NBP

National Bank of Poland

Monetary Policy Council

MINUTES OF THE MONETARY POLICY COUNCIL DECISION-MAKING MEETING HELD ON 23 NOVEMBER 2010

At the meeting, the Monetary Policy Council discussed the outlook for economic growth and inflation, the situation in the labour market, monetary and credit aggregates and the zloty exchange rate developments.

The Council emphasised further recovery of economic activity in Poland, which will most likely continue in the quarters to come. Some Council members pointed to the fact that international institutions had increased their forecasts of Poland's GDP growth for 2011. These members stressed that GDP growth was increasingly supported by domestic factors, in particular by individual consumption growth, which is encouraged by the improving labour market situation. They also pointed to the relatively high level of production capacity utilisation, which should translate into revival of enterprises' investment demand, particularly considering their very good financial situation. The continuation of high – in their assessment – GDP growth in the coming quarters should be additionally supported by the favourable outlook for exports, connected in particular with high economic activity in Germany and a fast increase in German exports. In the opinion of those Council members, in 2011 no significant demand reduction should be expected on the part of the public finance sector in Poland. On the other hand, other Council members argued that there was still a risk of a slowdown in the global economic growth, and that domestic demand was dependent on consumer sentiment, which had once again slightly deteriorated in November, and on the level of public investment, which could be delayed. In the opinion of those Council members, the postponement of public investment and the reduction of other expenditure of the public finance sector, in combination with a possible further increase in taxes, would also result from a necessary fiscal policy tightening in 2011, which in the short run would be slowing GDP growth. Moreover, some Council members pointed out that without a significant recovery in investment loans, it would be impossible to boost corporate investment.

While discussing the situation in the labour market, some Council members emphasised that the growth in the number of economically active persons meant that in the recent months the rising employment had not been matched by a declining rate of unemployment, which resulted in the fact that the level of labour market tensions was not growing, and wage pressure remained limited. The absence of significant wage pressure was also confirmed – in their opinion – by the data on wages in the economy, whose growth in 2010 Q3 was low. Other Council members, however, argued that a further increase in employment in the enterprise sector, combined with the growing number of job offers, signalled a revival in the labour market, which could contribute to a gradual build-up of wage pressure. According to those Council members, the very good financial results of companies could be conducive to accelerated wage growth, particularly in the state-controlled companies of the raw material sector. Some Council members continued to indicate that the opening of the German and Austrian labour markets in May 2011 constitute an uncertainty factor for the development of the labour supply in Poland. Some Council members emphasised that developments in the labour market, including the amount of labour supply, would also depend on changes in the tax and pension policy.

While discussing changes in credit aggregates, it was indicated that the slight slowdown in the growth of loans to households (resulting largely from the gradual implementation of Recommendation T) was accompanied by continued low growth of lending to the corporate sector. At the same time, some Council members noted that, taking into account the increasing percentage of irregular loans, banks would not be willing to ease their lending policies. This should reduce the risk of excessive credit expansion and asset price rises, as well as of the increase of inflationary pressures. According to these Council members, the limited risk of excessive inflationary pressure was also indicated by the decelerated growth of monetary aggregates over the recent period. Other Council members argued that the monthly increases in housing loans to households remained at a relatively high level (lower only to that in 2007-2008), while loans to companies had been steadily rising for several months. These Council members believe that the expected acceleration of GDP growth may be supporting an accelerated credit growth – on the one hand, by strengthening the private sector demand for credit and, on the other hand, by encouraging banks to ease their lending conditions. They pointed out that the decline in the growth of money supply in October had been due to the base effect resulting from an increased demand for short-term credit in October 2009 fuelled by the privatisation of PGE.

While analysing the rise in CPI inflation in October 2010 to 2.8%, it was pointed out that it had resulted from higher growth of energy and food prices, i.e. factors largely beyond the influence of monetary policy. Some Council members emphasised the fact that core inflation net of food and energy prices remained low, while some forecasts indicated that, after a temporary increase, CPI inflation would decline in the second half of 2011. Other members of the Council pointed out that other measures of core inflation had risen and the subsequent months could also bring an increase in core inflation net of food and energy prices. Moreover, those members argued that the increase in food and energy prices could not be considered temporary. In their assessment, it resulted largely from the impact of global factors (i.e. from a strong increase in commodity prices in the world markets associated with rising demand from the emerging economies). These factors could support high growth of prices of those goods also in the future.

The Council also discussed about inflation expectations and the risk of second-round effects. Some Council members argued that inflation expectations in Poland were to a large extent adaptive, so the rise in current inflation would translate to higher inflation expectations, increasing the risk of second-round effects. Expectations can also be raised by the growing prices of frequently purchased goods, and also the increase of most VAT rates in 2011. Other Council members assessed that the risk of the growing inflation expectations translating into wage growth was small, since trade unions had little power in the Polish economy. They also emphasised that the growth of unit labour costs was still low, which meant that due to increasing labour productivity a possible acceleration of wage growth would have only limited impact on inflation.

While analysing the impact of external conditions on the outlook for economic growth and inflation in Poland, some Council members pointed to the relatively high economic growth in the world, including the continued recovery in developed countries and a high growth of GDP in developing countries. According to these members of the Council, the growing activity in the global economy would support acceleration of GDP growth in Poland and maintaining high growth of commodity prices in the world markets in the years to come – translating into a rise in domestic inflationary pressures. Some Council members emphasised in particular the relatively favourable situation in Germany, which, through the positive impact on Polish exports and GDP growth, could also be conducive to a gradual rise in domestic inflationary pressure. Other Council members pointed out that activity in the German economy was heavily dependent on GDP growth in China, which was tightening its macroeconomic policies, which would be conducive to reducing Chinese economic growth. At the same time, Council members emphasised that an important uncertainty factor for the global economic growth remained the difficult fiscal situation of some euro-area countries and the effects of further expansionary fiscal and monetary policy in the United States, as well as tensions between the governments of the world's largest economies related to the exchange rate policies.

While discussing the changes in the external environment of the Polish economy which are likely to impact the developments of the exchange rate of the Polish zloty, members of the Council pointed, on the one hand, at the Fed's decision on increasing the scale of monetary expansion, and, on the other hand, at the deepening of budgetary problems in Ireland. Some Council members emphasized at this point that response of financial markets to both events was weaker than to similar developments observed previously. This may indicate that any further turmoil connected with the situation in some euro-area countries would have a limited impact on the investors' sentiment in the global financial markets. Some members of the Council argued, at the same time, that developments of the zloty exchange rate might be driven not only by external factors but also by domestic ones, especially by the size of the issue of treasury securities. Those members indicated that gradual reduction of the inflow of portfolio investments to Poland in the recent period could have been caused by a decrease in the issue of new bonds, resulting from satisfying the country's borrowing needs for 2010.

While addressing the impact of the domestic monetary policy on the zloty exchange rate amidst extended period of monetary expansion of major central banks, some members of the Council emphasized that importance of a possible rise in interest rate disparity might be limited due to growing – as a result of the crisis – role of changes in the global risk aversion to exchange rate developments. In the opinion of those Council members lower responsiveness of the exchange rate to changes in the disparity is a factor speaking in favour of tightening monetary policy in Poland as soon as possible. Those members also argued that a possible appreciation of the zloty would be most likely accompanied by the appreciation of currencies of other emerging economies. They pointed out that that the risk of the zloty appreciation being stronger than that of other emerging currencies was limited by high deficit in public finance sector in Poland. Other members of the Council emphasized that developments of the zloty exchange rate were an important factor affecting – together with the level of interest rates – the total restrictiveness of monetary conditions and thus they should be taken into consideration in the conduct of the monetary policy.

During the meeting, members of the Council also discussed about possible changes in the potential output growth of the Polish economy. Some members of the Council emphasized that regardless of changes in the potential output growth, two factors – on the one hand, a decline in the current account deficit considered safe by financial market participants, and, on the other hand, rising deficit in public finance – could support a possible increase of the equilibrium interest rate. Other members of the Council indicated that high level of liquidity in the global financial markets could support a possible decrease in the equilibrium interest rate.

The Council also discussed the balance of costs of a too late and too early tightening of the monetary policy.

While considering the decision on interest rates, some members of the Council assessed that the risk of growing wage and inflationary pressure connected with accelerating GDP growth and the risk of growing inflation expectations justified increasing the NBP interest rates. In their opinion, an increase of interest rates by 50 basis points could constitute a one-off adjustment of monetary policy parameters to the current economic situation, following a period of a strong economic slowdown caused by the global financial crisis. On the other hand, an increase of interest rates by 25 basis points could start a gradual tightening of the monetary policy, whose scale and pace would depend on the economic developments in the coming quarters.

In the opinion of the majority of Council members, the absence of a significant wage and inflationary pressures, persistently weak demand pressure and limited lending justified keeping the NBP interest rates unchanged in November. In the opinion of those members of the Council the persisting risk of excessive zloty appreciation connected with a strong monetary expansion in major developed economies as well as uncertainty related to economic developments abroad spoke also in favour of keeping the interest rates unchanged.

A motion to raise the NBP interest rates by 50 basis points was put forward at the meeting. The motion did not pass. Also a motion to raise the NBP interest rates by 25 basis points was put forward at the meeting. The motion did not pass. The Council kept the interest rates unchanged: the reference rate at 3.50%, the lombard rate at 5.00%, the deposit rate at 2.00%, the rediscount rate at 3.75% and the discount rate at 4.00%.

Publication date: 16 December 2010