Minutes from the Monetary Policy Council Decision Making Meeting held on 7 May 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 external developments, Council members pointed to a gradual improvement in business conditions. It was noted that after growth in the United States had come to a halt in early 2014, the latest data pointed to a rebound of economic activity. In addition, it was highlighted that – although the Federal Reserve was gradually reducing the scale of its asset purchases – monetary policy in the United States continued to be very accommodative.

Council members also pointed out that a gradual recovery continued in the euro area. It was emphasised that recovery in Germany – Poland's main trading partner – was somewhat stronger than in other euro area member states. However, weaker March industrial orders and business sentiment in Germany were brought to attention. It was also noted that sentiment in the financial markets of the euro area countries most severely affected by the debt crisis had improved, which should translate into easier access to credit, and further into a gradual improvement in economic conditions in some of these countries.

Council members emphasised that inflation in many countries, including in particular in the euro area, remained low despite the ongoing economic recovery. This may convince major central banks, including the ECB, to continue their accommodative monetary policies. A few Council members expressed the opinion that deflation in the euro area was increasingly less likely, as indicated by the upward revisions of some inflation forecasts for the euro area. These members also highlighted the risks to longer-term growth sustainability associated with further monetary policy easing by the ECB.

In their discussion on developments in the external environment of the Polish economy, a few Council members cited factors which could potentially be conducive to lower growth in developed countries in the coming years, particularly in the euro area. These factors included possible further fiscal consolidation, ageing population and a decline in investment outlays, including for R&D, in developed countries following the global financial crisis. Furthermore, a few Council members indicated that attempts by Chinese authorities to rebalance economic growth in China away from investments might weaken demand for Chinese imports of investment goods from developed countries, particularly from Germany.

Referring to economic conditions in emerging market economies, it was noted that Chinese growth had weakened in 2014 Q1. Attention was also drawn to a deterioration in economic outlook for Ukraine and Russia, which was related to the Ukrainian crisis.

While discussing the impact of the Ukrainian crisis on the Polish economy, the majority of the Council members judged that the mounting turmoil in Ukraine continued to pose a source of uncertainty for Polish economic growth outlook. They pointed out that a weaker economic growth outlook in Russia and Ukraine and a depreciation of their currencies might undermine Poland's trade with the Eastern markets. However, a few Council members were of the opinion that – given that Poland's trade with these markets was limited, and some of these exports could be redirected to other markets – the Ukrainian crisis would have a limited impact on Polish foreign trade, and in consequence, on economic growth in Poland. Council members also highlighted that the impact of the Ukrainian crisis on the sentiment in the international financial markets and the zloty exchange rate had been limited so far.

While discussing recent data releases in Poland, Council members pointed to ongoing growth in industrial output and retail sales as well as improved construction sector performance, all of which confirms continued recovery in domestic demand. It was indicated that, in contrast to earlier estimates, domestic demand had been the main driver of growth already in 2014 Q4, which had been – among others – due to much faster than expected rebound of investment spending. Yet, it was also emphasized that recent data on economic activity had been lower than expected and in some cases, including retail sales growth, export orders and leading indicators of business sentiment, had weakened. In the opinion of some Council members, the deterioration in sentiment could have been related with higher uncertainty due to an escalation of the conflict in Ukraine and weaker economic growth outlook in the trading partners in the East.

Council members noted that the rebound of economic activity was translating into improvement in labour market conditions. Employment in the corporate sector is gradually expanding, with a concurrent decline in unemployment. Yet it was emphasised that the unemployment rate persisted at an elevated level, which constrained wage pressure, as confirmed by slow unit labour cost growth. However, a few Council members expressed the opinion that – like in the previous recoveries – unit labour cost might be expected to pick up in the coming quarters, citing an acceleration in wage growth in recent months. On the other hand, some Council members argued that business conditions surveys did not point to an acceleration of wage growth in the near future.

Some Council members pointed to a slight improvement in lending growth, supported by low loan costs. At the same time, a few Council members drew attention to a low share of investment loans in financing of investment projects by small and medium-sized enterprises. Other Council members assessed that low interest on deposits continues to undermine the incentives to save in the banking system, which was reflected in increasingly weaker growth in corporate deposits.

In their discussion on inflation developments, Council members pointed to inflation remaining markedly below the NBP inflation target and still low core inflation, despite a rise in one of its measures. It was also emphasised that producer prices continued to

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decrease, and that inflation expectations remained low. Some Council members noted that the available forecasts pointed to a slightly slower rise in inflation in the coming months than envisaged in the March projection. Taking this into account, a few Council members expressed the opinion that inflation might return to the target later than forecasted in the March projection. Some Council members presented the view that accelerated economic growth might translate into a rise in inflation to a greater extent than currently forecasted. Moreover, a few Council members noted that the situation in Ukraine and the adverse weather conditions in many major food commodity exporters resulted in a considerable rise in their prices in the global markets. This is conducive to faster food price growth, whose deceleration – along with slow energy price growth – was previously one of the key factors keeping inflation down.

The Council decided that the NBP interest rates should remain unchanged at the current meeting. Furthermore, the Council maintained its assessment that the NBP interest rates should be kept unchanged for a longer period of time, i.e. at least until the end of the third quarter of 2014. The Council members observed that a more comprehensive assessment of macroeconomic outlook needed to change the horizon of keeping the interest rates at the current level will probably be possible during the July meeting of the Council, when a new NBP projection is to be presented.

The Council left the key NBP 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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