MINUTES OF THE MONETARY POLICY COUNCIL DECISION-MAKING MEETING HELD ON 30 APRIL 2008

During the meeting the Monetary Policy Council discussed the outlook for the future inflation developments in the context of the past, current and, primarily, anticipated economic situation.

The discussion at the meeting focused on: current inflation developments, including changes in administered prices and food prices, situation in the labour market, exchange rate developments, the outlook for economic growth and the level of interest rates in Poland and abroad. The Council discussed the influence of these factors on the future inflation in Poland.

While commenting on the current inflation, the Council analysed the reasons behind a slight decline in annual consumer price growth in March, which, however, remained above the upper limit for deviations from the NBP's inflation target set at 3.5%. It was argued that the fact that annual CPI inflation proved lower than in February followed from some decline in the annual food and fuel price growth. At the same time, it was pointed out that net core inflation increased in March, mainly due to a further acceleration in administered prices (prices of services connected with flat or house maintenance and some other services) and also because of an unexpected increase in prices of clothing and footwear. Some members of the Council emphasised that the heightened annual consumer price growth was mainly sustained by the continuing, despite some decrease, of the high growth of food and fuel prices and also by rises in administered prices in 2008 Q1. Those members also pointed out that the heightened inflation was also observed in many other countries and stressed that in Poland its level was lower than in other Central and Eastern European countries.

While discussing the outlook for inflation in 2008-2009, it was pointed out that rising administered prices, especially those of energy and natural gas, would be a factor increasing inflation. Some Council members underlined that rises in administered prices, combined with the previously observed strong increases in food and fuel prices, might translate into a rise in perceived inflation and thus also boost inflationary expectations. Those members pointed out that the surveys of inflation expectations of households in April revealed an increase in the percentage of respondents expecting inflation to stabilise at its current high level or to rise further. In this context, they pointed out that the monetary policy should account for the related increased risk of second-round effects. Moreover, some Council members assessed that the increased growth of the prices of clothing and footwear in March may be signalling a weakening in the disinflationary impact of globalisation processes and intensified competition in the market of internationally traded goods on the Polish economy. Other members of the Council, however, believed that it was difficult to assess at the moment whether the increased growth of clothing and footwear prices would indeed prove permanent.

While discussing the path of food prices, it was assessed that the high growth of these prices observed since the second half of 2007 would most probably ease in the months to come, which was indicated, among others, by the prices of futures contracts in the world food markets and the positive forecast of this year's harvest in Poland and other European countries.

Some Council members emphasised that high current inflation and the already introduced and expected rises of administered prices might be of importance for Poland as regards its compliance with the Maastricht price stability criterion. In this context, the Council members pointed to the need to appropriately coordinate the fiscal and monetary policies in the period preceding Poland's accession to the euro area.

While analysing developments in the environment of the Polish economy, it was pointed out that the symptoms of a slowdown in the United States had deepened and the activity in some Western European economies had lowered. It was stressed that there had been a downward revision of growth forecasts for the global economy in 2008-2009, particularly the forecasts for the United States and the euro area. Some Council members emphasised that the appreciation of the euro against the US dollar and pound sterling observed over the past months was a factor strengthening the negative impact that the economic slowdown in the United States and the United Kingdom had on GDP growth in the euro area. They assessed that the deceleration of economic growth in Western European countries, in combination with the zloty appreciation observed over the past months, may be lowering the growth rate of Polish exports and, consequently, have a negative impact on GDP growth in Poland. They also argued that the weakening of the foreign demand might persuade enterprises to limit their investment, which would additionally decrease GDP growth.

While assessing the outlook for economic growth in Poland, it was pointed out that the growth of industrial output and retail sales in March was lower than in the previous two months and significantly below expectations. In the opinion of some Council members those data may be a signal of reduced activity in the Polish economy in the coming period. Other members of the Council believed that it was difficult to assess at the moment whether the weaker than expected data for March indeed suggested a weakening economic growth. Those members argued that the low industrial output growth in March could have been connected with the Easter holiday break and the growing propensity of Poles to take more days off work in the holiday period. They pointed to the results of business confidence surveys, according to which the overall economic sentiment in Poland was still good. In the assessment of those Council members, the extent of a possible decline in economic growth in Poland would be significantly smaller than in the United States or the euro-area.

While addressing the situation in the labour market, it was pointed out that the wage and employment growth in the enterprise sector in March was still high, which was conducive to increasing the demand pressure. It was emphasised that wage growth was still exceeding productivity growth, resulting in a further rise in unit labour costs. Some Council members, however, pointed to the fact that the continuously high growth of wages would be conducive to deteriorating the financial standing of enterprises, which would make further high pay rises impossible. Moreover, some Council members argued that the wage pressure in the coming period may in fact be easing due to a probable reduction in the scale of economic emigration of Poles, connected with weaker economic growth and worsening situation in the labour markets of Western European countries, particularly the United Kingdom and Ireland. They pointed out that the scale of emigration may be reduced by the zloty exchange rate appreciation observed over the last months which decreased the zloty value of income of Poles working abroad.

Some Council members argued that, apart from high wage growth, domestic demand may be additionally driven by growth in credit aggregates, including consumption loans granted to households, which continued at a high level. Other members of the Council underlined that since the beginning of 2008 the deposits of households had been increasing rapidly, which might suggest an increased propensity to save and be conducive to easing the demand pressure. Moreover, they also argued that the positive balance of the central government budget in 2008 Q1 was additionally lowering the demand pressure.

While discussing the exchange rate developments, it was pointed out that in April the zloty exchange rate appreciated significantly both against the US dollar and against the euro and was stronger than accounted for in the February inflation projection. It was underlined that the zloty exchange rate appreciation was conducive to easing the domestic inflationary pressure, as it resulted in a reduction of prices of imported goods expressed in the zloty, and particularly that it weakened the impact of high fuel price growth in the world markets on the Polish economy. At the same time, however, some Council members pointed out that the zloty appreciation also reduced the zloty denominated value of EU structural funds allocated for the financing of investment projects, which may impede the implementation of those projects and lead to lowering investment growth.

While discussing monetary policy, some Council members stressed that against the background of other countries of the region the level of real interest rates in Poland was relatively high and that the monetary policy tightening in recent months had been effected at a relatively fast pace. Those members pointed out that some central banks had lowered their interest rates over the past months despite the persistently high inflation in those countries, and stressed that the appreciation of the real zloty exchange rate was additionally increasing the restrictiveness of monetary policy in Poland. They argued that a further monetary policy tightening in Poland would increase interest rate disparity between Poland on the one hand and the United States and the euro area on the other, which might encourage the inflow of short-term capital to Poland and be conducive to excessive zloty exchange rate appreciation. In the opinion of those members, this would weaken the competitiveness of the Polish economy and reduce the profitability of export production and thus would lead to further deepening of external imbalance. Other members of the Council, however, argued that, due to a large import intensity of export production, the zloty exchange rate appreciation did not significantly reduce the profits of exporters, which may be confirmed, among others, by the data on the financial results of enterprises in 2007. Moreover, some Council members thought that it was currently difficult to assess the sustainability of the factors which had led to the recent appreciation of the zloty. Some members of the Council also assessed that a rise in interest rate disparity would be increasing the share of loans denominated in foreign currencies in total loans, which might weaken the impact of domestic monetary policy on domestic demand. They pointed out that since the beginning of 2008 an increase had been observed in the share of housing loans denominated in foreign currencies in the total housing loan debt of individuals.

While discussing the interest rate decision, the Council assessed that the continuing high growth of wages and employment, along with the possibility of increased inflation expectations resulting from higher current inflation and the expected further increase of administered prices, both pointed to the risk of inflation remaining above the inflation target in the medium term. In the opinion of some Council members, these factors justified an interest rate increase already at the April meeting. In the opinion of the majority of the Council, however, the risk of a decrease in economic growth in Poland and of an excessive appreciation of the zloty exchange rate, both of which would be reducing inflation in the medium term, justified no interest rate change at the current meeting.

A motion to raise the key NBP interest rates by 25 basis points was put forward at the meeting. The motion did not pass. The Council kept the interest rates unchanged: the reference rate at 5.75%, the lombard rate at 7.25%, the deposit rate at 4.25% and the rediscount rate at 6.00%.

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