NBP Narodowy Bank Polski

Monetary Policy Council

# Report on monetary policy implementation in 2014

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Warsaw, May 2015

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 (Narodowy Bank Polski), 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 in the year the *Report* encompasses.

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 and that they are taken under uncertainty about future macroeconomic developments. Moreover, the economy is subject to macroeconomic shocks, which, while remaining outside the control of the domestic monetary policy, may to a large extent affect economic conditions and domestic inflation developments in the short, and sometimes in the medium term.

The *Report on monetary policy implementation in 2014* is a translation of the publication of Narodowy Bank Polski entitled *Sprawozdanie z wykonania założeń polityki pieniężnej na rok 2014*. In case of discrepancies, the Polish version prevails.

# Content

# 1. Monetary policy strategy in 2014

In 2014, the Monetary Policy Council conducted monetary policy as set out in *Monetary Policy Guidelines for 2014* adopted on 3 September 2014, whose main elements are stipulated below.

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 (Narodowy Bank Polski) of 29 August 1997 states in Article 3 Section 1 that “The basic objective of the activity of the NBP shall be to maintain price stability, while supporting the economic policy of the Government, 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 banks contribute to balanced economic growth. In pursuit of the task of maintaining price stability, central banks respond both to inflationary and deflationary threats.

Since 1998, the Council has based its monetary policy on inflation targeting (IT). Beginning in 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 when 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 Narodowy Bank Polski and other central banks shows that the IT strategy - applied with appropriate flexibility - is an effective tool to ensure price stability in the medium term and, at the same time, is supportive of macroeconomic stability. The global financial crisis has shown that in order to ensure macroeconomic stability, monetary policy should be pursued in such a way as to – while striving to stabilise inflation at the target level – limit the risk of accumulating imbalances in the economy, especially those resulting from unsustainable credit booms. The possibility to flexibly set the parameters and adjust implementation of available monetary policy instruments according to the situation in the domestic financial system is a factor, which may mitigate this risk.

Besides monetary policy, fiscal and macroprudential policy play an important role in maintaining macroeconomic stability. In order to maintain price stability in the longer term, it is necessary to conduct fiscal policy ensuring the long-term stability of public finances and a macroprudential policy which mitigates the risk of imbalances building up in the economy.

Domestic monetary policy is also largely conditional upon monetary policy conducted by major central banks, whose decisions (especially those concerning interest rates and quantitative easing programmes) – through their influence on global financing conditions, including risk premia embedded in individual assets prices – may fuel volatility of international capital flows, thus impacting domestic economic developments.

In its *Guidelines*, the Council stressed that in 2014, NBP's monetary policy will remain focused on meeting the medium-term inflation target. At the same time, the Council indicated that its monetary policy will be pursued in like with the following principles:

- First, the notion of permanent inflation target means that it refers to inflation measured as a change in prices of consumer goods and services in each month compared to the corresponding period of the preceding year. While analysing inflation developments 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.

- Second, monetary policy is unequivocally focused on maintaining inflation in the medium term 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 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 as well as the 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. The Council pointed out that when assessing the need for a response, it takes into account the extent to which inflation expectations are anchored, which affects the scale and persistence of the impact of demand and supply shocks on inflation.

- Fourth, monetary policy response to shocks 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 with a monetary tightening may lead to an even deeper plunge in output growth resulting from supply shock's negative impact on consumption and investment.

- 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 policy tightening that prevents inflation from being sustained at a heightened level.

In the case of shocks resulting from changes in risk perception, it is of prime importance to determine whether changes reflect economic fundamentals, and to what extent they can be reversed with the central bank's standard instruments. When changes in risk perceptions are transitory, a premature monetary policy response may lead to excessive interest rate volatility, and consequently to inflation and economic growth rate volatility. Therefore, in an environment marked by substantial and frequent changes in risk perception, it is crucial to adjust monetary policy parameters gradually.

The central bank's response to a shock depends also on the assessment of the persistence of its consequences, including the assessment of the risk of the so-called second round effects. Therefore, when assessing the risk of inflation stabilizing at a heightened level the important factors to be considered include the degree to which inflation expectations have been anchored and the overall macroeconomic conditions, which might either support or mitigate wage pressures.

As far as response to shocks is concerned , it is of particular importance that the central bank may specify the time horizon of inflation returning to the target flexibly, i.e. conditional on the nature of the shock and its persistence.

- Fifth, 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 of 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.

- Sixth, the stability of the financial system, economic balance and long-term stability of inflation are closely dependent on developments in lending. If lending expands significantly faster than GDP over a longer period, imbalances in the economy may escalate, especially if credit growth and real property prices reinforce each other in a feedback loop. Monetary policy supports macroprudential policy in preventing unsustainable booms in the mortgage markets, as their collapse can trigger a sharp and prolonged economic slump.

- Seventh, in order to preserve financial stability and curb the risk of imbalances building up in the economy, macroprudential policy is of particular importance, which, through selective impact on certain credit aggregates and asset prices may be a more adequate tool in limiting macroeconomic imbalances than monetary policy, as it involves less cost to the real economy.

- Eighth, in assessing the degree of monetary policy restrictiveness not only should the level of real interest rates (i.e. adjusted for inflation) be considered but also the level of the real exchange rate (i.e. adjusted for the price level at home and abroad). Thus understood restrictiveness of monetary policy impacts, along with the implemented fiscal and macroprudential policy, the total restrictiveness of macroeconomic policy. Ensuring price stability amidst an overly expansionary fiscal policy may justify a tight monetary policy, including keeping interest rates at a heightened level. In turn, if fiscal policy is tightened, monetary policy can be looser, in particular if fiscal tightening weighs heavily on economic activity.

- Ninth, monetary policy is pursued under uncertainty, which means that economic processes cannot be managed precisely. 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 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 its *Guidelines*, the Council also emphasised that due to the lags in the response of the economy to the monetary policy, the impact of current monetary policy on 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 assess this time lag only approximately. Turmoil in the domestic and international financial system may constitute an additional factor disrupting the monetary transmission mechanism. In view of the above factors, central banks allow the possibility of current inflation running temporarily outside the band for deviations from the target, while striving to maintain price stability in the medium term.

# 2. Monetary policy and macroeconomic developments in 2014

In 2014, price stability remained the main objective of the Monetary Policy Council, which is supportive of balanced economic growth. At the same time, monetary policy aimed to contain the risk of imbalances in the economy and support financial stability.

The Council's decisions were primarily based on the assessment of factors influencing inflation developments in the monetary policy transmission horizon, including the character and persistence of shocks resulting in inflation deviating from the target, as well as the outlook for inflation returning to the target. This assessment was changing over time, depending on the economic data and varying macroeconomic forecasts available at the time the decisions were made.

In the first half of 2014, the incoming information suggested sustained moderate growth in the global economy, with considerable differences across countries. In the United States, the economic recovery continued. In the euro area, in turn, the data releases in 2014 Q2 were suggesting that recovery in this economy could be coming to a halt. Economic conditions in Europe were also affected by an increase in uncertainty associated with the conflict between Russia and Ukraine. At the same time, the prices for coal, gas and – since 2014 Q2 – also agricultural commodities were declining. Falling commodity prices, along with moderate growth in aggregate demand, were lowering inflation in many countries. In consequence, major central banks were keeping the interest rates at historical lows. Nonetheless, monetary policy of major advanced economies started to diverge. The Federal Reserve (Fed) was gradually reducing the scale of quantitative easing (QE). This – along with the temporary escalation of geopolitical risks – resulted in weaker sentiment in the international financial markets and contributed to the depreciation of emerging market currencies. The European Central Bank (ECB) lowered its interest rates in mid-2014 and announced that it intended to introduce QE in the coming quarters.

In Poland, the data and forecasts released in the first half of 2014 pointed to a gradual acceleration in economic growth, accompanied by improving labour market conditions and an increase in lending growth rate. Consumer price growth decelerated, albeit mainly due to a decline in energy prices resulting from a fall in energy commodity prices and low food price growth rate due to favourable agrometeorological conditions and the embargo on pork exports to Russia, i.e. factors beyond the impact of the domestic monetary policy. Moreover, the forecasts suggested that inflation would gradually return to the target in the monetary policy horizon as the economic growth was projected to recover further. Against this background, and taking into account the impact of significant reduction in the interest rates in the previous years, the Council kept the interest rates unchanged in the first half of 2014.

In the second half of 2014, the risk of economic slowdown in the euro area intensified, while the conditions in commodity markets changed markedly. Moreover, the conflict between Russia and Ukraine escalated, which brought about the imposition of further trade restrictions between Russia and its trading partners, including Poland. At the same time, the decline in commodity prices, in particular for agricultural and energy commodities, has intensified. Particularly sharp drops were recorded for crude oil prices, which – given still moderate aggregate demand growth – supported the decline in inflation in many countries and the onset of deflation in many European countries. The monetary policy in the United States and the euro area diverged further. The Fed concluded its asset purchase programme and pointed to a likely interest rate increase in the following year, while the ECB started to purchase financial assets and carried out targeted longer-term refinancing operations.

In Poland, the economic growth weakened somewhat in the second half of 2015. The scale of the slowdown, however, was not significant. It was driven by external factors, i.e. falling export growth caused by deteriorating economic conditions in Russia and Ukraine, combined with low economic growth in the euro area. Alongside that, the labour market conditions continued to improve and the credit growth rate remained stable, which supported domestic demand growth. In spite of this, the drop in global commodity prices and new restrictions on trade with Russia contributed to a significant fall in food prices and deepening decline in energy prices in Poland, which resulted in the onset of deflation in the second half of the year. This was accompanied by lower price growth forecasts for the following quarters, as well as a significant downward revision in inflation expectations. As a result, the risk of inflation remaining below the target in the medium term increased. Given this, the Council lowered the NBP interest rates, including the reference rate by 0.5 percentage points to 2.0% and narrowed the spread between the deposit rate and the lombard rate (Table 1).[1] The Council also pointed to possible further monetary policy adjustments if, despite the interest rate cuts, the outlook for inflation returning to the target deteriorates. When deciding on the scale of the interest rate decrease, the Council took into account, on the one hand, the risks associated with inflation remaining below the target, and on the other hand, the risk of macroeconomic imbalances resulting from low interest rates.

**Table 1** Key NBP rates at 2013 year-end and at the end of respective months of 2014

| | Reference rate | Lombard rate | Deposit rate | Rediscount rate |
|---|---|---|---|---|
| **December 2013** | 2.50% | 4.00% | 1.00% | 2.75% |
| **January 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **February 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **March 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **April 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **May 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **June 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **July 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **August 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **September 2014** | 2.50% | 4.00% | 1.00% | 2.75% |
| **October 2014** | 2.00% | 3.00% | 1.00% | 2.25% |
| **November 2014** | 2.00% | 3.00% | 1.00% | 2.25% |
| **December 2014** | 2.00% | 3.00% | 1.00% | 2.25% |

Source: NBP.

The Council's decisions in 2014, together with underlying conditions in each quarter of 2014, are presented below.

[1] In October, the Council also changed the interest rate paid on the required reserve holdings. Since 9 October 2014, the interest rate has been calculated as 0.9 of the NBP reference rate (instead of 0.9 of the rediscount rate).

The data releases in 2014 Q1 pointed to ongoing moderate global economic growth. In the United States, the data suggested that the recovery continued, despite a temporary setback in GDP growth caused by severe winter. In turn, the euro area, including Germany – Poland's main trading partner, showed signs of economic recovery, however growth remained sluggish. Also in most emerging market economies, growth in economic activity was weak as for these countries. Moderate global growth contained demand pressure in many countries. Alongside that, prices for some energy commodities (gas and coal) declined and the agricultural commodity prices stabilized at a lower level compared to the previous quarters. As a result, in 2014 Q1 inflation in many countries levelled off, especially in advanced economies.

Central banks of major developed economies continued a strongly expansionary monetary policy in 2014 Q1, keeping their interest rates low. At the same time, the euro area was experiencing a passive tightening of monetary policy, as commercial banks were repaying the loans taken under three-year longer-term refinancing operations of 2011-2012. The Fed continued its asset purchases, however was gradually reducing their scale. The QE tapering by the Fed, and the emergence of interest rate increase expectations in the United States in a further perspective, were contributing to weaker sentiment in the international financial markets, especially with respect to emerging market economies. An increase in risk aversion was also driven by a rise in geopolitical tensions stemming from the political crisis in Ukraine and the annexation of Crimea by Russia. These tensions have resulted in import restrictions imposed by Russia on certain goods from the European Union member states, including Poland.

The data available in 2014 Q1 confirmed ongoing economic recovery in Poland. In 2013 Q4, GDP growth accelerated, and incoming data, together with the March projection, pointed to a further pick-up of GDP growth in the subsequent quarters. The rebound in economic activity was mainly driven by accelerating growth in domestic demand. This was accompanied by an improvement in economic indicators, especially in industry. Improvement was also seen in the labour market, with growing employment and unemployment on decline. Nonetheless, since the unemployment rate was still high, the wage pressure remained limited. The economic recovery contributed to a gradual rise in lending to the private sector in 2014 Q1. In addition to the improving economic conditions, the recovery in lending was also supported with lower nominal interest rates compared to previous years and easing in consumer lending conditions.

Consumer price inflation in 2014 Q1 rose insignificantly, but remained below the target and the projection of November 2013. Low inflation in early 2014 resulted mainly from a decline in energy prices and low food price growth, which was additionally reduced by the earlier decline in certain energy commodity prices, favourable weather conditions and Russia's embargo on Polish meat. The increase in prices was also contained by limited demand pressure. The March NBP projection was pointing to  inflation remaining significantly lower than previously projected, but gradually returning to the target in the following years.

Against this background, in particular accelerating economic growth in Poland and improvement in the labour market, which contained the risk of inflation remaining below target in the medium term, the Council kept interest rates unchanged in 2014 Q1, including the reference rate at 2.5%. At the same time, the Council pointed that the interest rates would probably remain stable in the coming quarters.[2]

In 2014 Q2, economic growth worldwide remained moderate, yet economic conditions varied across countries. In the United States, GDP – after a temporary decline at the beginning of the year – surged. The data coming from the euro area, including Germany, indicated that the economic recovery might be slowing down in these economies. Alongside that, the growth rate of economic activity in major emerging market economies remained low as for these countries, abating significantly in Russia and Ukraine. The slowdown in the euro area and low economic activity in the major emerging market economies contributed to a slowdown in export growth in the Central and Eastern European countries. Moderate global growth continued to contain demand pressure in many countries. At the same time, the prices of agricultural and energy commodities in the global markets decreased slightly. As a result, inflation remained low in many countries.

In 2014 Q2, central banks of major advanced economies continued a strongly expansionary monetary policy, although the Fed’s and the ECB’s monetary policies started to diverge. The Fed kept its interest rate close to zero, but continued the gradual withdrawal of the asset purchase programme. In turn, the ECB cut the interest rates, bringing the deposit rate below zero, and announced its intention to undertake additional measures aimed to increase the liquidity of the banking sector. The ECB’s monetary policy easing prompted an improvement in sentiment in the international financial markets, also towards the emerging market economies. However, the QE tapering by the Fed and a rise in geopolitical risks resulting from a return of tensions in the Middle East, as well as the ongoing conflict between Russia and Ukraine, was containing the improvement in market sentiment.

As a result of the deteriorating conditions in the environment of the Polish economy, the signs of a risk that economic conditions in Poland might also worsen started to appear. In particular, the industrial production and export growth decelerated, largely due to weakening economic conditions in the euro area and deteriorating conditions in Russia and Ukraine. At the same time, however, household sentiment continued to improve, accompanied by a pick-up in retail sales growth in real terms, and supported by a sustained improvement in the labour market. In 2014 Q2, unemployment continued to decrease and employment to increase, although this still did not lead to a rise in wage pressure. Moreover, incoming information pointed to the persistence of relatively high investment growth and a further rise in lending to the private sector.

In 2014 Q2, the price effects of the Russian embargo on Polish meat intensified. This was accompanied by an ongoing decline in agricultural commodity prices in the world markets and agrometeorological conditions in Poland favourable for the supply of agricultural products. Therefore, the annual growth rate of food prices turned negative, and the annual CPI growth rate approached zero, supported by limited demand pressure, even though domestic demand continued to accelerate.

[2] At its meetings held in January and February 2014, the Council assessed that interest rates should be kept unchanged at least until the end of the first half of 2014. In March – after becoming acquainted with the projection of inflation and GDP – the Council extended the period in which interest rates were likely to be kept unchanged to at least the end of 2014 Q3.

Taking into account the above considerations, including the acceleration in domestic demand and lending growth, an external nature of shocks beyond price declines and persisting uncertainty about the effects of the conflict between Russia and Ukraine, the Council kept the interest rates unchanged in 2014 Q2. At the same time, due to the signs pointing to the risk of weakening pace of economic recovery and a deepening decline in inflation, the Council revised its judgement about the probable period of interest rate stabilization. In June, the Council assessed that the interest rates should remain unchanged until the end of 2014 Q3, highlighting that a more comprehensive assessment of the monetary policy perspectives would be possible after the release of information in the coming months, including the NBP July projection. In this way, the Council did not extend the period of the probable stabilization of the interest rates.

In 2014 Q3, global economic growth remained moderate, and its pace continued to differ across economies. In the United States, the economic recovery continued, while in the euro area, also in Germany, economic growth remained low. In some major emerging market economies, China and Russia included, economic activity was declining. Moderate economic growth worldwide continued to contain demand pressure in many countries. Alongside that, the pace of a decline in prices for agricultural and energy commodity, including crude oil, accelerated. As a result, the consumer price growth rate started to decline more markedly in many countries, turning negative in some European countries.

In 2014 Q3, central banks of major advanced economies continued a strongly expansionary monetary policy with persisting differences between the Fed's and the ECB's monetary policy. The Fed kept interest rates at close to zero and continued the QE tapering. In turn, the ECB reduced the interest rates further, conducted the first targeted longer-term refinancing operation and announced its intention to resume purchases of financial assets of the private sector. The easing of the monetary policy in the euro area has been supportive of an improvement in market sentiment towards the emerging market economies. However, the QE tapering and a further increase in geopolitical risks, driven by both a further exacerbation of the situation in the Middle East and of the conflict between Russia and Ukraine were still acting in the opposite direction. In response to the escalation of the conflict between Russia and Ukraine, the United States and the European Union imposed economic sanctions on Russia. In response, Russia introduced additional import restrictions on food products from the European Union member states, including from Poland. The restrictions on trade between the European Union and Russia, as well as the risk that their scope could be extended further, increased the uncertainty about the foreign demand outlook.

Information on economic activity released at the beginning of 2014 Q3 suggested that despite unfavourable conditions in the environment of the Polish economy, GDP growth in 2014 Q3 might remain close to the previous quarter's level. Alongside that, the July projection indicated that the GDP growth rate in a further perspective might be lower than expected in the March projection, but until mid-2016 it would still be higher than the potential growth rate. Similarly to 2014 Q2, the signs of weaker economic conditions in 2014 Q3 appeared mostly in exports, which continued to decelerate. The data available in 2014 Q3 also pointed to a slight deceleration in retail sales growth, coupled with a slight deterioration in consumer confidence and low industrial production growth amidst abating sentiment in this sector. However, the labour market conditions continued to improve. Employment was rising and unemployment – descending, although this did not contribute to nominal wage growth. This was accompanied by stable rise in lending to the private sector.

In 2014 Q3, the growth rate of prices of consumer goods and services turned negative, which was largely driven by a fall in food prices that intensified further, due to the extension of the embargo on Polish food and an ongoing decrease in agricultural commodity prices in the global markets. Lower price level resulted also from a fall in energy prices associated with the intesification of the slump in global commodity prices, including oil. The accelerating drop in commodity prices also led to deeper fall in the producer price index. Core inflation excluding food and energy prices declined as well, which can be partly attributed to a negative base effect associated with a surge in waste disposal charges in 2013 Q3. This was accompanied by a downward revision in inflation expectations. Moreover, the July projection of inflation and GDP indicated that, even though negative price growth should be short-lived and the consumer price growth rate should be rising steadily in the following quarters, inflation would return to the target later than suggested by the March projection.

Given the expectations of only limited deceleration in GDP growth in the following years and a short-term nature of deflation, as well as considering the July projection of inflation and GDP, which indicated that at the end of 2016 inflation would return close to the NBP target, the Council decided to keep the interest rates unchanged. However, the Council no longer provided an assessment on the horizon over which the interest rates would likely remain unchanged, hinting hereby at the possibility of reduction in the interest rates in the following quarter.

In 2014 Q4, global economic growth remained moderate, and its pace continued to differ across economies. In the United States – despite a certain slowdown – it remained much faster than in the euro area. At the same time, the euro area saw a gradual upturn, although the economic growth was still low. However, in Germany, Poland’s main trading partner, GDP growth picked up. In turn, in the major emerging market economies, economic activity remained low as for these countries. The released data also pointed to a deepening recession in Ukraine and the likely decline in GDP growth in Russia. Weakening growth in the emerging market economies, combined with an increase in global crude oil supply, exacerbated the fall in crude oil prices. Alongside that, agricultural commodity prices remained relatively low. The decline in commodity prices in 2014 Q4 and in the previous quarters, amidst still limited demand pressure, contributed to a further fall in prices of consumer goods and services in many economies. In many European countries, including in the euro area, the consumer price index was negative at the end of 2014.

The central banks of the major developed economies kept the interest rates close to zero. At the same time, the ECB started to purchase private sector assets, whereas the Fed concluded its QE and pointed to a likely increase in its interest rates in 2015. The end of the QE and growing expectations for an interest rate increase in the United States contributed to a strong appreciation of the dollar and depreciation of many emerging market currencies. The pace of depreciation was particularly strong in the case of the Russian rouble, as it was exacerbated by the escalation of the Russian-Ukrainian conflict and the sharp fall in crude oil prices. The strong depreciation of the rouble and weakening of the currencies of emerging market economies led to a depreciation of the zloty in late 2014 and a higher uncertainty about the developments in the Central and Eastern European foreign currency markets.

In Poland, the incoming data pointed to a slowdown in economic activity in 2014 Q3 and the forecasts for 2014 Q4 suggested a further weakening in GDP growth. However, economic growth remained significantly higher than in the majority of European countries. Minor slowdown in activity was reflected in weaker growth in construction and assembly output and slightly lower retail sales growth rate. However, some factors were conducive to higher economic activity. In particular, growth in production and exports accelerated, driven by a gradual improvement in economic conditions in the euro area, including a significant increase in GDP in Germany. Alongside that, the labour market conditions continued to improve in Poland with nominal wages still rising moderately, which – combined with a negative price growth – led to an acceleration in real disposable households' income. This was accompanied by stable – despite slight weakening – growth in lending, which exceeded nominal GDP growth.

In 2014 Q4, prices of consumer goods and services continued to decrease due to a sharp fall in global crude oil prices and a further decline in food prices, driven by the intensification of price effects of both the Russian embargo on Polish food and the favourable weather conditions in 2014. Most measures of core inflation also declined, although inflation excluding food and energy prices increased on the previous quarter. Ongoing negative price growth with a drop in oil prices resulted in a further decline in inflation expectations.

The sharp fall in oil prices and a decline in food prices, combined with slight weakening of economic growth, led to a major revision of forecasts for growth of consumer goods and services prices for the following quarters. As a result, the November projection of inflation indicated that the period of negative growth in prices would be longer than previously assessed, with inflation remaining below the NBP inflation target in the medium term. According to the November GDP projection, economic growth – despite a slight decline in the short horizon – would remain stable in the coming years, standing at around 3%.

Taking into account the above considerations, especially a significant downward revision of forecasts for consumer price growth for the following years, increasing the risk of inflation remaining below the target in the medium term, the Council reduced the NBP interest rates in October, including the reference rate by 0.5 percentage points to 2.0%, and narrowed the spread between the deposit rate and the lombard rate.[3] Interest rate cuts were supportive of demand growth in the following quarters and bringing inflation back to the target in the medium term. The Council kept the interest rates unchanged in November and December. The Council judged that given the forecasts of a relatively stable economic growth in the following years, significant interest rate cuts effected in October should be sufficient to contain the risk of inflation remaining below the target in the medium term. In November and December, the Council signalled that it did not rule out the possibility of lowering interest rates in the following months if price growth forecasts continue to be revised downwards, which would result in lower probability of inflation returning to the target in the medium term. When

[3] In October, the Council also changed the interest rate paid on the required reserve holdings. Since 9 October 2014, the interest rate has been calculated as 0.9 of the NBP reference rate (instead of 0.9 of the rediscount rate).

taking the decision to lower interest rates in 2014 Q4, the Council took into account, on the one hand, the risks associated with inflation remaining below the target, and on the other hand, the risk of macroeconomic imbalances resulting from low interest rates.

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An important element in the implementation of monetary policy based on the direct inflation targeting strategy in 2014 was – like in the previous years – communication with the environment, which consisted in the Council presenting the information on the current and probable future decisions, along with an assessment of economic developments behind these decisions. As in previous years, the key communication instruments in 2014 included the cyclical publications: *Information from the meeting of the Monetary Policy Council* (and the accompanying press conferences held after Council meetings), *Minutes of the Monetary Policy Council decision-making meetings*,[4] *Inflation Reports* as well as the annual publications: *Report on monetary policy implementation in 2013* and *Monetary Policy Guidelines for 2015*.

[4] The *Minutes from the Monetary Policy decision-making meetings* contain a more detailed discussion on the issues and arguments behind the decisions taken by the Monetary Policy Council in 2014.

# 3. Monetary policy instruments in 2014

NBP interest rates were the key monetary policy instrument. The level of the reference rate determined the yields on open market operations. The deposit rate and the lombard rate, in turn, set the interest rate on standing facilities.

The set of policy instruments applied by NBP in 2014 was consistent with the adopted monetary policy strategy as well as with the persistent liquidity surplus in the domestic banking sector.

Developments in the domestic and foreign financial markets did not require any substantial changes in the monetary policy instruments set in 2014 regarding the one used by NBP in the previous year.

**Liquidity of the banking sector 2014**

In 2014, NBP pursued its monetary policy amidst liquidity surplus prevailing in the banking sector. [5] The amount of the liquidity surplus averaged PLN 108 816 million[6] i.e. PLN 17 725 million (14.0%) less than in 2013.

Throughout 2014 the excess liquidity of the banking sector gradually decreased and in the respective months of the year its level ranged from PLN 99 218 million (in December) to PLN 123 226 million (in January). This means the average excess liquidity level decreased by PLN 24 267 million (19.7%), when comparing the December 2014 figures with the December 2013 figures.

In 2014, the key factors affecting the level of liquidity in the banking sector (when comparing the December 2014 figures with the December 2013 figures) included the increase in the volume of currency in circulation and net sales of foreign currency by NBP. The growth in currency in circulation caused a decline in the level of liquidity surplus during the year by PLN 14 190 million, while foreign currency transactions led to a decline by PLN 11 820 million. Net sales of foreign currencies resulted primarily from the sale of currencies by NBP due to currency conversion of the EU membership fee that exceeded the purchase of currencies from the account of the Minister of Finance. In addition, the increase in the level of the required reserve during the year reduced liquidity by PLN 2 886 million.The key factor increasing the level of liquidity in the banking sector (also when comparing the December 2014 figures with the December 2013 figures) was the disbursement of the discount on NBP bills (PLN 2 654 million) and the payment of interest on the required reserve holdings (PLN 774 million). Other autonomous factors had smaller impact on the level of liquidity in 2014.

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

[6] During the required reserve maintenance period.

### NBP interest rates

An instrument of key significance with regard to the conduct of the monetary policy in 2014 was the NBP reference rate. Changes in the level of this rate set the direction of the monetary policy pursued by NBP. 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.

The range of fluctuations of interbank overnight interest rates was set by the NBP deposit and lombard rates.

### Open market operations

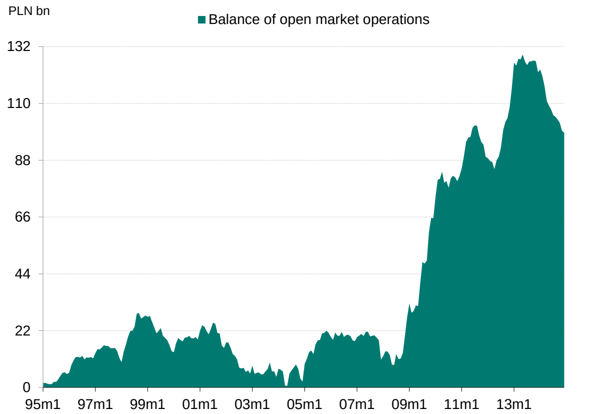
In 2014, NBP conducted its monetary policy in a way to allow the POLONIA rate[7] to run close to the NBP reference rate. This was achieved mainly by means of open market operations used by the central bank to manage liquidity in the banking sector.

The main open market operations were the key instrument used to manage the liquidity of the banking sector. Due to the permanent liquidity surplus in the banking sector, these were liquidity absorbing operations.

The main open market operations were conducted on a regular basis, once a week, in the form of the issuance of NBP bills with a 7-day maturity. The same yield equalling the NBP reference rate was offered at all tenders. In setting the levels of particular operations, NBP strived to ensure balanced liquidity conditions in the banking sector during the required reserve maintenance period.

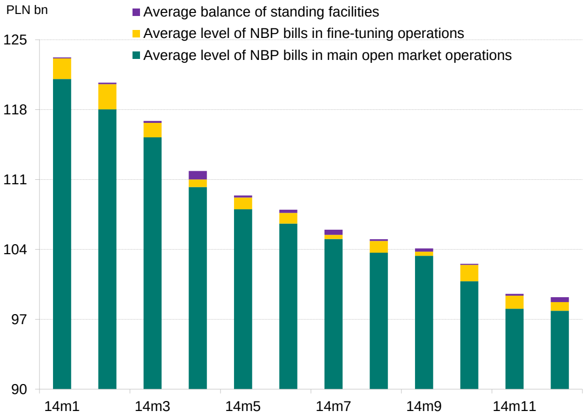
In 2014, NBP conducted 53 main open market operations. The average daily volume of bills categorised as the main open market operations amounted to PLN 107 280 million, and was PLN 16 952 million lower than the average 2013 level.

**Figure 1** Average monthly balance of open market operations in 1995-2014




Source: NBP data.

**Figure 2** Liquidity absorbing instruments in the respective months of 2014



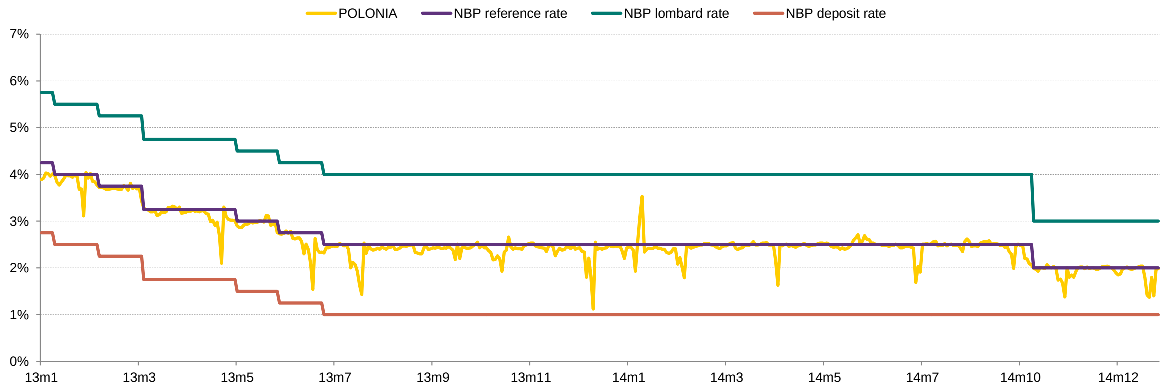

Source: NBP data.

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

In 2014, apart from main open market operations, NBP also conducted fine-tuning operations. They were executed on a regular basis on the last business day of each required reserve maintenance periods as well as on an ad-hoc basis within the required reserve maintenance periods whenever the liquidity conditions in the banking sector were substantially out of balance.

In 2014 fine-tuning operations were conducted only in the form of the issue of NBP bills whose maturity was shorter than the maturity of bills issued under main open market operations. Altogether 19 fine-tuning operations were conducted in 2014, i.e. 6 less than in the previous year. The average daily issue of NBP bills categorised as the mentioned operations amounted to PLN 1 238 million and was PLN 608 million lower than in 2013.

**Figure 3** NBP interest rates and the POLONIA rate in 2013-2014




Source: NBP data.

In 2014 the spread between the POLONIA rate and the NBP reference rate further decreased, as compared to the previous years. The average absolute deviation of the POLONIA rate from the NBP reference rate amounted to 11 bp versus 18 bp in 2013.[8]

The spread between the POLONIA rate and the NBP reference rate has been declining gradually since 2009 when it stood at 89 bp. At the same time, the range of deviations of the POLONIA rate from the NBP reference rate in 2014 was lower than the levels recorded in the period before the intensification of the financial crisis, i.e. before October 2008. The average value of the absolute difference between the POLONIA rate and the NBP reference rate was 16 bp in 2006, 23 bp in 2007 and 19 bp in the period January - September 2008.

Managing the banking sector liquidity in a consistent manner, primary by conducting open market operations, reduced banks' propensity to place their liquidity buffers in instruments with yields substantially lower than those on NBP open market operations (determined by the applicable level of the NBP reference rate). In particular, the impact of interest rate of the overnight deposit in the central bank(the NBP deposit rate) on the yield of unsecured transactions concluded in the interbank market has lessened, which resulted in reduction of the spread between the POLONIA rate and the NBP reference rate.

[8] The average deviation of the POLONIA rate was calculated based on the uniform base of 365 days in a year.

NBP's manner of managing banking sector liquidity also led to gradual reduction in the frequency of conducting ad-hoc fine-tuning operations (carried out within the required reserve maintenance period). In 2014 seven operations of this type were conducted as compared to 13 in 2013, 11 in 2012 and 20 in 2011.

**Reserve requirement**

The system of required reserves contributed to the stability of short-term market interest rates. This resulted from its averaged basis, according to which entities can freely determine the amount of holdings at the central bank during the reserve maintenance period, provided that the average balances held at NBP in the reserve 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 banks' disposal. Thus, amidst the prevailing liquidity surplus, the reserve requirement system enabled the central bank to reduce the scale of its liquidity-absorbing open market operations.

In 2014, the obligation to maintain required reserves applying to banks, branches of credit institutions and branches of foreign banks operating in Poland, was extended to include credit unions (SKOKs) and the National Association of Credit Unions. On 31 March 2014, the required reserves were deposited on NBP accounts for the first time by 55 credit unions and the National Association of Credit Unions.

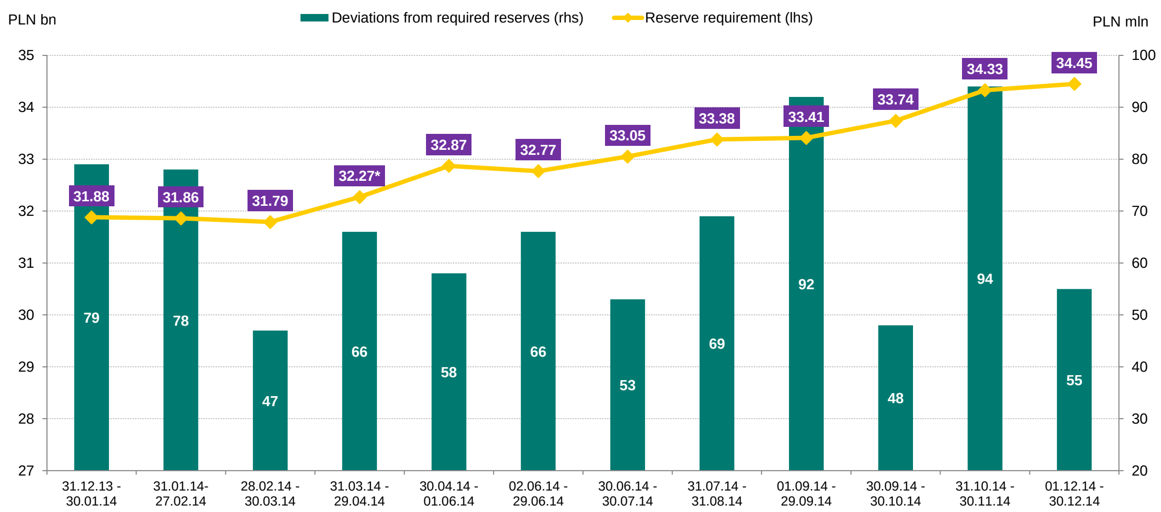
The required reserves were calculated on the basis of deposits collected on accounts and funds coming from the sale of securities, with the exception of funds taken out from another domestic bank, a credit union and the National Association of Credit Unions (KSKOK). Moreover, banks, branches of credit institutions and branches of foreign banks operating in Poland also excluded from reserve calculation funds acquired from foreign sources for the period of at least two years and funds deposited in credit and savings accounts of building societies, funds in individual retirement accounts (IKE) and individual pension security accounts (IKZE), and reimbursable funds received from Banking Guarantee Fund (BFG).

The required reserves were calculated and maintained in the Polish zloty. Entities reduced the amount of the calculated reserve requirement by the PLN equivalent of EUR 500 thousand. In 2014, the basic reserve requirement ratio amounted to 3.5% on all liabilities, except for funds received in respect of the 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 2014 stood at PLN 34 696 million, including the required reserve of commercial banks of PLN 32 201, the required reserve of cooperative banks of PLN 2 040 million, whereas the required reserve of credit unions and the National Association of Credit Unions stood at PLN 454 million. Overall, the required reserved exceeded the level of 31 December 2013 by PLN 2 820 million, posting an 8.8% increase. The main factors behind the higher level of the required reserved in 2014 included the increase in deposits in the banking sector on which the required reserve is calculated and the above mentioned extension of the required reserve system to include credit unions and the National Association of Credit Unions.

Until 8 October 2014, the remuneration on the required reserve balances held on accounts with NBP was equivalent to 0.9 of the NBP rediscount rate. Since 9 October 2014, the interest on the required reserve balances has been equivalent to 0.9 of the NBP reference rate. This change was aimed to keep the interest on the required reserve balances slightly below the yield on main open market operations, regardless of the level of the NBP reference rate.

The average interest on the required reserve holdings in 2014 was 2.32% as compared to 2.87% in 2013. The 0.55% decrease of interest on the required reserve balances in 2014 as compared to 2013 resulted from the decline in the average level of the NBP interest rates (rediscount rate and reference rate) on the basis of which interest on the required reserve holdings was calculated in this period.

**Figure 4** Changes in the required reserve level and deviations from the reserve requirement in 2014




* *extension of the required reserve system to include credit unions and the National Association of Credit Unions*

Source: NBP data.

In 2014, in each reserve maintenance period, there was a slight surplus in the average holdings on banks and credit unions' accounts as compared with the level of the required reserve. The excess reserves balance reached its minimum value in March (PLN 47.0 million) whereas the maximum was recorded in November (PLN 94.2 million). The average surplus of the required reserves holdings in 2014 amounted to PLN 67.1 million and accounted for 0.21% of the average level of required reserves.

In 2014, 4 instances of commercial banks failing to maintain the required reserve level occurred (in 2013 two such cases were recorded) and 1 instance of a credit union failing to meet the requirement. The deficient amount was PLN 1 375 thousand (all 4 banks) and PLN 49 966 thousand, respectively. Those entities were charged with penalty interest equalling twice the amount of the NBP lombard rate, namely of PLN 8 799 and PLN 246 409, respectively.

**Standing facilities**

Standing facilities (overnight deposit facility and lombard credit) were used to stabilize the liquidity level in the interbank market and limit of overnight market rate fluctuations. These operations were conducted at the initiative of commercial banks and were designed primarily to provide the short-term liquidity of the banking system or enable banks to deposit temporary excess free funds with NBP for one-day periods.

The interest rate of lombard credit, setting the maximum price of borrowing money at NBP, determines at the same time the upper limit of fluctuations of interest rates in the interbank market, while the deposit rate limited the band of their downward deviations. Additionally, the four-fold level of interest rate on the lombard credit determined the amount of the so-called maximum interest.

In 2014, as in the previous years, banks' usage of lombard credit was very limited. The total drawing on the lombard credit amounted to PLN 49 million, and was more than three times lower than in 2013 (PLN 163 million). The average daily recourse to the lombard credit amounted to PLN 133 thousand.

In 2014, banks placed overnight deposits at NBP totalling PLN 109 billion, (calculated for the period of their holding), i.e. 35.5% lower than in the previous year. The average daily overnight deposit amounted to PLN 298 million, as against PLN 463 million in 2013. Banks deposited the highest amounts with NBP on the last days of the reserve maintenance periods.

**Foreign exchange swaps**

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

In 2014, the central bank did not conclude any such transactions.

**Currency interventions**

Under the existing monetary policy strategy, NBP may purchase or sell foreign currency in the foreign currency market against the Polish zloty.

In 2014 the central bank did not carry out any such operations.

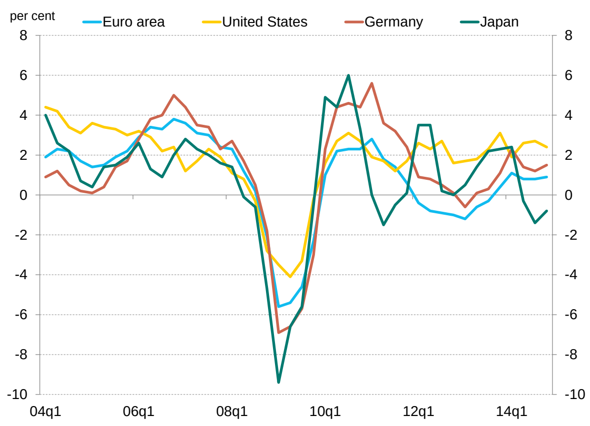
# Appendix 1. Economic developments abroad

In 2014, global economic growth remained moderate, with further divergence in economic conditions across countries (Figure 5, Figure 6). In the United States, following a temporary slowdown at the beginning of the year resulting from exceptionally unfavourable weather conditions, recovery continued. GDP growth in the United States was supported by rising consumer demand associated with gradual improvement in labour market conditions and expansionary monetary policy.

In the euro area, following two years of recession, the GDP growth rate was positive, but still low. Ongoing weakness in economic activity resulted mainly from structural problems of some member countries, including high level of private debt, which contributed to a decline in lending. In some euro area countries, in particular in Germany, GDP growth was contained by a decline in exports, associated with the conflict between Russia and Ukraine, accompanied by a lack of significant demand growth in other euro area countries.

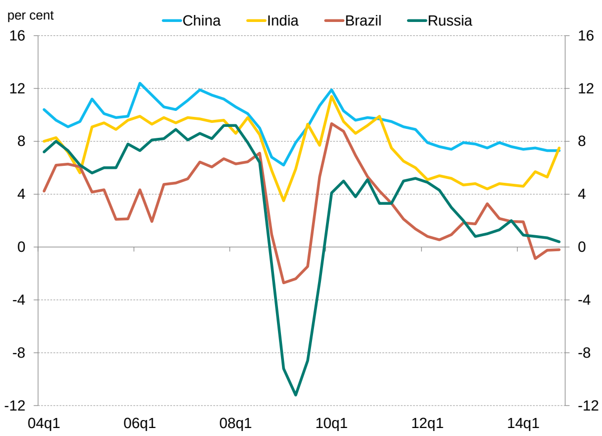
In the major emerging market economies GDP growth in 2014 remained low as for these countries. In most of them it slowed down. Economic slowdown was recorded in China and – more notably – Russia, where GDP decelerated to a particular strong extent. In China economic activity was affected by a downturn in the real estate market, while in Russia, the sharp slowdown of GDP growth was due to the economic aftermath of the war with Ukraine, accompanied – in the second half of the year – by falling crude oil prices and the currency crisis.

**Figure 5** GDP growth in the major advanced economies (y/y) in 2004-2014




Source: Bloomberg, Eurostat.

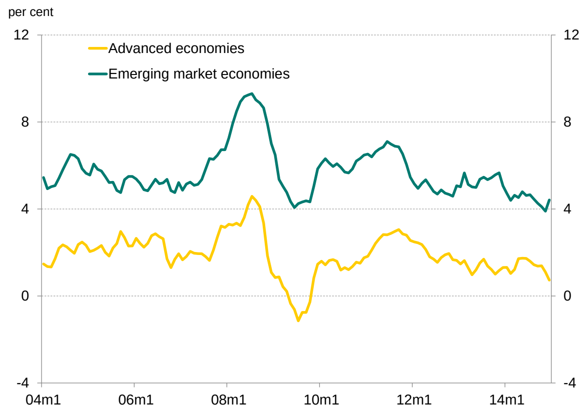
**Figure 6** GDP growth in the major emerging market economies (y/y) in 2004-2014




Source: Bloomberg, Ecowin.

The moderate global economic growth was conducive to low inflation, and even deflation in some economies (Figure 7). In addition, following a stabilisation at the beginning of 2014, prices of agricultural and energy commodities, particularly crude oil, started to decline strongly in mid-2014 (Figure 8). In December 2014, crude oil prices fell by 48.3% against December 2013, natural gas prices – 4.9%, hard coal prices – by 26.2%, and food prices – by 15.3%. The decline in agricultural commodity prices was caused by favourable agrometeorological conditions, whereas the fall in crude oil prices resulted mainly from an increase in supply of this commodity, accompanied by the low growth in the emerging market economies. As a consequence, in the second half of 2014 inflation in many economies decreased significantly. In the euro area and in some other European countries growth in consumer prices turned negative in late 2014.

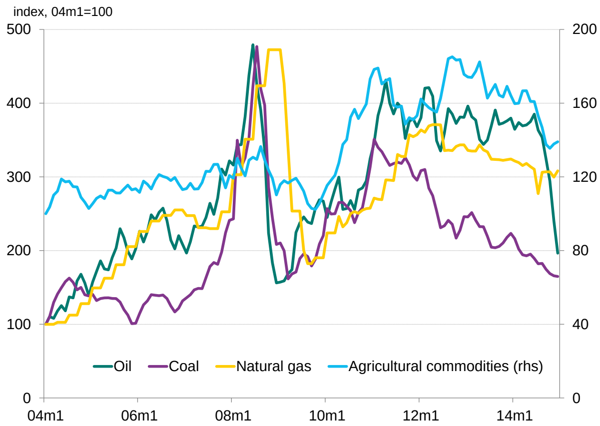
**Figure 7** Global inflation* in 2004-2014




Source: Bloomberg data, NBP calculations.

* Weighted average GDP inflation in the developed and the largest emerging economies (accounting for 80% of GDP in this group of countries).

**Figure 8** Index of commodity prices in the global markets in 2004-2014




Source: Bloomberg data.

Due to the moderate economic activity growth and low inflationary pressure, the monetary policy of the major central banks remained highly expansionary in 2014 (Figure 9, Figure 10). However, due to a different outlook for economic growth and inflation, the monetary policy of the major central banks was gradually diverging. The Federal Reserve (Fed) was reducing its asset purchases to conclude it in October but left its interest rate close to zero. The European Central Bank (ECB), in turn, increased the scale of its expansionary monetary policy. In particular, the ECB reduced its interest rates, introduced targeted longer-term refinancing operations (targeted LTRO) as well as a new programme of private sector asset purchases, and also announced a launch of government bond purchases.[9,10] The ECB decisions encouraged many central banks from countries with economic links to the euro area (including Switzerland, Sweden, Romania, Czech Republic, Hungary and Israel) to ease their monetary policies.

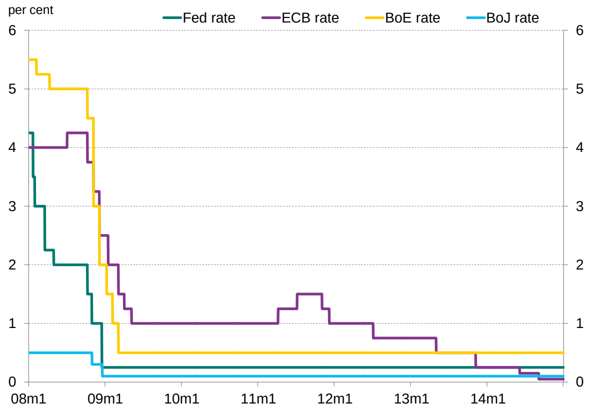
The strongly expansionary monetary policy of the major central banks supported the growth in prices of shares and bonds in some advanced economies. At the same time, the conclusion of the financial asset purchase programme and the expectations of interest rate increases by the Fed have led to the appreciation of the dollar against the currencies of many advanced and emerging market economies. In particular, the strong appreciation of the dollar against the euro and the currencies of countries strongly linked with the euro area was amplified by the ECB's monetary policy easing. The exchange rates of some currencies also weakened due to the increased geopolitical risk (the conflict between Russia and Ukraine and the escalation of tensions in the Middle East) as well as – in the case of countries exporting crude oil, particularly Russia – due to the strong decline in crude oil prices.

[9] The public sector purchase programme was finally announced in January 2015.

[10] The Bank of Japan also pursued a strongly expansive monetary policy, increasing the scale of asset purchases, mainly Treasury bonds and leaving interest rates close to zero.

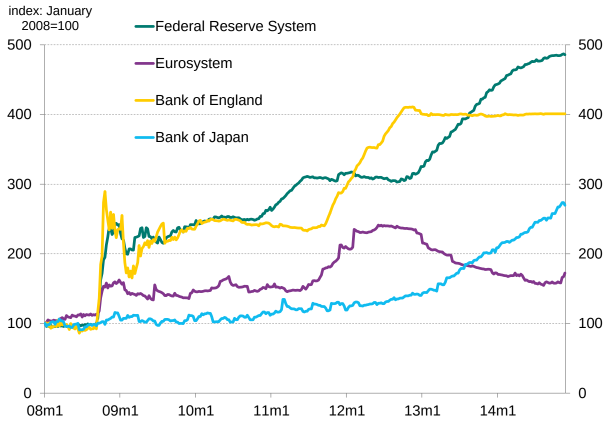
Currency depreciation prompted central banks of some emerging market economies to increase interest rates or intervene in the foreign exchange market.

**Figure 9** Interest rates of major central banks in 2008-2014




Source: Bloomberg.

**Figure 10** Balance sheets of major central banks in 2008-2014 (January 2008 = 100)

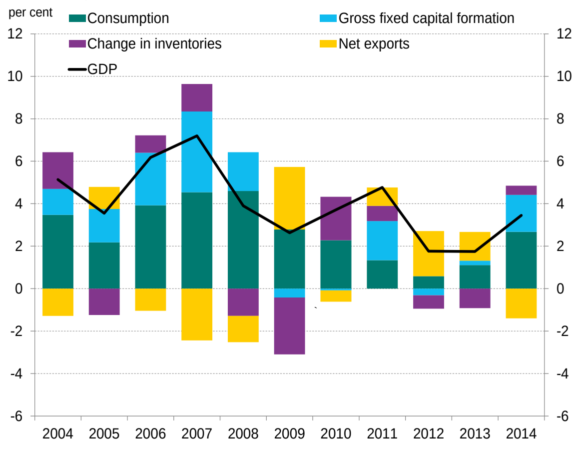



Source: Bloomberg data, NBP calculations.

# Appendix 2. GDP and domestic demand[11]

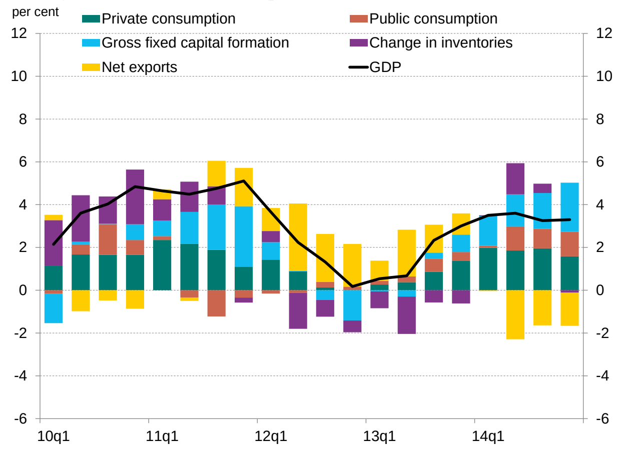
In 2014, the annual GDP growth rate amounted to 3.4% (as compared to 1.7% in 2013) and was lower than that of domestic demand. Consequently, net exports contributed negatively to GDP growth as imports accelerated due to the recovery in domestic demand, while exports growth was only moderate amid unfavourable economic conditions abroad.

**Figure 11** Contribution of aggregate demand components to GDP growth in 2004-2014 (annual data)




Source: GUS data, NBP calculations.

**Figure 12** Contribution of aggregate demand components to GDP growth in 2010-2014 (quarterly data)




Source: GUS data, NBP calculations.

Following the acceleration in the first half of 2014 (from 3.0% y/y in 2013 Q4 to 3.6% y/y in 2014 Q2), economic growth slowed down slightly in the second half of the year, but remained above 3%. The evolution of the main components of aggregate demand is discussed below.

In 2014, private consumption growth accelerated. Factors contributing to the recovery in consumption included the growth in the real income of households resulting from both an improvement in labour market conditions and decelerating, and then negative, price growth. The acceleration in private consumption growth was also supported by stable growth in consumer loans amidst a significant easing of lending conditions as well as an improvement in consumer sentiment throughout 2014. The decline in inflation – along with a freeze in nominal wages in the fiscal sector – has also contributed to the slight rise in public consumption.

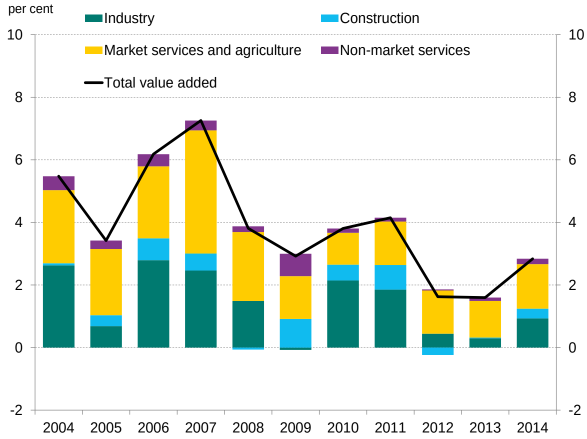
The growth of gross fixed capital formation in 2014 significantly accelerated compared from 2013. Investment growth in all sectors of the economy – the corporate sector, fiscal sector and households – contributed to the recovery in investment demand. Increasing propensity of firms to invest, associated with ongoing moderate economic growth and a high level of capacity utilization, contributed to the rise in capital expenditure of enterprises. The recovery of corporate investment was also supported by the sound financial position of companies as well as the high availability of financing, arising from

[11] The data concerning national accounts presented in Appendix 2 are compliant with the ESA 2010 methodology.

both easing of lending criteria and lower interest rates on loans, as compared to previous years.[12] However, demand uncertainty, associated mainly with the developments abroad contained corporate investment. In case of public investment, growth acceleration of resulted predominantly from a strong rise in investment projects of local governments, including investments co-financed under the EU perspective 2007-2013. In turn, growth in housing investment was supported by the improvement in labour market conditions and lower interest rates on mortgage loans compared with previous years.

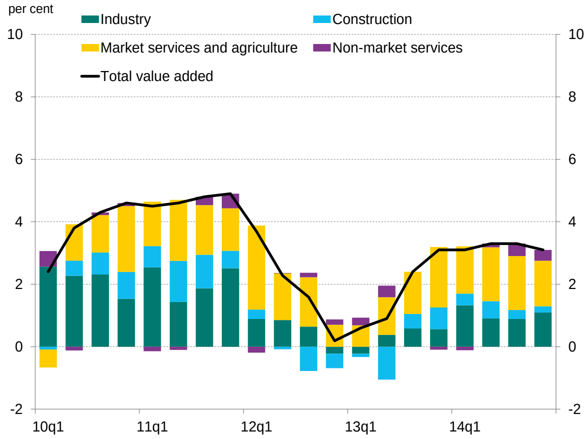
In 2014 – unlike in 2013 – net exports had a negative contribution to GDP growth, which resulted from a significant acceleration of imports accompanied by the stabilisation of export growth. An increase in imports growth is attributable to an ongoing recovery in domestic demand. Growth in exports was, in turn, limited by the persisting unfavourable economic conditions abroad, including low GDP growth in the euro area, a significant slowdown of economic activity in Russia and recession in Ukraine.

**Figure 13** Contribution to gross value added growth in 2004-2014 (annual data)




Source: GUS data, NBP calculations.

**Figure 14** Contribution to gross value added growth in 2010-2014 (quarterly data)




Source: GUS data, NBP calculations.

Gross value added growth increased from 1.8% y/y in 2013 to 3.2% y/y in 2014. It was supported by faster growth in value added in all sectors, especially in the industry.

[12] In 2014 Q1, one-off factors also contributed to an acceleration in growth of gross fixed capital formation, such as the temporary restoration of the possibility to deduct full VAT on the purchase of cars with truck certification and favourable weather conditions.

**Table 2** GDP and domestic demand in 2008-2014

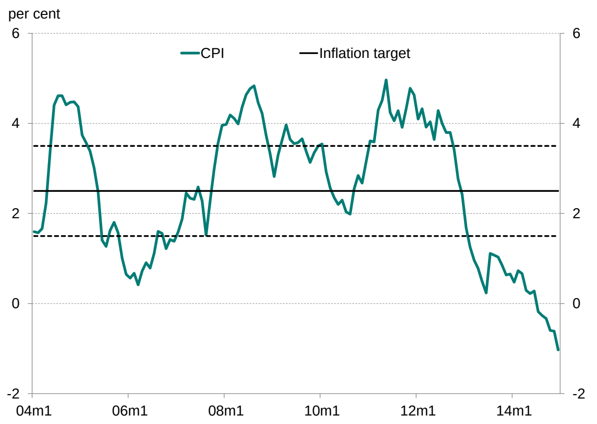
| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2014 | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | GDP annual growth and its components at constant prices (%) | | | | | | | | | | |
| | | | | | | | | Q1 | Q2 | Q3 | Q4 |
| **GDP** | 3.9 | 2.6 | 3.7 | 4.8 | 1.8 | 1.7 | 3.4 | 3.5 | 3.6 | 3.3 | 3.3 |
| **Domestic demand** | 5.0 | -0.3 | 4.2 | 3.8 | -0.4 | 0.4 | 4.9 | 3.6 | 6.1 | 5.1 | 5.0 |
| **Consumption** | 5.9 | 3.5 | 2.8 | 1.7 | 0.7 | 1.4 | 3.4 | 2.5 | 3.7 | 3.6 | 3.8 |
| **Private consumption** | 6.1 | 3.3 | 2.5 | 3.0 | 1.0 | 1.2 | 3.1 | 3.0 | 3.0 | 3.2 | 3.0 |
| **Capital formation** | 2.2 | -12.7 | 9.7 | 12.2 | -4.3 | -3.5 | 11.4 | 10.9 | 18.1 | 11.4 | 8.0 |
| **Gross fixed capital formation** | 8.3 | -1.9 | -0.4 | 9.3 | -1.5 | 1.1 | 9.2 | 11.4 | 8.7 | 9.2 | 8.6 |
| **Exports** | 7.0 | -6.3 | 12.9 | 7.9 | 4.3 | 4.8 | 5.7 | 7.6 | 6.0 | 3.6 | 5.6 |
| **Imports** | 9.4 | -12.4 | 14.0 | 5.5 | -0.6 | 1.8 | 9.1 | 8.0 | 11.7 | 7.4 | 9.5 |
| **Contribution of net exports to GDP growth (percentage points)** | -1.2 | 2.9 | -0.5 | 0.9 | 2.1 | 1.3 | -1.4 | 0.0 | -2.3 | -1.6 | -1.5 |
| | Structure of GDP at current prices (%) | | | | | | | | | | |
| **GDP** | 100, 0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | - | | | |
| **Domestic demand** | 104.9 | 100.8 | 101.8 | 101.8 | 100.2 | 98.1 | 98.5 | - | | | |
| **Consumption** | 80.6 | 80.5 | 80.8 | 79.5 | 79.6 | 79.0 | 78.3 | - | | | |
| **Private consumption** | 61.1 | 60.8 | 60.6 | 60.5 | 60.6 | 60.0 | 59.2 | - | | | |
| **Capital formation** | 24.3 | 20.2 | 21.0 | 22.2 | 20.6 | 19.1 | 20.2 | - | | | |
| **Gross fixed capital formation** | 22.6 | 21.1 | 19.8 | 20.3 | 19.4 | 18.8 | 19.5 | - | | | |
| **Exports** | 38.3 | 37.6 | 40.5 | 43.1 | 45.1 | 46.1 | 46.9 | - | | | |
| **Imports** | 43.2 | 38.3 | 42.3 | 44.9 | 45.3 | 44.2 | 45.4 | - | | | |
| **Net exports** | -4.9 | -0.8 | -1.8 | -1.8 | -0.2 | 1.9 | 1.5 | - | | | |

Source: GUS data, NBP calculations.

# Appendix 3. Consumer prices

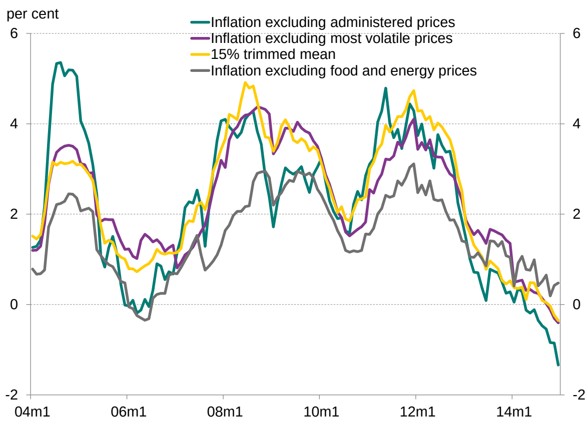
In 2014, the average annual growth rate of consumer prices index (CPI) was 0.0%, below the NBP inflation target of 2.5% +/- 1 percentage point (Figure 15, Figure 16). Price growth was weaker than in 2013 and significantly lower than forecasted. The decrease in inflation in 2014 – including its decline below zero in the second half of the year – was driven mainly by external factors, especially a fall in commodity prices in global markets. The price growth was also undermined by low inflation in the environment of the Polish economy and still limited domestic demand pressure (Figure 16).

**Figure 15** Annual CPI and the inflation target in 2004-2014




Source: GUS data.

**Figure 16** Core inflation indicesin 2004-2014 (y/y)




Source: GUS data, NBP calculations.

The major factor behind the decreasing price growth in 2014 was a fall in food prices driven by a large supply of main agricultural products associated with favourable agrometeorological conditions in Poland and abroad as well as trade restrictions imposed by Russia in January and August 2014. The decrease in inflation was also significantly supported by the ongoing decline in energy prices due to falling electricity and fuel prices related to a decrease in commodity prices, including the strong drop in crude oil prices. Inflation was also contained by the decline in prices for goods as well as the slowdown in prices for services amid low inflation abroad and moderate economic growth in Poland. Lower growth in consumer prices was also fostered by the deepening fall in producer prices, associated with the decrease in commodity prices. In turn, the scale of inflation decline was contained by significant reduction in the NBP interest rates in the previous years. The decrease in CPI inflation was additionally reduced by an increase in excise duty on tobacco products and spirits introduced in 2014 as well as growth of some administered prices (resulting from a rise in tariffs for natural gas and heat). In the second half of the year, the impact of the fall in global commodity prices on the CPI inflation was mitigated by a significant weakening of the zloty against the dollar.

The consumer price index reflects price developments in four main categories (i.e. food and non-alcoholic beverages, energy, goods and services; Figure 17, Figure 18). Specifically, in 2014 the price developments in individual categories were as follows:[13]

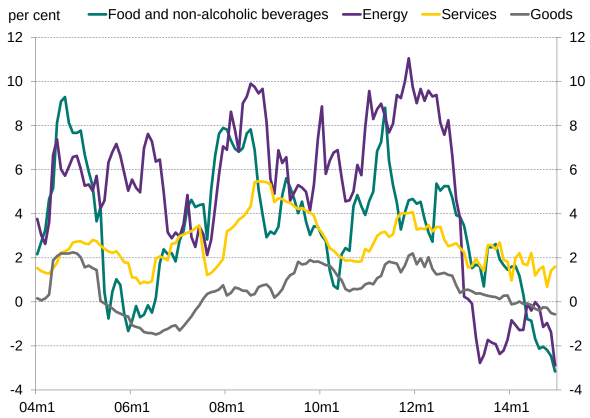
- Prices of **food and non-alcoholic beverages** decreased by 0.9% y/y, and their contribution to the change in the average annual CPI index reached -0.2 percentage points. The decline in prices in this category was driven mainly by:
  - a decrease in sugar prices (associated with a decline in sugar prices in the global markets and the large supply of domestic sugar);
  - a decline in fruit and vegetable prices (associated with high harvest in Poland and abroad, arising from favourable agrometeorological conditions and the Russian embargo imposed in August 2014 on the imports of agricultural and food products from the EU countries, including Poland);
  - falling meat prices (associated with the Russian embargo on imports of pork from Poland imposed at the end of January 2014).

- Prices of **energy** decreased by 1.0% y/y, and their contribution to the change in the average annual CPI index reached -0.2 percentage points. The following factors contributed to the decline in energy prices:
  - a fall in fuel prices, particularly strong in the second half of the year (associated with the drop in crude oil prices in the global commodity markets);
  - a decline in electricity prices (related to the reduction in tariffs as of January 2014 in response to falling energy commodity prices in the previous years);
  - a minor reduction in heating fuel prices in the second half of the year (associated with the slump in coal prices in the global markets accompanied by the low demand for heating fuel amidst mild winter).

- Prices of **goods** decreased by 0.2% y/y, contributing to the decline in the average annual CPI index by 0.1 percentage points. The decline in commodity prices was mainly due to the fall in clothing and footwear prices[14] persisting since 2002.[15]
- Prices of **services** increased by 1.6% y/y, adding to the change in the average annual CPI inflation 0.4 percentage points. The rise in those prices encompassed the majority of main categories of services and took place against continued moderate economic growth, accompanied by rising employment and wages.[16]

[13] The categories are listed in the order corresponding to their contribution to the changes in the overall CPI index in 2014, from categories with the highest negative contribution to categories with the highest positive contribution.
[14] The fall in the prices of goods was also caused – albeit to a lesser extent – by a decrease in prices of medical and pharmaceutical products (arising mostly from the OTC drug price promotions, as well as changes in the list of reimbursed drugs) as well as a decline in prices of vehicles, spare parts and accessories for vehicles.
[15] The growth in prices in the clothing and footwear category has been negative since January 2002, excluding May and June 2011.
[16] In 2014, prices of services associated with home maintenance, prices of recreation and culture services, services at restaurants and hotels, medical services and prices of telecommunication services increased.

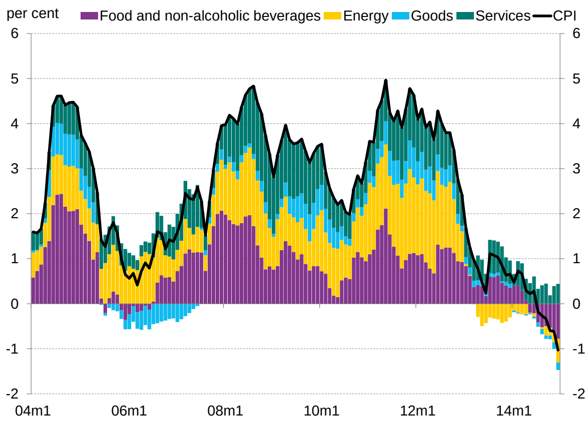
**Figure 17** Annual growth in the prices of food, non-alcoholic beverages, energy, goods and services in 2004-2014




Source: GUS data, NBP calculations.

*The category of energy includes energy carriers (electricity, gas, heating fuel) and engine fuels (for private means of transport); the category of goods is exclusive of food, non-alcoholic beverages and energy.

**Figure 18** Annual growth in the prices of consumer goods and services and the contributions of main price categories to CPI in 2004-2014




Source: GUS data, NBP calculations.

**Table 3** Annual growth in consumer goods and services prices and the contribution of the main price categories to CPI

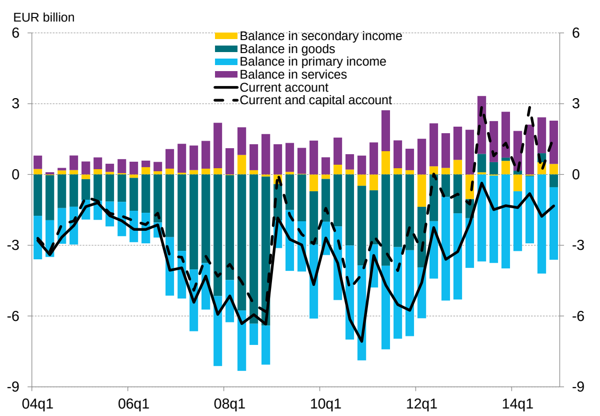
| | Weights 2014, % | Change (y/y, %) 2014 I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII | yearly average |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **CPI** | 100.0 | 0.5 | 0.7 | 0.7 | 0.3 | 0.2 | 0.3 | -0.2 | -0.3 | -0.3 | -0.6 | -0.6 | -1.0 | **0.0** |
| **Core inflation** | 57.1 | 0.4 | 0.9 | 1.1 | 0.8 | 0.8 | 1.0 | 0.4 | 0.5 | 0.7 | 0.2 | 0.4 | 0.5 | **0.6** |
| **Goods** | 29.5 | -0.1 | -0.1 | 0.0 | -0.1 | -0.1 | -0.1 | -0.3 | -0.4 | -0.2 | -0.3 | -0.5 | -0.6 | **-0.2** |
| **Services** | 27.6 | 1.0 | 2.0 | 2.2 | 1.7 | 1.7 | 2.2 | 1.2 | 1.5 | 1.6 | 0.7 | 1.4 | 1.6 | **1.6** |
| **Food and non-alcoholic beverages** | 24.6 | 1.6 | 1.6 | 1.2 | 0.3 | -0.8 | -0.9 | -1.7 | -2.1 | -2.0 | -2.2 | -2.5 | -3.2 | **-0.9** |
| Meat | 6.5 | 0.5 | 0.8 | -0.5 | -0.6 | -0.2 | -0.3 | -0.7 | -1.1 | -2.8 | -2.8 | -2.8 | -2.9 | **-1.1** |
| Vegetables | 2.4 | 11.3 | 10.6 | 6.3 | 2.3 | -8.6 | -4.4 | -9.9 | -12.8 | -8.4 | -9.6 | -9.0 | -13.2 | **-3.8** |
| Fruit | 1.3 | -0.3 | 0.1 | 5.6 | 3.4 | -0.8 | -7.8 | -9.4 | -10.2 | -4.2 | -1.3 | -3.2 | -3.5 | **-2.6** |
| **Processed** | 13.6 | 0.6 | 0.6 | 0.7 | 0.1 | 0.4 | 0.2 | 0.0 | -0.2 | -0.6 | -0.8 | -1.2 | -1.5 | **-0.1** |
| **Unprocessed** | 11.0 | 2.8 | 2.9 | 1.8 | 0.6 | -2.2 | -2.2 | -3.7 | -4.5 | -3.9 | -3.9 | -4.0 | -5.2 | **-1.8** |
| **Energy** | 18.2 | -0.8 | -1.1 | -1.3 | -1.3 | -0.1 | -0.4 | 0.0 | -0.2 | -1.1 | -1.0 | -1.4 | -2.9 | **-1.0** |
| **Energy carriers** | 12.8 | -0.2 | -0.2 | -0.2 | -0.2 | -0.3 | 0.4 | 0.5 | 0.4 | 0.4 | 0.4 | 0.2 | 0.1 | **0.1** |
| **Fuels** | 5.4 | -2.3 | -3.1 | -3.8 | -3.8 | 0.4 | -0.6 | -1.0 | -1.9 | -4.7 | -4.1 | -5.3 | -10.2 | **-3.4** |
| | | | | | | | according to 12 COICOP groups | | | | | | | |
| **Food and non-alcoholic beverages** | 24.6 | 1.6 | 1.6 | 1.2 | 0.3 | -0.8 | -0.9 | -1.7 | -2.1 | -2.0 | -2.2 | -2.5 | -3.2 | **-0.9** |
| **Alcohol and tobacco** | 6.6 | 3.4 | 3.6 | 3.7 | 3.9 | 3.9 | 4.0 | 4.0 | 3.8 | 3.6 | 3.6 | 3.6 | 3.5 | 3.7 |
| **Clothing and footwear** | 5.0 | -5.0 | -4.7 | -4.3 | -4.4 | -4.6 | -4.7 | -4.9 | -5.1 | -4.7 | -4.6 | -4.6 | -5.0 | **4.7** |
| **Home maintenance and energy** | 21.7 | 2.3 | 2.3 | 2.2 | 2.1 | 2 | 1.9 | 0.7 | 0.7 | 0.7 | 0.6 | 0.6 | 0.5 | **2.4** |
| **Home equipment** | 4.6 | 0.3 | 0.0 | -0.1 | -0.3 | -0.1 | -0.1 | -0.1 | -0.2 | -0.2 | 0.0 | -0.2 | -0.2 | **-0.1** |
| **Health** | 5.2 | 0.4 | 0.3 | 0.3 | 0.2 | 0.3 | 0.3 | 0.0 | 0.0 | 0.7 | 0.7 | -0.7 | -0.6 | **0.2** |
| **Transportation** | 9.2 | -1.5 | -1.8 | -2.7 | -2.1 | -0.1 | -0.6 | -1.0 | -1.5 | -3.2 | -3.0 | -3.7 | -6.5 | **-2.3** |
| **Telecommunications** | 5.4 | -7.8 | -3.2 | -0.3 | -1.7 | -1.1 | 1.3 | 2.6 | 3.9 | 4.0 | -0.4 | 3.0 | 3.0 | **0.3** |
| **Recreation and culture** | 6.4 | 3.0 | 2.8 | 1.9 | 0.3 | 0.3 | 0.7 | 0.7 | 0.9 | 0.0 | 0.1 | 0.6 | 1.3 | **1.1** |
| **Education** | 1.2 | -6.2 | -6.2 | -6.3 | -6.3 | -6.3 | -6.0 | -6.0 | -6.0 | 1.2 | 1.3 | 1.3 | 1.3 | **-3.7** |
| **Restaurants and hotels** | 4.6 | 1.5 | 1.5 | 1.6 | 1.6 | 1.5 | 1.4 | 1.3 | 1.3 | 1.4 | 1.3 | 1.3 | 1.3 | **1.4** |
| **Other goods and services** | 5.5 | -0.1 | -0.1 | -0.1 | -0.2 | 0.0 | -0.2 | -0.2 | -0.2 | -0.2 | -0.5 | -0.5 | -0.4 | **-0.2** |
| | **Weights 2014, %** | **Contribution to CPI (in p.p.) 2014 I** | **II** | **III** | **IV** | **V** | **VI** | **VII** | **VIII** | **IX** | **X** | **XI** | **XII** | **yearly average** |
| **CPI** | 100.0 | 0.5 | 0.7 | 0.7 | 0.3 | 0.2 | 0.3 | -0.2 | -0.3 | -0.3 | -0.6 | -0.6 | -1.0 | **0.0** |
| **Core inflation** | 57.1 | 0.2 | 0.5 | 0.6 | 0.4 | 0.4 | 0.6 | 0.2 | 0.3 | 0.4 | 0.1 | 0.2 | 0.3 | **0.4** |
| **Goods** | 29.5 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | -0.1 | -0.1 | -0.1 | -0.1 | -0.2 | -0.2 | **-0.1** |
| **Services** | 27.6 | 0.3 | 0.5 | 0.6 | 0.5 | 0.5 | 0.6 | 0.3 | 0.4 | 0.4 | 0.2 | 0.4 | 0.4 | **0.4** |
| **Food and non-alcoholic beverages** | 24.6 | 0.4 | 0.4 | 0.3 | 0.1 | -0.2 | -0.2 | -0.4 | -0.5 | -0.5 | -0.5 | -0.6 | -0.8 | **-0.2** |
| Meat | 6.5 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | -0.1 | -0.2 | -0.2 | -0.2 | -0.2 | **-0.1** |
| Vegetables | 2.4 | 0.3 | 0.3 | 0.2 | 0.1 | -0.2 | -0.1 | -0.2 | -0.3 | -0.2 | -0.2 | -0.2 | -0.3 | **-0.1** |
| Fruit | 1.3 | 0.0 | 0.0 | 0.1 | 0.0 | 0.0 | -0.1 | -0.1 | -0.1 | -0.1 | 0.0 | 0.0 | 0.0 | **0.0** |
| **Processed** | 13.6 | 0.1 | 0.1 | 0.1 | 0.0 | 0.1 | 0.0 | 0.0 | 0.0 | -0.1 | -0.1 | -0.2 | -0.2 | **0.0** |
| **Unprocessed** | 11.0 | 0.3 | 0.3 | 0.2 | 0.1 | -0.3 | -0.2 | -0.4 | -0.5 | -0.4 | -0.4 | -0.4 | -0.6 | **-0.2** |
| **Energy** | 18.2 | -0.2 | -0.2 | -0.2 | -0.2 | 0.0 | -0.1 | 0.0 | 0.0 | -0.2 | -0.2 | -0.3 | -0.5 | **-0.2** |
| **Energy carriers** | 12.8 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 | **0.0** |
| **Fuels** | 5.4 | -0.1 | -0.2 | -0.2 | -0.2 | 0.0 | 0.0 | -0.1 | -0.1 | -0.3 | -0.2 | -0.3 | -0.5 | **-0.2** |
| | | | | | | | according to 12 COICOP groups | | | | | | | |
| **Food and non-alcoholic beverages** | 24.6 | 0.4 | 0.4 | 0.3 | 0.1 | -0.2 | -0.2 | -0.4 | -0.5 | -0.5 | -0.5 | -0.6 | -0.8 | **-0.2** |
| **Alcohol and tobacco** | 6.6 | 0.2 | 0.2 | 0.2 | 0.3 | 0.3 | 0.3 | 0.3 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | **0.2** |
| **Clothing and footwear** | 5.0 | -0.3 | -0.2 | -0.2 | -0.2 | -0.2 | -0.2 | -0.2 | -0.3 | -0.2 | -0.2 | -0.2 | -0.3 | **-0.3** |
| **Home maintenance and energy** | 21.7 | 0.5 | 0.5 | 0.5 | 0.5 | 0.4 | 0.4 | 0.2 | 0.2 | 0.2 | 0.1 | 0.1 | 0.1 | **0.3** |
| **Home equipment** | 4.6 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | **0.0** |
| **Health** | 5.2 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | **0.0** |
| **Transportation** | 9.2 | -0.1 | -0.2 | -0.2 | -0.2 | 0.0 | -0.1 | -0.1 | -0.1 | -0.3 | -0.3 | -0.3 | -0.6 | **-0.2** |
| **Telecommunications** | 5.4 | -0.4 | -0.2 | 0.0 | -0.1 | -0.1 | 0.1 | 0.1 | 0.2 | 0.2 | 0.0 | 0.2 | 0.2 | **0.0** |
| **Recreation and culture** | 6.4 | 0.2 | 0.2 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | 0.0 | 0.0 | 0.0 | 0.1 | **0.1** |
| **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 | **0.0** |
| **Restaurants and hotels** | 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 | **0.1** |
| **Other goods and services** | 5.5 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | **0.0** |

Source: NBP calculations based on GUS data.

# Appendix 4. Balance of payments

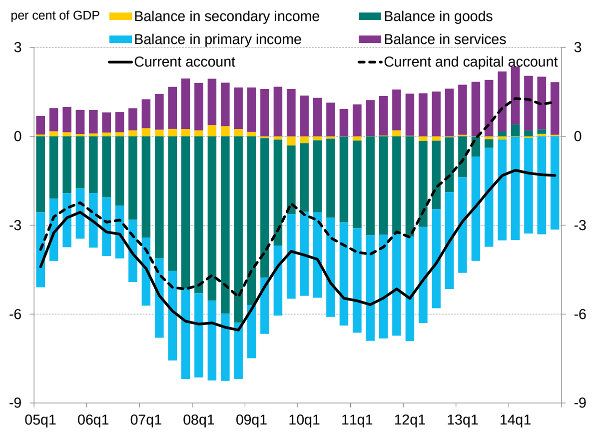
In 2014, the current account deficit remained relatively low, amounting to 1.4% of GDP (against the deficit of 1.3% of GDP in 2013, Figure 19, Figure 20). This was mainly the result of low – as compared to the long-term average – deficit of trade in goods and high surplus on the service account (the total external trade balance remained positive). Like in the previous year, the persistently negative current account balance was determined by the income of foreign direct and portfolio investors, as reflected in the primary income deficit.[17]

**Figure 19** Current account balance (EUR billion) in 2004-2014




Source: NBP data.

**Figure 20** Current and capital account balance to GDP (4 quarters rolling window) in 2004-2014




Source: NBP and GUS data.

In 2014, trade in goods saw a minor deficit, which was related to accelerating import growth amidst rising domestic demand. Import growth was constrained by the decline in import prices, partly driven by the drop in commodity prices. Growth in exports remained moderate, which was associated with a marked deterioration of economic conditions in Russia and recession in Ukraine.

The primary income deficit remained in 2014 close to2013. Like in the previous years, this was mainly related to sound financial conditions of Polish enterprises, which translated into high income of foreign direct investors.

In 2014, the capital account balance widened (to 2.5% of GDP against 2.3% in 2013), which was driven by a higher inflow of the European Union funds allocated for infrastructural investments. Consequently, the ratio of the combined current and capital account balances to GDP remained positive, reaching the highest level on record.

[17] Since 30 September 2014, NBP has been publishing the data on the balance of payments and the international investment position, aggregated on the basis of guidelines contained in the balance of payments manual (BPM6). More information concerning the new data presentation method can be found on the NBP website: http://www.nbp.pl/home.aspx?f=/aktualnosci/wiadomosci_2014/info-ds.html.

**Table 4** Main items on the balance of payments (EUR million) in 2004-2014[18]

| Balance of payments | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Current account** | -11 017 | -6 276 | -10 857 | -19 616 | -23 760 | -12 244 | -20 263 | -19 398 | -13 697 | -5 148 | -5 762 |
| **Balance of trade in goods** | -6 451 | -4 304 | -7 709 | -16 168 | -22 850 | -7 302 | -10 396 | -12 451 | -7 146 | 635 | -1 629 |
| **Balance of services** | 1 388 | 1 998 | 2 046 | 5 368 | 5 097 | 5 040 | 3 324 | 5 186 | 6 209 | 7 910 | 9 063 |
| **Balance of primary income** | -6 515 | -4 155 | -5 754 | -9 583 | -6 898 | -9 005 | -13 146 | -12 891 | -12 635 | -13 266 | -12 812 |
| **Balance of secondary income** | 561 | 185 | 551 | 767 | 891 | -977 | -45 | 758 | -125 | -427 | -384 |
| **Capital account** | 955 | 786 | 1 666 | 3 418 | 4 067 | 5 080 | 6 446 | 7 254 | 8 549 | 9 006 | 10 036 |
| **Financial account** | -5 919 | -5 700 | -8 496 | -18 239 | -28 402 | -14 089 | -22 610 | -19 686 | -8 746 | -5 292 | -2 618 |
| **Direct investment: assets** | 1 711 | 3 394 | 8 444 | 5 411 | 2 958 | 4 369 | 7 051 | 3 412 | 1 055 | -2 502 | 3 940 |
| **Direct investment: liabilities** | 11 170 | 8 930 | 17 021 | 18 253 | 9 718 | 10 110 | 13 356 | 13 274 | 5 634 | 70 | 10 479 |
| **Portfolio investment: assets** | 1 053 | 2 006 | 3 682 | 4 604 | -1 700 | 1 035 | 616 | -610 | 340 | 1 650 | 4 100 |
| **Portfolio investment: liabilities** | 8 487 | 11 797 | 1 484 | -23 | -3 656 | 11 302 | 21 885 | 11 730 | 15 635 | 1 688 | 2 881 |
| **Other investment: assets** | 9 629 | 2 179 | 3 194 | 1 324 | -4 080 | -3 859 | 2 281 | 2 716 | 1 716 | 262 | 1 737 |
| **Other investment: liabilities** | -813 | -1 129 | 7 890 | 22 182 | 17 835 | 5 936 | 9 634 | 5 014 | -2 812 | 3 146 | -493 |
| **Derivative financial instruments** | -154 | -138 | 549 | 1 456 | 744 | 1 301 | 821 | 119 | -2 133 | -552 | 16 |
| **Official reserve assets** | 686 | 6 457 | 2 030 | 9 378 | -2 427 | 10 413 | 11 496 | 4 695 | 8 733 | 754 | 456 |
| **Balance of errors and omissions** | 4 143 | -210 | 695 | -2 041 | -8 709 | -6 925 | -8 793 | -7 542 | -3 598 | -9 150 | -6 892 |

Source: NBP data.

The net foreign capital continued to inflow to Poland in 2004, although its scale was smaller than in 2013, which was reflected in the reduced financial account deficit. On the one hand, inflow of foreign capital to Poland increased, mainly in the form of direct investments, with the highest share of re-invested profits. On the other hand, however, the outflow of capital from Poland also rose due to a significant growth of Polish direct investment abroad, mainly in the form of shares and share-related investment. Similarly, the outflow of the Polish portfolio capital abroad strengthened, albeit to a lesser extent than in 2013, which was driven by a rise in investment and pension funds' allocations in foreign assets.

In 2014, some indicators of Poland's external imbalance improved compared to 2013 (Table ). In particular, the ratios of both foreign debt and net international investment position to GDP decreased.

[18] With regard to the financial account, the presented figures should be interpreted as follows: positive (negative) value of residents' investment abroad (items: direct investment: assets, portfolio investment: assets, other investment: assets, official reserve assets) denotes an increase (decrease) in Polish assets abroad. Conversely, positive (negative) value of non-residents' investment in Poland (items: direct investment: liabilities, portfolio investment: liabilities, other investment: liabilities) means an increase (decrease) in Polish liabilities against non-residents.

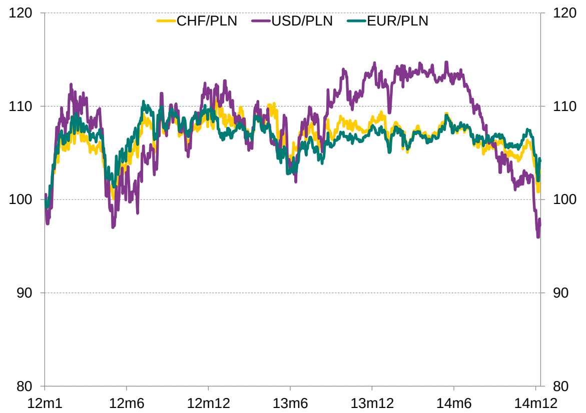
**Table 5** Selected external stability indicators in 2004-2014

| | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Current account balance/GDP (%)** | -5.4 | -2.6 | -4.0 | -6.2 | -6.5 | -3.9 | -5.6 | -5.2 | -3.6 | -1.3 | -1.4 |
| **Current and capital account balance/GDP (%)** | -4.9 | -2.2 | -3.4 | -5.2 | -5.4 | -2.3 | -3.8 | -3.3 | -1.3 | 1.0 | 1.0 |
| **Balance of trade in goods /GDP (%)** | -3.1 | -1.8 | -2.8 | -5.1 | -6.3 | -2.3 | -2.9 | -3.4 | -1.9 | 0.2 | -0.4 |
| **Balance of trade in goods and services/GDP (%)** | -2.5 | -0.9 | -2.1 | -3.4 | -4.9 | -0.7 | -2.0 | -2.0 | -0.2 | 2.2 | 1.8 |
| **Official reserve assets in terms of monthly imports of goods and services** | 4.3 | 4.9 | 4.0 | 4.1 | 3.4 | 5.5 | 5.5 | 5.4 | 5.7 | 5.3 | 5.3 |
| **Foreign debt/GDP (%)** | 46.4 | 45.9 | 47.2 | 50.5 | 47.9 | 61.7 | 66.2 | 67.5 | 72.8 | 71.3 | 70.8 |
| **Net international investment position/GDP (%)** | -45.4 | -43.9 | -46.0 | -52.1 | -47.3 | -60.9 | -65.8 | -59.5 | -67.7 | -70.1 | -66.7 |

Source: NBP calculations based on GUS and NBP data.

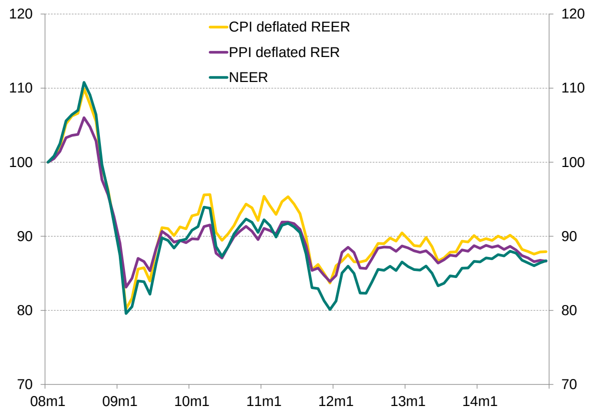
Low current account deficit and a decrease in foreign debt in 2014 favoured the relative stabilisation of the zloty exchange rate. In the first half of 2014, gradual appreciation of the effective zloty exchange rate continued, whereas in the second half of 2014 the zloty slightly depreciated, yet remaining somewhat stronger than in 2013 (Figure 21, Figure 22). The nominal zloty exchange rate was also driven by external factors – divergence in monetary policies of major central banks and changes in risk perception in the financial markets. In the second half of 2014, the zloty – similarly to the euro and other currencies of emerging market economies – depreciated against the dollar, due to the conclusion of financial asset purchases by the Federal Reserve and the expected beginning of interest rate increases in the United States in 2015. At the end of 2014, depreciation of currencies of many emerging market economies was also exacerbated by an increase in risk aversion due to the conflict in the Middle East and the escalation of the Russian-Ukrainian crisis, as well as by concerns about the impact of a fall in crude oil prices on economic outlook of its exporters.

**Figure 21** Nominal effective zloty exchange rate against major currencies in 2008-2014




Source: Bloomberg data.
Increase denotes appreciation.

**Figure 22** Real and nominal effective exchange rate in 2008-2014



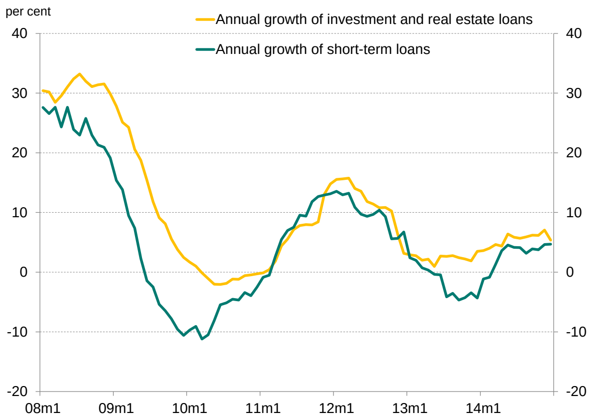

Source: Eurostat, OECD, Reuters data, NBP calculations.
Increase denotes appreciation.

# Appendix 5. Money and credit

In 2014, the growth in lending accelerated slightly against 2013, but remained moderate. The annual growth in debt of non-monetary financial entities in 2014 amounted to 6.3%, compared to 4.0% in the previous year.[19,20] Acceleration in lending in 2014 occurred amidst stronger economic growth than in the previous year, with investment demand rising at a relatively fast pace, which was accompanied by easing of lending conditions in the majority of credit market segments as well as a decrease in interest rates on loans.

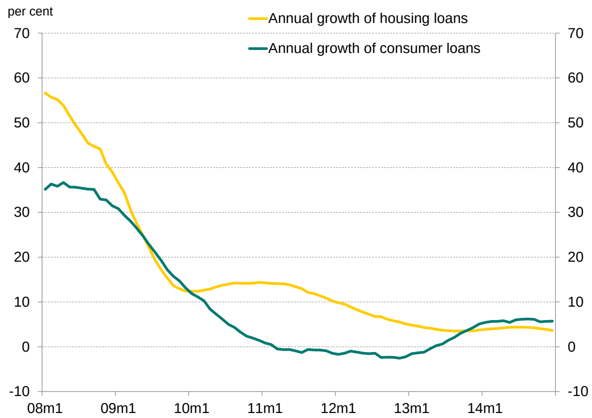
In 2014, lending to the corporate sector accelerated – gradually in case of investment loans and significantly in case of current loans (Figure 23)[21]. The corporate lending was supported by significant easing of credit standards, especially in the case of current loans, and lower interest rates on loans as compared to the previous year[22]. The growth in the corporate lending was also underpinned by the strong rise in investment demand of enterprises.

**Figure 23** Growth rate of investment and current loans to enterprises in 2008-2014




Source: NBP data.

**Figure 24** Growth rate of consumer and housing loans to households 2008-2014




Source: NBP data.

In the case of household loans, the stable growth in lending continued in 2014 as regards to both housing and consumer loans (Figure 24).[23]

Growth in consumer loans was driven by continued significant easing of lending criteria as well as a decline in interest rates on these loans, due to a reduction of margins by banks and decreases in the

[19] Growth rates in this chapter refer to transactional changes. Debt of non-monetary entities comprises debt of households, non-monetary financial institutions, enterprises, non-profit institutions for households, local government units and social insurance funds.

[20] The presented growth rates are annual growth rates for the private sector loans as of December 2013 and December 2014.

[21] The average monthly growth in current corporate loans in 2014 amounted to 3% y/y, against the average monthly decline by 1.64% in 2013, whereas for investment loans it reached 5.4% y/y against 2.4%.

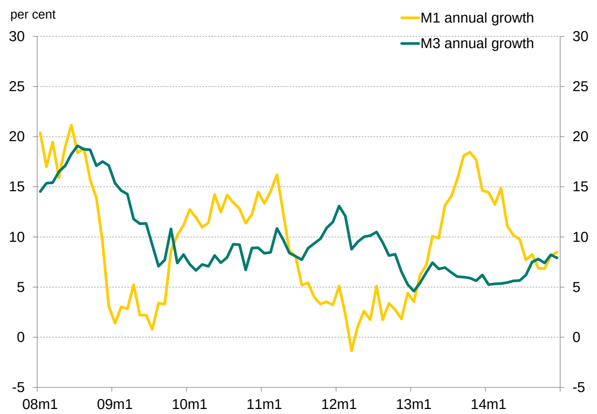
[22] The interest rates on corporate loans were lower by 0.9 percentage points in December 2014 than in December 2013.

[23] The average monthly growth of consumer loans in 2014 reached 5.8% y/y against 1.3% in the previous year, whereas for housing loans it amounted to 4.1% y/y against 3.9%.

NBP interest rates, including the strong reduction of lombard rate in October 2014[24]. In turn, the relatively weaker growth in loan demand, as declared by banks, could constrain the growth in consumer loans[25].

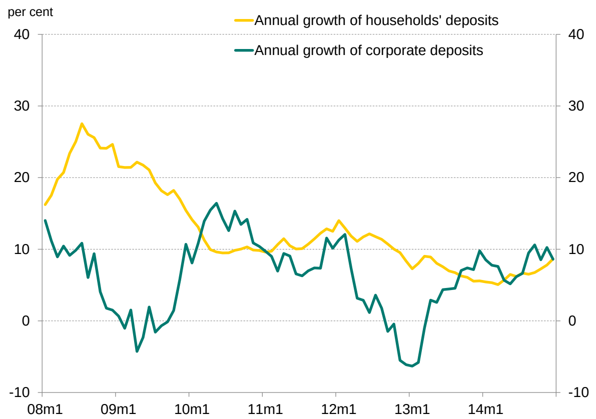
As regards housing loans, the growth in lending was supported by the favourable labour market conditions and lower interest rates on loans compared to the previous year. Alongside that, however, the tightening of both lending criteria and lending terms by banks (due to the amendment to the "Recommendation S" on increased borrower's own contribution while raising housing loan), was dragging down the growth in housing loans.

**Figure 25** M1 and M3 growth in 2008-2014




Source: NBP data.

**Figure 26** Growth in household and corporate deposits included in M3 in 2008-2014




Source: NBP data.

In 2014, the growth of M3 broad money accelerated, especially in the second half of the year, mainly due to weaker growth of household deposits (Figure 25)[26]. The corporate deposits growth in 2014 stabilised at a moderate level, which was associated with sound financial position of enterprises. In turn, the household deposit growth accelerated, supported by the improving labour market conditions (Figure 26). In the second half of the year, the household deposit growth was accompanied by a slowdown in the growth of households' more risky assets, which could relate to the increased price volatility in the financial markets.

The growth of M1 aggregate decreased in 2014 (Figure 25)[27], which resulted mainly from the change in term structure of deposits of enterprises and households in the first half of the year – a slower growth rate of current deposits and a stronger growth rate of term deposits.

[24] The reduction in banks' margins resulted in interest rate cuts on consumer loans to households from 13.6% in June to 12.5% in September 2014. The interest rates on consumer loans may not exceed the four-fold value of the NBP lombard rate.

[25] *Senior loan officer opinion survey on bank lending practices and credit conditions, 2014 Q2*, NBP.

[26] In transactional terms, M3 growth reached 7.9% (December 2014 on December 2013).

[27] The average monthly growth of M1 aggregate amounted to 10% y/y against 12.4% y/y in 2013.

# Appendix 6. Minutes of the Monetary Policy Council decision-making meetings

**Minutes of the Monetary Policy Council decision-making meeting held on 8 January 2014**

At its meeting, members of the Monetary Policy Council discussed the current and future monetary policy decisions in the context of macroeconomic developments in Poland and abroad.

While discussing the economic activity abroad, it was pointed out that the global economic conditions were gradually improving. Council members emphasized that the scale of this improvement remained diversified, but the magnitude of this diversification was different than in previous years. There have been signs that economy is recovering in developed countries. Meanwhile, economic growth in emerging market economies is low as for these countries.

In the United States, a marked acceleration in economic growth and declining unemployment rate (partly due to a decrease in the number of economically active persons) have prompted the Federal Reserve to start reducing the scale of quantitative easing. At the same time, the Federal Reserve extended the suggested horizon for keeping interest rates near zero. In the euro area, in turn, the sentiment of economic agents has improved. This improvement has so far not been coupled with a marked acceleration in economic growth. As no demand pressure is expected in the euro area, the European Central Bank has maintained its commitment to keep the interest rates at present or lower level. In this context, some Council members highlighted that the European banking sector was still in a difficult position. They indicated that by dampening lending growth in the euro area it contained GDP growth in the region. However, it was emphasized that economic conditions in Germany - Poland's main trading partner - remained sound compared to the rest of the euro area. At this point, it was highlighted that economic conditions in other countries of Central and Eastern Europe, which also have close links with the German economy, continued to improve. Nevertheless, it was noted that forecasts for Germany did not explicitly indicate that economic growth was recovering at a significant pace.

While discussing the situation in the environment of the Polish economy, it was also noted that global inflation was low. Low inflation is supported by moderate global economic activity and stabilisation of global commodity prices, especially for energy, underpinned by structural changes in the oil and natural gas markets. A few Council members assessed that in the coming years commodity prices could stabilize or fall.

When discussing developments in the financial markets, some Council members pointed out that the Federal Reserve's decision to reduce the scale of quantitative easing in the United States contributed to a slight increase in the volatility of asset prices in a number of emerging market economies. These members also pointed out that the prices of Polish assets had remained stable, which might indicate that fundamentals of the Polish economy are perceived positively by the markets.

Referring to domestic economic activity, a few Council members assessed that the recovery in the following quarters would be substantial and might close the output gap relatively fast. Some Council members indicated that retail sales and industrial output growth (adjusted for seasonal and calendar factors) had accelerated, while the decline in construction and assembly output had narrowed. Council members also pointed out that fiscal policy would be an important factor influencing the pace of GDP growth in 2014 and the subsequent years. A few Council members were of the opinion that there was a risk of some relaxation in the public sector wage discipline in the coming years. Other Council members argued that an acceleration in growth of government expenditure was rather unlikely in the following years due to ongoing Excessive Deficit Procedure for Poland. It was in particular highlighted that there was a risk of a decrease in EU fund inflows should measures to reduce the public sector imbalance came to a halt.

While discussing the likely structure of GDP growth in Poland in the following quarters, a few Council members emphasised that while Polish exports were supported by the high price competitiveness of Polish businesses to a great extent, the contribution of net exports to GDP growth might be expected to decrease due to an acceleration in consumer demand growth and an increase in gross fixed capital formation.

In particular, some Council members pointed out that the NBP surveys indicated an improvement in forecasts of corporate performance, including higher propensity to invest of businesses, which may be a sign of revival in domestic demand. Yet, other Council members indicated that growth in investment lending was still slow.

While assessing credit market conditions, Council members noted that the corporate lending was still low. This, however, is accompanied by accelerating consumer lending growth and a sustained increase in mortgage lending for households. In their discussion on the banking sector conditions, a few Council members indicated that the pace of household deposit growth continued to decelerate.

While discussing economic growth, Council members were also referring to long-term challenges relating to structural and regional policy and to the competitiveness of Polish enterprises. In this context, a few Council members highlighted that an increase in the EU funds share in co-financing research and development projects might be favourable for the Polish economy.

When discussing current labour market conditions, Council members pointed out that the unemployment rate was still elevated, which hampered wage growth and decreased the chance of a significant recovery in consumption. According to a few Council members, the economic recovery was still not robust enough to bring about a significant employment growth. However, a few Council members assessed that – as business climate continued to improve – demand for labour was likely to grow at a stronger pace, which was also reflected in NBP surveys. However, these surveys do not indicate a risk of a marked acceleration in corporate wage growth. A few Council members also noted that an increase in minimum wage at the beginning of this year, and the related increase in some social benefits indexed to minimum wage, might be conducive to an increase in consumer demand. It was, however, argued that the rise in productivity, which is typical of this stage of recovery, mitigated the risk of excessive cost pressures in the labour market in the coming quarters.

With reference to price developments, Council members indicated that in November the CPI index decreased and that inflation was still markedly below the target. Other signs of weak demand and cost pressure include low core inflation and declining producer prices in industry. Council members also pointed to continuously low inflation expectations of household and corporate sectors and the inflation forecasts of financial sector analysts.

Council members emphasised that in light of available forecasts the 2014 inflation would stay below the November projection. Nonetheless, in the first two quarters of 2014 the CPI index may increase moderately due to base effects. In the opinion of some Council members, inflation would stay below the target not only because of low demand pressure, but also due to stabilisation in energy prices. Yet, other Council members pointed to the factors which, in their opinion, could be conducive to higher inflation in the near future. These involve growing demand pressure and a raise in local taxes, as well as higher prices of gas and some services related to the general government sector.

The Council decided that the NBP interest rates should remain unchanged at the current meeting. Furthermore, the Council maintained its assessment that the gradual improvement in economic conditions was likely to continue over the coming quarters, while inflation pressure would remain limited. In this context, the Council confirmed that it would be justified to maintain the interest rates at the current level at least until the end of the first half of 2014. At the same time, Council members recognized that the findings of the March NBP projection would enable a more comprehensive assessment on the horizon of keeping the interest rates at the current level.

The Council left the basic interest rates unchanged at the following levels: reference rate at 2.50%, lombard rate at 4.00%, deposit rate at 1.00%, rediscount rate at 2.75%.

**Minutes of the Monetary Policy Council decision-making meeting held on 5 February 2014**

At its meeting, members of the Monetary Policy Council discussed the current and future monetary policy decisions in the context of macroeconomic developments in Poland and abroad.

While discussing economic activity abroad, it was indicated that the global recovery is still moderate. Data on euro area point to a slowly improving economic conditions. In turn, activity growth in the United States – which is visibly stronger than in the euro area – recorded signs of weakening in comparison to previous expectations. At the same time, in China and in other emerging economies, where growth has slowed down to a low level (considering their past performance), there is persisting uncertainty about future developments in GDP. A few members of the Council also highlighted that, taking into consideration the significant scale and limited effectiveness of the stimulus provided so far to the emerging economies, there is little scope for revival of economic activity through additional actions of these countries' authorities.

While analysing the external environment of the Polish economy, the Council also discussed reaction of the financial markets to the QE tapering of the Federal Reserve and to the increased risk of Argentina suspending its debt servicing. These events have had a negative effect on the sentiment of market participants. The deterioration in investor sentiment, in particular in relation to certain emerging economies, resulted in an outflow of capital from some of these countries and a weakening of their currencies. In order to limit the scale of the depreciation, some of the central banks intervened on the currency market or raised their interest rates. Some of the Council members pointed to the fact that monetary policy tightening was conducted in economies characterised by heightened inflation and substantial external imbalances. Therefore, the increase in interest rates in these countries was supporting the restoring of their macroeconomic equilibrium – both internal and external.

In Poland the exchange rate of the zloty – i.e. the currency of a country usually included in the group of emerging markets – has weakened relatively slightly. According to the Council members, the resilience of the zloty to changes in the sentiment of the financial markets is supported by the relatively favourable economic situation in Poland, including the lack of any significant imbalances.

Referring to domestic economic growth, it was stressed that preliminary GDP data for 2013, as well as monthly data on economic activity and indicators of economic conditions point to a continued gradual recovery of growth. The Council members drew attention to the fact that the implied GDP data for 2013 Q4 confirm that net exports are still contributing substantially to GDP growth, while domestic demand remained weak (this relates in particular to investment demand). Some of the Council members argued that the current structure of GDP growth – based to a large degree on exports, with only a gradual recovery of domestic demand – supports the maintenance of low inflationary pressure and, at the same time, contributes to the Polish economy remaining balanced.

According to some members of the Council, in successive quarters – together with further improvement in growth prospects – investment activity should increase significantly. Some of the Council members argued that taking into account good financial situation of companies and low credit costs, relatively high capacity utilization should be a factor encouraging firms to invest. These Council members emphasised that favourable prospects for corporate investment growth are indicated by the NBP business tendency surveys, which show an increase in investment outlays planned for 2014, as well as an increase in the percentage of companies intending to begin new projects. A few of the Council members pointed out that the revival of outlays on fixed assets should also be supported by a rebound of investments related to further inflow of EU funds, in particular to the local government sector.

While analysing the prospects for further recovery in consumption, the Council members indicated that growth of disposable income is still low, limiting the increase in household expenditure. At the same time, a few Council members assessed that low inflation and a gradual improvement in the situation on the labour market will be conducive to the revival in individual consumption in the coming quarters.

While discussing the outlook for external trade, some members of the Council pointed out that low labour costs in Poland continue to support high price competitiveness of Polish goods abroad, and hence – exports growth. The favourable outlook for exports performance is also related to the anticipated acceleration of growth in Poland's main trading partner countries, as signalled by the upward revisions of their GDP growth forecasts. At the same time, a few Council members assessed that stronger import growth resulting from the expected investment revival will dampen the contribution of net exports to GDP growth.

While analysing trends in lending, some of the Council members pointed to the still weak credit growth. In particular, corporate lending for financing investment continues to rise only slowly, which – in the opinion of those Council members – indicates persistently high risk aversion on the part of both banks and enterprises. Yet, a few Council members stressed that growth in credit to the private sector has accelerated. They highlighted, in particular, the increasing availability of corporate credit, evidenced by the rising percentage of loan applications being approved. With corporate investment expected to accelerate in the subsequent quarters, this will facilitate a revival in lending to that sector, especially amidst banks' declarations of looser lending criteria for some types of loans.

Addressing labour market conditions, some members of the Council pointed out that so far they have been improving very slowly. In particular, employment growth is insufficient to bring down the unemployment rate. In effect, as at the end of 2013, the unemployment rate was still relatively high. A few Council members were of the opinion that since the probability of finding a job has risen – as has the ratio of non-subsidised vacancies to the number of the jobless – the outlook for labour market developments is favourable. In the opinion of those Council members, positive signs in this respect include also some improvement in willingness of increasing employment declared by enterprises and a decline in fears of losing a job reported by private individuals.

In the context of labour market impact on inflation, some of the Council members observed that the persistently high unemployment rate has a mitigating effect on both cost and demand pressures (on the former, by restricting wage pressure, on the latter, by reducing disposable income). Those Council members noted that in the past few years wage and unit labour cost (ULC) growth has been slow. A few Council members assessed that, also over the next few quarters, ULC growth should remain slow. Yet other members of the Council argued that in response to the improving economic conditions, wage pressure may materialise fairly promptly, hence the pace of ULC growth may pick up substantially within a short span of time.

While analysing inflation developments, the Council members highlighted that inflation – including core inflation – continued to be very low, and the available forecasts point to it likely remaining low also in the subsequent quarters. Low core inflation is supported by a further decline in producer prices and sustained low inflation in Poland's main trading partners. In turn, the risk of substantial rise in energy or food prices is constrained by the conditions in international commodity markets, where the moderate scale of global economic recovery is conducive to price stabilisation. Therefore there is no significant risk of inflationary pressure rising markedly in Poland in the nearest future. At the same time, a few Council members argued that in its monetary policy decisions the central bank should take into account the fact that the current low inflation is partly related to temporary factors remaining beyond the influence of domestic monetary policy.

The Council decided that the NBP interest rates should remain unchanged at the current meeting. Furthermore, the Council maintained its assessment that the gradual improvement in economic conditions was likely to continue over the coming quarters, while inflation pressure would remain limited. In this context, the Council confirmed that it would be justified to maintain the interest rates at the current level at least until the end of the first half of 2014. At the same time, Council members recognized that the findings of the March NBP projection would enable a more comprehensive assessment of medium-term outlook for inflation and economic growth.

The Council left the basic interest rates unchanged at the following levels: reference rate at 2.50%, lombard rate at 4.00%, deposit rate at 1.00%, rediscount rate at 2.75%.

**Minutes of the Monetary Policy Council decision-making meeting held on 5 March 2014**

At its meeting, members of the Monetary Policy Council discussed the current and future monetary policy decisions against the background of global and domestic macroeconomic developments and the March projection of inflation and GDP.

Referring to the situation abroad, the Council pointed out that the recovery in the global economy is still moderate. It was emphasised that activity growth in the United States may recently have lost some momentum, and GDP growth in 2013 Q4 has been revised downward. At the same time, it was assessed that a certain deterioration in the US data may be partly due to unfavourable weather conditions. Council members highlighted further improvement in the business climate in the euro area, where economic growth is nevertheless unstable and much weaker than that in the United States. It was also observed that inflation in the euro area has remained low.

Referring to the situation in the emerging economies, some Council members observed that business climate indicators for China, the largest emerging economy, point to a slowdown in activity growth at the beginning of 2014. Yet, a few Council members argued that activity growth in many Central and Eastern European countries has been accelerating.

Council member expressed the opinion that heightened uncertainty related to future developments in Ukraine poses a risk to the economic situation in Poland's external environment. It was indicated that possible escalation of the conflict between Ukraine and Russia may undermine Poland's trade with the Eastern markets and dampen business sentiment and firms' propensity to invest. At the same time, it was judged that the potential weakening in Poland's exports to the Eastern markets, particularly food exports, could curb price growth in the domestic market. Yet, a few Council members argued that the risk related to future developments in the East may support the recently observed slight increase in global commodity prices and deterioration of the sentiment in the financial markets. In this context, other Council members observed that the recent hike in commodity prices may have been a temporary phenomenon, while the slowing demand in China could contribute to lower commodity prices in the longer term.

Addressing economic conditions in Poland, Council members underlined accelerating GDP growth in 2013 Q4. As expected, output growth was supported by higher domestic demand growth, primarily in terms of consumption, and – to a very small extent – investment. Yet, it was net exports that continued to be the main driver of GDP growth. Council members emphasised that monthly data from the beginning of the year point to a continued gradual recovery in the economy. In particular, retail sales and industrial production continued to rise, however a fall in construction and assembly output was also mentioned. Council members assessed that economic recovery is not accompanied by accumulation of any significant macroeconomic imbalances; the current account balance is improving.

A few Council members also highlighted that the economic rebound has been accompanied by a stable growth in lending to the private sector.

While analysing the situation in the labour market, the signs of improvement, albeit a sluggish one, were observed. It was mentioned, that according to LFS, the number of working persons rose slightly in 2013 Q4, which contributed to a certain decline in the unemployment rate (in annual terms). It was, however, pointed out that in January employment growth in the corporate sector was halted. A few Council members, on the other hand, pointed to a rising number of job offers and falling likelihood of losing a job, which suggests continued improvement in the situation in this market in the following quarters. However, it was emphasised that the unemployment rate has persisted at elevated levels, thus hampering wage pressure in the economy. The absence of wage pressure is confirmed by a slowdown in both wage and unit labour cost growth in 2013 Q4.

Council members emphasised that the observed gradual recovery is not translating into higher inflationary pressure in the economy. It was observed that in January inflation remained stable and well below the target, while core inflation decreased. The absence of inflationary pressure is also signalled by negative growth of producer prices, amidst low inflation expectations of economic agents. A few Council members pointed out at this point that the annual consumer price growth is boosted, at the beginning of the year, by the statistical base effects.

While analysing the outlook for economic growth, Council members assessed that in the next few quarters economic recovery will probably continue at the pace envisaged in the March projection. It was emphasised that GDP growth will be supported by the revival in consumer demand. It was pointed out that in line with the projection, investment may be expected to pick up, especially in terms of corporate investment. Yet, a few Council members argued that corporate business activity may be weakened by the growing tax burden imposed on businesses by local government units.

Council members expressed the opinion that despite stronger economic growth, inflation – in light of the March projection – will return to the target only gradually, and will remain below the target at least throughout this year. Some Council members also invoked external forecasts pointing to the same scenario. In this context, those members highlighted the fact that – according to the projection – the expected gradual return of inflation to the target will be related to the narrowing of the output gap and its subsequent stabilisation at a positive, yet close to zero level. Council members observed that in line with the projection, wage and unit labour costs will accelerate, yet their growth will not be strong enough to jeopardise the inflation target in the medium term.

A few Council members also observed that the March projection – in comparison with the November one – expects lower inflation this year, coupled with higher forecasts of GDP growth. They argued that the persistence of inflation below the target during this year will result, to a large extent, from the impact of factors beyond the direct influence of the domestic monetary policy, including slow energy price growth. As a result, in the case of higher than assumed in the current projection energy price growth in subsequent quarters, inflation may return to the target faster than anticipated in the projection. Those members also highlighted that resulting from the projection increase in ratio of labour costs to corporate revenues may contribute to lower price competitiveness of Polish enterprises in the international markets. In this context, they pointed out that the recovery may be conducive to the inflow of capital and appreciation of the exchange rate, which would further limit price competitiveness of Polish enterprises. As a result, factors of production might be shifted towards the non-tradable sector – including residential construction – posing, amidst low interest rates, a risk of imbalances arising in this sector. Therefore, a few Council members were of the opinion that an interest rate increase may be justified, even if inflation remains below the target.

Yet, other Council members held the view that a significant interest rate rise aimed at curbing the risk of imbalances in the real estate market may come at a higher cost to the economy as a whole than the application of macroprudential instruments. They also underlined that the gradual decrease of the LtV ratio in mortgage loans this year and in the following years applied by the Financial Supervision Authority should limit the risk of accumulation of significant imbalances in the real estate market.

The Council decided that the NBP interest rates should remain unchanged at the current meeting. The Council discussed the indicated period of the probable maintenance of the NBP interest rates at an unchanged level. Some Council members were of the opinion that, given the March projection, which pointed to a very gradual return of inflation to the target, it may be justified to keep the interest rates unchanged until the end of 2014. One of the factors justifying the extended period of interest rate stabilisation was – in the opinion of some Council members – the need to limit economic uncertainty under mounting international risk related to the tensions emerging in the East.

Some Council members emphasised that owing to the uncertainty about future macroeconomic developments abroad, including in Ukraine, the indicated period of the probable maintenance of NBP interest rate should not be longer than before. A few of these Council members also believed that a shorter indicated period of no interest rate change may also be justified by the ongoing economic recovery and the risk of an earlier than projected return of inflation to the target.

As a result of the discussion, the Council assessed that the current and expected economic situation, including the results of the March projection of inflation and GDP justify maintenance of the NBP interest rates at an unchanged level over a longer period of time, i.e. at least until the end of the third quarter of 2014.

The Council left the basic interest rates unchanged at the following levels: reference rate at 2.50%, lombard rate at 4.00%, deposit rate at 1.00%, rediscount rate at 2.75%.

**Minutes of the Monetary Policy Council decision-making meeting held on 9 April 2014**

At its meeting, members of the Monetary Policy Council discussed the current and future monetary policy decisions in the context of macroeconomic developments in Poland and abroad.

While discussing external developments, it was pointed out that activity growth in the global economy is still moderate. The Council members noted that – after a temporary slowdown – the latest data point to improved economic conditions in the United States, while recovery in the euro area continues to be slow. At the same time, the Chinese economy is most likely slowing down further.

The Council members emphasised that inflation is low in many countries, which – if continues – may impede the deleveraging process in the largest economies. A few Council members referred to the factors which in their opinion may translate into a permanent decrease of global inflation. These factors include: a slower economic growth of the world economy and a downturn in the long-term commodity price cycle. Some of the Council members argued that for the next few years economic growth in the largest emerging economies will have a positive impact on the growth of global economic activity, which should be conducive to higher inflation around the world.

While analysing the external environment, it was pointed out that inflation in the euro area decreased to a very low level, which convinced the ECB to signal a possibility of further monetary policy easing. At the same time, however, a few members of the Council pointed out that low inflation in the euro area is mainly the result of strongly negative growth in energy prices – a favourable supply shock, which supports revival of the demand in this economy. Falling unit labour costs in member states most severely affected by the debt crisis is also a factor lowering inflation in the euro area. Decreasing unit labour costs help those countries overcome the recession, while preserving the competitiveness of German exports against countries outside the euro area. Those Council members also argued that a possible deflation in the euro area would not be significant enough to discourage agents from purchases, so the risk of second-round effects of price decreases is not significant. At the same time, in the opinion of those members of the Council, the continuation of highly expansionary monetary policy by the ECB – by increasing the risk of bubbles arising in the asset market – may even contribute to decreasing inflation. Other Council members assessed that possible emergence of expectations on falling prices may strengthen deflation tendencies in the euro area, and therefore the ECB will probably attempt to counteract this situation.

While analysing the outlook for economic conditions, it was pointed out that increasing importance of domestic demand in economic growth in Germany is a positive development. At the same time, some Council members stressed that the slowdown in economic growth in China may be a factor of risk for the improvement of economic conditions in Germany, and thus also in Poland. A few Council members assessed that due to a sharp rise in Chinese internal debt after the global financial crisis, currently it is difficult to expect a stimulus to the Chinese economy.

The Council members pointed out another source of uncertainty surrounding the outlook for economic growth in Poland is the situation in Ukraine – including the scale of the expected recession in the Ukrainian economy and the risk related to disturbances in economic relations between Ukraine and Russia. It was indicated that possible escalation of the conflict between Ukraine and Russia may undermine Poland's trade with the Eastern markets. In the view of currently available information, it was judged that although the potential weakening in Poland's exports to the Eastern markets may negatively affect some companies, it will not be a factor significantly reducing economic activity growth in the whole economy.

While discussing the financial markets' response to the conflict between Russia and Ukraine, it was emphasised that the zloty exchange rate has remained relatively stable, the yields on Polish sovereign bonds have not changed significantly and the impact on stock valuations was temporary. In the opinion of some Council members, favourable foreign investor sentiment towards the Polish economy is supported by its strong fundamentals and the lack of macroeconomic imbalances.

While analysing current data, it was highlighted that the accelerating growth of industrial output and retail sales together with the rebound in construction activity confirm a continued gradual economic recovery. At the same time, strong readings of most business climate indicators suggest probable activity growth continuing also in the subsequent quarters. Some of the Council members assessed that the rise in GDP growth may be quite substantial due to the possible acceleration in corporate investment spending in the nearest future. However, at the same time, some Council members pointed to the weakening of firms' expectations regarding their export orders, which may signal slower external demand, stemming firms' propensity to invest. Furthermore, a few Council members argued that, as slower economic growth abroad is probably a more durable phenomenon, GDP growth in Poland may remain moderate. In their opinion, a factor which may hamper consumer demand growth is substantial long-term indebtedness of some households.

Council members emphasised that the recovery of the Polish economy is starting to translate into labour market conditions. Employment in the corporate sector is gradually rising, with a concurrent decline in unemployment. Yet it was stressed that the unemployment rate persists at an elevated level, which constrains wage pressure. At the same time, a few Council members argued that while wage growth continued to be moderate, yet – considering low inflation – households' real disposable income growth is rising, which supports higher consumption growth.

Some Council members emphasised that lending growth, while somewhat stronger, remains slow. It was observed that firms' higher propensity to invest – observed against the background of low interest rates and improving business climate – is accompanied by higher corporate credit growth. At the same time, a few Council members observed that low interest rates on deposits continue to limit the incentives to save in the banking system.

While discussing inflationary processes, Council members pointed to inflation remaining markedly below the NBP inflation target, core inflation continuing at low levels, further decline in producer prices and low inflation expectations. Some Council members emphasised that the available forecasts pointed to a very slow increase in inflation and the absence of risks to price stability in the medium term.

The Council decided that the NBP interest rates should remain unchanged at the current meeting. Furthermore, the Council maintained its assessment that the NBP interest rates should be kept unchanged for a longer period of time, i.e. at least until the end of the third quarter of 2014. The Council members observed that a more comprehensive assessment of a need to change the horizon of keeping the interest rates at the current level will probably be possible during the July meeting of the Council, when a new NBP projection is to be presented.

The Council left the NBP interest rates unchanged at the following levels: the reference rate at 2.50%, the lombard rate at 4.00%, the deposit rate at 1.00% and the rediscount rate at 2.75%.

**Minutes of the Monetary Policy Council decision-making meeting held on 7 May 2014**

At its meeting, members of the Monetary Policy Council discussed the current and future monetary policy decisions in the context of macroeconomic developments in Poland and abroad.

While discussing external developments, Council members pointed to a gradual improvement in business conditions. It was noted that after growth in the United States had come to a halt in early 2014, the latest data pointed to a rebound of economic activity. In addition, it was highlighted that – although the Federal Reserve was gradually reducing the scale of its asset purchases – monetary policy in the United States continued to be very accommodative.

Council members also pointed out that a gradual recovery continued in the euro area. It was emphasised that recovery in Germany – Poland's main trading partner – was somewhat stronger than in other euro area member states. However, weaker March industrial orders and business sentiment in Germany were brought to attention. It was also noted that sentiment in the financial markets of the euro area countries most severely affected by the debt crisis had improved, which should translate into easier access to credit, and further into a gradual improvement in economic conditions in some of these countries.

Council members emphasised that inflation in many countries, including in particular in the euro area, remained low despite the ongoing economic recovery. This may convince major central banks, including the ECB, to continue their accommodative monetary policies. A few Council members expressed the opinion that deflation in the euro area was increasingly less likely, as indicated by the upward revisions of some inflation forecasts for the euro area. These members also highlighted the risks to longer-term growth sustainability associated with further monetary policy easing by the ECB.

In their discussion on developments in the external environment of the Polish economy, a few Council members cited factors which could potentially be conducive to lower growth in developed countries in the coming years, particularly in the euro area. These factors included possible further fiscal consolidation, ageing population and a decline in investment outlays, including for R&D, in developed countries following the global financial crisis. Furthermore, a few Council members indicated that attempts by Chinese authorities to rebalance economic growth in China away from investments might weaken demand for Chinese imports of investment goods from developed countries, particularly from Germany.

Referring to economic conditions in emerging market economies, it was noted that Chinese growth had weakened in 2014 Q1. Attention was also drawn to a deterioration in economic outlook for Ukraine and Russia, which was related to the Ukrainian crisis. While discussing the impact of the Ukrainian crisis on the Polish economy, the majority of the Council members judged that the mounting turmoil in Ukraine continued to pose a source of uncertainty for Polish economic growth outlook. They pointed out that a weaker economic growth outlook in Russia and Ukraine and a depreciation of their currencies might undermine Poland's trade with the Eastern markets. However, a few Council members were of the opinion that – given that Poland's trade with these markets was limited, and some of these exports could be redirected to other markets – the Ukrainian crisis would have a limited impact on Polish foreign trade, and in consequence, on economic growth in Poland.

Council members also highlighted that the impact of the Ukrainian crisis on the sentiment in the international financial markets and the zloty exchange rate had been limited so far.

While discussing recent data releases in Poland, Council members pointed to ongoing growth in industrial output and retail sales as well as improved construction sector performance, all of which confirms continued recovery in domestic demand. It was indicated that, in contrast to earlier estimates, domestic demand had been the main driver of growth already in 2014 Q4, which had been – among others – due to much faster than expected rebound of investment spending. Yet, it was also emphasized that recent data on economic activity had been lower than expected and in some cases, including retail sales growth, export orders and leading indicators of business sentiment, had weakened. In the opinion of some Council members, the deterioration in sentiment could have been related with higher uncertainty due to an escalation of the conflict in Ukraine and weaker economic growth outlook in the trading partners in the East.

Council members noted that the rebound of economic activity was translating into improvement in labour market conditions. Employment in the corporate sector is gradually expanding, with a concurrent decline in unemployment. Yet it was emphasised that the unemployment rate persisted at an elevated level, which constrained wage pressure, as confirmed by slow unit labour cost growth. However, a few Council members expressed the opinion that – like in the previous recoveries – unit labour cost might be expected to pick up in the coming quarters, citing an acceleration in wage growth in recent months. On the other hand, some Council members argued that business conditions surveys did not point to an acceleration of wage growth in the near future.

Some Council members pointed to a slight improvement in lending growth, supported by low loan costs. At the same time, a few Council members drew attention to a low share of investment loans in financing of investment projects by small and medium-sized enterprises. Other Council members assessed that low interest on deposits continues to undermine the incentives to save in the banking system, which was reflected in increasingly weaker growth in corporate deposits.

In their discussion on inflation developments, Council members pointed to inflation remaining markedly below the NBP inflation target and still low core inflation, despite a rise in one of its measures. It was also emphasised that producer prices continued to decrease, and that inflation expectations remained low. Some Council members noted that the available forecasts pointed to a slightly slower rise in inflation in the coming months than envisaged in the March projection. Taking this into account, a few Council members expressed the opinion that inflation might return to the target later than forecasted in the March projection. Some Council members presented the view that accelerated economic growth might translate into a rise in inflation to a greater extent than currently forecasted. Moreover, a few Council members noted that the situation in Ukraine and the adverse weather conditions in many major food commodity exporters resulted in a considerable rise in their prices in the global markets. This is conducive to faster food price growth, whose deceleration – along with slow energy price growth – was previously one of the key factors keeping inflation down.

The Council decided that the NBP interest rates should remain unchanged at the current meeting. Furthermore, the Council maintained its assessment that the NBP interest rates should be kept unchanged for a longer period of time, i.e. at least until the end of the third quarter of 2014. The Council members observed that a more comprehensive assessment of macroeconomic outlook needed to change the horizon of keeping the interest rates at the current level will probably be possible during the July meeting of the Council, when a new NBP projection is to be presented.

The Council left the key NBP interest rates unchanged at the following levels: reference rate at 2.50%, lombard rate at 4.00%, deposit rate at 1.00%, rediscount rate at 2.75%.

**Minutes of the Monetary Policy Council decision-making meeting held on 3 June 2014**

At its meeting, members of the Monetary Policy Council discussed the current and future monetary policy decisions in the context of macroeconomic developments in Poland and abroad.

While discussing external developments, Council members indicated that growth in global activity remained moderate, but economic conditions varied across countries. Some Council members emphasized that recent data on activity in the major economies had been weaker than expected. In particular, in the United States GDP unexpectedly fell in the first quarter, albeit probably only temporarily. In the euro area, GDP growth was low, and some economic indicators pointed to a slowdown in recovery in the manufacturing sector in May 2014.

During discussion of the euro area, some Council members pointed to a dispersion in economic growth rates within the region. In Italy GDP declined in 2014 Q1, and in France output did not change. At the same time, in Germany – Poland's main trading partner – economic growth accelerated. A few Council members cited downside risks for German exports: still relatively low economic growth in China and economic slowdown in Russia. Some Council members also emphasized that the weakening of the Polish trade with Russia and Ukraine, recorded already in 2013, had intensified in the first months of 2014.

While discussing monetary policy abroad, Council members pointed out that the ECB had hinted it might ease its monetary policy at the June meeting. Some Council members emphasized that although the Federal Reserve was slowly reducing the scale of quantitative easing, monetary policy was still highly expansionary also in the United States. They also indicated that monetary policy in Central and Eastern Europe remained accommodative, and the National Bank of Hungary (MNB) had recently decreased its base rate to 2.4%. A few Council members emphasized that even though monetary policy of many central banks had been expansionary in recent years, inflation remained low worldwide.

When discussing inflation developments abroad, Council members pointed out that inflation in the euro area was still low, not only owing to a fall in food and energy price index, but also due to low core inflation. It was noted that inflation in the euro area remained well below the ECB's definition of price stability. In this context, the opinion was expressed that persistence of low inflation impeded deleveraging in the euro area member states most severely affected by the debt crisis. It was also highlighted that inflation in Central and Eastern Europe had also declined in recent months to only slightly above zero, or even reaching negative levels. It was pointed out that a decline in CPI inflation in Central and Eastern Europe over recent months was – like in the euro area – accompanied by a fall in core inflation.

Referring to the economic conditions in Poland, Council members indicated that GDP growth in 2014 Q1 had been close to the March projection and confirmed a gradual recovery of the Polish economy. Attention was paid to the favourable composition of GDP growth. In particular, there was an acceleration in domestic demand, especially investment demand, while foreign trade continued to record a surplus. However, some Council members pointed out that some indicators of activity in manufacturing sector had levelled off due to weakening in orders, employment and output sub-indices. In the opinion of these Council members, a decline in some economic indicators may reflect risks to further recovery of the Polish economy.

A few Council members noted that investment in Poland remained weak in relation to GDP compared to other countries in Central and Eastern Europe. They also indicated that the share of private investment was low compared to other EU member states. In this context, it was noted that corporate lending, including for investments, had rebounded.

Council members highlighted that the recovery in economic activity was translating into an improvement in the labour market conditions. Employment in the Polish economy is slowly rising, and unemployment is falling. It was emphasized that – in spite of a gradual recovery in the labour market – wage pressure remained limited, owing to a concurrent rise in labour force participation.

While discussing inflation developments, Council members pointed out that inflation had decreased in April, remaining markedly below the inflation target and considerably below the March projection. A fall in inflation in April was due to a decline in core inflation and falling food price growth. Some Council members indicated that a decline in inflation in recent months was driven by a fall in prices of an increasing number of goods. A few Council members also drew attention to continued fall in producer prices, decline in retail sales prices and further decrease in import prices.

With regard to expected inflation developments in months ahead, Council members pointed out that according to several short-term forecasts, inflation was likely to remain below the March projection. Some Council members also emphasized that – according to available forecasts – the probability of a temporary fall in inflation below zero in summer had risen. It was also noted that long-term breakeven inflation expectations had fallen. A few Council members, however, were of the opinion that – if the current pace of economic growth continued – a revival in demand pressure would be conducive to higher inflation. They also argued that due to reduced oil production in some countries, oil prices could rise in the coming period.

The Council decided that the NBP interest rates should remain unchanged at the current meeting. The Council maintained its assessment that the NBP interest rates should be kept unchanged until the end of 2014 Q3. While discussing future decisions, the majority of Council members pointed out that the expected inflation was lower than in the March projection, while uncertainty had risen, particularly with respect to the pace of economic recovery in the coming quarters and the outlook for monetary policy abroad. Given this, Council members observed that a more comprehensive assessment of the monetary policy perspectives and potential adjustment of interest rates would be possible after the Council got acquainted with incoming information, including the July NBP projection.

The Council left the key NBP interest rates unchanged at the following levels: reference rate at 2.50%, lombard rate at 4.00%, deposit rate at 1.00%, rediscount rate at 2.75%.

**Minutes of the Monetary Policy Council decision-making meeting held on 2 July 2014**

At its meeting, members of the Monetary Policy Council discussed the current and future monetary policy decisions against the background of macroeconomic developments in Poland and abroad and the July projection of inflation and GDP.

While discussing business conditions abroad, Council members underlined that global activity growth remained moderate. It was emphasised that the recovery in the euro area continued at a slow pace, despite a certain improvement in the business climate in the peripheral economies of the monetary union. Some Council members also pointed out that following the data revision in the United States, 2014 Q1 GDP growth had been negative and weaker than originally estimated. Other Council members underlined, that the fall in GDP had been related to weather conditions and the second quarter should see a considerable rebound in GDP growth. With reference to the situation in major emerging economies, including Russia, it was indicated that economic activity growth in these countries remained slow. However, it was emphasised that recovery continued in countries of Central and Eastern Europe.

At the meeting monetary policy in the external environment of the Polish economy was discussed. Attention was drawn to the easing of monetary policy by the European Central Bank (including interest rates cut and the introduction of a new liquidity provision to the banking system programme, conditional upon increased lending) and by some banks in emerging economies. It was emphasised that the ECB might announce further quantitative easing programmes in the subsequent quarters. Some Council members pointed out that the easing of monetary policy by the ECB increased the interest rate differential between Poland and majority of the countries in its environment as well as the importance of this differential for exchange rate developments.

While discussing the effectiveness of the non-standard measures undertaken by the major central banks, some Council members were of the opinion that those measures allowed to meet the rising demand for liquidity from economic entities. It was argued that in the absence of those measures, the growth in economic activity in the largest economies would probably have been slower. Some Council members argued, however, that the effectiveness of the non-standard measures taken by the major central banks is low. Amidst still not fully restructured balance sheets in the banking sector and uncertainty persisting in the economy, this measures fail to boost lending and aggregate spending while producing an undesirable effect of excessive growth in the prices of some assets. Those members also pointed out that although quantitative easing provided liquidity to the economy and gave banks and enterprises time to restructure, the maintenance of interest rates close to zero undermined the incentives for restructuring.

Council members also observed that the strongly expansionary monetary policy of the major central banks had not, as yet, driven up inflation to any significant degree, and that inflation in Poland's immediate environment remained very low. A few members argued that low inflation in the global economy might persist for a longer time, considering the limited demand growth and the absence of commodity price growth in the global markets.

While discussing the economic situation in Poland, Council members emphasised that economic activity growth might have slowed down in the past few months, which might be partly – and in the assessment of a few Council members primarily – the effect of the conflict between Ukraine and Russia. The slowdown in economic activity growth was reflected in lower growth in industrial output, construction and assembly output as well as in retail sales. It was highlighted that some business climate indicators declined and employment growth in the corporate sector ground to a halt. The Council also underscored considerable uncertainty concerning the permanence of the recent slowdown in economic activity. A few Council members presented the view that the accelerating growth in lending suggested a continuation of the recovery in domestic demand in the subsequent months. At the same time they emphasised that as economic recovery continues, lending might accelerate further and exceed nominal GDP growth markedly.

With reference to current inflation, it was observed that in May the annual consumer price growth had decreased again and was significantly below expectations. It was also emphasised that producer prices in industry in year-on-year terms continued to fall and that inflation expectations of households and enterprises remained low. It was argued that low inflation resulted not only from supply shocks (including the decline in fruit and vegetable prices), but also from moderate demand growth reflected in low levels of core inflation. Some members of the Council also pointed to a negative growth in import prices as an important source of low inflation in Poland. Some members of the Council noted that the lower than expected inflation was conducive to a rise in real interest rates.

While analyzing the July projection of inflation and GDP, members of the Council pointed out that, although in the subsequent quarters GDP growth was not likely to accelerate significantly, it might exceed potential GDP growth. As a result, the output gap, which is now negative, should be gradually closing within the projection horizon. Some Council members underlined, however, that at the end of the projection horizon GDP growth would be close to potential output growth. Council members also pointed out that – in line with the projection – all the components of domestic demand as well as exports were supposed to rise and that a certain slowdown in investment growth at the end of the projection horizon might be driven by a reduction in the EU-financed public investment. It was emphasized that in line with the projection, economic recovery in the coming quarters would, to a certain extent, boost wage growth in the economy, which should, however, remain below the long-term average. It was pointed out, however, that wage growth is expected to outpace labour productivity growth, which would lead to a gradual increase in unit labour costs growth. Some Council members underlined that in the long-term projection horizon, the growth of unit labor costs could exceed the NBP inflation target.

While analyzing the inflation projection, members of the Council emphasized that in the coming quarters inflation would be lower than expected in the March projection. They indicated that inflation might fall below zero in the coming months, and in the subsequent few quarters would continue to be very low. It was pointed out that inflation would rise close to the target at the end of the projection horizon. It was argued that, in line with the projection, the increase in inflation would be supported by the projected improvement in the labour market as well as a certain rise in food and energy prices. A few Council members pointed out, however, that a growth in those two price categories should be – according to the projection – lower than long term average.

Referring to the possible effects of the expected temporary fall in inflation below zero in the coming months, a few members of the Council were of the opinion that it would boost the real purchasing power of consumers and expand consumer demand. Other members of the Council believed that the likely fall in inflation below zero could prompt households to postpone consumption. Those members were of the opinion, that present interest rates level under current macroeconomic developments could deepen deflation.

Members of the Council pointed to the risks associated with the projection of inflation. Some of them emphasized that the distribution of risks in the projection was asymmetric and the probability of inflation running below the central path was higher than the probability of inflation running above the path. However a few members of the Council were of the opinion that higher than assumed energy prices, possibly being the result of the Middle East conflict, might be a risk factor for higher inflation. Other Council members argued that core inflation in the projection rose to a level which in the past had occurred only when CPI inflation had been higher than the upper limit for deviations from the inflation target.

The Council decided that the NBP interest rates should remain unchanged at the current meeting. The rationale for this decision was the ongoing economic recovery, which should contribute to inflation rising close to the NBP inflation target over the projection horizon. Yet, Council members were of the opinion that there persisted uncertainty regarding a possible deterioration in the business climate and the pace of return of inflation to the target. Therefore, a few Council members pointed out that interest rate decrease could be necessary in the near future. The Council was of the opinion, that decisions in the coming months should depend on the assessment of incoming data from the point of view of the prospects for further economic recovery and inflation developments in the medium term.

**Minutes of the Monetary Policy Council decision-making meeting held on 3 September 2014**

Members of the Monetary Policy Council discussed the current and future monetary policy decisions against the background of macroeconomic developments in Poland and abroad.

While discussing the economic conditions abroad, Council members emphasized that since the previous meeting the uncertainty in the environment of the Polish economy had increased significantly. The growth in uncertainty was driven by an escalation of the conflict in the East and signs of the euro area returning to stagnation. It was pointed out that growing uncertainty about unfolding military crisis in the East as well as economic sanctions would have an adverse impact on economic conditions in Poland and Europe. Attention was drawn to a deepening recession in Ukraine and an ongoing economic downturn in Russia, accompanied by a depreciation in currencies of both countries. These factors have a negative impact on Polish exports and – in consequence – on domestic economic activity.

Some Council members, on the other hand, expressed an opinion that economic sanctions, though severe for some industries, would probably have a limited impact on Poland's trade and domestic economy. Moreover, it was noted that – despite elevated uncertainty driven by growing geopolitical risk in the recent period – the zloty had been relatively stable. A few Council members, however, pointed to a slight depreciation in the zloty since the previous meeting. Furthermore, they were of the opinion that the likelihood of a sharp fall in financial asset prices in the event of a sudden increase in risk aversion had recently increased, especially amidst limited volatility and low turnover in the financial markets.

Council members emphasized that developments in the euro area were an important source of external risk for the economic growth in Poland. In 2014 Q2, the euro area returned to stagnation, which was mainly due to economic conditions in the largest economies of this region. In particular, GDP remained unchanged for the second quarter in a row in France and fell in Italy and Germany. Council members also pointed to a decline in industrial activity indicators in the euro area. At the same time, a few Council members were of the opinion that a rebound in economic activity in the United States since 2014 Q2 might translate into global economic recovery, including in the emerging market economies. As a result, this could have a positive impact on activity of the German economy, and consequently on activity of the Polish economy.

It was pointed out at the meeting that inflation in the euro area had declined near zero. A few Council members expressed a view that low inflation would – through lower indexation of household incomes – affect demand growth and contribute to extending the period of stagnation in the euro area. Council members pointed out that since the Council's previous meeting, expectations of additional monetary easing by the European Central Bank had increased. Attention was also drawn to interest rate cuts in economies having strong links to the euro area, as well as rising interest rate differential between Poland and its immediate environment.

While discussing the economic conditions in Poland, it was emphasized that incoming data point to a decline in economic growth. Although the annual growth rate of GDP in 2014 Q2 decreased slightly, it was supported to a large extent by a built-up in inventories amidst a decline in net exports and growth in investment. According to some Council members, this may indicate a risk of adjustment in production in the coming quarters to a decrease in sales growth. Weakening economic activity is also confirmed by the data on industrial production and leading industrial indicators, which in the recent months were significantly lower than a few months ago. Moreover, it was stressed that consumer sentiment had declined in the recent period and construction and assembly output growth was came almost to a halt in July. Some Council members also indicated that the pace of recovery in the labour market slowed down as well, as shown by a decrease in employment growth, wage growth and unit labour costs in 2014 Q2.

A few Council members, however, expressed the opinion that elevated uncertainty associated with the escalation of the crisis in Ukraine could have been a major factor behind weakening investment growth in 2012 Q2 and deterioration in economic indicators in the recent period. Therefore, the persistence of the weakening in economic indicators and investment growth is hard to assess. Some Council members assessed that the economic growth could stay close to previous quarters. They indicated that a slight acceleration in private consumption growth in 2014 Q2 and a certain increase in retail sales in July pointed to a continued increase in consumer demand. The rise in consumer demand is supported by the ongoing recovery in the labour market and a steady increase in real wages amidst very low price growth. A few Council members also pointed to a certain growth in industrial production in July.

Referring to the current price developments, it was pointed out that annual inflation had fallen below zero in July, which had been in line with the July projection, although clearly below the expectations formed several quarters earlier. It was emphasized that the decline in inflation below zero was due to a negative growth of food prices amidst stagnant energy prices. At the same time, attention was drawn to the lack of demand pressure confirmed by historically low values of all core inflation measures and the persistence of negative growth of retail sales deflator. It was also indicated that despite recovery in the labour market, there was no wage pressure in the economy. Neither were there any cost pressures, as confirmed by a two-year decline in producer prices. It was pointed out that a significant decline in inflation and inflation expectations was conducive to rising real interest rates, despite a stabilization of nominal interest rates.

With regard to the economic growth outlook, Council members assessed that, similarly to 2014 Q2, economic growth in the coming quarters is likely to be lower than expected in the July projection, although – as pointed by a few Council members – will remain close to early 2014. Lower GDP growth than in the July projection is indicated mainly by weaker economic conditions in the environment of the Polish economy. Council members also emphasized that declining sentiment of domestic economic agents driven by growing uncertainty about developments in Ukraine might limit domestic activity.

While analyzing the outlook for inflation in the coming months, it was pointed out that in the following months it would probably be slightly lower than in the July projection. Lower inflation than expected in July will most likely be driven by a stronger decline in food prices (due to embargo imposed on Polish fruit and vegetables and reduced food commodity prices in the international markets), as well as weaker demand pressure associated with slower economic growth than expected in July. Some Council members also indicated that the expected persistence of very low inflation in the euro area would – through strong trade ties with the euro area – add to a reduction in price pressure in Poland. At the same time it was pointed out that – in line with available forecasts – inflation would rise above zero already in 2014, probably on the back of a higher growth rate of energy prices and food price growth rate turning positive.

While discussing decision on interest rates, the majority of Council members assessed that in the near future it would probably be justified to adjust the level of NBP interest rates. In their opinion, signs of economic slowdown in Poland and abroad, an absence of price pressure and increased risk of inflation remaining below the target in the medium term, as well as monetary policy easing in the euro area, are factors in favour of lowering interest rates. These members also assessed that, given moderate economic growth and persisting uncertainty, a risk of macroeconomic imbalances build-up following a probable decrease in interest rates was small. Some Council members considered that NBP interest rates should be reduced already at the current meeting. They argued that – considering a rise in risk of economic slowdown and inflation remaining well below the target in Poland in the coming quarters – it was justified to lower interest rates as soon as possible. Other Council members pointed to uncertainty about the persistence of economic slowdown and developments in the East, which justified – in their opinion – keeping interest rates unchanged at the current meeting. They also noted that in previous meetings the Council had signalled a stabilization of the interest rates till the end of 2014 Q3. At the same time, they emphasized that if the incoming data failed to alter significantly the assessment of economic conditions and inflation developments, it would be justified to begin monetary policy adjustment at the following meeting.

Yet, some Council members assessed that the adjustment of monetary policy in Poland was not currently justified. In their opinion, despite signs of economic slowdown, it is possible that the economic growth will remain stable in the coming quarters. They pointed out that given high uncertainty, the impact of interest rate changes on decision-taking by economic agents was limited. In their view, given limited demand for corporate loans, additional monetary stimulus would have little impact on corporate lending. In addition, they argued that any exchange rate depreciation – accompanying interest rate cuts – would affect purchasing power of households with liabilities denominated in foreign currencies. They also pointed out that should the uncertainty diminish, a reduction in interest rates might be conducive to emergence of macroeconomic imbalances.

At the meeting a motion was submitted to lower NBP interest rates by 0.50 percentage points. The motion did not pass. A motion was also submitted to lower NBP interest rates by 0.25 percentage points. The motion did not pass. The Council decided to keep NBP interest rates at the following levels: the reference rate at 2.50%, the lombard rate at 4.00%, the deposit rate at 1.00%, the rediscount rate at 2.75%.

**Minutes of the Monetary Policy Council decision-making meeting held on 8 October 2014**

Members of the Monetary Policy Council discussed the current and future monetary policy decisions against the background of macroeconomic developments at home and abroad.

While discussing business conditions in Poland's external environment, Council members pointed out that global activity growth remained moderate and varied considerably across the regions. They emphasised that recovery continued in the United States, although its pace remained slower than in the previous business cycles. Council members observed that GDP growth in the euro area had been weak and that business climate indicators had deteriorated recently. Some Council members also drew attention to the downward revisions of growth forecasts for the euro area by international institutions. Council members also pointed to deteriorating business conditions in Germany, Poland's main trading partner, reflected in the declining levels of the PMI and IFO indices in the past few months, and in the sharp fall in industrial output and new orders in August. Council members indicated that in other large euro area economies, including Italy and France, economic activity growth remained slow and hampered by structural problems of these countries.

While discussing economic situation in the largest emerging economies, it was observed that the Russian economy might be in recession in 2014 Q3, while growth in China had probably slowed down. It was argued that the deteriorating economic situation of these countries would adversely impact Germany's exports, which in turn might subsequently weigh on the growth of Polish exports.

Council members highlighted a significant decline in the prices of commodities over the recent months, which supported a decrease in inflation in Poland and in its environment, including the euro area. It was observed that the euro area inflation had been gradually trending down towards zero.

While discussing monetary policy abroad, Council members underlined that the tapering of quantitative easing by the Federal Reserve was occurring against the background of the ECB stepping up its monetary expansion. It was pointed out that due to the divergence between monetary policy of the Federal Reserve and the ECB, the euro has recently weakened against the dollar, which would boost the euro area's price competitiveness vis-a-vis the US economy. The euro weakening was also accompanied by the złoty depreciation against the dollar.

It was indicated that the ECB launched the first conditional liquidity provision operations to banks in September and announced the start of asset purchases in 2014 Q4. Some Council members assessed that the ECB's strongly expansionary monetary policy – given the structural nature of weak economic growth and sluggish demand for credit – would prove ineffective in boosting economic growth in the euro area. Other Council members highlighted that although the scale of further quantitative easing by the ECB was unknown, it would last – according to the announcements of the ECB – for at least 2 years. Thus – they argued – the monetary policy in Poland's environment would remain highly expansionary for an extended period, which, assuming unchanged NBP interest rates, might be conducive to the inflow of short-term capital to Poland. However, a few Council members judged that the anticipated monetary policy tightening by the Federal Reserve could have more significant impact on financial markets – including the prices of Polish assets – than the monetary policy loosening by the ECB. Those members also underscored that in some emerging economies and developed economies which had been only slightly affected by the financial crisis, interest rates remained higher than in Poland.

While discussing economic situation in Poland, Council members pointed out that economic growth had slowed down in recent months. Some Council members emphasised that economic activity had proved weaker than forecasted in the July projection of NPB. At the same time, those members pointed to the flagging industrial output growth, stagnant construction and assembly output as well as the PMI index running below 50 points. They also observed that economic activity growth in Poland had been dragged down by a strong fall in exports to the former Soviet Union countries and a marked weakening in exports growth to the euro area. They argued that while retail sales continued to rise, the pace of this growth was below that observed in the first half of 2014. They also expressed the opinion that the weakening of GDP growth might not be temporary, and a few of them believed that there was a risk of further decrease in GDP growth in subsequent quarters.

In contrast, some Council members argued that economic growth had decelerated only slightly and its pace was currently close to potential output growth. They pointed to the gradually improving situation in the labour market, including a decline in the unemployment rate and further steady wage growth, which supported retail sales growth. They also argued that relatively robust economic activity was accompanied with sound financial situation of enterprises. A few of those Council members observed that both economic growth and domestic demand growth in Poland remained higher than forecasted a few quarters ago, when the Council had decided about the last interest rates cut. They also underlined that – according to the forecasts – GDP growth next year might be higher than this year.

Some members of the Council pointed out that GDP growth in the coming year would be affected by fiscal policy. A few members of the Council were of the opinion that the increase in social spending announced by the government suggested that the coming year might bring greater than previously planned rise in public expenditures. A few Council members pointed also to a possible increase in expenditures co-financed with the European Union funds. Some Council members believed, however, that the government-announced increase in social spending would be small (about 0.2% of GDP), and the deficit in 2015 would remain close to its 2014 level. Moreover, part of the public expenditures would be related to a repayment of liabilities incurred a few years ago. They also argued that the possibility of fiscal policy easing was limited due to the excessive deficit procedure being in force. A few Council members assessed, however, that budget deficit in 2014 will be probably markedly lower than it was planned in the budget act, which will mean easing of fiscal policy in the next year.

While analyzing the inflationary developments, members of the Council highlighted the fact that CPI inflation continued to run below zero. The majority of the Council members emphasized that no cost pressure had been seen in the economy, as evidenced by the negative growth in producer prices and persistently low wage growth. They also argued that there were no signs of demand pressure, as indicated by the negative retail sales deflator and core inflation persisting close to zero. They also pointed to continuing decline in inflation expectations. They drew attention to increase in risk of longer than previously expected period of inflation remaining below the target, as suggested by the revisions of inflation forecasts.

According to some members of the Council, such a sharp decline in CPI inflation is largely supply driven, as evidenced by the deepening decline in food prices. They argued that the observed positive supply shocks improved the financial situation of enterprises and enhanced debt service capacity of economic agents. A few of them also pointed out that August brought a slight increase in one of the core inflation measures.

While discussing NBP interest rates level, the majority of Council members believed that due to the sluggish economic activity, the risk of further weakening of economic growth, the deepening of the negative output gap and, consequently, higher risk of inflation remaining below target in the medium term, it was justified to cut interest rates significantly. They pointed to the signs of economic slowdown in Poland and its environment, further decline in prices and inflation expectations and the absence of wage pressure. At the same time, they emphasized that interest rate adjustment was necessary due to the increase in real interest rates resulting from the decline in inflation and inflation expectations observed in the past few quarters. In this context, they stressed that the current real interest rates had become relatively high as compared with those in the recent years. They also pointed out the lack of inflationary risks in the Poland's environment and the growing scale of monetary expansion in the euro area, leading to an increase in the disparity of interest rates in Poland as compared with its environment. Those members also emphasized that a moderate level of credit growth in the economy and the absence of signs of imbalance in the housing market limited risks to financial stability. These members also believed that due to lags in the transmission mechanism of monetary policy, the adjustment of NBP interest rates should be rather quick and significant. In this context, a few Council members assessed, that a significant interest rates cut would be justified if it was accompanied with the statement, that this decision denoted the one-off adjustment in the interest rates to the current economic forecasts.

Some Council members believed, however, that NBP interest rates should remain unchanged. They pointed out that the slowdown in economic activity in the recent period was driven by factors beyond the impact of domestic monetary policy, namely external shocks and persistent uncertainty. Accordingly, in the current situation, monetary policy instruments might prove ineffective in stimulating economic activity. They argued that low inflation resulted mainly from supply shocks, which boosted real incomes of households and enterprises, and thus should not be offset by monetary policy. A few of those Council members also believed that lower interest rates were likely to slow down the process of corporate restructuring. Other Council members assessed, that interest rates cut would be justified only in the case of a considerable slowdown in economic growth.

A few members of the Council additionally argued that interest rates cuts, through stimulating domestic demand, amidst weak demand abroad, could bring deterioration of the current account balance. Other members of the Council pointed out, however, that in the recent quarters Poland had experienced a trade surplus, and the current account deficit had been so far financed by foreign direct investment and the inflow of EU funds.

A few Council members also underlined that interest rate cuts may contribute to the fall in deposits in the banking sector. Other Council members pointed out, however, that the sharp decline in deposits, and consequently, an increase in currency in circulation, would be a rather unlikely development in response to NBP interest rates cuts. They also emphasized that the possible conversion of deposits into cash by economic agents would not negatively affect the stability of the banking sector considering the persistently high liquidity surplus in the Polish banking sector. They underlined that deposits withdrawn from the banking sector could be spent on consumption and investments.

The Council also discussed the width of the interest rate corridor of standing facilities. It was pointed out that should the reference rate be lowered, the current width of the corridor would be very large in relation to the basic interest rate level. It was also emphasized that the resulting reduction in the lombard rate would have an impact on the ceiling for the so-called maximum interest. The Council members also noted that should the reference rate and the rediscount rate be lowered, the interest on the required reserve – assuming it was computed using the current method – would be higher than the interest rate of basic open market operations.

At the meeting a motion was submitted to lower NBP reference rate and NBP rediscount rate by 0.5 percentage points as well as a motion to lower NBP lombard rate by 1.0 percentage point. The motions passed. The motion was also submitted to change the remuneration on the required reserve funds to 0.9 of the reference rate. The motion passed.

The Council set the NBP interest rates at the following levels: the reference rate at 2.00%, the lombard rate at 3.00%, the deposit rate at 1.00%, the rediscount rate at 2.25%.

**Minutes of the Monetary Policy Council decision-making meeting held on 5 November 2014**

Members of the Monetary Policy Council discussed the monetary policy decisions against the background of macroeconomic developments in Poland and abroad, as well as the November projection of inflation and GDP.

Some Council members emphasized that current and expected economic conditions in Poland's external environment had deteriorated in recent months. It was noted that forecasts for global economic growth prepared by external institutions had been again revised downwards. This included also forecasts for growth in the euro area, which is expected to remain stagnant in the coming quarters. It was emphasized that concerns about a prolonged stagnation in the euro area were rising. Some Council members also pointed to economic slowdown in major emerging market economies. It was indicated that growth in China was weakening and economic stagnation was likely to have occurred in Russia, while recession in Ukraine was deepening. Some Council members assessed that slower economic growth in emerging market economies would affect GDP growth in the euro area. This concerns in particular Germany, Poland's main trading partner, whose export share to these economies is large. However, other Council members pointed to signs of improvement in industry, including in the euro area and Germany, that were appearing irrespective of unfavourable external conditions. Attention was also drawn to ongoing moderate economic recovery in the United States. Moreover, according to these Council members, economic growth in the euro area next year may be slightly faster than this year.

While discussing inflation developments abroad, it was highlighted that inflation in many economies was still low, including countries with relatively robust growth. Council members pointed out that inflation in the euro area was very low and still declining. Few Council members observed that in some countries strongly linked to the euro area, price growth was negative. It was emphasized that low global inflation resulted from a decline in commodity prices in global markets and relatively weak global economic growth, which – according to few Council members – indicates that attempts to accelerate price growth by means of domestic monetary policy would prove ineffective.

While discussing monetary policy abroad, it was noted that it remained strongly expansionary in the case of major central banks. Particularly, although the Federal Reserve had concluded its financial asset purchases, it would continue to roll over maturing debt securities. Few Council members pointed out that the Federal Reserve was signalling interest rate increases in the following year. On the other hand, the European Central Bank started purchasing securities in October, whereas the Bank of Japan increased financial asset purchases to a significant extent. In this context, it was highlighted that the European Central Bank intended to continue purchasing securities for at least two years, and the interest rates in the euro area might stay close to zero even over a longer term. Attention was also drawn to interest rate decreases in countries strongly linked to the euro area, including economies which were still growing at a relatively fast pace. Moreover, few Council members pointed out that the expansionary monetary policy of the major central banks had resulted in an increased upward pressure on currencies of some countries with a significant interest rate differential to the major economies.

While discussing economic conditions in Poland, the Council members emphasized that in 2014 Q3 the economic growth had probably continued to decelerate. Some Council members indicated the slowdown in economic growth could be shallow. It was noted that the slowdown had been caused mainly by weaker external demand, which was translating into slower export growth, and declining sentiment of economic agents, which resulted in a deceleration in private investment outlays. These factors of economic slowdown are reflected in the incoming data, which show that export growth has almost come to a halt and export orders have decreased, while industrial production in 2014 Q3 grew slower than a quarter before, on average. However, some Council members pointed out that recent data readings might indicate recovery in economic activity in the coming quarters. In particular, in September both industrial production and construction output increased, while sentiment improved after several months of decline. Moreover, a gradual acceleration of corporate lending and stable growth of housing loans suggest that growth in investment demand in 2014 Q3 might remain moderate. Some Council members also pointed to still favourable consumer confidence, stable retail sales growth and a steady increase in employment. They indicated that the probability of finding a job had increased, while the probability of losing a job remained stable.

While discussing the economic outlook for Poland, Council members highlighted that the November projection pointed to lower GDP growth than in the previous round. However, some Council members emphasized that in accordance with the central projection path, i.e. the most likely outcome, the annual GDP growth would start to slightly accelerate in 2015 Q2. Economic growth should then stabilise above 3%, i.e. will grow at a pace close to potential output growth. This underpins the view expressed by these Council members that – notwithstanding the adverse external conditions – economic outlook for Poland remains favourable. Furthermore, these members cited external forecasts, which also suggested that moderate recovery of the Polish economy could resume in the following quarters. At the same time, some Council members stressed that the probability of economic growth being weaker than indicated by the central projection path was significant. This is demonstrated in strong asymmetry of the probability distribution in GDP projection, associated mainly with the risk of prolonged weak economic growth in the euro area. These members also highlighted that several external institutions had revised their forecasts for economic growth in Poland downwards and that the uncertainty related to global economic conditions continued.

Referring to inflation developments in Poland, Council members noted that in September the annual growth of consumer price index was still negative. It was emphasized that although deflation in Poland had been caused largely by external factors (reflected, in particular, in a decline in food and energy prices), the price growth in Poland had been also dampened by no demand pressure, as most core inflation indicators were at zero. In this context, it was highlighted that wage and cost pressures in the economy were still low, as shown by the weak growth of unit labour costs and the continued decline in producer prices on an annual basis.

With regard to the outlook for inflation, it was emphasized that in the November projection the inflation path was below the July projection, and stayed below the NBP inflation target throughout the projection horizon. At the same time, some Council members highlighted that, like for the GDP projection, the asymmetry in the balance of risks for the inflation forecast was significant. This points to a relatively high probability of inflation staying below the central path. These members pointed out that, in contrast with the July projection, the output gap would remain negative throughout the November projection horizon. Therefore, the period of low demand pressure will be longer than envisaged in the previous projection. They also argued that external forecasts supported the view that inflation in Poland would remain low. On the other hand, other Council members emphasized that, in line with the central projection path from November, inflation should rise gradually, to return to the band for deviations from the target by the end of the projection period. According to these Council members, inflation might be slightly higher than in the November projection, returning close to target within the monetary policy horizon, as indicated by several forecasts.

While discussing the interest rate decision, some Council members assessed that the monetary policy adjustment should be continued at the November meeting. In their opinion, factors in favour of further interest rate adjustment included ongoing deflation, very low inflation expectations and the forecasts indicating that inflation would remain below the target in the following years. Further monetary policy adjustment was also justified by a deceleration in domestic economic growth and a risk of further slowdown due to the weakening economic growth outlook in the external environment of the Polish economy. In the opinion of these Council members, further decrease in interest rates would cushion the adverse impact of weakening external demand on domestic economic activity growth. Moreover, they emphasized that the persistence of the significant interest rate differential between Poland and its external environment might result in later return of inflation to its target through upward pressure on the zloty. Few Council members noted that interest rate decreases would reduce the public debt servicing costs and therefore support the economic policy of the Government.

Nonetheless, the majority of Council members were of the opinion that the interest rates should remain unchanged at the November meeting. These members argued that the slowdown in GDP growth could be temporary and shallow. They also emphasized that the decrease in inflation and the weakening in economic activity were mainly driven by factors beyond the impact of domestic monetary policy, including significant uncertainty undermining the growth of spending by private agents. Few Council members stressed that after the NBP reference rate had been decreased in October, another large cut would imply that the real interest rates deflated by inflation expected over the monetary policy horizon would be near zero or even negative, which could result in emergence of economic imbalances. In the opinion of some Council members, further interest rate decreases could stimulate excessive credit growth in the economy and weaken the incentives to restructure enterprises. In the assessment of the Council members who were in favour of keeping interest rates unchanged, given the current level of interest rates there is still space for monetary policy easing, should it become necessary in case of significant turbulence in global financial markets.

Some of the Council members who supported keeping interest rates unchanged assessed that the October adjustment of interest rates provided sufficient monetary policy impulse to support the return of inflation to close to the target within the monetary policy horizon, in the light of the current data and the November projection results. Few of them also emphasized a need for an assessment period to analyse the impact of the October interest rate cut. They also highlighted that prudent monetary policy was a value which should be preserved in order to maintain macroeconomic and financial stability. However, these members indicated that uncertainty over economic conditions in the future had recently increased. Hence, they did not exclude a possibility of further monetary policy adjustment if economic conditions deteriorate in Poland and abroad, particularly in the euro area.

At the meeting a motion was submitted to lower NBP interest rates by 1.00 percentage point. The motion did not pass. A motion was also submitted to lower NBP interest rates by 0.50 percentage points. The motion did not pass. A motion was also submitted to lower NBP interest rates by 0.25 percentage points. The motion did not pass. The Council decided to keep NBP interest rates at the following levels: the reference rate at 2.00%, the lombard rate at 3.00%, the deposit rate at 1.00%, the rediscount rate at 2.25%.

**Minutes of the Monetary Policy Council decision-making meeting held on 3 December 2014**

Members of the Monetary Policy Council discussed the monetary policy decisions against the background of macroeconomic developments in Poland and abroad.

While discussing business conditions in Poland's external environment, Council members pointed out that global activity growth remained moderate. It was emphasized, that the business conditions in the United States remained favourable. Few Council members also noted that the economic situation in the euro area had slightly improved. However, some Council members pointed out that economic growth in the euro area remained sluggish and business climate indicators point to low activity growth probably continuing in the following quarters. Slow GDP growth in Germany – Poland's main trading partner – was highlighted, along with the decline in the PMI index for that country. With regard to the situation in the largest emerging economies, it was observed that also in these countries economic activity remained relatively slow, with growth weakening further in China.

While discussing monetary policy abroad, it was stressed that major central banks continued to pursue highly expansionary monetary policy. In particular, the European Central Bank was keeping its interest rates at a historically low level, while simultaneously running an asset purchase programme; the European Central Bank does not exclude the possibility that the programme might be expanded to include more instruments. According to few Council members this could limit the risk of deflation in the euro area.

While discussing economic situation in Poland, Council members observed that GDP growth in 2014 Q3 had weakened only slightly and was higher than expected. Some Council members also highlighted the favourable structure of GDP growth. They pointed to flagging external demand as the principal source of weaker economic growth. Domestic demand, in turn, remained relatively robust, supported by a stable expansion in consumer demand and steeper growth in investment spending. Some Council members also pointed to rising business climate indicators, faster than a year ago credit growth and a further improvement in labour market conditions. Other Council members emphasized that retail sales growth and industrial output growth had remained low in October, while construction and assembly output had declined, which might signal further growth weakening in 2014 Q4. Few Council members believed that this enhanced the risk of slower growth in investment expenditures in the Polish economy. Some Council members also drew attention to the fact that nominal GDP growth – due to GDP deflator having sunk almost to zero – was running at one of the lowest levels in the past decade. Slow nominal growth hampers the process of reducing the debt in relation to GDP – both public and private. In the opinion of those Council members, moderate real GDP growth coupled with core inflation running close to zero, corroborate the existence of negative output gap in Poland. Yet, other Council members believed that despite a slight slowdown, GDP growth was running close to that of the potential output, with domestic demand growing even faster. According to those Council members, should robust expansion in domestic demand be sustained, it might boost the current account deficit, currently being contained by the declining commodity prices.

While discussing the prospects for economic growth in Poland, some Council members stressed that both the baseline scenario of the November projection and internal short-term forecasts pointed to only slight weakening of GDP growth in the coming quarters, with a subsequent return of moderate recovery. Council members pointed out that since the current weakening of GDP growth had mainly been driven by external factors, future economic growth in the euro area would be of particular significance to economic activity trends in Poland. Few Council members argued that a slight rise in economic growth expected in the euro area over the next few quarters would support GDP growth in Poland. Yet, other Council members highlighted the continued risk of prolonged low economic growth in the euro area, which might adversely affect GDP growth in Poland in the longer term.

With regard to inflationary processes at home, it was pointed out that the annual consumer price growth fell yet again in October and was running below the forecasts. Consumer prices deflation was accompanied by a further decline in producer prices in industry. Some Council members emphasized that inflation in Poland was currently driven mainly by external factors bringing about, above all, a decrease in energy and food prices. Few of the Council members were of the opinion that such sources of negative price growth were indicated by sound – despite a rapid rise in the corporate wage bill – financial performance of enterprises, as well as a decline in corporate operating costs, in particular costs of materials. Some Council members, in turn, emphasized the absence of demand pressure as a factor, which, along with external factors, contributed to lower inflation. In the opinion of those Council members this was indicated by a further decline in core inflation indices, whose average – for the first time on record – sank below zero.

Some Council members also pointed to very low inflation expectations of households and businesses, and declining inflation expectations of professional forecasters. At the same time, it was emphasized that inflation forecasts had been once again revised downwards, indicating that deflation was likely to persist somewhat beyond the end of 2014. In the opinion of few Council members, CPI growth in Poland might remain relatively low in the longer term, due to the persistent downward trend in commodity prices in the global markets. Yet, other members of the Council argued that the impact of lower commodity prices on inflation should be short-lived. While discussing the outlook for inflation, attention was also drawn to a significant impact of future exchange rate of the zloty on price developments.

While referring to the possible effects of deflation in Poland, it was emphasized that considerable uncertainty remained as to its impact on decisions of economic agents, in particular enterprises. In addition, it was noted that economic consequences of deflation would depend on its level, sources and duration. Some Council members pointed out that extended period of negative price growth increased the risk of inflation expectations remaining at low levels and – as a consequence – adverse effects of deflation on the economy. Other Council members argued, however, that no negative effects of deflation on decisions of businesses and households had been observed so far. They pointed out that 2014 Q3 brought an acceleration in growth of consumption and investment, and enterprises continued to post good financial results. Financial results of enterprises were supported by declining production costs driven by falling commodity prices. In the opinion of few members of the Council, deflation in the coming months would not adversely affect economic growth; on the contrary, it could rather support consumption and investment, as its main driving force was the decline in agricultural and energy commodity prices.

While discussing the interest rate decision, most members of the Council believed that at the current meeting interest rates should remain unchanged. Some Council members indicated that the decline in GDP growth was slight, and its growth prospects in the coming quarters remained relatively favourable. According to those Council members, the weakening of GDP growth and deflation were mainly driven by external factors and therefore the impact of domestic monetary policy on economic processes was limited. Few members of the Council pointed out that – considering current inflation forecasts – the level of real interest rates ex ante was at present relatively low, while other Council members stressed that the real interest rates deflated with current CPI were higher than the nominal interest rates. According to few members of the Council, further interest rate cuts could lead to external imbalances and excessively boost credit growth in the economy, including lending to households, which did not finance investments supporting growth of potential output. Those members were also of the opinion that low interest rates weakened the selection of economic agents and – consequently – inhibited productivity growth. In this context, they pointed to the recent years' very low contribution of the movement of production factors between sectors to productivity growth. Other Council members indicated that without growing consumption and with flagging external demand also private investment would decelerate.

Few Council members also argued that interest rates if kept unchanged at the current meeting would leave room for possible easing of monetary policy in the event of a significant economic downturn or disturbances in the financial system.

Some Council members who were in favour of keeping interest rates unchanged at the current meeting emphasized that they did not rule out the possibility of a further adjustment of interest rates. In the opinion of those members, lowering of interest rates could be justified by longer periods of price declines, increasing the risk of adverse effects of deflation on the economy. Interest rate adjustment would also be justified if the incoming data confirm that the slowdown in domestic economic activity would prevail and that weak growth in the environment of the Polish economy was likely to continue. Some Council members also pointed out that persisting significant spread in interest rates between Poland and its environment would increase the risk of appreciation of the zloty, which, in turn, could delay the return of inflation to the target. Few members argued that interest rate cuts would reduce the spread between the deposit rate and the expected rates of return on investment, which would, in turn, support growth in investment outlays and limit the negative impact of deflation on businesses' propensity to invest.

Few Council members were of the opinion that amidst persistently negative price growth and moderate GDP growth, as well as the high likelihood of inflation remaining below the target in the event of low probability of significant acceleration of economic growth in the coming quarters, it was justified to lower interest rates considerably already at the current meeting. According to those members of the Council, such decision was also supported by the fact that interest rate cuts in the absence of inflation risk would reduce the public debt servicing costs and thus support the government's economic policy. These members also believed that interest rate cuts – reducing their spread between interest rates in the environment of the Polish economy – would minimize the risk to the country's financial stability related to the potential inflow of speculative capital and its subsequent outflow.

At the meeting a motion was submitted to lower the NBP interest rates by 1.00 percentage point. The motion did not pass. The Council decided to keep the NBP interest rates at the following levels: the reference rate at 2.00%, the lombard rate at 3.00%, the deposit rate at 1.00%, the rediscount rate at 2.25%.

# Appendix 7. Voting records of the Monetary Policy Council members on motions and resolutions

Voting records of Monetary Policy Council Members on motions and resolutions in 2014 are presented below:

- **Date: 8 January 2014**

Subject matter of motion or resolution:
Resolution No. 1/GP/2014 on granting consent to the member of the Monetary Policy Council Jerzy Osiatyński to participate in activities of an international organisation.

Voting of the MPC members:

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

- **Date: 21 January 2014**

**Subject matter of motion or resolution**:
Resolution No 2/GP/2014 on granting consent to the member of the Monetary Policy Council Adam Glapiński to participate in activities of international organisations.

**Voting of the MPC members**:

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

A. Bratkowski was absent.

### ▪ Date: 18 February 2014

**Subject matter of motion or resolution**:
Resolution No. 3/GP/2014 on granting consent to the member of the Monetary Policy Council Jerzy Hausner to participate in activities of an international organisation.

**Voting of the MPC members**:

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

### ▪ Date: 8 April 2014

Subject matter of motion or resolution:
Resolution No. 1/2014 on approving the Annual Financial Report of the National Bank of Poland prepared as of 31 December 2013.

Voting of the MPC members:

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

**Date: 6 May 2014**

Subject matter of motion or resolution:
Resolution No. 2/2014 on approving the report on monetary policy implementation in 2013.

Voting of the MPC members:

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

**Date: 6 May 2014**

Subject matter of motion or resolution:
Resolution No. 3/2014 on the evaluation of the activities of the NBP Management Board as regards the implementation of the monetary policy guidelines for the year 2013.

Voting of the MPC members:

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

### Date: 20 May 2014

Subject matter of motion or resolution:
Resolution No. 4/2014 on approving the report on the operations of the National Bank of Poland in 2013.

**Voting of the MPC members:**

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

### Date: 3 September 2014

Subject matter of motion or resolution:
Motion to lower the NBP interest rates by 0.5 percentage points.

**MPC decision:**
Motion did not pass.

**Voting of the MPC members:**

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

J. Winiecki was absent.

### ▪ Date: 3 September 2014

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

J. Winiecki was absent.

### ▪ Date: 16 September 2014

Subject matter of motion or resolution:
Resolution No. 5/2014 on adopting Monetary Policy Guidelines for 2015.

**Voting of the MPC members:**

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

A. Zielińska-Głębocka was absent.

### ▪ Date: 8 October 2014

**Subject matter of motion or resolution:**

Motion to lower the NBP reference and rediscount rates by 0.5 percentage points.

**MPC decision:**

Motion passed.

**Voting of the MPC members:**

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

### ▪ Date: 8 October 2014

**Subject matter of motion or resolution:**

Motion to lower the NBP lombard rate by 1.0 percentage point.

**MPC decision:**

Motion passed.

**Voting of the MPC members:**

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

**Date: 8 October 2014**

**Subject matter of motion or resolution:**

Resolution no 6/2014 on reference rate, refinancing credit rate, deposit rate and rediscount rate at NBP.

**MPC decision:**

The Council lowered the NBP reference and rediscount rates by 0.5 percentage points and the NBP lombard rate by 1.0 percentage point.

**Voting of the MPC members:**

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

**Date: 8 October 2014**

**Subject matter of motion or resolution:**

Resolution No. 7/2014 on the required reserve ratios for banks, cooperative savings and credit unions and the National Association of Cooperative Savings and Credit Unions and the remuneration of required reserves.

**MPC decision:**

The Council decided that required reserve funds will be remunerated at 0.9 of the NBP reference rate.

**Voting of the MPC members:**

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

E. Chojna-Duch and J. Winiecki were absent.

### ▪ Date: 5 November 2014

**Subject matter of motion or resolution:**
Motion to lower the NBP interest rates by 1.0 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
E. J. Osiatyński
A. Rzońca
J. Winiecki
A. Zielińska-Głębocka

### ▪ Date: 5 November 2014

**Subject matter of motion or resolution:**
Motion to lower the NBP interest rates by 0.5 percentage points.

**MPC decision:**
Motion did not pass..

**Voting of the MPC members:**

**For:** M. Belka
A. Bratkowski
E. J. Osiatyński
A. Zielińska-Głębocka

**Against:** E. Chojna-Duch
A. Glapiński
J. Hausner
A. Kaźmierczak
A. Rzońca
J. Winiecki

## ▪ Date: 5 November 2014

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

## ▪ Date: 3 December 2014

**Subject matter of motion or resolution:**

Motion to lower the NBP interest rates by 1.0 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 |
| | | | E. J. Osiatyński |
| | | | A. Rzońca |
| | | | J. Winiecki |
| | | | A. Zielińska-Głębocka |

## Date: 3 December 2014

**Subject matter of motion or resolution:**

Resolution No. 8/2014 on approving the Financial Plan of the National Bank of Poland for 2015.

**Voting of the MPC members:**

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

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