Minutes of the Monetary Policy Council decision-making meeting held on 8 November 2017

Members of the Monetary Policy Council discussed macroeconomic developments abroad analysing their impact on economic conditions in Poland. It was indicated that GDP growth in the euro area in 2017 Q3 was close to that observed in the first half of the year, thus significantly higher than in the previous year. It was pointed out that GDP growth in the euro area was still driven mainly by growth in consumption, although in 2017 Q3 it was probably accompanied by a recovery in investment and exports. It was underlined that, according to the November projection, in 2018 economic conditions in this economy would remain favourable, although GDP growth would slow down slightly. While analysing economic conditions in other economies, it was pointed out that in 2017 Q3 economic growth in the United States – despite the negative impact of adverse weather conditions on economic activity – was close to that observed in the previous quarter. In China, in turn, GDP growth decelerated somewhat in 2017 Q3.

Referring to price developments in the world economy, it was underlined that inflation abroad remained moderate, and continued good economic conditions in many economies were not accompanied by a significant rise in inflationary pressure. It was judged that the observed weakened correlation between economic conditions and price growth could result from several structural factors. The opinion was expressed that under current conditions the risk of a sharp rise in inflation in the majority of developed countries was limited. However, certain Council members drew attention to the recent slight increase in price growth in some economies.

While analysing commodity price developments, it was pointed out that oil prices were higher than in the previous month, but that in recent days there had been signs of their stabilisation. It was judged that oil prices were boosted by the decrease in oil inventories, as well as expectations of a possible extension of the agreement between oil exporting countries. Certain Council members were of the opinion that fundamental factors – in particular, the elastic supply of shale oil in the United States – should lower oil prices in the coming quarters. Referring to remaining energy commodities, other Council members drew attention to the significantly higher coal prices compared to the first half of the year.

Regarding monetary policy abroad, it was highlighted that the European Central Bank was keeping interest rates close to zero, including the deposit rate below zero, and continued to announce that they would remain at their current levels even after the end of the asset purchase programme. At the same time, the ECB extended the duration of the asset purchase programme to at least September 2018, while limiting the monthly scale of purchases by half from 2018. In turn, in the United States, the Federal Reserve began reducing its balance sheet, although – as it was stressed – the scale of monetary expansion was being reduced gradually.

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While discussing developments in Poland's real economy, the Council members judged that GDP growth in 2017 Q3 was probably higher than in the previous quarter. It was emphasised that economic growth was still driven primarily by increasing consumer demand, supported by rising employment and wages, disbursement of benefits and very good consumer sentiment. It was underlined that the faster construction and assembly output growth than in the first half of the year pointed to a probable recovery in investment. However, certain Council members pointed out that information incoming in the last month – including data on industrial output, construction and assembly output, and the PMI – was somewhat worse than earlier readings.

It was indicated that – in accordance with the November projection – in 2018 the favourable economic conditions were expected to continue, although GDP growth would probably slow down. It was underlined that the expected weakening in economic activity in the euro area, including in Germany, would result in some slowdown in economic growth. The gradual fading of the statistical effects of the "Family 500 plus" programme would also dampen GDP growth. At the same time, the recovery in both public and corporate investment should support GDP growth next year. However, certain Council members assessed that the scale of the recovery in investment in 2018 – particularly corporate investment – was subject to significant uncertainty. Moreover, it was pointed out that even with the expected investment growth, the investment rate in the economy would remain relatively low. However, other Council members were of the opinion that the increasing scale of child benefit payments along with the rising birth rate, the improvement in the financial situation of some consumers due to the lowering of the statutory retirement age, and in 2019 also the possible increase in social benefits and wages in the budget sector, could boost GDP growth.

With reference to labour market conditions, attention was drawn to the gradual growth in employment and fall in unemployment. It was underlined that this was accompanied by higher wage growth in enterprises and faster rise in unit labour costs than in the previous quarters. While certain Council members drew attention to the high growth in the wage bill in enterprises, other Council members underlined that in September wage growth in the corporate sector had slowed down somewhat. It was judged that the inflow of foreign employees to Poland as well as higher labour force participation among Poles continued to contain wage growth.

It was pointed out that in the coming years wage growth and unit labour cost growth – according to the November projection – would increase slightly. At the same time, some Council members stressed that there was still uncertainty about the impact of the lowering of the statutory retirement age on labour supply and wage pressure, although – according to certain of these members – the scale of this impact would be reduced by the high proportion of non-working persons among those retiring. Certain Council members expressed the opinion that the low propensity of firms to increase wages amid high competition and a fall in profitability in the recent period could contain wage growth in the coming quarters. However, other Council members pointed out that a possible

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restriction to the inflow of foreign employees and a likely increase in wage pressure in the budget sector could lead to faster than expected wage growth.

When analysing price developments in Poland, it was pointed out that the annual consumer price growth remained moderate. Some Council members underlined that in October annual inflation had decreased somewhat. These Council members stressed that price growth was currently driven up by the rise in oil and food prices, thus the factors beyond the direct impact of domestic monetary policy. At the same time, internal inflationary pressure remained – in the assessment of these Council members – limited, and no significant influence of accelerated wage growth on consumer price growth could be seen. Certain Council members also underlined that price growth took place amid continued moderate lending growth. Other Council members, in turn, drew attention to the increase in all core inflation measures in the recent period, which – in their assessment – indicated an intensification of domestic inflationary pressure. These Council members also pointed to a certain increase in the inflation expectations of households and enterprises as well as the gradually rising producer price growth.

While discussing the outlook for price growth, it was indicated that according to the November projection, it would gradually rise to reach the annual average level of 2.3% in 2018 and 2.7% in 2019. The majority of Council members recognised that the results of the November projection indicated that in the coming years inflation would remain close to the target. However, some Council members underlined that the inflation path in the November projection was higher than in the previous forecasting round, and that in 2019 inflation would exceed 2.5%. These Council members judged that the expected inflation growth would be driven by an intensification of domestic inflationary pressure as evidenced by the forecast growth in both core inflation and the value added deflator. They also pointed out that inflation could be higher than forecast by the current projection due to the possible stronger growth in wage and cost pressure. Certain of these Council members drew attention to higher coal prices compared to the previous year, which – in their opinion – would boost production costs of many goods, including food products, and would impact directly the prices of some consumer goods.

While discussing NBP monetary policy, the Council decided that currently interest rates should remain unchanged. The Council judged that – given the available information – in the coming years inflation would run close to the inflation target. As a result, the current level of interest rates was conducive to keeping the Polish economy on a sustainable growth path and maintaining macroeconomic stability.

The majority of Council members expressed the opinion that, taking into account the present information, interest rates were also likely to remain stable in the coming quarters. These Council members judged that the stabilisation of interest rates would allow to meet the inflation target, which – as they underlined – is of a symmetric nature. At the same time, taking into account the expected slowdown in GDP growth in the coming years, it was indicated that a stabilisation of interest rates would support the maintenance of balanced economic growth, including the expected recovery in investment. Moreover,

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these Council members pointed out that the need to take into account monetary conditions in the immediate environment of the Polish economy, including the prospect of maintaining negative interest rates in the euro area next year, also spoke in favour of keeping the current level of interest rates.

In the opinion of some Council members, should data and forecasts incoming in the following quarters suggest a more marked intensification of inflationary pressure, it might be justified to consider an increase in the NBP interest rates in the quarters to come. In the opinion of these Council members, interest rate decisions should take into account in particular the impact of negative real interest rates on lending, asset prices and savings in the Polish economy, as well as growth in the unit variable costs. An opinion was also expressed that future decisions of the Council should account for developments in inflation expectations. Certain of these Council members judged that a possible increase in interest rates would have a limited impact on investment growth.

A view was expressed that in the event of a significant decline in economic indicators accompanied by a marked deterioration in consumer and corporate sentiment, in the longer run it might be justified to consider a decrease in interest rates.

Some Council members underlined that in the face of uncertainty about the determinants of monetary policy in the longer term, the March projection of inflation and GDP would be an important prerequisite for an assessment of its prospects.

The Council decided to keep the NBP interest rates unchanged: the reference rate at 1.50%, the lombard rate at 2.50%, the deposit rate at 0.50%, the rediscount rate at 1.75%.

During the meeting the question of lowering the reserve requirement ratio on funds raised from domestic entities for at least a two-year period was also discussed. It was indicated that this ratio currently stood at 3.5%. Taking into consideration that funds raised from abroad for the same period are not subject to reserve requirements, it was judged that it would be justified not to calculate reserve requirements also for the remaining funds raised for at least a two-year period, which would mean the equal treatment of such funds. It was indicated that the application of uniform reserve requirement ratios for all funds raised for at least 2 years would bring the Polish reserve requirement system closer to the solutions applied by the Eurosystem. Moreover, it was pointed out that the introduction of the discussed change could help to lower the scale of the maturity mismatches between assets and liabilities of Polish institutions subject to mandatory reserve requirements.

The Council adopted a resolution according to which the reserve requirement ratio for funds raised for at least a two-year period will stand at 0%. The resolution will come into force on 1 March 2018 and will apply starting with the reserve requirement to be maintained from 30 April 2018.

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