NBP

National Bank of Poland

Monetary Policy Council

# MINUTES OF THE MONETARY POLICY DECISION TAKING MEETING HELD ON 9 JANUARY 2013

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

While analysing the external conditions, it was pointed out that the global economic conditions remained weak. Yet, the uncertainty about the short-term global economic outlook had abated, mainly due to a partial agreement on the scale of fiscal tightening in 2013 in the US, development of institutional reforms in the euro area and further monetary policy easing by main central banks. These factors had also contributed to an improvement in financial market sentiment. At the same time, attention was drawn to protracted recession and continued fiscal tightening in a majority of the euro area member states. It was also indicated that the attempts to reduce general government sector imbalances might curb GDP growth and trigger a further rise in the unemployment rate in some euro area countries in the short term. A few members of the Council argued, however, that in 2013 Germany, Poland's main trading partner, was likely to experience higher GDP growth compared with other euro area countries. Yet, other Council members judged that although some improvement in the global economic conditions might be expected in the coming quarters, economic growth abroad would remain relatively weak.

While addressing economic conditions in Poland, the Council members agreed that the incoming data confirmed further weakening in economic activity in 2012 Q4. It was emphasised that the slowdown was driven by both external and internal factors. It was pointed out that the economic growth in 2012 Q4 was most probably below the November projection.

In the opinion of some Council members, the incoming data, including retail sales data, suggested that the consumption growth could be close to zero in 2012 Q4. While analysing factors behind a slowdown in consumption growth, the Council members pointed to a decline in real disposable income, driven, in particular, by deteriorating labour market conditions. It was emphasised that the slowdown in consumer spending growth was accompanied with a decline in the savings rate to its historical low.

While addressing investment activity, the opinion was expressed that investment growth had probably remained negative in 2012 Q4. Attention was drawn to considerable cuts in public investment expenditure, in particular of local governments, at the end of 2012, related to the necessity of reduction in fiscal imbalances. As regards corporate investment, a few Council members pointed out that in the previous years, strong investment growth had been supported by excessively optimistic sentiment in corporate sector and EU funds inflow.

While discussing the recent developments in the banking sector, a few Council members pointed to still tight lending conditions and slowing deposit growth. Against this background, they also indicated that, following interest rate cuts by the NBP at the previous Council meetings, the interest on deposits fell significantly stronger compared with the interest on loans.

While addressing the Polish economic outlook, the Council members pointed out that GDP growth would stay low in the coming quarters. Consumption would be still adversely affected with slow growth in disposable income of households, driven by the deteriorating labour market conditions, and a higher effective personal income tax rate as of 2013. As regards the labour market conditions, some Council members expected further deterioration, which would be likely reflected in a further rise in the unemployment rate. A few Council members pointed out that the rise in the disability pension contribution in 2012 and a relatively high relation between the minimum and the average wage might dampen the labour demand. Moreover, consumption will be adversely affected with limited room for a further decline in savings rate. While analysing the investment outlook, the Council members assessed that, in particular, a further decline in the estimated value of newly launched investment projects suggested that the investment growth would stay negative in the coming quarters. It was pointed out that a decline in investments of central government and of local governments co-financed with the EU funds would also be conducive to a fall in investment expenditure. At the same time, it was assessed that economic growth would further be supported mainly by net exports. Therefore, demand prospects in the euro area posed a risk to Polish economic outlook. Some Council members were of the opinion that economic growth in Poland might increase along with the likely rebound in economic activity abroad in the second half of 2013.

While addressing inflation developments in the Polish economy, the Council members pointed out that the CPI inflation had declined notably in recent months and had been close to the NBP target in November. It was emphasised that the decline in CPI inflation had been largely driven by slower growth in the commodity prices, including food and energy, which previously had contributed to faster price growth. Core inflation had also declined, indicating no demand pressure. Against this background, attention was paid to a downward revision in inflation expectations of both households and corporates. At the same time, the majority of the Council members believed that in the coming months inflation would decline further and then stabilize below the inflation target for at least one year. In the opinion of the Council members, the decline in inflation would be driven by both decreases in energy prices as of January 2013, negative output gap and lack of wage pressure in the economy. At the same time, some Council members pointed at uncertainty about inflation developments in the longer term. This uncertainty was driven, in particular, by possible considerable changes in commodity prices in the global markets as well as in utility prices. Moreover, a few Council members pointed out that although in 2013 a further decline in core inflation could be expected, it would probably stay elevated considering this business cycle stage.

While discussing the NBP interest rates, as at previous meetings, it was assessed that at the current meeting the NBP interest rates should continue to be lowered, which should support economic activity and reduce the risk of inflation falling below the target in the medium term. Yet, the Council members differed in their opinion as to the scale of cuts in NBP interest rate, both at the present meeting and during the entire cycle.

The majority of the Council members indicated that the incoming data – confirming the previously anticipated decline in inflation and protracted economic slowdown – did not justify a greater scale of cuts in the NBP interest rates at the current meeting. In the opinion of these Council members, also the risks related to growth in prices, in particular for commodities, advocated for maintaining the current scale of interest rate cuts. A few Council members also indicated that a sharp decrease in interest rates might lead to further decline in the propensity to save.

On the other hand, in the opinion of a few Council members, as the inflation was likely to stay below the NBP inflation target in the coming quarters, the NBP interest rates should be lowered more – or even far more – at the current meeting. These members pointed out that in particular the length of lags in the transmission mechanism would justify a relatively prompt monetary policy easing.

While referring to future decisions, the majority of the Council members did not rule out further monetary policy easing, should the incoming data, including the 2012 GDP data, confirm a protracted economic slowdown and should the risk of increase in inflationary pressure remain limited. In turn, other Council members declared that the already effected interest rate cuts were sufficient to limit the risk of inflation running significantly below the target in the medium term, and that the impact of potential further cuts in the NBP rates on economic activity would be small. At the same time, in the opinion of a few of these Council members, further monetary policy easing could, in the longer term, trigger a growth in imbalances in the Polish economy.

At the meeting, a motion was submitted to lower the NBP basic interest rates by 1.25 percentage points. The motion did not pass. A motion was also submitted to lower the NBP basic interest rates by 0.50 percentage points. The motion did not pass. At the meeting, a motion was also submitted to lower the NBP basic interest rates by 0.25 percentage points. The motion passed. The Council decided to decrease the NBP basic interest rates by 0.25 percentage points to the following levels: reference rate to 4.00%, lombard rate to 5.50%, deposit rate to 2.50% and rediscount rate to 4.25%.

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