Minutes from 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

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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%.

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