

Warsaw, 25 February 2005

INFORMATION FROM THE MEETING OF THE MONETARY POLICY COUNCIL

Held on 24-25 February 2005

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

- **reference rate 6.5% on an annual basis;**
- **lombard rate 8.0% on an annual basis;**
- **deposit rate 5.0% on an annual basis;**
- **rediscount rate 7.0% on an annual basis.**

The Council adopted an easing monetary policy bias.

=====

In the period since the last meeting of the Monetary Policy Council no significant changes were observed in the external environment of the Polish economy. Similarly to the previous month, the assessments of the economic climate both on the part of consumers and euro-area enterprises remained at a moderate level. In the United States, there was a continuation in the high dynamics in retail sales as well as positive sentiment among consumers and enterprises alike. Preliminary data on GDP growth in 2004 Q4 in the euro area and United States were slightly lower than expected. Crude oil prices in world markets persist at a high level.

On the basis of preliminary figures of GDP in 2004 it can be assumed that the economic growth rate in Poland in 2004 Q4 decreased as compared to the previous quarters and stood at slightly above 4% (y/y). Preliminary estimates indicate that private consumption dynamics in 2004 Q4 was lower than in 2004 Q3. In the same period the dynamics of real wages in the economy rose from 0.7% to 1.1% y/y. Full assessment of the consumption and savings dynamics will only be possible after the publication of the data for 2004 Q4. In line with expectations the dynamics of fixed capital formation increased. It can be assessed that a step-up in investments in 2004 Q4 was accompanied by a drop in net exports and that their contribution to the annual GDP growth rate in Q4 was negative.

NBP

In January 2005 industrial output rose by 4.7% in year-on-year terms. GUS business tendency survey – in seasonally adjusted terms – points to the continuation in February of a positive assessment of the economic climate in manufacturing and a considerable improvement in sentiment in retail trade. Also, the assessment of the condition in construction is still favourable; the construction and assembly output grew for another month in a row. The January analysis of other economic climate indicators monitored by the NBP reveals that the economic situation is positively assessed, whereas for several months most of the indicators have been signalling the tendency to a gradual deceleration in the pace of the recovery.

Available data suggest a gradual improvement of the situation in the labour market. Due to seasonal factors, in January the registered unemployment rate rose to 19.5%, however, in relation to the corresponding period of the previous year it dropped by over 1 percentage point. January marked a significant rise in the employment in the enterprise sector (of 1.4% m/m and 1.2% y/y). These data support with some delay the trend of rising employment in industry and services visible in Labour Force Surveys since 2003. Such a significant rise in employment in January may in part result from the fact that employment in many small companies crossed the threshold of 9 people and consequently these companies were considered in the examined pool of enterprises. This is reflected in a sizeable employment growth in sections with a large share of small companies e.g. in trade and repairs (4.2%), hotels and restaurants (8.3%).

No indications have been observed that would point at the emergence of wage pressure in the enterprise sector arising from higher inflation expectations (second-round effects). In 2004 Q4 the growth rate of nominal wage in the enterprise sector fell down to 2.7% y/y (from 3.8% y/y in 2004 Q3), while in the economy as a whole the nominal wage dynamics increased to 5.6% (compared with 5.1% in the previous quarter). In January the growth rate in nominal wages in the enterprise sector was still low and amounted to 2.6% y/y.

In January 2005 inflation decreased to 4.0% y/y but remained above the inflation target (2.5%), although its level was lower than anticipated. The January decrease in inflation mainly resulted from lower dynamics of food and fuel prices. It is estimated that net inflation remained at a level close to that in December (when it stood at 2.4% y/y). February saw a decline in inflation expectations of households (to 3.9% from 4.1% in January 2005). At the same time, there was a fall in the dynamics of producer prices in industry (from 5.6% y/y in December 2004 to 4.4% y/y in January 2005.).

NBP

After a period of exchange rate fluctuations the zloty appreciated again. Strong zloty appreciation reduces inflation. However, the appreciation tendency may, at the same time, contribute to the weakening in the economic growth.

According to the inflation projection presented in the *Inflation Report* due to be published on 28 February 2005, the GDP growth rate in 2005 is expected to reach 4.0%-4.5%, and thus to be slightly lower than forecast in the *November Report*, mainly as a result of the currently expected lower contribution of net exports to GDP growth. Starting from 2005 the impact of investments as an economic growth factor will be rising. In 2006-2007 acceleration in the GDP dynamics to 4.5%-5.5% is expected, provided that the expected increase in investments does occur.

The Council maintains its conviction that the sustainability of the economic growth will hinge upon implementation of reforms that would result in decreasing state expenditure and, consequently, lead to a reduction in public finance sector deficit, and which would remove barriers to employment growth.

According to the February inflation projection the price growth rate should be lower than that expected in the *November Report*. Assuming unchanged interest rates inflation will with a 50-percent probability stay in the range of 1.2%-4.0% in 2005 Q4 (2.5%-5.2% in the previous projection), 0.4%-4.2% in 2006 Q4 (1.3%-4.8% in the previous projection) and 0.5%-4.6% in 2007 Q4.

In the Council's assessment for the past several months there has been a change in the balance of risks for future inflation, which resulted in a situation that the current balance may be more favourable than that presented in the February projection. This is because, the hitherto scale of zloty appreciation was larger than what was accounted for in the projection and the dynamics of food prices may be declining faster than assumed. Still, the Council acknowledges the uncertainty related to *inter alia* the developments in oil prices and the zloty exchange rate.

Considering the above the Council adopted an easing monetary policy bias.

The next meeting of the Council will be held on 29-30 of March 2005.