N a t i o n a l B a n k o f P o l a n d
Monetary Policy Council

MINUTES OF THE MONETARY POLICY COUNCIL DECISION-MAKING MEETING HELD ON 11 JANUARY 2012

At its meeting, the Monetary Policy Council discussed current and future monetary policy decisions against the background of expected growth and inflation trends in Poland, which will be strongly affected by both external conditions (growth outlook abroad, situation in the financial markets, commodity prices) and domestic factors, as well as the exchange rate developments.

While analysing the situation in the Polish economy, the members of the Council pointed out that current data on industrial output, construction and assembly output and retail sales indicate that growth continues to be relatively strong. Few members of the Council also highlighted a stable rise in loans - despite prior interest rate increases - as a sign of relatively good business conditions still prevailing. At the same time, it was emphasised that in the coming quarters, a slowdown in economic activity at home can be expected. It was pointed out that uncertainty related to the external environment of the Polish economy, including the scale of the slowdown abroad and potential impact of the turmoil in the global financial markets on the Polish economy, combined with the uncertain pace and structure of further fiscal tightening at home, make it difficult to assess how strong the deceleration in the growth of demand in Poland would be.

While discussing the external conditions of the domestic economic climate, members of the Council indicated that tensions in the financial markets resulting from the sovereign debt crisis in the euro area persist, and growth forecasts for the region continue to be revised downwards. Few members of the Council emphasised the risk of heavy lending constrains in the euro area countries, which would further deteriorate growth outlook for the region. Other members of the Council, however, assessed the risk of further marked weakening in growth forecasts for the euro area as limited, in particular for countries being Poland's main trading partners.

In the opinion of few members of the Council, tensions in the European banking system may translate into constraints on lending in Poland. However, with reference to the risk that foreign banks might curb the funding for lending purposes in Poland, other members of the Council assessed it to be small, and given the significant number of enterprises financing themselves from their own funds or directly from abroad, possible constraints on lending imposed by domestic banks should not significantly undermine enterprises' activity in Poland.

Referring to the outlook for foreign trade, some members of the Council argued that a weaker zloty would alleviate the effects of the decreasing foreign demand for Polish goods by improving their price competitiveness. Other members of the Council pointed out that due to a large share of intra-corporate trade in Polish exports, the volume of foreign trade is hardly sensitive to exchange rate fluctuations. Most members of the Council assessed, however, that in the subsequent quarters Poland's trade balance should improve and net exports should contribute positively to GDP growth.

In the opinion of some members of the Council, a slowdown in economic activity in Poland may be weaker than previously expected, as output growth remains relatively stable in spite of a decline in the leading business climate indicators. Moreover a continued rise in investment loans to enterprises and a steep growth in mortgage loans to households additionally support this opinion. Those members of the Council also pointed out that activity in the euro area will be the weakest in the countries most severely affected by the debt crisis, whose links with the Polish economy are not

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particularly close. They also emphasised that in the previous years, the Polish economy developed at a relatively fast rate even in the face of sluggish growth in the euro area.

Few members of the Council indicated, instead, that the economic slowdown in Poland may be more severe than previously anticipated. In the opinion of those members of the Council, this scenario is supported by worsening investment outlook of enterprises combined with the expected weakening in the public sector investment activity. At the same time, other element of fiscal tightening - the freeze on wages in the government sector - will curtail the growth of consumption. A similar effect will be brought about by unemployment rate persisting at an elevated level, which may dampen wage growth throughout the economy.

When discussing inflationary developments, attention was drawn to a higher than expected rise in inflation in November 2011 and an upward revision of inflation forecasts for the coming year, both resulting to a large degree from the hitherto depreciation of the zloty. It was pointed out that the persisting elevated inflation was accompanied by a considerable rise in inflation expectations of individuals and enterprises.

Some members of the Council emphasised that while inflation should gradually decrease over the coming months, it would probably remain above the NBP target for a longer time than hitherto envisaged. Increases in the rates of indirect taxes and in administered prices were indicated as the factors continuously contributing to rising inflation.

Moreover, few members of the Council additionally pointed out that unit labour costs might limit inflationary pressure to a lesser extent than in the previous years. In their opinion, a significant increase in minimum wages, a rise in disability pension contribution and the rising percentage of long-term unemployed - who are less competitive as compared with employees and those actively seeking jobs - combined with decreasing labour productivity resulting from the expected deterioration in business climate, will trigger a higher growth in unit labour costs.

Referring to the external conditions for inflationary processes, few members of the Council emphasised that in the medium term a significant curbing of inflation in Poland would be made difficult by the persistently elevated inflation abroad and continuously high commodity prices in the global markets, related - in their opinion – to strongly expansionary monetary policy pursued by major central banks, including considerable excess liquidity in the global financial markets. Apart from expansionary monetary policy, high commodity prices will be also supported by: continued growth in demand from the developing countries and a possible mounting of political tensions in the commodity-exporting countries. According to those members of the Council, a lowering of inflation at home will be additionally made difficult by weaker anti-inflationary impact of imports from low-cost countries, where rate of growth of labour costs exceeds that of labour productivity and a relative appreciation of their currencies follows.

As regards the monetary policy decisions implemented so far, the members of the Council assessed that the NBP interest rate increases in the first half of 2011 and the following stabilisation of monetary policy parameters in the second half of 2011 have been conducive to maintaining macroeconomic stability. In the last months of 2011, earlier signs of significant economic slowdown in Poland were not confirmed, while inflation increased, thus adding to the risk of inflation persisting above the target. Few members of the Council additionally pointed out that although the NBP interest rates remained unchanged, the depreciating exchange rate and rising inflation have resulted in easier monetary conditions in the recent months.

While discussing the decision on the NBP interest rates, the members of the Council agreed they should remain unchanged at the current meeting. As a main argument in favour of this decision a high uncertainty of economic activity in the coming quarters was mentioned. With reference to future monetary policy decisions, on the other hand, most members of the Council were of the opinion that should the relatively fast domestic growth, elevated inflation and high inflation expectations continue, the increase in NBP interest rates cannot be ruled out. It was pointed out that in assessing the outlook for medium-term growth and inflation, the incoming data on economic activity and inflationary processes in Poland in the coming months as well as the NBP March projection would be helpful.

Most members of the Council emphasised that a possible future decision to raise the NBP interest rates would be justified if the economic activity were to decelerate only slightly and inflation were not be in a clear downward trend. An important argument in favour of such a decision would also be the end of downward revisions of the euro area growth forecasts. Moreover, those members of the Council pointed out that future decisions on monetary policy would be greatly affected by the assessment of the implementation of further fiscal tightening.

At the same time, few members of the Council argued that in case of a considerable economic slowdown or a significant appreciation of the zloty, a cut in the NBP interest rates may prove justified.

The Council decided to keep the NBP interest rates unchanged at the following levels: reference rate at 4.5%, lombard rate at 6.00%, deposit rate at 3.00%, rediscount rate at 4.75%.

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