

Warsaw, 28 March 2007

INFORMATION FROM THE MEETING OF THE MONETARY POLICY COUNCIL

held on 27-28 March 2007

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 meeting of the Council in February 2007 the outlook for inflation in 2007 in the euro area has been slightly lowered. The forecasts for inflation in the United States have not changed. For the euro area the forecasts of economic growth in 2007 have been revised upwards, while they have remained unchanged for the United States. In February, the annual inflation in the euro-area was unchanged (at 1.8%), while in the United States it increased (to 2.4% from 2.1% in January). The current price of crude oil has gone up since the February meeting of the Council (by USD 3.2, i.e. 5.5%). The commodity's price forecast for 2007-2008 has edged up.

GUS (CSO) data on industrial output, construction and assembly output and retail sales in January-February 2007 point to the continuation of economic growth acceleration in 2007 Q1. The rise in industrial output in February 2007 was consistent with the expectations of NBP analysts and external forecasters and amounted to 12.9% y/y (compared with 15.4% y/y in January), which in seasonally adjusted terms represented 13.0% y/y (compared with 15.5% in January). Construction and assembly output grew by 57.1% y/y (compared with 60.5% y/y in January) and in seasonally adjusted terms -- by 30.9% y/y (compared with 30.1% in January). Apart from the strong rise in demand, the annual growth of construction and assembly output continued to be supported by exceptionally favourable weather conditions in contrast to particularly adverse conditions a year before. In February the high growth in retail sales was also sustained (at 17.5% y/y in nominal terms as compared to 16.5% y/y in January).

Since the middle of 2005 growth in consumer loans has been running high (a rise of 23.7% y/y in February). The growth rate of housing loans is still increasing (to 62.9% y/y in February). The significant growth in loans to enterprises has also been sustained (at 14.3% y/y in February). The currently observed growth in corporate lending, combined with substantial own funds of enterprises resulting from their very good financial results in 2006, may indicate that the currently high investment growth will be sustained. In 2006 net earnings of non-financial enterprises employing 50 and more people rose in relation to the corresponding period of the previous year by 35.8% reaching PLN 69.8 billion, while the net profit rate went up by 0.8 percentage point (to 4.7%).

The fast economic growth is accompanied by dynamically growing demand for labour. In February the employment in enterprises grew by 4.3% y/y (compared to 3.8% y/y in January), which was the highest increase since the beginning of the 1990s. According to the data from Labour Offices the unemployment rate fell in February to 14.9% (against 18.0% one year earlier).

Economic growth is also accompanied by fast growing wages. In February the rise in nominal wages in enterprises was 6.4% y/y as compared to 7.8% y/y in January (6.5% y/y after adjusting for the impact of shifts in one-off components of wages in some sections). 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 attained in the conditions of private ownership. This also calls for wage discipline in the public sector.

In February the annual growth rate of consumer prices rose to 1.9% (in comparison to the downward adjustment of 0.1 percentage point to 1.6% in January). 'Net' core inflation stood at 1.6% y/y (against 1.5% y/y in January). In March inflation expectations of households rose to 1.7% y/y (from 1.4% in February). In February the annual growth of producer prices in industry reached 3.6% compared to 3.1% in January (0.3% m/m against 0.6% m/m in January), while in manufacturing it was 3.0% (versus 2.3% in January). In February the nominal effective exchange rate of the zloty remained stable and was close to that recorded one year before.

In the Council's assessment in the short-term both CPI inflation and net core inflation will be markedly lower than in the January projection.

In the medium term, the gradual increase in wage growth is likely to be sustained, which may lead to higher inflation. The Council believes that this increase in inflation will be probably moderate, provided that the strong productivity growth and low growth of external prices are sustained, the latter being associated with globalisation and the ensuing increased competition in the market of internationally traded goods and services.

Maintaining inflation close to target of 2.5% and thus creating conditions for sustainable long-term economic growth may require monetary policy tightening in the near future. The scale of the tightening will depend, to a large extent, on whether the incoming data confirm the expectations that the high growth of domestic demand, which most probably outpaces the growth of potential GDP, will be sustained in the next few quarters. Future decisions will also depend on other economic developments in Poland and in the world and on their impact on future inflation in Poland.

In the opinion of the Council, the currently observed high rate of economic growth creates convenient conditions for the implementation of reforms which would permanently contain 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 next meeting of the Council will be held on 17 April 2007 and will be devoted to discussing the draft *Inflation Report*. The *Report* will be finally approved at the Council's meeting held on 24-25 April 2007.