

## Information on the meeting of the Monetary Policy Council on April 25-26, 2001

The Monetary Policy Council held its meeting on April 25-26th, 2001. The Council was submitted the materials prepared by the Management Board and departments of the NBP, documents by other domestic institutions (inter alia, Central Statistical Office, Ministry of Finance, Ministry of Economy, Government Center for Strategic Studies) and international institutions (inter alia, OECD, IMF), and also information and analytical materials prepared by research institutes and commercial banks. The mentioned materials served as a basis for Council's discussion of inflation processes in Poland and development tendencies in the world economy. As a result of the discussion, the Council decided:

**not to change parameters of monetary policy, i.e. maintain the central bank interest rates at the actual level and maintain a neutral position in the area of monetary policy.**

### JUSTIFICATION

#### I.

The Monetary Policy Council observes positive tendencies in the area of inflation processes. However, there are also maintained threats to the process of inflation reduction, mainly in mid term. The Council has decided that - according to the forecast of its previous meeting - we need time to be able to be convinced whether the balance of forces forming the future inflation is being improved.

#### II.

The Council observes the following positive tendencies in the area of inflation processes formation:

##### 1. Inflation indices.

In March this year, the increase of consumer goods and services prices amounted to 0.5% and the consumer price index (CPI) calculated at the twelve-month scale lowered to the level of 6.2% from 6.6% in February this year. The further drop was also noted in case of base inflation indices calculated at the NBP. The industrial output prices rose by 0.2% in March this year as compared to the previous month. The twelve-month producer price index (PPI) lowered to the level of 3.9% from 4.2% in February 2001. The drop was also noted in case of the twelve-month construction price index from 6.5% in February to 6.1% in March.

##### 2. Inflation expectations.

According to the forecasts, a further drop of inflation expectations of individuals took place in April this year. In the second month in a row they are maintained within the range of the Council's inflation target for 2001. The drop was also observed - although a slight one - in case of banks' inflation expectations that are now slightly below the lower border of the inflation target for this year.

##### 3. Money supply and loans

The growth of money supply (M2) is maintained in a range 14-15% annualized. In March 2001, the money supply was bigger by 14.8% as compared to the end of March 2000. There is still maintained a big growth pace of deposits in PLN placed by individuals (in March this year 22.4% annualized). The growth pace of lending decreases systematically and in March it amounted to approximately 15% annualized (as compared to 17% in January and approximately 16% in February). At the same time, lending to individuals grew at a pace of approximately 28% and to businesses at a pace of approximately 12%.

##### 4. Output, domestic demand, labor market.

In March this year, the sold industrial output was bigger by 2.8% than in March 2000. In the 1st quarter this year the sold industrial output was bigger by 4.1% than in the same period in 2000. The drop pace of industrial output dynamics was decreased what together with available data on further increase of imports and exports gives rise to the expectation that the growth pace of GDP in the 1st quarter 2001 will be maintained at the level noted in the 4th quarter last year. Within the structure of demand the share of exports is growing while the dynamics of domestic demand is still low. Both the dynamics of output and the structure of demand do not cause inflation threats.

The unemployment is still growing, although its growth pace decreased. The situation on labor market reduces pressure on salary increase what reduces the inflation pressure connected with both the increase of production costs and the expenses of the population.

### III.

At the same time, the Council observes the maintained threats to the process of inflation reduction.

#### 1. Inflation indices.

Lower growth of consumer goods and services price index in March this year mainly resulted from a considerable (by 3.4% as compared to February this year) drop of fuel prices that, in turn, resulted from a favorable influence of external factors (drop of import price). The majority of base inflation measures decreased at a lower pace than the consumer price index. In March this year, base inflation measures were bigger than the consumer goods and services price index (6.5% - 7.1%). On the basis of the analysis of particular indices it can be expected that the insofar-big pace of disinflation will be subject to some decrease in the nearest months.

#### 2. Situation in public finance sector:

A threat to the process of disinflation is still the situation in public finance sector. The budget deficit at the end of March exceeded 73% of the amount planned for the whole year 2001. A further worsening in this area is expected in April. Such a big advancement of the deficit in the 1st quarter - the biggest since 1990 - causes a threat in a form of expenses cumulating and it may result in additional inflation pressures. The observed difficulties in a planned realization of the budget, inter alia, in the area of timely transfer of funds to Open Pension Funds, increase the danger of exceeding the level of economic deficit planned for this year (1.8% of GDP).

#### 3. Money supply.

A stable pace of money supply in nominal terms in conditions of decreasing inflation means an accelerated growth of money supply in real terms. The growth pace of M2 deflated by CPI increased within the last 6-month period from approximately 3.5% to approximately 7.5%. The maintenance of this tendency for a longer time may lead to the increase of inflation pressures.

#### 4. Remaining factors of uncertainty and potential threats:

- The acceleration of consumer demand is possible as a result of a cumulated effect of payoffs of different compensations and single money benefits.
- The agricultural products and foodstuffs market still remains a source of potential inflation pressures. Lately observed price increases of foodstuffs prove high sensitivity of these prices to supply and demand fluctuations.

### IV.

The Council evaluated in very detail the situation in the real sector of the economy, including mainly unfavorable tendencies in the area of production and employment. In the Council's opinion, monetary policy now has got very limited abilities to improve the situation in the real sector. Especially, potential interest rate cuts are not able to change the situation on the labor market in a perceptible and permanent way and they would be able to threaten the achievement of the inflation target. A basic role in new jobs creation in the present situation is to be played by fiscal policy, including systematic cut of fiscal costs of labor, and structural policy.

That is why the Council notes that the discussion, and mainly actions to increase employment and achieve a higher pace of economic growth, should be focused on necessary structural reforms of the Polish economy, especially liquidation of barriers to undertake and run businesses, privatization, a reform of labor market and public finance sector.

With the lack of a basic improvement in these areas, interest rate cuts made too early or too thoroughly would lead to the reverse of the decreasing trend of inflation without an effect in the area of employment increase and strengthening the development of the economy.

The next meeting of the Monetary Policy Council will be held on May 21st, 2001. The subject of this meeting will be:

- Report of monetary policy guidelines accomplishment in 2000,
- Report of activities of the National Bank of Poland in 2000.