2012 the growth in prices of tobacco products rose considerably and then declined. On the other hand, prices of clothes and footwear declined heavily in May as a result of a different timing of sales as compared to 2011.

Table Z.2.1

Annual price growth in consumer goods and services and contribution of main price categories to CPI.

	Weights 2012 (%)	Growth rate (y/y, in %)											
		2012											
		I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
CPI	**100.0**	**4.1**	**4.3**	**3.9**	**4.0**	**3.6**	**4.3**	**4.0**	**3.8**	**3.8**	**3.4**	**2.8**	**2.4**
Core inflation	**58.2**	**2.5**	**2.6**	**2.4**	**2.7**	**2.3**	**2.3**	**2.3**	**2.1**	**1.9**	**1.9**	**1.7**	**1.4**
Goods	29.6	1.7	2.0	1.6	2.0	1.5	1.2	1.3	1.3	1.2	1.2	0.7	0.4
Services	28.6	3.3	3.3	3.3	3.5	3.2	3.4	3.4	2.8	2.5	2.6	2.7	2.4
Food and non-alcoholic beverages	**24.2**	**4.5**	**4.5**	**3.7**	**3.2**	**2.7**	**5.4**	**5.1**	**5.3**	**5.3**	**4.7**	**3.9**	**3.9**
Processed	13.5	6.4	5.7	4.8	4.9	4.5	4.3	4.1	3.7	3.7	3.4	3.1	2.8
Unprocessed	10.7	2.1	3.1	2.5	1.0	0.6	6.7	6.3	7.3	7.4	6.6	5.0	5.3
Energy	**17.6**	**9.0**	**9.7**	**9.1**	**9.6**	**9.3**	**9.4**	**8.1**	**7.6**	**8.2**	**6.7**	**4.6**	**3.8**
Energy carriers	12.6	6.8	6.8	6.9	8.1	8.0	7.9	7.2	6.6	6.4	5.7	5.2	5.1
Fuels	5.0	14.8	17.2	14.9	13.4	12.7	13.1	10.6	10.2	13.0	9.2	3.2	0.7
		As broken down to 12 COICOP categories											
Food and non-alcoholic beverages	24.2	4.5	4.5	3.7	3.2	2.7	5.4	5.1	5.3	5.3	4.7	3.9	3.9
Alcoholic beverages and tobacco products	6.1	3.6	4.6	4.8	5.0	4.7	4.1	3.8	3.7	3.7	3.7	3.6	3.6
Clothes and footwear	4.9	-2.1	-1.8	-4.4	-2.6	-4.6	-5.0	-5.1	-5.1	-5.0	-4.6	-4.8	-4.7
Home maintenance and energy	21.3	6.0	6.0	6.0	6.8	6.6	6.5	6.0	5.6	5.5	5.1	4.8	4.7
Home equipment and household maintenance	4.6	2.6	2.4	2.3	2.6	2.5	2.4	2.3	2.2	2.2	2.3	1.9	1.9
Health	5.0	4.0	4.1	4.2	4.1	3.7	3.6	3.7	3.8	3.4	3.2	1.3	-0.2
Transportation	9.1	9.2	10.3	9.3	8.7	8.1	8.2	6.8	6.5	8.0	6.0	3.1	1.1
Communication	4.3	-0.5	-0.3	-0.3	1.2	2.3	3.3	3.6	0.1	0.1	-0.1	0.1	0.1
Recreation and culture	7.8	0.7	1.4	1.7	1.7	0.6	0.9	1.3	1.3	0.9	0.9	0.7	0.6
Education	1.2	5.1	5.1	5.0	5.0	5.0	4.9	4.7	4.9	2.5	2.7	2.7	2.7
Restaurants and hotels	6.4	3.7	3.3	3.1	2.9	2.9	2.9	2.9	3.0	2.9	2.9	2.8	2.8
Other goods and services	5.1	3.1	3.0	2.5	2.4	2.5	2.3	2.0	2.1	2.0	1.8	1.8	1.5

	Weights 2012 (%)	Contribution to CPI (in %)											
		2012											
		I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
CPI	**100.0**	**4.1**	**4.3**	**3.9**	**4.0**	**3.6**	**4.3**	**4.0**	**3.8**	**3.8**	**3.4**	**2.8**	**2.4**
Core inflation	**58.2**	**1.4**	**1.5**	**1.4**	**1.6**	**1.3**	**1.3**	**1.4**	**1.2**	**1.1**	**1.1**	**1.0**	**0.8**
Goods	29.6	0.5	0.6	0.5	0.6	0.4	0.4	0.4	0.4	0.4	0.4	0.2	0.1
Services	28.6	0.9	1.0	0.9	1.0	0.9	1.0	1.0	0.8	0.7	0.7	0.8	0.7
Food and non-alcoholic beverages	**24.2**	**1.1**	**1.1**	**0.9**	**0.8**	**0.7**	**1.3**	**1.2**	**1.3**	**1.2**	**1.1**	**0.9**	**0.9**
Processed food	13.5	0.8	0.8	0.6	0.7	0.6	0.6	0.6	0.5	0.5	0.5	0.4	0.4
Unprocessed food	10.7	0.2	0.3	0.3	0.1	0.1	0.7	0.7	0.7	0.7	0.7	0.5	0.6
Energy	**17.6**	**1.6**	**1.7**	**1.6**	**1.7**	**1.6**	**1.6**	**1.4**	**1.3**	**1.5**	**1.2**	**0.8**	**0.7**
Energy carriers	12.6	0.9	0.9	0.9	1.0	1.0	1.0	0.9	0.8	0.8	0.7	0.7	0.6
Fuels	5.0	0.7	0.8	0.7	0.7	0.6	0.7	0.5	0.5	0.6	0.5	0.2	0.0
		As broken down to 12 COICOP categories											
Food and non-alcoholic beverages	24.2	1.1	1.1	0.9	0.8	0.7	1.3	1.2	1.3	1.2	1.1	0.9	0.9
Alcoholic beverages and tobacco products	6.1	0.2	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Clothes and footwear	4.9	-0.1	-0.1	-0.2	-0.1	-0.2	-0.3	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Home maintenance and energy	21.3	1.3	1.3	1.3	1.4	1.4	1.4	1.3	1.2	1.2	1.1	1.0	1.0
Home equipment and household maintenance	4.6	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Health	5.0	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.1	0.0
Transportation	9.1	0.8	0.9	0.8	0.8	0.7	0.7	0.6	0.6	0.7	0.6	0.3	0.1
Communication	4.3	0.0	0.0	0.0	0.1	0.1	0.1	0.2	0.0	0.0	0.0	0.0	0.0
Recreation and culture	7.8	0.1	0.1	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.0
Education	1.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.0
Restaurants and hotels	6.4	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Other goods and services	5.1	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1

Source: GUS data and NBP calculations based on GUS data.

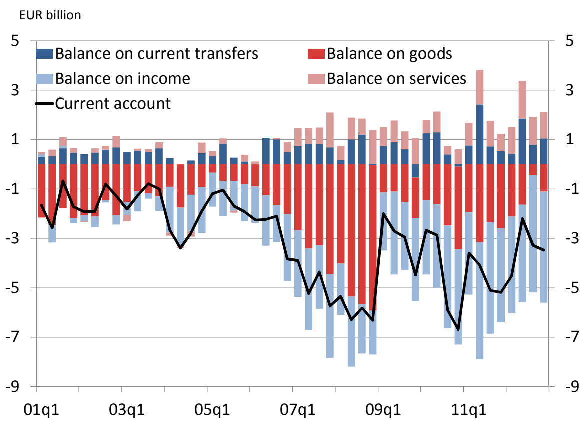
Appendix 3

BALANCE OF PAYMENTS

In 2012, the deficit on the current account amounted to EUR 13.5 billion, against EUR 18.0 billion in 2011. The improvement in the current account balance resulted primarily from considerably narrowed deficit on trade in goods. Also higher surplus on the trade in services supported the improvement. Factors working in the opposite direction included the increasingly negative balance on income and somewhat lowered surplus on current transfers (Figure Z.3.1, Figure Z.3.2, Table Z.3.1).

Figure Z.3.1

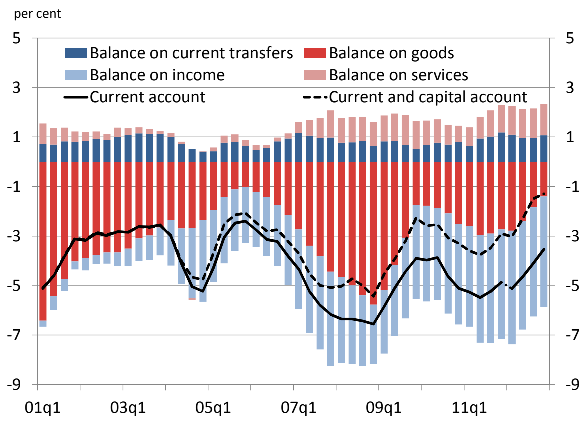
Current account balance (EUR billion).



Source: NBP data.

Figure Z.3.2

Current and capital account balance to GDP (4 quarters rolling window).



Source: NBP data.

In 2012, Poland's external trade slowed down substantially. As imports decelerated more than exports, the deficit on trade in the goods narrowed materially (to EUR 5.3 billion from EUR 10.1 billion in 2011). Slower import growth was driven by sluggish consumption combined with declining inventory levels and weak demand for intermediate goods from exporters [17]. Export trends, on the other hand, were largely determined by the economic situation in Poland's main export markets. In particular, sluggish economic growth in the European Union countries – the main recipients of Polish exports – dampened export growth, which, while remaining positive, was markedly slower than the previous years' average. At the same time, the slowdown was curbed by the robust expansion in import demand from the Commonwealth of Independent States.

The 2012 improvement in the current account balance was, to some extent, also the result of higher surplus on the trade in services (of EUR 4.8 billion, against EUR 4.0 billion in 2011). This was primarily the result of improved balances on transport services and foreign travels.

[17] Import growth deceleration was limited due to increasing prices of energy commodities at the beginning of the year and the appreciation of the zloty observed in the final months of 2012.

On the other hand, growing deficit on income (of EUR 17.1 billion against EUR 16.4 billion in 2011) limited the improvement of the current account. As in the previous years, the negative balance on this account was primarily attributable to high income obtained by non-residents on their Polish investment, including, in particular, direct and portfolio investment. In 2012 a certain decline in foreign investors' income on direct investment was visible, amidst a substantial rise in income from portfolio investment.

The surplus on current transfers – while still high – declined somewhat (to EUR 4.1 billion against EUR 4.4 billion in 2011). The decrease in the surplus supported narrowing current account deficit in 2012.[18]

Table Z.3. 1
Main items of the balance of payments (EUR million) [19].

Balance of payments	2005	2006	2007	2008	2009	2010	2011	2012
Current account	-5 856	-10 425	-19 245	-23 799	-12 152	-18 129	-17 977	-13 480
Balance on trade in goods	-2 508	-5 829	-13 827	-20 928	-5 427	-8 893	-10 059	-5 313
Balance on trade in services	585	582	3 441	3 475	3 427	2 334	4 048	4 816
Balance on income	-5 490	-7 728	-11 928	-8 685	-11 828	-14 415	-16 381	-17 082
Balance on current transfers	1 557	2 550	3 069	2 339	1 676	2 845	4 415	4 099
Capital account	786	1 666	3 418	4 068	5 080	6 453	7 254	8 545
Financial account	12 151	10 586	27 621	25 924	24 597	30 936	22 019	16 234
Polish direct investment abroad	-2 792	-7 137	-4 020	-3 072	-3 335	-5 484	-5 276	644
Foreign direct investment in Poland	8 330	15 741	17 242	10 128	9 343	10 507	13 646	2 664
Portfolio investment - assets	-2 008	-3 685	-4 606	1 701	-1 009	-799	527	-314
Portfolio investment - liabilities	11 797	1 485	-20	-3 655	11 303	20 041	11 415	15 671
Other investment - assets	-2 181	-3 137	-1 321	4 039	3 911	-2 837	-2 507	-1 622
Other investment - liabilities	-1 132	7 868	21 804	17 527	5 681	10 090	4 614	-3 067
Derivative financial instruments	137	-549	-1 458	-744	-1 297	-582	-400	2 258
Errors and omissions	-627	204	-2 414	-8 621	-7 111	-7 767	-6 602	-2 562
Overall balance	6 454	2 031	9 380	-2 428	10 414	11 493	4 694	8 737
Official reserve assets	-6 454	-2 031	-9 380	2 428	-10 414	-11 493	-4 694	-8 737

Source: NBP data.

In 2012, lower deficit on the current account was accompanied by a marked increase in the surplus on the capital account (to EUR 8.5 billion against EUR 7.3 billion in 2011) driven by higher inflow of funds under settlement of the completed investment projects co-financed by the EU. As a result, the total balance of the current and capital accounts improved significantly, reaching -1.3% of the GDP (Table Z.3.2).

[18] A decrease in the surplus on current transfers resulted from a slump in the positive balance of private transfers. This, in turn, stemmed from rising deficit on the so-called other transfers, amidst a virtually unchanged surplus of workers' remittances.

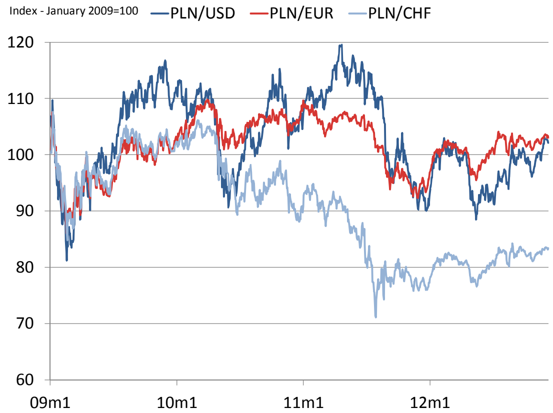
[19] With regard to the financial account, the presented figures should be interpreted as follows: positive (negative) amounts of residents' investment abroad (items: Polish direct investment abroad, portfolio investment: assets, other investment: assets) denote a decrease (increase) in Polish assets abroad. Conversely, positive (negative) amounts of non-residents' investment in Poland (items: foreign direct investment in Poland, portfolio investment: liabilities, other investment: liabilities) mean an increase (decrease) in Polish liabilities towards non-residents. The sum of items A to D is equivalent to the value of transactions by the NBP. As a result, in the balance of payments convention, the opposite sign is used with respect to the item "change in official reserve holdings": a negative sign denotes increase in the official reserve assets, while a positive sign denotes decrease in these assets.

In 2012, there was a significant decrease in the inflow of foreign direct investment to Poland. Consequently, although the combined current and capital account deficit was substantially curbed, its financing with foreign direct investment declined as compared to 2011[20]. On the other hand, the surplus on the financial account was boosted by the portfolio investment surplus, which was largely related to an increase in non-residents' investment in debt securities issued on the domestic market.

In the course of 2012, the zloty exchange rate appreciated vis-a-vis major currencies (by 9.3% against the euro, by 8.9% against US dollar and by 7.7% against the Swiss franc; Figure Z.3.3), although periods of zloty depreciation were occasionally observed during the year[21]. The nominal effective exchange rate (NEER) strengthen by 7.9% in 2011[22].

Figure Z.3.3

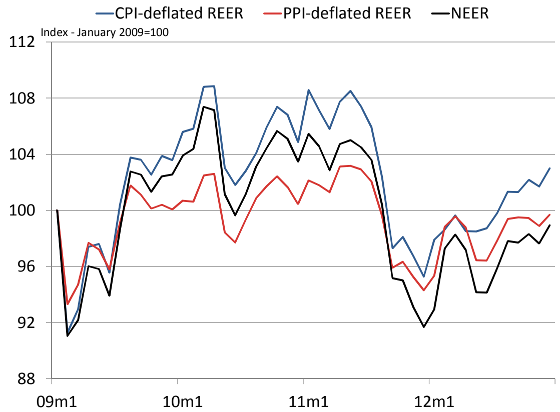
Zloty exchange rate against major currencies.



Source: Ecowin data.
Increase denotes appreciation.

Figure Z.3.4

Zloty real and nominal effective exchange rate.



Source: NBP calculations based on Eurostat, OECD, Reuters data.
Increase denotes appreciation.

In 2012 some indicators of Poland's external imbalance improved, while others deteriorated. In particular, there was a significant reduction in the deficit on the current and capital accounts in relation to the GDP. In turn, the international investment position, after a marked improvement observed in 2011, in 2012 again weakened.

[20] The balance of foreign direct investment in Poland in 2012 was affected by one-off transactions related to the phenomenon of capital in transit. This was observed in particular in 2012 Q1 and Q4.

[21] Change calculated as difference between the average rates in December 2012 and December 2011.

[22] Exchange rate in December 2012 as against exchange rate in December 2011.

Table Z.3. 2

Selected indicators of external imbalances.

	2005	2006	2007	2008	2009	2010	2011	2012
Current account balance/GDP(%)	-2.4	-3.8	-6.2	-6.6	-3.9	-5.1	-4.9	-3.5
Current and capital account balance/GDP (%)	-2.1	-3.2	-5.1	-5.4	-2.3	-3.3	-2.9	-1.3
Balance on trade in goods/GDP (%)	-1.0	-2.1	-4.4	-5.8	-1.7	-2.5	-2.7	-1.4
Current account balance/current account inflows (%)	-0.8	-1.9	-3.3	-4.8	-0.6	-1.8	-1.6	-0.1
Gross foreign direct investment /current account balance (%)	142.2	151.0	89.6	42.6	76.9	58.0	75.9	19.8
Gross foreign direct investment /current and capital account balance (%)	164.3	179.7	108.9	51.3	132.1	90.0	127.3	54.0
Foreign debt/GDP (%)	4.7	3.8	3.9	3.3	5.3	5.4	5.2	5.6
Official reserve assets in terms of monthly imports of goods and services	45.9	47.4	50.9	47.9	62.4	66.9	67.2	74.0
Short-term foreign debt/total foreign debt (%)	20.4	20.4	26.1	26.9	25.0	24.4	22.4	19.3
Short-term foreign debt/official reserve assets (%)	63.6	71.3	92.6	106.0	88.0	82.6	73.4	64.1
Net international investment position/GDP (%)	-44.2	-46.4	-52.6	-47.5	-61.8	-66.0	-59.3	-69.0

Source: NBP calculations based on GUS and NBP data.

Appendix 4

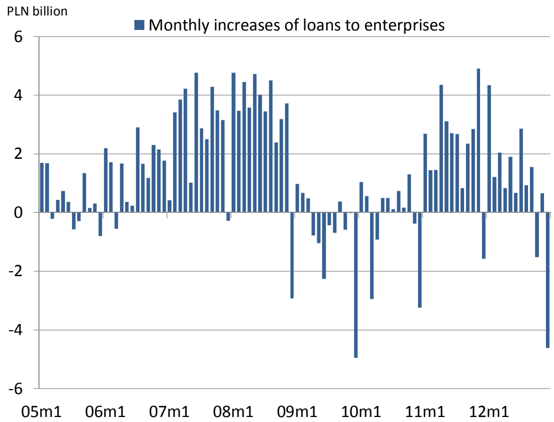
MONEY AND CREDIT

In 2012, lending to both corporates and households continued to rise; yet, in the course of the year, the pace of growth gradually lost momentum, and was substantially weaker than in 2011 (Figure Z.4.1, Figure Z.4.3).

The deceleration of corporate lending in 2012 was the combined effect of a slowdown in both current loans and investment loans. This could have been partly driven by weaker corporate investment demand, amidst banks' tighter lending policy.

Figure Z.4.1

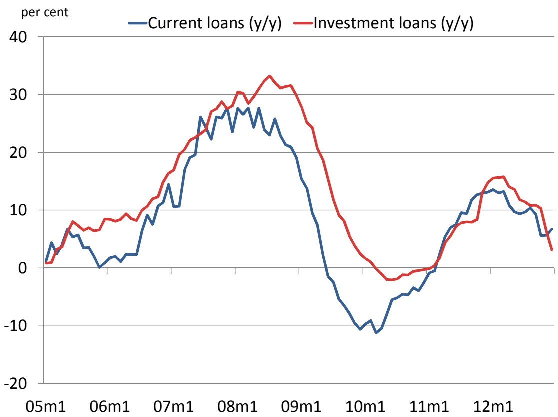
Month-on-month changes in loans to enterprises.



Source: NBP data.

Figure Z.4.2

Investment and current loan growth.



Source: NBP data.

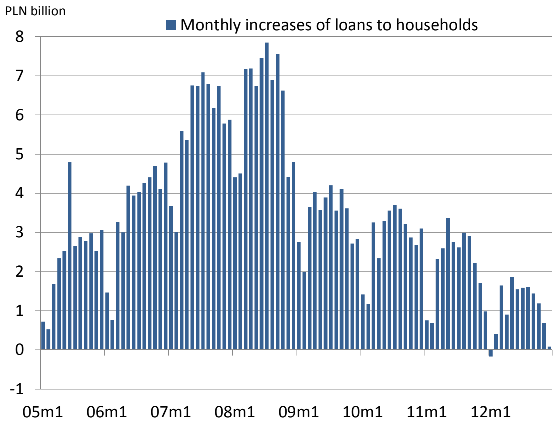
In 2012, banks continued to tighten both their lending criteria and lending terms, in particular by increasing collateral requirements on corporate loans and raising margins and non-interest cost of credit.[23] Heightened macroeconomic risk relating to the future economic situation was quoted by banks as the main reason behind changes in their lending policy.

Weaker household lending growth in 2012 resulted from a slower rise in housing loans and a sharper than before fall in consumer loans (Figure Z.4.4.). Growth in housing loan declined due to a fall in foreign currency-denominated loans, combined with a certain slowdown in zloty-denominated lending. As a consequence, the share of zloty-denominated loans in total loans continued to rise steadily in 2012, adding to the efficiency of the monetary policy transmission mechanisms.

[23] An exception was 2012 Q2 when banks temporarily relaxed their lending criteria and most of the lending terms. Lending policy easing in this period resulted primarily from better assessment of the current or anticipated capital position of banks, mounting competitive pressure and a temporary decrease in risk related to the future economic situation.

Figure Z.4.3

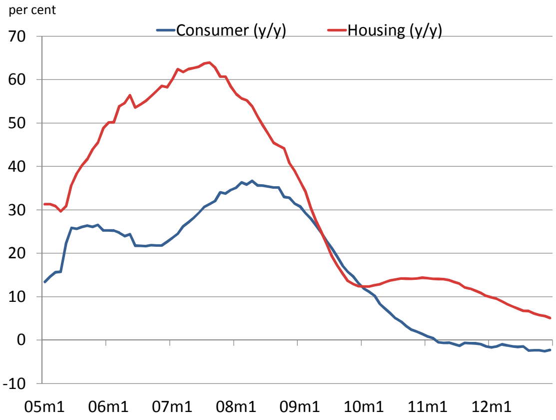
Month-on-month changes in new zloty loans to households.



Source: NBP data.

Figure Z.4.4

Annual growth in consumer and housing loans to households.



Source: NBP data.

The 2012 rise in housing loans was hampered by substantial lowering of price limits applicable to government-subsidized housing scheme *Rodzina na swoim* (*Family on their own*), and the deteriorating economic situation of households, which was coupled with banks' tighter lending policy and a certain rise in interest on loans[24]. Banks tightened both their lending criteria and lending terms, especially the cost of credit. To an increasing extent, they justified the change in their policy with credit risk related to the anticipated economic situation and unfavourable outlook for the housing market.

With regard to consumer loans, their further decline was partially driven by a certain tightening of the criteria for this type of loans introduced by banks, combined in the second half of 2012 with lower household demand for credit. Since the banks raised their credit margins, interest on consumer loans rose as well.[25] Banks' more stringent lending policies with regard to consumer loans were related to the rising share of non-performing loans in the banks' loan portfolio and heightened uncertainty about future economic situation.

In 2012, broad money (M3) growth decline, however it remained slightly above nominal GDP growth (Figure Z.4.5).[26] Slower M3 growth was driven by a decline in corporate deposits amidst weaker growth in household deposit (Figure Z.4.6). As current deposit growth decelerated, the more liquid components of M3, included in the M1 aggregate, also recorded a slowdown. As a result, in 2012, M1 grew at a slower pace than the broad money.

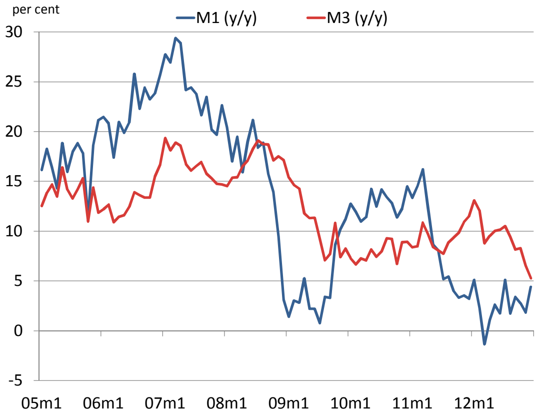
[24] Average annual interest on housing loans was 0.4 pp higher in 2012 than in 2011.

[25] Average annual interest on consumer loans was 0.6 pp higher in 2012 than in 2011.

[26] In terms of transactions, M3 growth amounted to 5.3% (December 2012 to December 2011) as against nominal GDP growth of 4.9% in 2012.

Figure Z.4.5

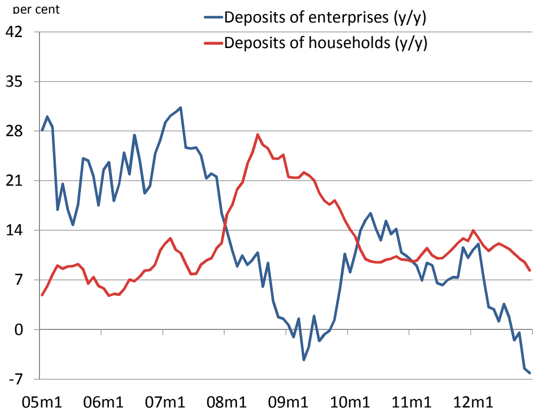
Annual M1 and M3 growth rates.



Source: NBP data.

Figure Z.4.6

Corporate and household bank deposit growth.



Source: NBP data.

In 2012, the total value of corporate deposits decreased substantially (by PLN 12.5 billion)[27]. At the beginning of the year, the annual growth of corporate deposits was relatively high, but in the following quarters it steadily declined, turning negative in 2012 Q4. The fall in corporate deposits observed despite a rise in the interest paid on deposits could have been related to some deterioration in firms' financial situation[28].

On the other hand, the total value of household deposits increased in 2012. Yet, the growth in these deposits decreased in the course of the year (particularly in the second half of 2012) and the total increase was substantially lower than in 2011. Weaker deposit growth was driven by deteriorating economic condition of households. The scale of the slowdown could have been reduced by a certain rise in interest paid on deposits [29].

[27] It was the first such significant decline in total corporate deposits in annual terms. A slight decline in the stock of deposits (of PLN 0.5 billion) was recorded in 2000. In 2009, despite a contraction observed throughout several months, the stock of corporate deposits rose by PLN 15.9 billion.

[28] Annual average interest on corporate deposits was 0.5 pp higher in 2012 than in 2011.

[29] Average annual interest on household deposits was 0.6 pp higher in 2012 than in 2011.

Appendix 5

MINUTES OF MPC DECISION-MAKING MEETINGS HELD IN 2012

Minutes of the Monetary Policy Council decision-making meeting held on 11 January 2012

At its meeting, the Monetary Policy Council discussed current and future monetary policy decisions against the background of expected growth and inflation trends in Poland, which will be strongly affected by both external conditions (growth outlook abroad, situation in the financial markets, commodity prices) and domestic factors, as well as the exchange rate developments.

While analysing the situation in the Polish economy, the members of the Council pointed out that current data on industrial output, construction and assembly output and retail sales indicate that growth continues to be relatively strong. Few members of the Council also highlighted a stable rise in loans - despite prior interest rate increases - as a sign of relatively good business conditions still prevailing. At the same time, it was emphasised that in the coming quarters, a slowdown in economic activity at home can be expected. It was pointed out that uncertainty related to the external environment of the Polish economy, including the scale of the slowdown abroad and potential impact of the turmoil in the global financial markets on the Polish economy, combined with the uncertain pace and structure of further fiscal tightening at home, make it difficult to assess how strong the deceleration in the growth of demand in Poland would be.

While discussing the external conditions of the domestic economic climate, members of the Council indicated that tensions in the financial markets resulting from the sovereign debt crisis in the euro area persist, and growth forecasts for the region continue to be revised downwards. Few members of the Council emphasised the risk of heavy lending constrains in the euro area countries, which would further deteriorate growth outlook for the region. Other members of the Council, however, assessed the risk of further marked weakening in growth forecasts for the euro area as limited, in particular for countries being Poland's main trading partners.

In the opinion of few members of the Council, tensions in the European banking system may translate into constraints on lending in Poland. However, with reference to the risk that foreign banks might curb the funding for lending purposes in Poland, other members of the Council assessed it to be small, and given the significant number of enterprises financing themselves from their own funds or directly from abroad, possible constraints on lending imposed by domestic banks should not significantly undermine enterprises' activity in Poland.

Referring to the outlook for foreign trade, some members of the Council argued that a weaker zloty would alleviate the effects of the decreasing foreign demand for Polish goods by improving their price competitiveness. Other members of the Council pointed out that due to a large share of intra-corporate trade in Polish exports, the volume of foreign trade is hardly sensitive to exchange rate fluctuations. Most members of the Council assessed, however, that in the subsequent quarters Poland's trade balance should improve and net exports should contribute positively to GDP growth.

In the opinion of some members of the Council, a slowdown in economic activity in Poland may be weaker than previously expected, as output growth remains relatively stable in spite of a decline in the leading business climate indicators. Moreover a continued rise in investment loans to enterprises and a steep growth in mortgage loans to households additionally support this opinion. Those members of the Council also pointed out that activity in the euro area will be the weakest in the countries most severely affected by the debt crisis, whose links with the Polish economy are not particularly close. They also emphasised that in the previous years, the Polish economy developed at a relatively fast rate even in the face of sluggish growth in the euro area.

Few members of the Council indicated, instead, that the economic slowdown in Poland may be more severe than previously anticipated. In the opinion of those members of the Council, this scenario is supported by worsening investment outlook of enterprises combined with the expected weakening in the public sector investment activity. At the same time, other element of fiscal tightening - the freeze on wages in the government sector - will curtail the growth of consumption. A similar effect will be brought about by unemployment rate persisting at an elevated level, which may dampen wage growth throughout the economy.

When discussing inflationary developments, attention was drawn to a higher than expected rise in inflation in November 2011 and an upward revision of inflation forecasts for the coming year, both resulting to a large degree from the hitherto depreciation of the zloty. It was pointed out that the persisting elevated inflation was accompanied by a considerable rise in inflation expectations of individuals and enterprises.

Some members of the Council emphasised that while inflation should gradually decrease over the coming months, it would probably remain above the NBP target for a longer time than hitherto envisaged. Increases in the rates of indirect taxes and in administered prices were indicated as the factors continuously contributing to rising inflation.

Moreover, few members of the Council additionally pointed out that unit labour costs might limit inflationary pressure to a lesser extent than in the previous years. In their opinion, a significant increase in minimum wages, a rise in disability pension contribution and the rising percentage of long-term unemployed - who are less competitive as compared with employees and those actively seeking jobs - combined with decreasing labour productivity resulting from the expected deterioration in business climate, will trigger a higher growth in unit labour costs.

Referring to the external conditions for inflationary processes, few members of the Council emphasised that in the medium term a significant curbing of inflation in Poland would be made difficult by the persistently elevated inflation abroad and continuously high commodity prices in the global markets, related - in their opinion – to strongly expansionary monetary policy pursued by major central banks, including considerable excess liquidity in the global financial markets. Apart from expansionary monetary policy, high commodity prices will be also supported by: continued growth in demand from the developing countries and a possible mounting of political tensions in the commodity-exporting countries. According to those members of the Council, a lowering of inflation at home will be additionally made difficult by weaker anti-inflationary impact of imports from low-cost countries, where rate of growth of labour costs exceeds that of labour productivity and a relative appreciation of their currencies follows.

As regards the monetary policy decisions implemented so far, the members of the Council assessed that the NBP interest rate increases in the first half of 2011 and the following stabilisation of monetary policy parameters in the second half of 2011 have been conducive to maintaining macroeconomic stability. In the last months of 2011, earlier signs of significant economic slowdown in Poland were not confirmed, while inflation increased, thus adding to the risk of inflation persisting above the target. Few members of the Council additionally pointed out that although the NBP interest rates remained unchanged, the depreciating exchange rate and rising inflation have resulted in easier monetary conditions in the recent months.

While discussing the decision on the NBP interest rates, the members of the Council agreed they should remain unchanged at the current meeting. As a main argument in favour of this decision a high uncertainty of economic activity in the coming quarters was mentioned. With reference to future monetary policy decisions, on the other hand, most members of the Council were of the opinion that should the relatively fast domestic growth, elevated inflation and high inflation expectations continue, the increase in NBP interest rates cannot be ruled out. It was pointed out that in assessing the outlook for medium-term growth and inflation, the incoming data on economic activity and inflationary processes in Poland in the coming months as well as the NBP March projection would be helpful.

Most members of the Council emphasised that a possible future decision to raise the NBP interest rates would be justified if the economic activity were to decelerate only slightly and inflation were not be in a clear downward trend. An important argument in favour of such a decision would also be the end of downward revisions of the euro area growth forecasts. Moreover, those members of the Council pointed out that future decisions on monetary policy would be greatly affected by the assessment of the implementation of further fiscal tightening.

At the same time, few members of the Council argued that in case of a considerable economic slowdown or a significant appreciation of the zloty, a cut in the NBP interest rates may prove justified.

The Council decided to keep the NBP interest rates unchanged at the following levels: reference rate at 4.5%, lombard rate at 6.00%, deposit rate at 3.00%, rediscount rate at 4.75%.

Minutes of the Monetary Policy Council decision-making meeting held on 8 February 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of external and domestic macroeconomic developments, including inflationary processes in the Polish economy.

While discussing the external conditions of the Polish economy, attention was drawn to the further downward revisions of GDP growth forecasts for the euro area, suggesting stagnation in the euro area economy in 2012. Some Council members pointed out that banks' efforts to increase their equity capital posed risk of further reduction in lending in the euro area countries, what would additionally worsen the outlook for the euro area growth. At the same time, it was noted that the business climate in the United States had improved, although some members of the Council argued that the acceleration in consumption in 2011 Q4, may turn out to be temporary and it should be expected that subsequent quarters will bring weaker growth in the US economy.

While analysing the external environment of the Polish economy, members of the Council drew attention to the fact that despite persisting uncertainty connected with the fiscal crisis in some euro area countries, the sentiment in the global financial markets improved. This was reflected in the appreciation of currencies of developing economies, including the zloty. At the same time, the Council members emphasised that it was difficult to assess whether zloty strengthening would be sustained. This was due to the fact that although the equilibrium exchange rate most probably remained stronger than the market rate, the zloty exchange rate is currently primarily driven by global factors, including, in particular, changes in risk aversion in the financial markets.

While discussing the outlook for the growth in domestic economy, members of the Council pointed to signs of weakening in economic activity, in particular, to slowdown in the growth of Polish exports to the euro area, persistently heightened unemployment rate and weaker growth in household lending. Yet, in the opinion of some Council members, the slowdown in the domestic economic activity may be less pronounced than previously anticipated, which is suggested by an improvement in some economic climate indicators pointing to a relative resilience of the Polish economy to the worsening of business activity abroad.

Some members of the Council assessed, however, that GDP growth in Poland was likely to decline substantially, what, in their opinion, would be driven, on the one hand, by further fiscal tightening, and, on the other hand, by weaker private consumption growth, being the result of the rebuild of household savings, following a considerable fall in the savings rate observed in the recent period. At the same time, according to those Council members, slight decline in production capacity utilization, considerable uncertainty and a large share of replacement investment in total corporate investments, which can easily be discontinued, make further investment acceleration rather unlikely. Additionally, the appreciation of the zloty, amidst worsening business climate abroad, is likely to lower net exports contribution to domestic GDP growth.

While discussing inflationary developments, members of the Council emphasized that the anticipated weakening of the domestic economic activity, connected with both slowdown in the global economic growth, as well as, tightening of the domestic fiscal policy, would support gradual decline in inflation. Also, the appreciation of the zloty at the beginning of 2012 would be a factor lowering inflation. It was pointed out that inflationary pressure in the subsequent quarters would also be curbed by elevated unemployment and low wage pressure.

At the same time, some members of the Council pointed out that inflation in Poland had been running above the upper limit for deviations from the target, i.e. 3.5%, for a year now. Members of the Council also emphasized that despite some decline in inflation, the NBP short-term forecasts pointed to a risk of inflation remaining above the target of 2.5% throughout 2012. In turn, in the opinion of few Council members, inflation persisting above the target for an extended period of time creates a risk of wider indexation of contracts, including wage contracts, which would be a factor strengthening inflation persistence and preventing it from returning to the target. Those Council members pointed out that a similar effect may be brought about by inflation expectations of both households and corporates running at an elevated level.

Members of the Council emphasized that growth in energy prices would continue to push up domestic inflation. Against this background, it was noted that the persistently growing demand for oil in the global economy, amidst limited growth of oil supply (especially, taking into account geopolitical tensions in the oil mining regions), may contribute to higher crude oil prices also in the long-term, limiting inflation decline in Poland. Some members of the Council pointed out that the NBP surveys showed an increase in the number of companies intending to raise prices of their products in response to the expected further surge in prices of commodities and materials. In the opinion of few Council members, domestic inflation may also be increased by higher inflation abroad, should the expansionary policy pursued by major central banks, including continued quantitative easing, translate into global inflationary pressure.

Few Council members additionally pointed out that amidst the expected decline in domestic economic activity, budget revenues growth may be lower than assumed what, considering the planned scale of fiscal tightening, posed a risk of indirect tax increases. This would, in turn, translate into further price increase in the Polish economy, extending the period of heightened inflation.

Moreover, few Council members noted that despite keeping the NBP interest rates unchanged in the recent period, interest rate increase in the interbank market in 2011 Q4 meant that monetary policy conditions in Poland became more restrictive, in particular, taking into account the appreciation of the zloty at the beginning of 2012.

However, some members of the Council argued that the real interest rates were not high, considering the structural factors and the current macroeconomic situation in Poland. Those Council members also pointed out that the total increase in interest on loans to the private sector in 2011 was, despite interest rate rise in the interbank market at the end of 2011, somewhat lower than the increases in the NBP reference rate implemented by the Council in the first half of 2011. Moreover those Council members emphasized that the growth in money supply had been on the rise, reaching now a relatively high level.

While discussing the decision on the NBP interest rates, the members of the Council agreed that they should remain unchanged at the current meeting. As regards future monetary policy decisions, the majority of the Council members maintained their view that should the relatively fast domestic economic growth, elevated inflation and high inflation expectations continue, the increase in the NBP interest rates cannot not be ruled out. The majority of the Council members also pointed out that the decrease in inflation driven by the expected decline in demand might prove slower than previously anticipated. In this context, it was still emphasized that the incoming data on economic activity and inflationary processes in Poland in the coming months, as well as the NBP March projection, would be helpful in assessing the outlook for medium-term growth and inflation.

The Council decided to keep the NBP interest rates unchanged at the following levels: reference rate at 4.50%, lombard rate at 6.00%, deposit rate at 3.00% and rediscount rate at 4.75%.

Minutes of the Monetary Policy Council decision-making meeting held on 7 March 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of external and domestic macroeconomic developments, including inflationary processes and the NBP's March projection of inflation and GDP.

While referring to the external conditions of the Polish economy, some members of the Council indicated that the recently published favourable data on the US and euro area economy supported optimistic sentiment in the global financial markets. Few members of the Council also pointed out that considering the current data, economic slowdown in the euro area might turn out less pronounced than previously expected.

Other members of the Council emphasized that problems related to the fiscal crisis in the euro area had not been solved yet, and implementation of the fiscal package would be a long-term process. This means that should fiscal problems in some euro area countries escalate again, improved sentiment in the financial markets might prove short-lived and the outlook for economic growth in the euro area worse than currently anticipated. As regards the outlook for economic growth, those members of the Council drew particular attention to the lack of prospects for revival in lending by European banks despite a considerable liquidity provision by the European Central Bank.

While discussing the monetary policy of major central banks, members of the Council pointed to their continued monetary expansion through increasing liquidity provision to the financial system, even though inflation in the United States, the euro area and Great Britain is running markedly above the target. In the opinion of some Council members, expansionary monetary policy will fuel price pressure.

Data on economic activity in Poland, including data on output, retail sales and corporate lending, indicate that GDP growth in 2012 Q1 may continue at a relatively high level. At the same time, however, members of the Council emphasized that according to the forecasts for subsequent quarters, considering the relatively low level of most leading economic indicators, domestic economic growth, and, in particular, consumption are to weaken. It was also pointed out that consumption weakening may be partly driven by the observed lower lending to households. Moreover, some members of the Council indicated that the appreciation of the zloty exchange rate, affecting primarily import volume, would lead to lower contribution of net exports to GDP growth.

Few members of the Council emphasized that in line with the NBP's March projection, despite the forecast considerable slowdown in domestic economic activity, output gap might remain positive till the end of projection horizon. Likewise, throughout the projection horizon unemployment rate was supposed to run below the equilibrium unemployment rate as estimated in the NECMOD model. However, other members of the Council emphasized that both potential output and equilibrium unemployment rate were non-observable variables, and therefore their estimates as well as conclusions regarding the condition of the economy based on them should be read with caution.

While addressing the situation in the labour market, members of the Council pointed out that the January data on employment and wages in the enterprise sector might be considerably distorted by temporary factors. Some members of the Council assessed that the persistently elevated unemployment had a mitigating effect on wage pressure, and, consequently, inflationary pressure. Other members of the Council argued that moderate wage growth in the recent period, combined with heightened inflation observed for more than a year now, increasing household maintenance costs, posed a risk of higher wage pressure. Few members of the Council also claimed that the observed moderate wage growth had been largely driven by rising labour supply, and, the anticipated halting of labour supply growth might consequently add to wage pressure.

While analysing the inflationary developments, some members of the Council emphasized that decline in January inflation was more pronounced than had been forecast, and in the absence of zloty depreciation, inflation might be expected to decrease further by the end of the year. Those Council members also pointed to lowering core inflation in January 2012.

Other members of the Council indicated, however, that despite some decline, inflation continued to run considerably above the target as well as above the upper limit for deviations from the target, and in line with the NBP's March projection, inflation was also likely to remain above 3.5% in a one-year horizon. Moreover, in comparison with the November 2011 projection, the period during which inflation is forecast to remain at a heightened level had been extended. Those members of the Council additionally emphasized that by the end of the projection horizon, core inflation was also to continue at a relatively high level. In the opinion of those Council members, growth in the prices of energy commodities in the global markets and the effects of implementing the EU climate and energy package continue to be risk factors for a marked decrease in inflation. Those Council members also indicated that it was difficult to assess the likelihood of reductions in VAT rates in 2014.

Some members of the Council argued that interest rates were currently at a relatively low level, considering the macroeconomic situation in Poland, and even assuming for the possibility of a decline in the natural interest rate driven by the global financial crisis. Those Council members also assessed that high growth in monetary aggregates pointed to a merely slight decline in the natural interest rate in Poland. In the opinion of those Council members, low interest rates posed a risk of rising inefficiency in the economy.

Yet, other members of the Council indicated that amidst growing monetary expansion abroad, keeping the NBP interest rates unchanged, additionally accompanied by a rise in WIBOR 3M rate in October 2011, and zloty appreciation at the beginning of the year, would mean a relative tightening of monetary policy in Poland.

While discussing the decision on the NBP interest rates, members of the Council agreed that, given the heightened uncertainty about the global and domestic economic developments, it was justified to keep NBP interest rates unchanged at the current meeting. As regards future monetary policy decisions, the majority of the Council members maintained their view that NBP interest rates increase in the subsequent months could not be ruled out.

Some members of the Council argued that – should the expected economic slowdown in Poland prove less pronounced than previously anticipated and, consequently, should the prospects of inflation returning to the target fail to improve – keeping the NBP interest rates unchanged could be conducive to both inflation expectations and inflation persisting at the elevated levels.

At the same time, in the opinion of few members of the Council, a possible rise in the NBP interest rates in the subsequent months – amidst the expected weakening of economic activity abroad and in Poland – posed a risk that such monetary policy tightening would lead to an excessive weakening of demand in the Polish economy. Some members of the Council assessed that the NBP interest rates should be increased if the already visible decline in inflation was proceeding too slowly. In the opinion of those Council members, a decision to increase the NBP interest rates, if any, should depend on the pace of inflation decline in subsequent months and performance of the real sphere of the Polish economy.

On the other hand, few members of the Council indicated that considering the NBP's March projection of inflation and its balance of risks, in mid-2013 inflation should come close to the target and in 2014 it should run markedly below the target. Thus, the NBP interest rates increases might not be justified.

The Council decided to keep the NBP interest rates unchanged at the following levels: reference rate at 4.50%, lombard rate at 6.00%, deposit rate at 3.00% and rediscount rate at 4.75%.

Minutes of the Monetary Policy Council decision-making meeting held on 4 April 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of the external and domestic macroeconomic developments, including inflationary processes.

While analysing the external conditions of macroeconomic developments in Poland, some Council members pointed out that GDP growth abroad was likely to remain weak in the coming quarters. In particular, it was emphasised that should there be no substantial improvement in the US labour market, the revival in the United States may slow down, especially amidst the announced fiscal tightening in this economy. Attention was also drawn to the fact that economic activity in the euro area was significantly weaker than in the United States, albeit considerable differences could be seen across countries. Few Council members argued that notwithstanding the slow economic growth in the euro area, the German economy– the main recipient of Polish exports – was in a relatively good condition.

Council members indicated that in many countries inflation persisted at a high level. This largely resulted from rising global prices of energy commodities, which were partly driven by unconventional monetary policy measures undertaken by the major central banks. Some Council members indicated at this juncture that increasing commodity prices would continue to drive up inflation also in the medium term. Increasing commodity prices will be supported by both – rising demand, especially on the part of the major emerging economies, and by expanding production of biofuels.

While discussing the outlook for domestic economic growth in the current year, some Council members assessed that the economic slowdown in Poland was likely to be smaller than previously expected, which might be indicated by strong data incoming over the first few months of 2012. These Council members underlined, in particular, that private consumption would most probably remain to be a factor supporting economic growth in the nearest quarters; yet amidst temporarily slow real income growth, consumption would be financed, to a greater degree, by decrease in savings rate. Few Council members argued at that point that the observed lower propensity to save might be the effect of heightened inflation eroding the real value of savings. In the opinion of some members of the Council, the expected economic slowdown will also be mitigated by a further inflow of EU funds supporting investment growth.

However, few Council members stressed that consumption growth had been gradually decreasing since mid-2011 and it could not be ruled out that its contribution to GDP growth would continue to shrink in the subsequent quarters. Moreover, these members of the Council argued that since firms' propensity to invest highly depends on business conditions abroad, amidst the expected slow global growth, the contribution of private investment to GDP growth might also decrease in the coming quarters. Thus, in the opinion of those Council members, the weakening in economic growth in Poland might turn out significant.

Some Council members argued however that even if economic slowdown in the nearest quarters turned out significant, 2013 might be expected to bring gradual acceleration of GDP growth. In the opinion of those Council members, growth would be supported by rising private sector demand. Acceleration of consumption in 2013 will be driven by the expected fall in inflation, which will boost real disposable income growth, whereas acceleration of investment will be supported by the anticipated improvement in economic conditions abroad. Improved external conditions should also be conducive to exports expansion in 2013. Moreover, the extent of further fiscal tightening in Poland is likely to be smaller than in 2012, thus its dampening impact on the 2013 domestic demand growth will be limited.

While discussing inflationary developments, Council members stressed the fact that – like in other countries – heightened inflation had been largely driven by external factors, including rising global prices of energy commodities, which translated into higher prices of energy, and in particular into higher prices of fuels. February saw also a rise in domestic prices of tobacco products, following an increase in excise tax, which also increased core inflation rate.

Council members pointed out that over the next few months, elevated inflation would continue to be driven, above all, by fast-growing prices of energy and food. Moreover, in the opinion of few members of the Council, due to European Football Championship, restaurant and hotel prices could be expected to increase in some Polish cities in June 2012; these prices might not fall back to their previous levels immediately after Euro 2012. According to few Council members, an additional risk to inflation in the short term is the likely rise in prices of services and fees that are at the discretion of local government units.

As regards the impact of the exchange rate on inflation, few Council members assessed that the likely appreciation of the equilibrium exchange rate would limit the anti-inflationary influence of the exchange rate appreciation at the beginning of 2012 on domestic prices. At the same time, these Council members pointed out that exchange rate fluctuations were closely connected to shifts in risk aversion in the global financial markets that are hard to predict. In this context, attention was drawn to the persisting uncertainty concerning the situation in the financial markets, especially in Europe.

The Council members emphasised that inflation was now expected to remain above the target levels for longer than previously anticipated, which, according to most members of the Council, increased the risk of inflation persisting at an elevated level and provided grounds for considering monetary policy tightening. Most Council members pointed that – as elevated inflation was largely driven by factors beyond the direct influence of the domestic monetary policy - the increase in the NBP interest rates should primarily prevent persisting heightened inflation expectations, mounting wage pressures and emerging of second-round effects. However, few Council members argued that amid continued elevated unemployment, still moderate wage growth and further fiscal tightening constraining public sector wage growth, the risk of second-round effects was limited.

Referring to the level of interest rates, some Council members emphasised that, notwithstanding the monetary policy tightening of 2011, interest rates were currently at moderate levels, what is reflected – in their opinion – in a relatively fast growth of monetary aggregates. In the opinion of these members of the Council, moderate level of interest rates in Poland was further evidenced by the comparison of inflation deviation from the target and the estimated output gaps in Poland and other countries. However, other Council members assessed that amidst strongly expansionary monetary policies of the world's major central banks, monetary policy easing by central banks in developing countries and persisting uncertainty about the economic outlook abroad, the monetary policy conducted by the NBP was not overly accommodative. Moreover, few Council members also stressed that the transmission of the monetary policy tightening in the first half of 2011 was so far not full. In the opinion of few Council members the impact of the 2011 interest rates increases on economic activity seemed rather small.

Some Council members pointed out that restricted availability of foreign currency loans to households had strengthened the impact of NBP interest rates increases on credit growth, and thus on private demand.

With regard to the decision on the NBP interest rates, the majority of Council members found that – given a likely persistence of factors fuelling inflation that are beyond the direct influence of domestic monetary policy – the limited scale of expected economic slowdown might not decrease inflationary pressure to a degree sufficient for inflation returning to the target in the medium term. The risk of inflation running above the target in the medium term is additionally increased by elevated inflation expectations. In view of the above, the Council members deemed it appropriate to consider monetary policy tightening in the near future. In the opinion of some Council members, the tightening should take place as soon as possible; hence, in their opinion, it was justified to increase interest rates at the current meeting. However, most Council members argued that a possible increase in interest rates should be preceded by a more thorough assessment of the state of the economy and the scale of the expected economic slowdown. This assessment will be feasible after the data on the subsequent months of 2012 has been analysed, since the January and February 2012 data might have been distorted by one-off factors. Therefore they decided that the NBP interest rates should be kept unchanged at the current meeting. Nevertheless, monetary tightening might prove justified in the nearest future, unless signs of considerable economic weakening in Poland appear and the outlook for inflation returning to the target improves.

In the opinion of few Council members, should weakening in the domestic economic growth in the subsequent quarters prove considerable due to low activity abroad, monetary policy tightening might not be necessary.

A motion to raise the NBP interest rates by 25 basis points was put forward at the meeting. The motion did not pass. The Council decided to keep the NBP interest rates unchanged: reference rate at 4.50%, lombard rate at 6.00%, deposit rate at 3.00%, rediscount rate at 4.75%.

Minutes of the Monetary Policy Council decision-making meeting held on 9 May 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of external and domestic macroeconomic developments, including inflationary processes.

While analysing the external conditions of macroeconomic developments in the Polish economy, members of the Council pointed to the continued uncertainty about the situation in the euro area. Some members of the Council argued that the results of the elections held in France and Greece suggested the possibility of changes in economic policy of those countries and hence a weaker support for restrictive fiscal policy in some euro area countries. In this context, some members of the Council pointed to the risk of intensification of the crisis in some euro area countries which would, in turn, translate into further economic weakening. At the same time, some members of the Council argued that notwithstanding economic stagnation in the euro area, in Germany – Poland's main trading partner – a gradual recovery in economic activity is expected.

Members of the Council emphasized that uncertainty in the external environment of the Polish economy had remained elevated for a long time and could be expected to continue at a high level in the coming quarters. Some members of the Council assessed that heightened uncertainty about economic developments in the euro area and in other developed countries was becoming a permanent feature of the balance of risks for inflation and GDP; therefore, it should not be the key factor in the conduct of monetary policy in Poland. Other members of the Council argued, however, that such a high uncertainty limited the possibility of interest rate adjustments.

While discussing the economic activity in Poland, some members of the Council pointed out that March had seen a significant slowdown in manufacturing and construction production. Yet, the data released in the previous months suggest that in 2012 Q1 economic growth remained relatively robust in Poland. At the same time, those members emphasised that according to the NBP's business climate surveys, in 2012 Q1 economic situation of enterprises remained sound, with production capacity utilization improved and the number of companies planning to boost production and employment in 2012 Q2 increased. Also corporate lending rose rapidly in the first few months of 2012 and a relatively high growth in zloty housing loans to households continued, although total growth in housing loans was still decreasing. In the opinion of those members of the Council this might mean that the scale of the expected economic slowdown would be smaller than previously expected. Good financial situation of enterprises might additionally support this scenario.

Few members of the Council argued, however, that weak economic activity abroad would translate into lower contribution of net exports to GDP growth in Poland, whereas heightened inflation and lower employment growth would undermine consumer demand. It was pointed out that decline in consumer loans was another factor conducive to weaker consumer demand. Those members also argued that uncertainty about the outlook for both export demand and domestic demand posed a risk of slump in corporate investment, and, consequently, sharper decline in GDP growth in Poland in the coming quarters.

While analysing inflationary processes, some members of the Council pointed out that although CPI and core inflation declined slightly in March, subsequent months were likely to see, once again, higher price growth. The rise in inflation may be primarily fuelled by gas price increases and temporary rise in the prices of restaurant and hotel services (the impact of the European Football Cup in Poland).

On the other hand, while addressing the outlook for inflation in the medium-term, some members of the Council emphasized that the coming quarters were likely to see continued upward pressure of external factors on inflation in Poland. Those factors included high commodity prices in the global markets, being largely the result of both rising demand for energy and food in the rapidly growing emerging markets and strongly expansionary monetary policy in the main developed countries. In the opinion of those members of the Council, as a result of the above factors inflation is expected to remain above the target for a longer time.

Other members of the Council pointed out that should the recently observed decline in oil prices continue – especially amidst zloty strengthening – inflation might fall considerably by the end of 2012. In the opinion of those members of the Council, such a possibility was also indicated by considerably weaker producer price growth, suggesting that companies did not increase their margins.

While addressing inflation expectations, it was emphasised that although one-year ahead inflation forecasts by financial sector analysts were consistent with the NBP's inflation target, expectations of households and enterprises were largely based on current inflation. As a result, private sector's expectations have continued, for a long time, well above the inflation target. Few members of the Council also argued that, notwithstanding still elevated unemployment rate, high inflation expectations persisting in the longer term increased the risk of their impact on contracts concluded by enterprises and consequently on the dynamics of the costs of production, including labour costs. In this context, attention was also paid to the announced minimum wage increase in 2013 as a factor likely to boost wage pressure.

Other members of the Council emphasized that high inflation expectations had not so far translated into higher wage demands, which is evidenced by lowering growth in the wage bill. Few members of the Council pointed out that wage freeze in the public sector was conducive to limiting wage pressure in the whole economy.

While discussing monetary policy stance, some members of the Council argued that despite the fact that heightened inflation was largely the result of factors beyond the impact of domestic monetary policy, when considering its negative consequences for the economy, efforts should be made to stabilise price growth at a low level. Those members pointed out that monetary policy should be pursued in such a way so as to support lowering of inflation expectations. Moreover, members of the Council emphasised that interest rate decisions should take into account, in the first place, expectations about macroeconomic developments over the period of 6-8 quarters. In the opinion of few members of the Council, over that horizon an acceleration in economic growth may be expected.

Other members of the Council emphasised, however, that considering the fact that the currently heightened inflation was driven by supply factors, in order to curb inflation economic activity would have to fall below potential. On the other hand, excessively high interest rates might not only put a strong downward pressure on GDP growth over the next several quarters but also adversely affect domestic economic activity in the longer term.

With regard to the decision on the NBP interest rates, the majority of Council members argued that the limited scale of the expected economic slowdown amidst heightened inflation persisting for over a year and its forecasted only slow decline over the coming quarters justified the NBP interest rate increase at the May meeting. In the opinion of those members of the Council, the outlook for inflation returning to the target had not improved since the last meeting, especially considering the persistently strong inflationary impact exerted by factors beyond the influence of domestic monetary policy and continuously heightened inflation expectations. At the same time, signals coming from the real economy did not clearly point to significant slowdown in economic activity in Poland. The majority of the Council members also emphasized that NBP interest rate increase was an adjustment to the current and anticipated macroeconomic situation in Poland and was aimed to ensure that real interest rates are kept above zero. At the same time, some members of the Council assessed that it might be necessary to adjust the NBP interest rates again in order to affect inflation expectations.

Other members of the Council argued that it was still difficult to assess the scale of the anticipated economic slowdown and the decision about a possible adjustment of the NBP interest rates should be postponed. In the opinion of those members of the Council, only the data released in the coming months will enable the assessment whether economic slowdown in Poland will be strong or limited. Those members assessed that amidst high uncertainty about Poland’s external environment and continued fiscal tightening, it was justified to keep interest rates unchanged at the current meeting.

A motion to raise the NBP interest rates by 25 basis points was put forward at the meeting. The motion was passed. The Council decided to increase the NBP interest rates to the following levels: reference rate to 4.75%, lombard rate to 6.25%, deposit rate to 3.25%, rediscount rate to 5.00%.

Minutes of the Monetary Policy Council decision-making meeting held on 6 June 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of external and domestic macroeconomic developments, including inflationary processes.

While analysing developments in the external environment of the Polish economy, the Council members pointed to a moderate economic growth in the United States, stagnation in activity in the euro area and a weakening growth in several major emerging economies. While discussing the outlook for the euro area, the Council highlighted mounting concerns about the developments in the countries most affected by the sovereign debt crisis. Those concerns translated into deteriorating sentiment and rising risk aversion in the international financial markets. Weakening confidence has in turn resulted in depreciation of the exchange rates of the emerging currencies, including the zloty, and decrease of global commodity prices.

Some Council members assessed that despite the deteriorating economic outlook for the euro area, GDP growth in Poland's main trading partners was set to remain firmly positive. However, these Council members also pointed out that the slowdown observed in major emerging economies, which are important recipients of German exports, might translate – through trade links between Poland and Germany – into further weakening in Polish exports.

While addressing economic developments in Poland, it was pointed out that the data released in May, particularly concerning the GDP in 2012 Q1 and its composition, confirmed the gradual weakening in the Polish economic activity. The Council members pointed especially to a relatively slow consumption growth coupled with weakening investment and exports. Furthermore, in the opinion of some Council members, recent data on industrial production and retail sales, as well as a significant number of leading business climate indicators justify the expectation of slower GDP growth in 2012 Q2 in comparison to Q1. While addressing the outlook for growth in the subsequent quarters, some Council members stated that, apart from likely continued decline in external demand, the GDP growth will probably be further dampened by the on-going fiscal tightening, combined with a weaker consumption growth due to slow real wage growth and decelerating household lending. However, other members of the Council argued that the slowdown in the Polish economy may prove moderate. This could be indicated by some April data, in particular, further rise in the corporate investment lending and zloty-denominated mortgage lending, flattening downward trend in industrial production growth and an acceleration in construction and assembly output. At the same time, some Council members claimed that the increase in zloty-denominated mortgage lending was partly due to falling demand for foreign-currency mortgage lending.

While discussing the prospects for lending expansion, few Council members highlighted that the deteriorating position of the euro area banking sector may to have an adverse effect on the credit supply by domestic banks. These Council members were of the opinion that credit supply may additionally be negatively affected by a decline of private sector deposits held in the banking sector seen over recent months, in part as a result of the deposits being transferred to the investment funds. Other Council members argued that amid persisting liquidity surplus in the banking sector, the above factors might not necessarily translate into weaker lending, as credit supply is far more responsive to the assessment of risks related to economic developments as well as changes in the credit standing of the potential borrowers.

While analysing the labour market developments, some Council members pointed out that the LFS (Labour Force Survey) data for 2012 Q1 suggest slower annual growth of the employment in the economy, coupled with a rise in the unemployment rate compared to a year ago. Similar trends may be observed in the monthly data on employment in the enterprise sector and unemployment as registered by the Labour Offices. At the same time, wage growth accelerated somewhat in 2012 Q1, which – coupled with a simultaneous deceleration in GDP growth – added to an increase in unit labour costs in the economy. Yet, some Council members argued that the 2012 Q1 pick-up in wages might have been driven by one-off factors (i.e. expedited payments of some remuneration components before an increase in disability contributions). This may be corroborated by the corporate wage growth decelerating since February and running currently at low levels. In this context, some Council members assessed that the economy was not experiencing any intensification in wage pressures. In the opinion of few Council members, wage pressures were additionally mitigated with a wage freeze in the public sector. Other Council members emphasised, however, that for the last two years corporate sector had seen upward trend in labour costs.

While discussing the risk of an increase in wage pressures, it was highlighted that inflation expectations were persisting at a relatively high level. Given their adaptive nature, they might also remain elevated in the coming months. Yet, some Council members assessed that the risk of the second-round effects was limited due to slowing employment growth and heightened unemployment.

With reference to inflation developments, it was pointed out that April saw a rise in both the CPI and core inflation. It was also highlighted that the current elevated inflation was driven, to a great extent, by factors beyond the impact of the domestic monetary policy. On the other hand, some Council members pointed out that in comparison with other countries in the region – in which inflation was influenced by similar external factors – inflation in Poland remained relatively high.

While discussing the short-term outlook for inflation, it was indicated that the nearest months might be expected to see inflation continue above the upper limit for deviations from the target. This will be driven by the sustained steep growth in administered prices, accompanied with accelerating annual food price growth. The sharp rise in administered prices is partially an effect of increased fees and prices controlled by the general government units. These increases were related to measures aimed at curbing the general government deficit. Amongst other factors raising inflation in Poland, the Council also mentioned the recently observed depreciation of the zloty related to deteriorating sentiment in the global markets as well as the risk of a temporary hike in restaurant and hotel prices in some cities connected to the European Football Cup.

With regard to inflation trends in longer run, some Council members highlighted that some forecasts pointed to a risk of inflation remaining above the target for longer period. These Council members in particular pointed to the relatively high core inflation, which might continue to run at relatively high levels also in the subsequent quarters. This, given a low – in their opinion – likelihood of any substantial drop in growth of energy and food prices, would impede inflation returning to the target. Few Council members emphasised at this point that the recently observed decline in commodity prices might prove temporary, particularly amid political tensions in some major commodity economies. Other Council members indicated that the contribution of food and energy price growth to CPI inflation might decline substantially in the coming quarters, due to, in particular, favourable base effects for both categories.

While analysing the current monetary policy, some Council members assessed that the current level of interest rates might be adequate to maintain price stability over the medium term, particularly considering the economic slowdown. At the same time, few Council members argued that any further interest rate increases may – through their dampening effect on demand growth – impede the reduction of the general government deficit in relation to the GDP, which in turn, by forcing additional fiscal adjustment, may ultimately result in an excessive curbing of economic growth. Yet, other Council members argued that – despite the already implemented adjustment – the current level of interest rates in Poland may prove slightly too low to stem the risk of inflation persisting at a heightened level over the medium term, given particularly the risk of persistently elevated core inflation. Few Council members pointed out that too low interest rates might negatively affect the saving rate in the economy.

While discussing decisions on the NBP official interest rates, the Council members decided that these should be left unchanged at the current meeting. Some Council members emphasised that amidst the on-going economic slowdown, the increase of the NBP rates at the previous meeting was probably a sufficient adjustment of interest rates to the current and anticipated macroeconomic developments in Poland. Such an assessment is also supported – in their opinion – by the risk of deteriorating situation in the euro area economy. Other Council members believed that another interest rate adjustment might be justified in the coming period, should the expected period of inflation persisting above the target protract, and the scale of the anticipated economic slowdown prove moderate. In the opinion of most Council members, a more comprehensive assessment whether another interest rate increase was justified should take into account the data released in the coming period as well as results of the NECMOD projection and of other forecasts.

The Council decided to keep the NBP interest rates unchanged at the following levels: reference rate at 4.75%, lombard rate at 6.25%, deposit rate at 3.25%, rediscount rate at 5.00%.

Minutes of the Monetary Policy Council decision-making meeting held on 4 July 2012

At its meeting, the Monetary Policy Council discussed current and future monetary policy decisions against the background of external and domestic macroeconomic developments, including inflationary processes and also the results of the July 2012 inflation projection.

While analysing the external conditions of macroeconomic developments in Poland, the Council members pointed to the recently observed signs of weakening of the global economic activity. When addressing the economic developments in the United States, the Council members highlighted that the US GDP growth was moderate and might slow down in the subsequent quarters. When discussing the situation in the euro area, attention was drawn to the stagnation in this economy and the persisting uncertainty related to resolving the sovereign debt crisis faced by some euro area member states. Council members stressed that economic activity weakening – apparent in the euro area – was also observed in Germany, driven by economic slowdown in the largest emerging economies, which are major recipients of German exports.

During the discussion, the Council pointed out that weakening of external economic activity, in particular in Germany, translated into a pronounced deceleration in Polish exports growth. At this point, few Council members argued that the situation of Polish exporters was diversified, as some exporting companies reported increasing sales.

When discussing the situation in the financial markets, it was pointed out that growing concerns about the global economic activity had boosted investor expectations of further monetary policy easing by major central banks. At the same time, some Council members assessed that as a result of uncertainty about the scale and consequences of increased monetary expansion in major economies, improvement in sentiment observed recently in the global financial markets might be short-lived. Attention was also drawn to the continuing decline in commodity prices in the global markets.

While analysing the situation in Poland, some Council members pointed out that the current data on economic activity as well as business climate indicators pointed to further slowdown in domestic economic growth. Those Council members stressed that growth in both industrial output and retail sales in 2012 Q2 had been significantly slower than in the previous quarters, and the above-expectations retail sales results in May could have been partly driven by the Euro 2012 football championship. According to those members of the Council, weaker business climate indicators about the expected economic conditions, in particular regarding outlook for demand, orders and production, were a sign of adverse prospects for domestic economic activity. Yet, few members of the Council expressed an opinion that the recently incoming data indicated rather a slight economic downturn. Those Council members pointed to some strengthening of industrial output and retail sales growth in May (that could be driven not only by one-off factors), a sustained strong financial standing of firms and an improvement in liquidity indicators in the corporate sector in 2012 Q2 – as showed by the NBP surveys. Few Council members argued that the relatively sound business conditions in Poland were reflected in further growth in lending, although credit supply might be adversely affected by worsening situation in the euro area.

While assessing the GDP growth outlook in the subsequent quarters against the NBP July projection, some Council members emphasised that the projection envisaged further economic slowdown – deeper than forecast in the March projection. Growth is supposed to be dampened by further weakening in domestic and external demand. In the opinion of some Council members, weaker domestic demand will result from slower investment and private consumption growth, driven by the lack of improvement in the labour market, tighter lending conditions and earlier sharp fall in savings rate. Fiscal tightening and lower inflow of EU funds, the latter related primarily to cuts in public investment, may also contribute to weaker growth. At the same time, few Council members deemed economic growth in the coming years likely to run markedly below the levels assumed in the NBP projection.

Other members of the Council assessed, however, that the impact of lower inflow of EU funds on GDP growth in 2013 would be relatively small. In their opinion, the effect of further fiscal tightening is also likely to be limited. At the same time, a simultaneous decline in inflation may – by increasing real disposable income – support consumption growth. As a consequence, following a marked slowdown this year, GDP growth may gradually pick up in the course of 2013. In this context, few Council members noted that the majority of currently available forecasts of external institutions suggested – in contrast to the NBP July projection – that the 2013 GDP growth might be higher than that observed in 2012.

While discussing the risk of an increase in wage pressures, some Council members pointed out that the risk was limited, as evidenced by still moderate wage growth in the enterprise sector. The continued high unemployment rate was also highlighted as a factor preventing potential escalation of wage pressure. Yet, few Council members were of the opinion that amidst elevated inflation and the resulting growth in living costs, there was a risk of a rise in wage demands.

While discussing inflationary developments, it was pointed out that CPI inflation in May was running substantially below the forecasts and approached the upper limit for deviations from the NBP target. Decline in core inflation was also highlighted. Yet, few Council members stressed that as compared with other EU countries – where inflation is influenced by similar external factors – inflation in Poland remained relatively high.

While discussing short-term outlook for inflation, the members of the Council pointed to a likely rise in the CPI in the nearest months, resulting from the statistical base effect in food prices. In the immediate future, inflation may be also heightened by steeply rising administered prices, partially due to increases in charges and prices set by general government units. At the same time, it was noted that considerable uncertainty was related to the zloty exchange rate changes and its impact on inflationary processes.

While discussing long-run inflation trends, some Council members pointed out that the July inflation projection was lower than the March projection, which means a faster than expected return of inflation to the target. According to the July projection, at the end of 2012 CPI inflation will be running below the upper limit for deviations from target, and may come close to the inflation target of 2.5% in the first half of 2013. Few Council members noted that towards the end of the inflation projection horizon, CPI inflation may even fall below 2.5%, though remaining within the limit for deviations from the target. Moreover, those Council members pointed that external forecasts are also suggesting a decline in inflation in 2013, down to a level close to the inflation target.

Few Council members argued that in line with the July projection, however under the assumption that VAT rates are not reduced in 2014, core inflation will remain at a relatively high level, which might impede the return of CPI inflation to the target. Besides, in the opinion of these Council members, the economic slowdown is likely to be moderate and therefore no substantial decrease in inflationary pressures should be expected.

While considering monetary policy decisions, the majority of Council members presented the opinion that – given the economic slowdown and the return of inflation to the target within a few quarters, as assumed in the July projection – the current level of the NBP interest rates is appropriate. Those Council members also argued that the interest rates adjustment implemented in May 2012 – being conducive to lower inflation – contributed to sustained macroeconomic stability of the domestic economy. In the opinion of those Council members, data and forecasts which had been released since the previous meeting of the Council did not provide grounds for further NBP interest rate increases, though they did not completely rule out the possibility of raising the NBP interest rates. According to those Council members, current or forecast macroeconomic situation did not justify interest rate cuts. In turn, few Council members assessed that the current level of the NBP interest rates – given the signs of a possible significant economic downturn and the risk of inflation falling below the target in the medium term – is too high and thus may lead to excessive deceleration of economic growth. These Council members also argued that interest rate reduction, by mitigating the slowdown in GDP growth, would support the currently implemented fiscal policy tightening.

At the meeting, a motion to lower the NBP interest rates by 0.50 percentage point was put forward. The motion did not pass. Also a motion to lower the NBP interest rates by 0.25 percentage point was put forward. The motion did not pass. The Council decided to keep the NBP interest rates unchanged at the following levels: reference rate at 4.75%, lombard rate at 6.25%, deposit rate at 3.25%, rediscount rate at 5.00%.

Minutes of the Monetary Policy Council decision-making meeting held on 5 September 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of the external and domestic macroeconomic conditions, especially including inflation developments.

While analysing external conditions for economic activity in Poland, Council members pointed out that the global activity remained low. In this context, it was indicated that economic growth in the United States was moderate and conditions in the euro area had weakened significantly, with continued recession and adverse outlook for this economic region. At the same time, it was pointed out that – despite the on-going recession in many euro area countries – the German economy, Poland's key trading partner, continued to grow, albeit at a slower pace. Economic slowdown in major emerging economies, which were hitherto relatively resilient to deteriorating economic growth outlook in advanced economies, was also emphasised.

With regard to the situation in the global markets, Council members pointed to a sharp rise in energy and agricultural commodity prices, caused by disruptions on the supply side, and a further improvement in investor sentiment resulting from expectations for further monetary policy easing by the major central banks.

Referring to the situation in Poland, Council members emphasised that recent data on economic activity, including GDP, as well as economic conditions indicators, pointed to a sharper deceleration in domestic economic growth this year than was assumed in the July projection and anticipated by external forecasters. Addressing the national accounts data for 2012 Q2, it was highlighted that economic slowdown was mainly attributable to a decline in domestic demand. Demand contraction was driven by both slower consumption growth as well as a sharp deceleration in investment spending growth in private sector and a decrease in general government investments. It was emphasised that the positive contribution of net exports to economic growth resulted from a fall in imports – on the back of a decrease in domestic demand – rather than a rise in exports.

While discussing current conditions indicators, few Council members pointed out that retail sales growth in July was faster than in 2012 Q2 on average. Yet, other Council members highlighted that the monthly retail sales indicators, based solely on data from larger companies, i.e. with more than 9 employees, are not a good indicator for total household consumption expenditure. It was pointed out that also industrial production rose faster in July than in 2012 Q2 on average. However, at the same time construction and assembly production declined and downward trend in most leading indicators continued. Attention was also drawn to increasingly sluggish growth in lending, including investment loans, a rise in the number of entities lacking creditworthiness as well as deteriorating financial performance of companies, including falling revenues and deteriorating liquidity indicators.

With reference to economic growth outlook in the subsequent quarters, some Council members emphasised that the structure of GDP growth in 2012 Q2 pointed to a possible further slowdown ahead. Downward revisions of external forecasts for economic growth also point to a higher probability of slower GDP growth next year. In the opinion of few Council members, there is a risk that economic growth in Poland in the second half of 2012 and 2013 may be substantially lower than forecast in the July projection and by the external forecasters. Yet, few Council members assessed that the observed slowdown may be only temporary and its scale will depend, to a large extent, on the situation in the external environment, which according to most forecasts will improve in 2013.

In the opinion of Council members, economic growth will be particularly dampened by further weakening in domestic demand, which was the key driver of economic growth over recent years. Weaker domestic demand will probably result not only from a reduction in investment but also from a slowdown in private consumption growth. Investment will be reduced in the public sector amidst the fiscal tightening in place and – most likely – in the private sector due to weaker corporate expectations of future economic conditions. Consumption growth may be affected by lower disposable income growth triggered by deteriorating labour market conditions. In this context, it was pointed out that in 2012 Q2 and in July the unemployment rate was higher than a year before, and employment growth continued to slow down. With further reference to consumption outlook, it was observed that private consumption may also be adversely affected by deteriorating consumer confidence, decelerating household lending as well as the saving rate running close to zero. Few Council members pointed to an unfavourable phenomenon of a decrease in household deposits growth in the banking sector.

While discussing inflation developments and short term inflation outlook, few Council members pointed out that – following a temporary rise in June – the CPI inflation in July had decreased more steeply than had been expected. Council members highlighted that the annual CPI may decline further in the coming months, in part due to a statistical base effect. At the same time, limited wage pressure reflected in moderate wage growth will drag on inflation. In the opinion of some Council members, towards the end of 2012, CPI inflation will run below the upper limit for deviations from the target. Yet, few Council members pointed out that despite a decrease expected by the end of 2012, inflation would probably remain elevated, while the pace at which the inflation would decrease in 2013 remained uncertain.

In the opinion of some Council members, the increase in food commodity and oil prices observed over the past few months may pose an upside risk to inflation. At the same time, it was highlighted that the future levels of the zloty exchange rate and consequently its impact on inflation developments were highly uncertain. Few Council members pointed to a reduction in lending by foreign parent banks from their Polish subsidiaries.

With regard to inflation trends in longer run, some Council members pointed out that the inflation could return to the target sooner than had been previously expected, which may be supported by deeper than envisaged economic slowdown. In the opinion of few Council members, despite a recent oil price increase, the annual CPI may be reduced in 2013, owing to a statistical base effect relating to a relatively high level of fuel prices in the first half of 2012. In the opinion of some Council members, in the first half of 2013, inflation will be probably close to the NBP inflation target (2.5%). Yet, other Council members pointed to substantial uncertainty regarding the magnitude of the impact of the economic slowdown on inflation, as well as the fact that despite the downward revision of the economic growth forecasts many external forecasts continue to expect inflation to stay above 2.5% in 2013.

While considering monetary policy decisions, the majority of Council members judged that the NBP interest rates should be kept unchanged at the current meeting. In their opinion, this decision was justified by the uncertainty about the scale and duration of the economic slowdown, which would determine inflation developments over the monetary policy horizon. It was also highlighted that there was a risk of inflation persisting at heightened level in the subsequent months, which would be attributable to the observed rise in commodity prices in the global markets.

At the same time, most Council members concluded that the information received since the previous meeting, i.e. about the deteriorating growth outlook in the euro area and sharper than expected deceleration in Polish GDP growth in 2012 Q2, had changed the view on the economic conditions, including the assessment of whether inflation would be above or below the target over the medium term.

In the opinion of few Council members, data received since the previous meeting do not indicate that the NBP interest rates should be increased. However, they do not warrant their reduction either, as the real interest rate is tailored to the expectations of inflation returning to the target and expected moderate economic growth. However, in the opinion of some Council members, the risk of a deeper and longer than expected economic slowdown, along with the prospect of inflation returning to the target in 2013, may provide an argument in favour of lower interest rates in the subsequent months.

Few Council members, in turn, were of the opinion that amidst the probably further substantial weakening business conditions and the resulting risk of inflation dropping below the target within the monetary policy horizon, and given a limited room for fiscal policy easing and persisting uncertainty about the situation in the euro area, monetary policy easing was justified already at the current meeting.

As a result, the Council decided to consider a monetary policy adjustment, should the incoming data confirm a further slowdown and the risk for inflationary pressure mounting remain limited. The assessment of whether any interest rate adjustment was justified should take into account the data incoming in the coming period, as well as – in the opinion of some Council members – the results of the November NBP projection.

A motion to decrease the basic NBP interest rates by 0.50 percentage point was submitted at the meeting. The motion was rejected. A motion was also submitted to decrease the basic NBP interest rates by 0.25 percentage point. The motion was rejected. The Council left the basic interest rates unchanged at the following levels: reference rate at 4.75%, lombard rate at 6.25%, deposit rate at 3.25%, rediscount rate at 5.00%.

Minutes of the Monetary Policy Council decision-making meeting held on 3 October 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of the external and domestic macroeconomic conditions, including inflation developments.

While analysing external conditions for economic activity in Poland, the Council members pointed out that data released since the September meeting confirm a slowdown in global economic activity, including ongoing recession in the euro area, merely moderate growth in the United States and economic slowdown in emerging economies. In this context, attention was drawn to the fact that the unfavourable outlook for economic growth had prompted the central banks of the largest developed economies to further ease their monetary policy, which improved sentiment in the global financial markets. However, according to some Council members, the improvement may prove to be temporary. In particular, the European Central Bank announced the launch of new programme of purchasing government bonds issued by countries most severely affected by the sovereign debt crisis, withdrawing its previous bond purchase programme at the same time. In turn, the Federal Reserve shifted the declared date of the first interest rates increases from the end of 2014 to mid-2015, and implemented a new MBS purchase programme. Some Council members were of the opinion that measures undertaken by major central banks should support revival of economic activity in Poland's external environment, in particular, in the euro area, where improvement in consumer and investor confidence about the prospects for overcoming the crisis may be expected.

While analysing economic situation in Poland, the Council members pointed out that the deceleration of industrial production, a further decline in construction output and weaker retail sales growth indicate that Poland's GDP growth continues to decrease. This is also signalled by worsening of business sentiment indicators, including deteriorating forecasts of demand and orders. At the same time, some Council members pointed to the data that could indicate a limited scale of further economic slowdown. These include some improvement of liquidity position of enterprises in 2012 Q3 and only slightly weaker growth in lending to the private sector (visible in data adjusted for exchange rate changes).

When discussing the current business conditions in Poland and their outlook, some Council members highlighted that the situation in the labour market was deteriorating faster than expected. They pointed to a decrease in employment and slow wage growth in the corporate sector, as well as to the gradually rising unemployment. In their opinion, weak growth in households' real disposable income will constrain consumption, especially since there is no room for further significant reduction in savings rate and availability of consumer loans is limited. Considering that at the initial stage of the global financial crisis, consumption was one of the factors spurring domestic economic activity, the currently observed deceleration in consumption – according to those Council members – points to the risk of a significant economic slowdown in the coming quarters. At the same time, deteriorating outlook for demand dampens investment prospects, already undermined by rising spare capacity utilisation. Those Council members also argued that the coming quarters might be expected to see lower net exports contribution to GDP and further fiscal tightening. The impact of the above mentioned factors is reflected in the downward revision of the 2013 economic growth forecasts for Poland released by external institutions.

Some Council members deemed however, that at present it is difficult to assess the scale of further economic slowdown, which – according to few of them – may prove moderate and relatively short-lived. Consequently, GDP growth is likely to run only slightly below the potential output growth. Furthermore, few Council members pointed out that consumption and investment may be expected to pick up gradually as early as 2013, boosting GDP growth. In their opinion, this scenario will be supported by the improvement of business conditions in Poland's external environment, that may be larger than had been expected before the announcement of additional expansionary monetary policy measures by major central banks. Few Council members also pointed out that the intended relaxation by the Polish Financial Supervision Authority of recommendations related to household loans will positively influence domestic activity. Moreover, the reduction of fiscal deficit may be lower than anticipated for in the Convergence Programme, 2012 Update.

While discussing inflation developments, it was emphasised that price growth is decelerating while inflation still remains above the NBP inflation target as well as above the upper limit of deviations from the target. It was pointed out that the elevated inflation level results largely from supply-side factors which are beyond the direct influence of domestic monetary policy, amidst gradually declining core inflation. Some Council members stressed that weakening economic activity accompanied with decline in wage pressure and employment, significantly limits the risk of second-round effects, and thus, should support inflation decline over the next few quarters.

Some Council members assessed however, that inflation returning to the target is subject to risk posed by global commodity prices, whose further growth may be supported by strongly expansionary monetary policy conducted by major central banks. These Council members argued that this factor may limit the scale of inflation decline, as inflation is expected to decrease largely on account of slower growth in food and energy prices, i.e. price categories closely related to developments in global commodity prices. This was reflected in some upward revision of some short-term inflation forecasts prepared by the NBP. These Council members also pointed out that short-term forecasts (with horizon of 12 months) do not point to the risk of inflation falling significantly below the target within their horizon.

Other members of the Council argued that global commodity price growth should decelerate, as growth in demand for commodities from the largest emerging economies is weakening. Gradually slowing down economic growth in those countries makes commodity prices, which are already high, unlikely to continue to rise at the present pace. Therefore, according to these Council members, the developments in global commodity prices will support inflation decline in 2013. Moreover, it was pointed out that all the available macroeconomic forecasts, including the NBP July projection, suggest that inflation is to decline. The July NBP projection expects inflation to reach a level close to 2.5% in the first half of 2013, and subsequently fall below the target. Those Council members emphasised that the risk of inflation falling significantly below 2.5% is at the moment greater than assessed in July, due to a more severe than anticipated worsening of economic outlook and labour market conditions.

During the discussion, Council members also highlighted exchange rate developments. Some members argued that the zloty exchange rate is currently determined mainly by investors' assessments of the outlook for domestic economic growth. Other Council members pointed out that exchange rate movements may be also affected by interest rate disparity between Poland and the euro area.

While considering monetary policy decisions, some Council members argued that the NBP interest rates should be lowered at the current meeting. In the opinion of those Council members, the anticipated slowing of economic growth to levels significantly below potential output growth poses a risk of inflation falling below the target in the longer term, which justifies monetary policy easing. Moreover, the forecast decline in inflation to level consistent with the inflation target in the coming quarters will keep real interest rates deflated by the expected inflation – even if NBP rates are lowered – clearly positive, while at the moment real interest rates in Poland are high relative to other countries. In the assessment of these Council members, monetary policy easing is also justified by the likely persistence of low economic activity abroad and further fiscal tightening in Poland in 2013. Few Council members additionally observed that a serious economic slowdown might impede the process of reducing the general government deficit, which could, in turn, weaken the zloty and increase inflation. Hence, in their opinion, monetary policy should be eased relatively fast to limit the risk of strong economic downturn.

Other members of the Council concluded that a potential interest rate cuts should take into account the outlook for medium-term economic growth and inflation that will be presented in the November projection of the NBP. Some Council members pointed out that the current interest rates level might be appropriate to enable inflation returning to the target over the next few quarters, while interest rate cuts amidst continuing weak economic climate abroad might have limited impact on the domestic economic activity. Few Council members assessed that one should still take into consideration a risk of strong negative shock in the external environment of the Polish economy, whose accommodation through increase in private consumption or expansionary fiscal policy depends on the amount of savings in the economy. Given the currently observed very low household savings rate and still excessive fiscal deficit, interest rate cuts would further undermine propensity to save. This would, in turn, weaken the economy’s ability to accommodate any negative shock in the future.

The majority of Council members were of the opinion that the NBP interest rates should be kept unchanged at the current meeting. Yet, should the incoming data, including the November inflation projection of the NBP, confirm that economic slowdown would become protracted, while the risk of increase in inflationary pressure be limited, the Council will ease monetary policy.

A motion to lower the basic NBP interest rates by 0.50 percentage point was submitted at the meeting. The motion did not pass. A motion was also submitted to lower the basic NBP interest rates by 0.25 percentage point. The motion did not pass. The Council left the basic interest rates unchanged at the following levels: reference rate at 4.75%, lombard rate at 6.25%, deposit rate at 3.25%, rediscount rate at 5.00%.

Minutes of the Monetary Policy Council decision-making meeting held on 7 November 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of the results of the November inflation and GDP projection as well as current and expected macroeconomic developments in Poland and abroad.

While analysing the external conditions, it was noted that data incoming recently pointed to a lack of improvement in macroeconomic developments in the euro area. However, few Council members drew attention to the fact that economic outlook for Germany, Poland's major trading partner, remains favourable compared to other countries of the euro area (owing to strong economic ties between Germany and hitherto faster-growing emerging economies). At the same time, some Council members emphasized that the external conditions influenced the Polish economy not only via trade channel. Accordingly, the adverse conditions in the euro area may have a much stronger dampening impact on the economic activity in Poland than would follow from solely trade channel.

When discussing the current developments in Poland and their outlook, it was highlighted that a decline in industrial output and retail sales as well as a deeper decrease in construction and assembly pointed to more pronounced economic slowdown than previously anticipated.

It was stressed that the NBP November projection implied risk of persistent economic slowdown. It was pointed out that the currently forecast GDP growth for the next years runs below the July projection. This downward revision was due to lower investment and consumption forecast. The Council concluded, in line with the projection, that both factors will contribute to lower than previously expected GDP growth.

According to the Council, low consumption growth will result from tepid household disposable income growth and limited room for a further fall in the savings rate, related i.a. to limited lending. The disposable income growth will be curbed due to the ongoing deterioration in labour market conditions along with lower remittances to Poland from migrants abroad. It was emphasized that, in the previous stage of the global financial crisis, favourable financial conditions of households supported continued growth in their consumption and helped to absorb shock of increased costs of servicing their foreign currency loans resulting from zloty depreciation. It was also highlighted that in 2009 consumption growth was strengthened by fiscal loosening, while in the coming quarters the fiscal tightening will likely continue.

Turning to investment activity, in the Council's opinion, adverse demand outlook, deteriorating business sentiment and termination of EU financial perspective 2007-2013 will hamper investment growth. However, few Council members pointed to currently still favourable liquidity position of enterprises, which could trigger corporate investment growth should the demand outlook improve.

Few Council members assessed that the economic growth in 2012 could be lower than implied in the NBP November projection. At the same time, other Council members stressed that over the previous 20 years similar slowdown episodes had been relatively short-lived and that the magnitude of the current slowdown compared to the previous ones – though stronger than expected – had been so far relatively shallow. Few Council members claimed that the steady improvement in the external environment of the Polish economy, assumed for the coming years in the NBP November projection and in external forecasts, would support a gradual recovery in Polish foreign trade, and consequently a gradual recovery in the domestic economic growth.

While discussing current inflation developments, it was emphasized that price growth continued on a downward trend. Yet, annual inflation remained above the upper limit of deviation from the NBP inflation target. It was pointed out that the elevated annual inflation was driven largely by factors beyond the direct impact of the domestic monetary policy. These developments are accompanied by weakening domestic demand pressure, as indicated by declining core inflation.

While referring to the inflation outlook against the background of the NBP November projection, the majority of the Council members stressed that the projection confirmed a significant decline of risk that the coming quarters would bring intensification of demand pressure. At the same time, the risk of inflation falling below the target over the medium term has increased. In line with the November projection, modest economic growth and deteriorating labour market conditions will support a decline in inflation. According to the majority of the Council members, weakening economic growth along with decreasing wage pressure and employment, substantially reduce the risk of second round effects and should be conducive to a marked fall in inflation in the coming quarters, even despite still elevated commodity prices. Some Council members argued that although changes in prices of commodities, including energy commodities, remain a significant risk factor for global price stability, the recent information on annexation of the Yamal contract reducing the import prices for natural gas to Poland, allows to expect lower energy price growth in Poland.

The majority of the Council members argued that the growth of prices for consumer goods and services over the monetary policy horizon might run below the inflation target, albeit above the November projection path. Some of these Council members assessed that deceleration of unit labour costs could be milder than assumed in the projection, which might reduce the decline in inflation. According to these Council members, higher growth of unit labour costs relative to the path anticipated in the projection will result from lower labour productivity growth than accounted for in the projection and stronger increase in NAWRU due to hysteresis. Those Council members also noted that in the face of the fiscal imbalance it could not be ruled out that the VAT rate will be left unchanged at 23% in 2014.

According to some Council members, food and energy price growth is particularly likely to run above the November projection path. Few of those Council members were of the opinion that, apart from considerable volatility of global food and energy prices, an additional source of uncertainty for inflation in Poland – larger than assumed in the projection – lies in the impact of the EU Energy and Climate Package on energy prices in Poland. In their opinion, it is equally difficult to assess the transmission of new agreements on gas import prices on domestic energy prices.

As regards current and future interest rate decisions, the majority of the Council members decided that the NBP interest rate should be decreased at the current meeting. The incoming economic data had confirmed a marked deterioration in economic conditions in Poland, while the NBP November projection pointed to a risk of a protracted economic slowdown, which will curb demand pressure and pose risk of inflation falling below the target in the medium term. Interest rate cuts will limit the scale of economic downturn, and, consequently, reduce the risk of inflation falling below the target.

However, few Council members were of the opinion that the NBP interest rates should be kept unchanged due to persistently elevated current inflation and remaining uncertainty about global energy commodity prices. Moreover, in their opinion, a decrease in interest rates may have a limited impact on lending amid still tight lending conditions in the banking sector. They also pointed out that a decrease in interest rates could discourage household savings in the banking system. Yet, those Council members did not rule out decreases in the interest rates at subsequent meetings of the Council might be justified, should the impact of the economic slowdown on inflation be more pronounced and the likelihood of further increases in energy prices fall.

A motion to lower the NBP interest rates by 0.50 percentage point was submitted at the meeting. The motion did not pass. A motion was also submitted to lower the basic NBP interest rates by 0.25 percentage point. The motion was passed. The Council decided to lower the basic interest rates to the following levels: reference rate to 4.50%, lombard rate to 6.00%, deposit rate to 3.00%, rediscount rate to 4.75%.

Minutes of the Monetary Policy Council decision-making meeting held on 5 December 2012

At its meeting, the Monetary Policy Council discussed the current and future monetary policy decisions against the background of the domestic and external macroeconomic conditions, especially including inflation developments.

While analysing the external conditions, the Council observed that the persistently unfavourable economic climate in the external environment of Poland has an adverse impact on domestic economic activity. At the same time, the Council members pointed to the scale of fiscal tightening in the United States in 2013 as a factor posing uncertainty to the global economic growth in the nearest term. However, some Council members emphasised that in the second half of 2013 GDP growth may accelerate somewhat in Western European economies, including Germany, Poland's main trading partner. Also, a few Council members drew attention to the structural adjustments in the peripheral economies of the euro area, which in the longer term should contribute to higher growth in these countries and bring an improvement in the economic situation of the entire euro area.

While addressing economic conditions in Poland, a further slowdown in the economy was pointed out, confirmed by the 2012 Q3 GDP data. It was emphasised that the slowdown is driven not only by external but also domestic factors. While analysing factors behind the decline in domestic demand in 2012 Q3, the Council members highlighted a decrease in investment and consumption growth deceleration. They observed that household consumption is adversely affected by a decline in real disposable income. As households strive to smooth consumption, it is accompanied by savings rate declining to its historical low. It was pointed out that a decrease in disposable income is in particular related to deteriorating labour market conditions.

While analysing the incoming labour market data, it was pointed out that wage growth decelerated in 2012 Q3, which was accompanied by a further decrease in unit labour costs growth rate. At the same time, some Council members argued that the rising unemployment rate does not indicate a risk of higher wage demands. A few Council members argued that higher unemployment rate may be partially linked to rising equilibrium unemployment rate, which, in their opinion, is suggested by the growth in the number of vacancies and rising employee recruitment costs.

With reference to the outlook for economic growth in Poland, the Council members pointed out that GDP growth will remain weak in the subsequent quarters. Consumption will continue to be hampered, in particular, by deteriorating labour market conditions. Another factor negatively affecting consumption is households' limited capacity to increase consumption through further reduction in the savings rate. In the opinion of the Council, investment growth in the subsequent quarters will continue to be negative, as indicated, in particular, by further decline in the cost estimate value of newly launched investment projects. It was pointed out that declining public investment, including projects co-financed with EU funds, will remain a factor dampening investment. A few Council members observed that the scale of decline in investment may be curbed by the "Polish Investment" government programme, whose effects, however, will be noticeable in the second half of 2013 at the earliest. At the same time it was anticipated that economic growth will continue to be driven by net exports. Yet, in this context, future demand from the euro area and the zloty exchange rate developments constitute a risk factor. Some Council members argued that as the economic conditions abroad are expected to improve, economic growth in Poland may also accelerate in the second half of 2013. Other Council members observed, in turn, that despite possible economic climate improvement in Poland in the second half of 2013, current data indicate considerable weakening in economic activity and rising risk of recession.

According to some Council members, the observed slowdown in GDP growth partially reflects a decline in potential economic growth due to the fact that factors hitherto enhancing competitiveness of the Polish economy are on the wane. Therefore, these Council members were of the opinion that the negative output gap in the Polish economy may be moderate. Yet, other Council members indicated that potential GDP growth may have declined only slightly in the aftermath of the crisis, and consequently, given the current GDP growth rate, the output gap in the economy is widening.

While addressing inflation developments, the Council members drew attention to the fact that both CPI and core inflation has recently declined. A downward revision in households' inflation expectations was also emphasised. At the same time, the majority of the Council members expressed an opinion that the subsequent quarters will see a considerable decline in inflation. According to the Council members, lower inflation will be supported by supply factors, including cuts in the prices of natural gas as of January 2013, as well as the widening output gap and the lack of wage pressure in the economy. At the same time, some Council members pointed to uncertainty about future inflation developments. The uncertainty is related, in particular, to the developments in the zloty exchange rate which is affected by investors' volatile sentiment. These factors may lead to a reversal in capital flows and increased volatility of the zloty exchange rate. At the same time, a few Council members pointed to the risk related to the strongly expansionary monetary policy of major central banks, which may eventually result in inflation rising significantly across the global economy.

Yet, some Council members presented the opinion that given the persistence of the factors hitherto increasing inflation, inflation is unlikely to decline significantly in the nearest years. In this context, some Council members pointed out that decline in inflation expected in the subsequent quarters will be driven by supply factors and hence will not have any significant impact on wage and inflationary pressures in the economy. These members also pointed to a possible acceleration in economic growth in the second half of 2013, which may somewhat increase inflationary pressure.

It was assessed that the NBP interest rates should be lowered at the current meeting, which should support economic activity and reduce the risk of inflation falling below the target in the medium term. The Council members differed in their opinions as to the scale of the NBP interest rate cuts, both at the current meeting and during the entire cycle.

Most Council members pointed out that given the persistence of inflation and the risks related to price growth within the horizon of the strongest monetary policy impact , the reduction in the NBP interest rates should not be significant. A few of these members additionally indicated that interest rate cuts may weaken the zloty exchange rate, and thus negatively affect inflation, as well as prompt households to deposit savings outside the banking system. At the same time, a few Council members argued that deep interest rate cuts may bring further decline in the savings rate, thus contributing to building imbalances in the economy.

Other Council members, in turn, considered that in the current economic conditions, even a somewhat deeper interest rate reduction would not lead to inflationary and wage pressure in the subsequent quarters. In the opinion of those Council members, considering the degree of economic downturn and growing risk of inflation falling below the NBP's inflation target in the coming quarters, it was advisable at the current meeting to reduce the NBP interest rates more than previously, and according to a few Council members – far more than previously. Those members observed that the arguments in favour of a relatively prompt monetary policy easing include, in particular, the length of lags in the monetary policy transmission mechanism. In the opinion of those Council members, when making decisions concerning interest rates in Poland it was also necessary to consider the level of interest rates across the world, including in the main developed economies.

At the meeting, a motion was submitted to lower the basic NBP interest rates by 1.50 percentage point. The motion did not pass. A motion was also submitted to lower the basic NBP interest rates by 0.50 percentage point. The motion did not pass. At the meeting, a motion was also submitted to lower the basic NBP interest rates by 0.25 percentage point. The motion was passed. The Council decided to lower the basic interest rates by 0.25 percentage point, to the following levels: reference rate at 4.25%, lombard rate at 5.75%, deposit rate at 2.75%, rediscount rate at 4.50%.

Appendix 6

VOTING RECORDS OF MPC MEMBERS ON MOTIONS AND RESOLUTIONS IN 2012

Voting records of Monetary Policy Council Members on motions and resolutions in 2012 are presented below:

- **Date:** 4 April 2012

Subject matter of motion or resolution:
Resolution No. 1/2012 on approving the Annual Financial Report of the National Bank of Poland prepared as of 31 December 2011.

Voting of the MPC members:

For:	**Against:**
M. Belka A. Bratkowski E. Chojna-Duch Z. Gilowska A. Glapiński J. Hausner A. Kaźmierczak A. Rzońca J. Winiecki A. Zielińska-Głębocka	

- **Date:** 4 April 2012

Subject matter of motion or resolution:
Motion to raise the NBP interest rates by 0.25 percentage point.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For:	**Against:**
Z. Gilowska	M. Belka
A. Glapiński	A. Bratkowski
A. Kaźmierczak	E. Chojna-Duch
	J. Hausner
	A. Rzońca
	J. Winiecki
	A. Zielińska-Głębocka

- **Date:** 8 May 2012

Subject matter of motion or resolution:
Resolution No. 2/2012 on the evaluation of the activities of the NBP Management Board as regards the implementation of the monetary policy guidelines for the year 2011.

Voting of the MPC members:

For:	**Against:**
M. Belka	
A. Bratkowski	
E. Chojna-Duch	
Z. Gilowska	
A. Glapiński	
J. Hausner	
A. Kaźmierczak	
A. Rzońca	
J. Winiecki	
A. Zielińska-Głębocka	

- **Date:** 8 May 2012

Subject matter of motion or resolution:
Resolution No. 3/2012 on approving the report on monetary policy implementation in 2011.

Voting of the MPC members:

For:		Against:	
	M. Belka		
	A. Bratkowski		
	E. Chojna-Duch		
	Z. Gilowska		
	A. Glapiński		
	J. Hausner		
	A. Kaźmierczak		
	A. Rzońca		
	J. Winiecki		
	A. Zielińska-Głębocka		

- **Date:** 9 May 2012

Subject matter of motion or resolution:
Resolution No. 4/2012 on the level of the reference rate, lombard rate, deposit rate and rediscount rate of the National Bank of Poland.

MPC decision:
The MPC increased the interest rates by 0.25 percentage point.

Voting of the MPC members:

For:		Against:	
	M. Belka		A. Bratkowski
	Z. Gilowska		E. Chojna-Duch
	A. Glapiński		
	J. Hausner		
	A. Kaźmierczak		
	A. Rzońca		
	J. Winiecki		
	A. Zielińska-Głębocka		

- **Date:** 22 May 2012

Subject matter of motion or resolution:
Resolution No. 5/2012 on approving the report on the operations of the National Bank of Poland in 2011.

Voting of the MPC members:

For:
M. Belka
A. Bratkowski
E. Chojna-Duch
Z. Gilowska
A. Glapiński
J. Hausner
A. Kaźmierczak
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

Against:

- **Date:** 4 July 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.50 percentage point.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For:
A. Bratkowski

Against:
M. Belka
E. Chojna-Duch
A. Glapiński
J. Hausner
A. Kaźmierczak
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

Z. Gilowska was absent.

- **Date:** 4 July 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.25 percentage point.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For:		**Against:**	
	A. Bratkowski		M. Belka
	E. Chojna-Duch		A. Glapiński
			J. Hausner
			A. Kaźmierczak
			A. Rzońca
			J. Winiecki
			A. Zielińska-Głębocka

Z. Gilowska was absent.

- **Date:** 5 September 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.50 percentage point.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For:		**Against:**	
	A. Bratkowski		M. Belka
	E. Chojna-Duch		A. Glapiński
			J. Hausner
			A. Kaźmierczak
			A. Rzońca
			A. Zielińska-Głębocka

Z. Gilowska and J. Winiecki were absent.

- **Date**: 5 September 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.25 percentage point.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For: A. Bratkowski
E. Chojna-Duch

Against: M. Belka
A. Glapiński
J. Hausner
A. Kaźmierczak
A. Rzońca
A. Zielińska-Głębocka

Z. Gilowska and J. Winiecki were absent.

- **Date:** 18 September 2012

Subject matter of motion or resolution:
Resolution No. 6/2012 on adopting *Monetary Policy Guidelines for 2013*.

Voting of the MPC members:

For: M. Belka
A. Bratkowski
Z. Gilowska
A. Glapiński
J. Hausner
A. Kaźmierczak
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

Against:

E. Chojna-Duch was absent.

- **Date:** 18 September 2012

Subject matter of motion or resolution:
Resolution No. 7/2012 on setting the ceiling for liabilities arising from loans and credits drawn by the NBP at foreign banking and financial institutions in 2013.

Voting of the MPC members:

For: M. Belka
A. Bratkowski
Z. Gilowska
A. Glapiński
J. Hausner
A. Kaźmierczak
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

Against:

E. Chojna-Duch was absent.

- **Date:** 3 October 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.50 percentage points.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For:		**Against:**	
	A. Bratkowski		M. Belka
	E. Chojna-Duch		A. Glapiński
			J. Hausner
			A. Kaźmierczak
			A. Rzońca
			J. Winiecki
			A. Zielińska-Głębocka

Z. Gilowska was absent.

- **Date:** 3 October 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.25 percentage points.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For:		**Against:**	
	M. Belka		A. Glapiński
	A. Bratkowski		J. Hausner
	E. Chojna-Duch		A. Kaźmierczak
	A. Zielińska-Głębocka		A. Rzońca
			J. Winiecki

Z. Gilowska was absent.

- **Date:** 7 November 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.50 percentage points.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For: M. Belka
A. Bratkowski
E. Chojna-Duch
A. Zielińska-Głębocka

Against: Z. Gilowska
A. Glapiński
J. Hausner
A. Kaźmierczak
A. Rzońca
J. Winiecki

- **Date:** 7 November 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.25 percentage points.

MPC decision:
Motion passed.

Voting of the MPC members:

For: M. Belka
A. Bratkowski
E. Chojna-Duch
J. Hausner
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

Against: Z. Gilowska
A. Glapiński
A. Kaźmierczak

- **Date:** 7 November 2012

Subject matter of motion or resolution:
Resolution no 8/2012 on reference rate, refinancing credit rate, fixed-term deposit rate and rediscount rate at the NBP.

MPC decision:
The MPC lowered NBP interest rates by 0.25 percentage points.

Voting of the MPC members:

For: M. Belka
A. Bratkowski
E. Chojna-Duch
J. Hausner
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

Against: Z. Gilowska
A. Glapiński
A. Kaźmierczak

- **Date:** 20 November 2012

Subject matter of motion or resolution:
Resolution no 9/2012 amending the resolution on the principles for the application of foreign exchange swaps by the National Bank of Poland.

Voting of the MPC members:

For:	M. Belka A. Bratkowski E. Chojna-Duch Z. Gilowska A. Glapiński J. Hausner A. Kaźmierczak A. Rzońca J. Winiecki A. Zielińska-Głębocka	**Against:**

- **Date:** 4 December 2012

Subject matter of motion or resolution:
Resolution no 10/2012 on interest rates on short-term loans granted to the Bank Guarantee Fund, and interest rates on the provisioning and supplementary contributions to the stabilization fund granted to the National Association of Cooperative Savings Credit and Unions by the NBP.

Voting of the MPC members:

For:	M. Belka A. Bratkowski E. Chojna-Duch A. Glapiński J. Hausner A. Kaźmierczak A. Rzońca A. Zielińska-Głębocka	**Against:**

Z. Gilowska and J. Winiecki were absent.

- **Date:** 5 December 2012

Subject matter of motion or resolution:
Resolution no 11/2012 on approving the Financial Plan of the National Bank of Poland for 2013.

Voting of the MPC members:

For:	Against:
M. Belka	
A. Bratkowski	
E. Chojna-Duch	
Z. Gilowska	
A. Glapiński	
J. Hausner	
A. Kaźmierczak	
A. Rzońca	
J. Winiecki	
A. Zielińska-Głębocka	

- **Date:** 5 December 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 1.50 percentage points.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For:	Against:
A. Bratkowski	M. Belka
E. Chojna-Duch	Z. Gilowska
	A. Glapiński
	J. Hausner
	A. Kaźmierczak
	A. Rzońca
	J. Winiecki
	A. Zielińska-Głębocka

• **Date:** 5 December 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.50 percentage points.

MPC decision:
Motion did not pass.

Voting of the MPC members:

For: A. Bratkowski
E. Chojna-Duch
Z. Gilowska
A. Glapiński

Against: M. Belka
J. Hausner
A. Kaźmierczak
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

• **Date:** 5 December 2012

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.25 percentage points.

MPC decision:
Motion passed.

Voting of the MPC members:

For: M. Belka
A. Bratkowski
E. Chojna-Duch
Z. Gilowska
A. Glapiński
J. Hausner
A. Kaźmierczak
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

Against:

- **Date:** 5 December 2012

Subject matter of motion or resolution:
Resolution no 12/2012 on reference rate, refinancing credit rate, fixed-term deposit rate and rediscount rate at the NBP.

MPC decision:
The MPC lowered the NBP interest rates by 0.25 percentage points**.**

Voting of the MPC members:

For:		Against:
	M. Belka	
	A. Bratkowski	
	E. Chojna-Duch	
	Z. Gilowska	
	A. Glapiński	
	J. Hausner	
	A. Kaźmierczak	
	A. Rzońca	
	J. Winiecki	
	A. Zielińska-Głębocka	