

Warsaw, 20 December 2006

## INFORMATION FROM THE MEETING OF THE MONETARY POLICY COUNCIL

held on 19-20 December 2006

The Council decided to keep the NBP interest rates unchanged, i.e.:

- reference rate **4.00% on an annual basis**;
  - lombard rate **5.50% on an annual basis**;
  - deposit rate **2.50% on an annual basis**;
  - rediscount rate **4.25% on an annual basis**.
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Since the Council's meeting in November 2006 there have been no changes in the forecasts of economic growth and inflation in the euro area for 2006-2007. In the United States both the forecasts of economic growth in 2007 and inflation in 2006-2007 have been slightly lowered. In November, the annual inflation increased both in the euro area (from 1.6% in October to 1.9%) and in the United States (from 1.3% y/y to 2.0% y/y). Since the November meeting of the Council the current price of crude oil has increased by USD 4.6 (i.e. 7.9%), while the oil price forecast for 2007-2008 has not changed (according to the analysts polled by Reuters).

GUS data on the GDP in Q3 have confirmed that the Polish economy is in a strong and consolidating recovery, which encompasses all sectors of the economy. The real GDP growth in 2006 Q3 reached 5.8% y/y and was higher than the projection and external expectations. Higher than the projection proved the growth of private consumption at 5.5% y/y (compared to 4.9% y/y in 2006 Q2), which was the highest growth since 1999 Q4. Similarly, higher than the projection was the growth in gross fixed capital formation, which accelerated to 19.8% y/y (down from 14.8% y/y in 2006 Q2) and was the highest since 1997 Q4. The rise in public consumption (of 1.1% y/y) was consistent with the projection, while the contribution of net exports to GDP growth (at -0.3 percentage points) proved less negative than in the projection.

GUS data on industrial and construction and assembly output in October and November 2006 indicate the continuation of strong business activity. The November growth in industrial output was consistent with expectations of the NBP staff and lower than expected by external forecasters. It amounted to 11.7% y/y (compared to 14.8% y/y in October). In seasonally adjusted terms, the growth in industrial output was 10.2% y/y (compared to 12.5% y/y recorded in October). In line with expectations of the NBP staff, the surge in construction and assembly output was sustained (at 23.4% y/y against 28.6% y/y in October, which in seasonally adjusted terms corresponds to 25.0% y/y compared to 28.2% y/y).

According to the preliminary data on money creation factors available as of 20 December, the lending to the private sector in November 2006 grew by 22.7% y/y. Since the middle of 2005 lending to households has been growing strongly and in November it accelerated to 31.4% y/y (compared to 30.1% in October and 13.3% in December 2004, when it was the lowest in the last two years). Starting from 2006 Q2 acceleration in loans to enterprises has been observed; in

November their growth reached 13.1% y/y and in April 2006, when it was the lowest in the current year, it stood at 3.3% y/y. The current growth in corporate lending, combined with substantial own funds of enterprises resulting from their very good financial results in the first three quarters of 2006, may indicate that the high investment growth will be sustained.

The strong economic growth is accompanied by a dynamically growing demand for labour. Since December 2004 the employment growth in the corporate sector has been constantly accelerating – in November 2006 the growth of corporate employment amounted to 3.8% y/y, compared to 3.6% y/y in October, which was the highest since the beginning of the 1990s.

Economic growth is also accompanied by a high growth of wages. In November 2006, the growth in nominal wages in enterprises amounted to 3.1% y/y compared to 4.7% y/y in October. However, according to NBP estimates the wage growth in enterprises adjusted for the impact of one-off shifts in wage components in several sections was 5.7% y/y in November against 5.6% y/y in October. The latest data on GDP in Q3, combined with data on the nominal wage growth in the economy (5.0% y/y in Q3) and the growth of the number of working persons outside private farming (6.9% y/y in Q3), confirm preliminary assessments formulated in November that the growth of unit labour costs (outside private farming) stepped up significantly in Q3 (to 6.1% y/y against 4.5% y/y in Q2 and 2.7% in 2006 Q1). This growth was slightly higher than estimated in the October projection. Strong economic growth which would not pose a threat to the achievement of the inflation target can only be sustained on the condition that the growth in wages does not outpace the growth in labour productivity. This requires strong and productivity-oriented corporate governance in enterprises, which is usually more easily achieved under private ownership. This also requires wage discipline in the public sector.

In November the annual growth of consumer prices rose to 1.4% from 1.2% in October. The rise in the annual inflation primarily reflected an increase in the annual growth of prices in telecommunications and recreation and culture.

In November the annual growth of producer prices in industry was 2.6% against 3.2% in October (i.e. 0.5% m/m both in October and November), with 1.3% in manufacturing. In November the nominal effective exchange rate of the zloty appreciated 5.6% in year-on-year terms.

The latest data suggest that annual CPI inflation in 2006 Q4 will be lower than indicated in the October projection. ‘Net’ core inflation will run close to the path expected in the projection. Some factors may arise in 2007 which can be temporarily pulling (CPI) inflation down in some periods.

The analysis of inflation outlook indicates that maintaining inflation close to the target of 2.5% in the medium term may require monetary policy tightening.

In the opinion of the Council, the currently observed strong economic growth creates convenient conditions for the implementation of reforms which would permanently reduce the public finance imbalance. The Council maintains its belief that it would be the most favourable for Poland to adopt an economic strategy focused on creating conditions that would guarantee the introduction of the euro at the earliest possible date. The constraining of public finance imbalance would be conducive, both *per se* and by creating conditions for the introduction of the euro, to accelerating the long-term economic growth.

The Council has adopted a resolution approving *The Financial Plan of the National Bank of Poland for 2007* and *The Resolution on the principles of setting and releasing provisions for the exchange rate risk of the zloty against foreign currencies at the National Bank of Poland*.

In line with the time schedule, the next meeting of the Council will be held on 23 January 2007 and will be devoted to discussing the draft *Inflation Report*. The *Report* will finally be adopted at the Council's meeting on 30-31 January 2007.