MINUTES OF THE MONETARY POLICY DECISION MAKING MEETING HELD ON 8 MAY 2013

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

Referring to external conditions, it was emphasized that signs of renewed weakening in the global economic conditions had appeared in recent months. It was indicated that in Q1 GDP growth in the United States had been lower than expected by market participants and the sentiment of the local economic agents had deteriorated. It was further argued that continued measures to reduce the general government sector imbalances in the United States might contain the economic growth in the coming quarters. Meanwhile, the euro area is likely to have remained in recession and a renewed deterioration in leading indicators in most of its member states, including Germany, may imply that the economic recovery may be delayed. A few Council members indicated at the same time that, according to external forecasts, economic conditions in Germany, the main trading partner of Poland, were set to improve gradually in the second half of the year. Referring to the recent data on economic activity abroad, it was also pointed out that the deteriorating economic conditions in developed countries translated into weaker growth in major emerging market economies.

While discussing price developments abroad, it was noted that inflation had declined in many economies, including the euro area. A few Council members emphasized, however, that core inflation in the euro area had remained stable, whereas lower price growth in the region, as in other economies, had largely resulted from a decrease in commodity prices, including food and energy, observed in recent months.

While referring to the monetary policy of the major central banks, it was highlighted that the European Central Bank had decreased interest rates in May, which had led to an increase in the spread between the interest rates in Poland and the euro area. Council members emphasized that highly expansionary monetary policy of major central banks may continue to contribute to stronger portfolio capital inflows to emerging economies, including Poland. This contributes to a rise in sovereign bond prices. However, this can lead to an increase in the volatility of sovereign bond prices over time, in particular amid rapid changes in risk aversion in global markets.

While discussing the recent data on the Polish economy, Council members pointed out that estimate of GDP in 2012 Q4, including investment expenditure, had been revised down. It was assessed that in 2013 Q1 economic growth had probably remained low, as indicated by a decline in industrial and construction output and real retail sales growth, which had been close to zero. Council members also emphasized that economic indicators in April – after a temporary improvement in previous months – had weakened again.

Council members expressed a view that the labour market conditions were not conducive to accelerating consumer demand growth. In particular, the employment in the corporate sector continues to decline, while the seasonally-adjusted unemployment rate increases, which translates into a weak wage growth. In this context, it was pointed out that the wage growth in the enterprise sector had been low and the real wage fund had declined. A few Council members noted, however, that the decline in inflation, in particular resulting from lower energy price growth, was conducive to strengthening the purchasing power of household incomes and to improving the financial position of enterprises.

While discussing the monetary developments, some Council members pointed out that the household and corporate loan growth had weakened further. At the same time, it was indicated that household and corporate deposits had increased in March. According to some Council members, the growth in household deposits could have been caused by an increase in the propensity to save amid economic slowdown and deterioration of the labour market. Against this backdrop, falling deposit interest rates do not contain the propensity to save. In this context, it was also noted that the decreases of NBP interest rates to date had been passed on into deposit rates to a greater extent than rates on loans, including in particular consumer loans.

While assessing the outlook for the economic activity in Poland, some Council members recognized that the uncertainty over the pace and timing of economic recovery had recently increased. This results in particular from deteriorating economic outlook abroad, which may translate into a lower contribution of net exports, the key demand factor of economic growth in the previous quarters, to GDP growth. Furthermore, some Council members emphasized no signals of a possible significant increase in domestic demand in the coming quarters. Some Council members also indicated that – due to higher than scheduled general government deficit in relation to GDP in 2012 and the likely upholding by the EU of excessive deficit procedure imposed on Poland – further fiscal tightening should be expected in the coming years, which would continue to contain demand growth. A temporary reduction in the investment co-financed with EU funds may be also conducive to lower economic activity. However, other Council members were of the opinion that the expected improvement in economic activity in Germany in the second half of 2013 should translate into a recovery in the Polish export sector. It was also noted that capacity utilization in the economy had grown in 2013 Q1, and that – in line with available forecasts – GDP growth should not decrease further and it is expected to accelerate gradually over coming quarters.

With reference to price developments, the majority of the Council members highlighted a further decrease of the CPI annual index, which has been running below the lower limit for deviations from the NBP inflation target since February 2013. Hence, the CPI inflation declined below the March projection. It was also stressed that core inflation had continued to decline, which confirms low demand pressure in the economy. At the same time it was indicated that a decline in food and energy price growth had significantly contributed to a decrease in inflation over recent months.

While assessing the outlook for inflation, the majority of Council members were of the opinion that in the coming quarters the CPI inflation was likely to stay below the March projection, which – along with the uncertainty over the pace of economic recovery in Poland – increases the risk of inflation running below the target in the medium term. Low inflation will also result from a decline in commodity prices in the global markets. Low inflation expectations of economic agents also point to no risk of a significant acceleration in the price growth. However, some Council members pointed out that given an expected global recovery in the second half of 2013, commodity prices in global markets may increase back in one-year time horizon. These members also emphasized that the March projection did not account for the impact of the maintaining heightened VAT rate on the level of inflation in 2014. However, other Council members noted that, even if no decrease in VAT rate was taken into account, inflation should remain below the March projection.

While discussing the level of the NBP interest rates, the majority of Council members assessed that they should be lowered at the current meeting. However, their opinions differed as to the scale of the decrease. In turn, other Council members were of the opinion that the interest rates should be kept unchanged.

The majority of Council members were of the opinion that an adjustment of monetary policy easing cycle was justified, as the incoming data did not indicate any clear signs of economic recovery in the Polish economy and its environment, while the decline in inflation was stronger than in the projection, which raised the risk of inflation staying below the target in the medium term. Moreover – despite the lowering of interest rates to date – faster than previously forecasted decline in inflation and inflation expectations had translated into an increase in real interest rates. At the same time, some Council members pointed out that – amid ample liquidity in global markets – a relatively high interest rate spread between Poland and developed economies might excessively intensify the portfolio capital inflows into Poland. According to a few Council members, the NBP interest rates should be adjusted as fast as possible, which supports the greater scale of their reduction at the current meeting.

However, other Council members believed that due to expected acceleration in the GDP growth in the coming quarters and upside risks to inflation, the NBP interest rates should not be lowered at the current meeting, and furthermore, a few of those Council members argued that the cycle of the monetary policy easing should be terminated. In their opinion, the NBP interest rates were already at their historical lows and further decreases in the NBP interest rates would not support demand in the economy to a significant extent. In their opinion, the current slowdown was attributable mainly to weak sentiment of economic agents and a low external demand growth. Moreover, a few Council members were of the opinion that further lowering of interest rates could also adversely affect the restructuring in the Polish corporate sector, which influences economic growth over longer run. Low interest rates might also boost excessively risky investment projects.

With reference to future decisions, some Council members reckoned that further interest rate decreases could be justified in the coming months if the probability of inflation running below the NBP target over the medium term rose. In the opinion of a few Council members, the results of the next inflation projection should be considered when assessing whether it could be justified to decrease the interest rates.

At the meeting, a motion was submitted to lower the NBP basic interest rates by 0.50 percentage points. The motion did not pass. A motion was also submitted to lower the NBP basic interest rates by 0.25 percentage points. The motion passed. The Council decided to lower the NBP basic interest rates by 0.25 percentage points to the following levels: reference rate to 3.00%, lombard rate to 4.50%, deposit rate 1.50%, rediscount rate to 3.25%.

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