MINUTES OF THE MONETARY POLICY DECISION-MAKING MEETING HELD ON 6 JUNE 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.

While analysing developments in the external environment of the Polish economy, the Council members pointed to a moderate economic growth in the United States, stagnation in activity in the euro area and a weakening growth in several major emerging economies. While discussing the outlook for the euro area, the Council highlighted mounting concerns about the developments in the countries most affected by the sovereign debt crisis. Those concerns translated into deteriorating sentiment and rising risk aversion in the international financial markets. Weakening confidence has in turn resulted in depreciation of the exchange rates of the emerging currencies, including the zloty, and decrease of global commodity prices.

Some Council members assessed that despite the deteriorating economic outlook for the euro area, GDP growth in Poland's main trading partners was set to remain firmly positive. However, these Council members also pointed out that the slowdown observed in major emerging economies, which are important recipients of German exports, might translate – through trade links between Poland and Germany – into further weakening in Polish exports.

While addressing economic developments in Poland, it was pointed out that the data released in May, particularly concerning the GDP in 2012 Q1 and its composition, confirmed the gradual weakening in the Polish economic activity. The Council members pointed especially to a relatively slow consumption growth coupled with weakening investment and exports. Furthermore, in the opinion of some Council members, recent data on industrial production and retail sales, as well as a significant number of leading business climate indicators justify the expectation of slower GDP growth in 2012 Q2 in comparison to Q1. While addressing the outlook for growth in the subsequent quarters, some Council members stated that, apart from likely continued decline in external demand, the GDP growth will probably be further dampened by the on-going fiscal tightening, combined with a weaker consumption growth due to slow real wage growth and decelerating household lending. However, other members of the Council argued that the slowdown in the Polish economy may prove moderate. This could be indicated by some April data, in particular, further rise in the corporate investment lending and zloty-denominated mortgage lending, flattening downward trend in industrial production growth and an acceleration in construction and assembly output. At the same time, some Council members claimed that the increase in zloty-denominated mortgage lending was partly due to falling demand for foreign-currency mortgage lending.

While discussing the prospects for lending expansion, few Council members highlighted that the deteriorating position of the euro area banking sector may to have an adverse effect on the credit supply by domestic banks. These Council members were of the opinion that credit supply may additionally be negatively affected by a decline of private sector deposits held in the banking sector seen over recent months, in part as a result of the deposits being transferred to the investment funds. Other Council members argued that amid persisting liquidity surplus in the banking sector, the above factors might not necessarily translate into weaker lending, as credit supply is far more responsive to the assessment of risks related to economic developments as well as changes in the credit standing of the potential borrowers.

While analysing the labour market developments, some Council members pointed out that the LFS (Labour Force Survey) data for 2012 Q1 suggest slower annual growth of the employment in the economy, coupled with a rise in the unemployment rate compared to a year ago. Similar trends may be observed in the monthly data on employment in the enterprise sector and unemployment as registered by the Labour Offices. At the same time, wage growth accelerated somewhat in 2012 Q1, which – coupled with a simultaneous deceleration in GDP growth – added to an increase in unit labour costs in the economy. Yet, some Council members argued that the 2012 Q1 pick-up in wages might have been driven by one-off factors (i.e. expedited payments of some remuneration components before an increase in disability contributions). This may be corroborated by the corporate wage growth decelerating since February and running currently at low levels. In this context, some Council members assessed that the economy was not experiencing any intensification in wage pressures. In the opinion of few Council members, wage pressures were additionally mitigated with a wage freeze in the public sector. Other Council members emphasised, however, that for the last two years corporate sector had seen upward trend in labour costs.

While discussing the risk of an increase in wage pressures, it was highlighted that inflation expectations were persisting at a relatively high level. Given their adaptive nature, they might also remain elevated in the coming months. Yet, some Council members assessed that the risk of the second-round effects was limited due to slowing employment growth and heightened unemployment.

With reference to inflation developments, it was pointed out that April saw a rise in both the CPI and core inflation. It was also highlighted that the current elevated inflation was driven, to a great extent, by factors beyond the impact of the domestic monetary policy. On the other hand, some Council members pointed out that in comparison with other countries in the region – in which inflation was influenced by similar external factors – inflation in Poland remained relatively high.

While discussing the short-term outlook for inflation, it was indicated that the nearest months might be expected to see inflation continue above the upper limit for deviations from the target. This will be driven by the sustained steep growth in administered prices, accompanied with accelerating annual food price growth. The sharp rise in administered prices is partially an effect of increased fees and prices controlled by the general government units. These increases were related to measures aimed at curbing the general government deficit. Amongst other factors raising inflation in Poland, the Council also mentioned the recently observed depreciation of the zloty related to deteriorating sentiment in the global markets as well as the risk of a temporary hike in restaurant and hotel prices in some cities connected to the European Football Cup.

With regard to inflation trends in longer run, some Council members highlighted that some forecasts pointed to a risk of inflation remaining above the target for longer period. These Council members in particular pointed to the relatively high core inflation, which might continue to run at relatively high levels also in the subsequent quarters. This, given a low – in their opinion – likelihood of any substantial drop in growth of energy and food prices, would impede inflation returning to the target. Few Council members emphasised at this point that the recently observed decline in commodity prices might prove temporary, particularly amid political tensions in some major commodity economies. Other Council members indicated that the contribution of food and energy price growth to CPI inflation might decline substantially in the coming quarters, due to, in particular, favourable base effects for both categories.

While analysing the current monetary policy, some Council members assessed that the current level of interest rates might be adequate to maintain price stability over the medium term, particularly considering the economic slowdown. At the same time, few Council members argued that any further interest rate increases may – through their dampening effect on demand growth – impede the reduction of the general government deficit in relation to the GDP, which in turn, by forcing additional fiscal adjustment, may ultimately result in an excessive curbing of economic growth. Yet, other Council members argued that – despite the already implemented adjustment – the current level of interest rates in Poland may prove slightly too low to stem the risk of inflation persisting at a heightened level over the medium term, given particularly the risk of persistently elevated core inflation. Few Council members pointed out that too low interest rates might negatively affect the saving rate in the economy.

While discussing decisions on the NBP official interest rates, the Council members decided that these should be left unchanged at the current meeting. Some Council members emphasised that amidst the on-going economic slowdown, the increase of the NBP rates at the previous meeting was probably a sufficient adjustment of interest rates to the current and anticipated macroeconomic developments in Poland. Such an assessment is also supported – in their opinion – by the risk of deteriorating situation in the euro area economy. Other Council members believed that another interest rate adjustment might be justified in the coming period, should the expected period of inflation persisting above the target protract, and the scale of the anticipated economic slowdown prove moderate. In the opinion of most Council members, a more comprehensive assessment whether another interest rate increase was justified should take into account the data released in the coming period as well as results of the NECMOD projection and of other forecasts.

The Council decided to keep the NBP interest rates unchanged at the following levels: reference rate at 4.75%, lombard rate at 6.25%, deposit rate at 3.25%, rediscount rate at 5.00%.

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