MINUTES OF THE MONETARY POLICY COUNCIL DECISION-MAKING MEETING HELD ON 7 MARCH 2012

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

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

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

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

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

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

While addressing the situation in the labour market, members of the Council pointed out that the January data on employment and wages in the enterprise sector might be considerably distorted by temporary factors. Some members of the Council assessed that the persistently elevated unemployment had a mitigating effect on wage pressure, and, consequently, inflationary pressure.

Other members of the Council argued that moderate wage growth in the recent period, combined with heightened inflation observed for more than a year now, increasing household maintenance costs, posed a risk of higher wage pressure. Few members of the Council also claimed that the observed moderate wage growth had been largely driven by rising labour supply, and, the anticipated halting of labour supply growth might consequently add to wage pressure.

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

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

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

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

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

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

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

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

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

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