Minutes of the Monetary Policy Council decision-making meeting held on 6 May 2015

Members of the Monetary Policy Council discussed the monetary policy in the context of the current and expected macroeconomic developments in Poland and abroad.

While discussing the situation in Poland's external environment, members of the Council pointed to the improvement in economic situation in the euro area and expected further increase in activity growth in this economy. Attention was drawn to the decline in the unemployment rate, pick-up in retail sales and improvement in consumer sentiment in the recent period. It was argued that economic activity in the euro area had been supported by the previously observed steep decline in commodity prices. Certain Council members emphasized in particular favourable economic situation in Germany – Poland's main trading partner – including the increase in consumption and improvement in industry.

Some Council members assessed that the economic situation in the euro area had been supported by the quantitative easing programme conducted by the European Central Bank, which had contributed to the weakening of the euro and higher price competitiveness of this currency area. Those members also pointed to other positive effects of the ECB's quantitative easing, including the easing of credit standards and interest rate decrease, which might suggest the onset of a revival in lending. Certain Council members emphasized that the ECB's quantitative easing programme might also stimulate growth in demand through the wealth effect related to the increase in the prices of assets held by households. It was also noted that the ECB's quantitative easing had heightened inflation expectations in the euro area.

Some Council members, however, pointed to possible negative consequences of quantitative easing programmes, including the possibility of the formation of bubbles in the asset markets. Some Council members assessed at the same time that the asset purchase programme in the euro area had no significant effect on activity in the real economy. In this context, certain members cited the example of the United States, where short-term positive effects of quantitative easing resulted – in their opinion – from directing a large part of the central bank's programme at the purchase of real estate assets. As the ECB's asset purchase programme concerns largely Treasury bonds, it would have – in their opinion – only a minor impact on the real economy.

Some Council members assessed that further developments in the Greek economy were a source of risk for economic growth in the euro area. Certain members of the Council

Narodowy Bank Polski ul. Świętokrzyska 11/21 00-919 Warszawa tel. +48 22 185 28 88 sekretariat.rpp@nbp.pl

emphasized, however, that the effects of a possible insolvency of Greece for the financial markets might be limited, due to the ECB's current quantitative easing programme, as well as the relatively small share of the private sector among Greek creditors.

While analysing the economic situation in the United States, Council members pointed to a slowdown in GDP growth in 2015 Q1. Factors that could adversely affect activity in the US economy were highlighted, including the cold winter, the appreciation of the dollar, and the previously observed strong decline in oil prices, which had dragged down profitability and had reduced investment of oil producers in this country. It was emphasized that deteriorating data in the recent period had postponed the expectations for interest rate hikes in the United States. Some members of the Council assessed that it had been difficult to determine the persistence of the slowdown, although recovery had been still expected to continue. Certain Council members assessed that since the economic crisis, the trend of GDP growth in the US had been generally constant. They also pointed out that GDP growth projections in the United States had been overoptimistic for the past few years, which forced their subsequent downward revisions. Certain Council members argued that the long-term GDP growth in the US economy could be adversely affected by the quantitative easing programmes conducted in the past by the Federal Reserve.

Members of the Council pointed out that improvement in the outlook for growth in developed economies had been accompanied by slowing GDP growth in many emerging economies. Attention was also drawn to the recession in Russia and Ukraine. Certain members of the Council pointed out that a possible further escalation of the conflict between these countries had posed a risk to economic growth in the external environment of the Polish economy. Some Council members also underlined the decline in economic growth in China. They assessed that imbalances in this economy, which could be observed in the real estate market, and in the recent period also in the stock market, posed a risk of a sharp drop in GDP growth. Certain Council members argued, however, that the rising share of consumption (at the expense of investment) in GDP growth might reduce the risk of a sharp drop in demand.

Council members pointed out that price growth in the global economy, including in the euro area and in the United States, had been still very low, however deflation in the euro area had decreased. It was emphasized that a certain rise in oil prices in the world markets in recent weeks had been accompanied by a slight decline in food prices. Certain members of the Council argued that the observed decline in commodity prices had been a symptom of a downward phase in the long-term cycle in the commodity market. Therefore, they argued that global inflation would remain low in the coming years.

While analysing the situation in the Polish economy, members of the Council pointed to the continuing economic recovery and the prospects for a gradual pick-up in economic growth, driven by both internal factors, and the expected further improvement in the economic situation in the euro area. Council members assessed that the continuing economic recovery was reflected in good data from industry, particularly in export-related branches, as well as the pick-up in production in the construction and the persistently favourable financial situation of enterprises. It was assessed that the retail sales data and consumer sentiment indicators had suggested continuing steady growth in consumption. It was argued that economic conditions had been supported by the improvement of the labour market situation, including wage and employment growth. Certain Council members pointed out that suggested wage growth in the public sector could support wage growth in the economy. Yet certain members of the Council pointed to the structural problems faced by the Polish economy: high unemployment and low wages, and thus the small share of wages in GDP growth. These factors – they argued – limited consumption of households.

Council members pointed to high investment growth, which supported growth in domestic economic activity. In this context, a significant percentage of enterprises planning to embark on new investments in business surveys was noted. Some Council members emphasized that in the coming quarters investment growth in the economy would be fuelled by the inflow of EU funds under the new budgetary perspective. Certain Council members also pointed to a possible pick-up in housing investment, driven by the improvement in the labour market situation and the decline in interest rates on loans. These members also assessed that accelerating investment would be accompanied by high growth in inventory, usually strongly pro-cyclical.

Certain members of the Council argued, however, that although in the first half of 2015 investment growth might slow down – which in their opinion may be a delayed effect of the economic slowdown recorded in the second half of 2014 – the coming quarters were expected to see its continued recovery. They argued that the continuing strong growth in investment might be connected to low investment growth recorded in the previous years. Other Council members judged that due to the much faster growth in investment than consumer demand, investment growth might decrease in the coming quarters.

While analysing trends in lending, some Council members assessed that lending had continued to expand moderately. In this context, certain Council members highlighted, in particular, the absence of any significant pick-up in the growth of corporate investment loans, despite the decline in interest rates charged on those loans. These members additionally pointed out that as interest rates on fixed term deposits had diminished, so had the share of those deposits in total household deposits, which had been accompanied by acceleration in inflows of capital to investment funds.

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Certain Council members pointed out that following several years of fiscal policy tightening, the impact of this policy on demand growth in the economy would be probably neutral this year. With regard to public finance, certain Council members deemed that as the deficit of this sector had declined, the Excessive Deficit Procedure with regard to Poland might be lifted, which would be favourable in terms of the rating of Polish bonds, and hence the cost of debt servicing. Yet, other Council members argued that the public sector deficit was relatively high if the current rise in domestic demand was taken into account, while the sources of reducing the deficit applied in the past years had been exhausted. As a result, they believed that in the event of a next slowdown, fiscal policy might have limited scope for supporting demand in the economy.

Some Council members assessed that despite the recovery, a negative output gap prevailed in the economy. As a result, the annual price growth, including most core inflation measures, remained negative. These members also emphasised the absence of cost pressure in the economy, as indicated by a further producer price decline resulting from the previous sharp fall in commodity prices and moderate wage growth. In this context, business surveys were cited, which pointed to the absence of the risk of wage pressure arising in the nearest future. The consistently low level of inflation expectations of economic agents were also highlighted. Considering the above circumstances, these members assessed that the return of inflation to the target would be gradual.

Yet some Council members were of the opinion that the prolonged deflation was primarily the result of supply shocks related to the fall in commodity prices as well as low inflation in the euro area. Certain Council members also underlined that the decline in prices in Poland had been supported by the embargo on exports of certain Polish goods to Russia and by rising labour productivity. Certain Council members emphasised that as the impact of the supply shocks wore away, inflation in Poland would rise faster than the March NBP projection envisaged. In their opinion the steeper rise in inflation would also result from a higher than was assumed in the projection GDP growth in Poland and its external environment, which would be accompanied by faster domestic unit labour cost growth. At the same time they argued that in their opinion domestic demand growth had already exceeded potential output growth, which could lead to a deterioration in the current account balance, especially if the improvement in the terms of trade were to come to a halt.

Council members assessed that the annual price growth would remain negative in the coming quarters, mainly due to the previously observed sharp fall in commodity prices. At the same time, the expected gradual acceleration of economic growth, amidst recovery in the euro area and good situation in the domestic labour market, reduced the risk of inflation remaining below the target in the medium term. Therefore, the Council decided to keep the NBP interest rates unchanged: the reference rate at 1.50%, the lombard rate at 2.50%, the deposit rate at 0.50% and the rediscount rate at 1.75%.

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Narodowy Bank Polski ul. Świętokrzyska 11/21 00-919 Warszawa tel. +48 22 185 28 88 sekretariat.rpp@nbp.pl