National Bank of Poland

Monetary Policy Council

Report on monetary policy implementation in 2011

Warsaw, May 2012
Report on monetary policy implementation in 2011
## TABLE OF CONTENTS

1. Monetary policy strategy in 2011 .............................................................................................................. 5
2. Monetary policy and macroeconomic developments in 2011 .............................................................. 9
   2.1. Macroeconomic developments in 2011 ............................................................................................. 9
   2.2. Monetary policy in 2011 ..................................................................................................................... 16
3. Monetary policy instruments in 2011 ..................................................................................................... 23
   Appendix 1. GDP and aggregate demand ............................................................................................... 31
   Appendix 2. Prices of consumer goods and services ............................................................................... 35
   Appendix 3. Balance of payments .......................................................................................................... 39
   Appendix 4. Money and credit ............................................................................................................... 43
   Appendix 5. Minutes of MPC decision-making meetings held in 2011 ................................................ 47
   Appendix 6. Voting records of MPC members on motions and resolutions ............................................. 77
In presenting the *Report on monetary policy implementation*, the Monetary Policy Council acts in accordance with Article 227 of the Constitution of the Republic of Poland, which imposes an obligation on the Council to present a report on the implementation of monetary policy guidelines within 5 months following the end of the fiscal year. In accordance with Article 53 of the Act on the National Bank of Poland, the *Report on monetary policy implementation* is published in the Official Gazette of the Republic of Poland, the *Monitor Polski*.

The Report presents the main elements of the implemented strategy of monetary policy, a description of macroeconomic conditions and decisions taken with respect to monetary policy in the reported year, as well as a description of the applied monetary policy tools.

The Report is accompanied by Appendices presenting the development of important macroeconomic variables, as well as by *Minutes of the Monetary Policy Council decision-making meetings* and the voting records of the Council’s members on motions and resolutions.

An ex post assessment of the conduct of monetary policy should take into account, above all, that the decisions of monetary authorities affect the economy with considerable lags, with the strongest impact being observed after several quarters. Moreover, the economy is subject to macroeconomic shocks, which, while remaining in most cases outside the control of the domestic monetary policy, may to a large extent affect the economic situation and domestic inflationary processes in the short, and sometimes in the medium term.

This *Report on monetary policy implementation in 2011* is a translation of the National Bank of Poland’s *Sprawozdanie z wykonania założeń polityki pieniężnej na rok 2011* in Polish. In case of discrepancies, the original prevails.
Chapter 1.

MONETARY POLICY STRATEGY IN 2011

In 2011, the Monetary Policy Council, henceforth “the Council”, implemented the Monetary Policy Guidelines for 2011, adopted on 29 September 2010. In the Guidelines, the main elements of the monetary policy strategy implemented in 2011 were presented as follows.

According to Article 227 section 1 of the Constitution of the Republic of Poland “the National Bank of Poland shall be responsible for the value of Polish currency”. The Act on the National Bank of Poland of 29 August 1997 states in Article 3 section 1 that “the basic objective of NBP activity of shall be to maintain price stability, and it shall, at the same time, act in support of Government economic policies, insofar as this does not constrain the pursuit of the basic objective of the NBP”. Nowadays central banks understand price stability in terms of inflation as low as not to negatively affect decisions taken by economic agents, including investment and savings decisions. Ensuring thus understood price stability is a fundamental way in which the central bank contributes, by means of its decisions, to high and sustainable economic growth. In pursuit of the task of maintaining price stability, central banks respond both to inflationary and deflationary threats.

Since 1998 the Council, has based its monetary policy on inflation targeting (IT). Beginning 2004, the Council adopted a permanent inflation target of 2.5% with a symmetrical band for deviations of ± 1 percentage point. The Council pursues the strategy under a floating exchange rate regime. However, the floating exchange rate regime does not rule out foreign exchange interventions should they turn out necessary to ensure domestic macroeconomic and financial stability, which is conducive to meeting the inflation target in the medium term.

The experience of the National Bank of Poland, hereinafter “the NBP”, and other central banks shows that IT is an effective way to ensure price stability. The global financial crisis has shown that in order to ensure long-term price stability factors related to financial system stability should play a more pronounced role in monetary policy than to date. Inflation targeting enables the pursuit of such a policy while providing support for the regulatory and supervisory policies addressed to the financial sector.

In pursuing monetary policy the Council is guided by the following principles, which – to a significant extent – remain unchanged of their hitherto understanding:

- First, the notion of permanent inflation target means that it refers to inflation measured as a year-on-year change in prices of consumer goods and services in each month compared to the corresponding period of the preceding year. For a better understanding of inflation processes the use of quarterly and annual inflation indices is also justified, such as those applied in the NBP’s inflation projection, in the state budget and in the statistics of the European Union, hereinafter
“the EU”, including the harmonized index of consumer prices – HICP. An important role in the assessment of inflationary pressure is also played by core inflation indices which make it easier to distinguish between temporary changes in the consumer price index from more sustained changes in inflation pressure.

- Second, monetary policy is unequivocally focused on maintaining inflation as close as possible to the target of 2.5% and not just within the band. This is to facilitate the anchoring of inflation expectations and thus to allow the central bank to change monetary policy parameters less frequently in response to potential shocks affecting current inflation. It may also lead to lower volatility of long-term interest rates.

- Third, the occurrence of shocks in the economy is inevitable. Depending on the strength of the shock and the degree of inertia of inflation expectations, the scale and the duration of inflation deviation from the adopted target may differ. In countries with sustained low inflation, the central bank usually does not respond to deviations from the inflation target if it deems them temporary, even when inflation leaves the band. When assessing the need for response, the Council will, however, take into account the fact that in Poland low inflation expectations have not been sufficiently anchored. The extent to which inflation expectations are anchored affects the scale and persistence of the impact of supply and demand shocks on inflation. In the case of shocks which, in the Council’s opinion, may lead to a relatively permanent increase in inflation expectations and, as a result, to the rise in inflation due to the emergence of the so-called second-round effects, the central bank will adjust its monetary policy parameters accordingly.

- Fourth, the monetary policy response to shocks also depends on their causes and nature. In the case of demand shocks inflation and output move in the same direction. An interest rate increase weakens economic activity in the short term and, subsequently, inflationary pressure. In the case of supply shocks output and inflation move in opposite directions. An attempt to fully neutralise the impact of a supply shock on inflation using monetary policy instruments may lead to an unnecessary plunge in output growth which is already lowered by the supply shock’s negative impact on consumption and investment. On the other hand, an attempt to fully accommodate – by pursuing expansionary monetary policy – the real effects of a supply shock resulting in a rise in inflation and a decline in output growth usually leads to persistently higher inflation. This, in turn, requires far more restrictive monetary policy in subsequent periods. This leads to a stronger deceleration in economic growth than the monetary tightening that prevents inflation from being sustained at a heightened level. The response of the central bank to the shock should depend on the assessment of the persistence of the shock’s effects, including the assessment of the risk of second-round effects.

- Fifth, because of the lags in the response of output and inflation to the monetary policy, the impact of monetary policy on the current inflation is limited. Current decisions of the monetary authorities affect price developments in the future just as the current inflation is influenced by interest rate changes made several quarters before. However, the time lag between an interest rate decision and its strongest impact on real variables (output, employment) and then on inflation is not constant. It depends, to a large extent, on structural and institutional changes in the economy. Changes in the monetary transmission mechanism means that central banks can only
Chapter 1. Monetary policy strategy in 2011

approximately assess this time lag. Turmoil in the domestic and international financial system may constitute an additional factor disrupting the monetary transmission mechanism.

- Sixth, monetary policy should take into account the need to maintain financial stability which is indispensable to ensure price stability in the longer term and which enables effective functioning of the monetary policy transmission mechanism. In this context, when assessing the balance of risks to future inflation and economic growth, asset price developments are of particular importance. Excessive interest rates cuts and the long-lasting maintaining lowered interest rates amidst low inflation and simultaneous fast economic growth may lead to a rapid asset price growth, thus increasing the risk of the so-called speculative bubbles. Rapid asset price growth is accompanied by the growing likelihood of asset price deviation from the levels justified by fundamentals, which increases the risk of an abrupt and significant decline in asset prices in the future. Rapid increase in asset prices, especially if it is accompanied by a fast rise in lending, poses a threat to the financial system stability, and consequently – in the longer term – to sustainable economic growth and price stability. Monetary policy supporting financial system stability is thus consistent, in the longer term, with the achievement of the basic objective of the central bank’s activity i.e. ensuring price stability, although it may occasionally pose a risk of temporary deviation of inflation from the target. In order to maintain consistency between attempting to keep inflation at the target and supporting financial system stability, under certain conditions it may be necessary to lengthen the inflation target horizon.

- Seventh, in assessing the risk of turmoil in the financial system and the inflation outlook in the longer run, it is useful to analyse monetary and credit aggregates. A fast increase in these aggregates may lead to growing macroeconomic imbalances in the economy, including imbalances in the asset markets. Monetary policy decisions should take into account the risk connected with excessive increase in these aggregates. Regulatory and supervisory policies in the financial sector that have an impact on credit growth and its structure are an important factor influencing monetary policy.

- Eighth, in assessing the degree of monetary policy restrictiveness not only should the level of real interest rates be considered but also the level of the real exchange rate. Thus understood restrictiveness of monetary policy impacts, along with the implemented fiscal policy, the total restrictiveness of macroeconomic policy. Ensuring price stability amid an overly expansive fiscal policy may require keeping interest rates at a higher level.

- Ninth, monetary policy is pursued under uncertainty which excludes strict control of economic processes. This uncertainty means that while taking decisions related to monetary policy it is necessary to take into account all available information relevant for inflation developments, rather than the results of inflation projection only. Models used by central banks to forecast inflation may be imperfect in adequately reproducing behaviour of the economy if only because of its ongoing structural changes. In addition, it is not possible to adopt a simple policy rule which could be known *ex ante* to market participants.

- Tenth, an important input into the monetary policy decision-making process is the balance of factors affecting the probabilities of future inflation running above or below the target. This balance is based on the assessment of the actual economic developments, including the inflation
projection. While assessing the factors affecting future inflation, the Council takes into consideration the past inflation developments since they have a bearing on the anchoring of inflation expectations at the inflation target. In particular, the Council takes into account the length of the period in which inflation remained close to the target and the length of the period in which it deviated from the target.

In the *Guidelines for 2011*, the Council announced that if a decision was taken on Poland joining the ERM II, the Council would make all necessary adjustments of the monetary policy strategy and – in consultation with the Council of Ministers – of the exchange rate policy to conditions ensuing from the necessity of meeting the convergence criteria required for the euro adoption. In the *Guidelines* the Council also stated that Poland’s accession to ERM II and the euro area should take place at the earliest possible date after meeting all the required legal, economic and organizational conditions.
Chapter 2.
MONETARY POLICY AND MACROECONOMIC DEVELOPMENTS IN 2011

2.1. Macroeconomic developments in 2011

In 2011, the global economy grew at a rate slower than the year before and gradually decelerating (Figure 2.1). The improvement in global business conditions in the first half of 2011 was undermined by the natural disaster in Japan, which disrupted the supply chain in the industrial sector, leading, in effect, to a considerable slowdown in the world’s output growth. In the second half of 2011, as the debt crisis in some euro area countries intensified, the sentiment of economic agents deteriorated significantly and the forecasts of global growth were revised downwards. Throughout 2011, economic activity in many countries was curbed by high commodity prices, which also drove inflation up. At the same time, like in the previous years, business conditions in many countries continued to be adversely affected by on-going adjustments in the balance sheets of both financial and non-financial sectors, as well as the persistently unfavourable situation in labour market. Uncertainty surrounding both future business conditions and the situation in the financial and public finance sectors dampened economic growth in the developed and emerging economies, although the situation continued to vary across regions and countries (Figure 2.1, Figure 2.2).

In the United States, economic growth was driven by the relatively steady rise in domestic demand. Within the euro area the situation was highly diversified. Economic activity in Germany, Poland’s main trading partner, was supported by strong demand from emerging economies – notwithstanding the disturbances related to the natural disasters in Japan – combined with favourable domestic conditions, including a favourable situation in labour market situation. In turn, in the euro area economies affected by the debt crisis, economic activity remained low amidst fiscal tightening, considerable uncertainty about future business conditions and a continued weak labour market. Emerging economies saw robust economic growth in the first three quarters of 2011, which, however, decreased somewhat towards the end of the year in response to prior tightening of their macroeconomic policies and weakening demand from the advanced economies. However, the scale of the slowdown in the emerging economies varied across countries and was the largest in those most closely linked to the euro area.
In 2011, central banks in major developed economies increased the scale of monetary expansion, although during the year, their policies differed to some extent (Figure 2.3, Figure 2.4). The Federal Reserve Bank (Fed) and the Bank of Japan (BoJ) maintained their interest rates at a level close to zero. The European Central Bank (ECB) raised interest rates twice in the first half of 2011 and subsequently cut them twice in 2011 Q4, down to the level from before the hikes. Until mid-2011, the Fed continued the asset purchase programmes launched in 2010. In the second half of 2011, in response to the signs of economic slowdown, the Fed started to gradually extend the average maturity of the assets held (the so-called Operation Twist). BoJ and ECB continued their programmes of quantitative easing of monetary policy throughout 2011. In the second half of 2011, the ECB decided to supplement its liquidity providing programmes with one- and three-year long-term refinancing operations. Following a tightening in 2010 and the first half of 2011, monetary policy in many emerging economies and small open developed economies – in contrast to Poland – was eased in the latter half of 2011, amidst global slowdown and weaker inflationary pressure.
In 2011, in spite of governments’ activities aimed at curbing the public finance sector imbalances, the general government deficits remained high in most developed countries, and their public debt continued to rise (Figure 2.5, Figure 2.6). Measures launched by some governments to cut fiscal imbalances, in particular in the peripheral countries of the euro area, were deemed insufficient by investors, which led to heightened concerns over the solvency of these countries. These concerns were reflected in considerable surge in yields, rating downgrades of bonds issued by many euro area countries and increasing turmoil in the global financial markets (Figure 2.8).

In response to tensions in the financial markets resulting from mounting concerns about the solvency of euro area peripheral countries, EU institutions, the ECB and the governments of the EU countries took a range of measures to mitigate the risk of the financial crisis exacerbating in Europe.
The first half of 2011 saw a sustainable, albeit somewhat lower than in 2010 capital inflow to the emerging markets. However, in the latter half of 2011, rising risk aversion in the global financial markets triggered a capital outflow from the emerging markets. This considerably affected the emerging economies of Central and Eastern Europe, i.e. those with close links to the euro area. Amidst decreasing capital inflow, many emerging market currencies significantly depreciated in the second half of 2011. At the same time, the currencies of some developed economies strongly appreciated (Figure 2.7). Part of the countries – both with depreciating and appreciating currencies – intervened in the market.

In 2011, commodity prices were significantly higher than a year before (Figure 2.9) The sharpest increase, supported by the sustained high demand in the emerging markets, was observed in prices of energy commodities. Political unrest in the Middle East, natural disasters in Asia and Pacific regions and ample liquidity in the global financial markets additionally fuelled global commodity prices, in particular in the first half of 2011. Surging commodity prices contributed to growth in global inflation, which in 2011 – in spite of a decline at the end of the year – remained elevated (Figure 2.10). In some countries, inflation was additionally boosted by the depreciation of their currencies, or by certain measures aimed at curbing the general government deficit, such as indirect tax and administered price increases.
In Poland, fairly robust growth continued in 2011, driven primarily by steady rise in domestic demand (Figure 2.11, Appendix 1). The gradually decelerating, over the year, consumer demand was coupled with accelerating investment (Figure 2.12). In the second half of 2011, higher economic activity was additionally supported by a positive contribution of net exports to GDP growth.

Rise in households’ consumption demand was dragged down by a slow real disposable income growth resulting from sluggish rise in employment in the second half of 2011, elevated inflation and a slow increase in social benefits. In the second half of 2011, private consumption was additionally dampened by the zloty depreciation and the resulting rise in the zloty value of the previously taken currency loans, coupled with tightening credit policies for granting consumer loans to households. In this environment, household sentiment weakened, with an adverse effect on consumption growth. At the same time, investment growth accelerated steadily in 2011. Rising investment outlays were largely driven by robust public investment growth supported by the inflow of EU funds. Moreover,
corporate investment picked up, fuelled by relatively high capacity utilisation and a good financial situation of enterprises. Similarly, households’ housing investment rebounded in 2011, following a dip in 2010.

In spite of the slowing demand from Poland’s main trading partners, the country's balance of trade improved due to the weaker growth in import demand in Poland and the depreciation of the zloty in the latter half of 2011.

In the first half of 2011, favourable business conditions were conducive to an increase in the number of working persons, although in the second half of the year the increase became markedly more subdued. As in the previous year, in 2011 the number of economically active persons increased. Also in parallel to 2010, labour supply growth exceeded that of labour demand, contributing to higher unemployment rate. Throughout 2011, unemployment rate remained slightly higher than in 2010, thus hampering wage growth in the economy\(^1\) (Figure 2.14). As labour productivity growth continued at a relatively stable rate, moderate wage growth was conducive to sustained slow unit labour cost dynamics.

In 2011, the general government deficit was considerably reduced (from 7.8% of GDP in 2010 to 5.1% of GDP, in ESA95 terms). Its narrowing in relation to GDP resulted from measures set forth in the 2011 Budget Act, the reduction of social security contribution transferred to the Open Pension Funds (OFE) enacted in March 2011, and the relatively high GDP growth. Slower public expenditure growth – including, in particular, expenditure by local government units and the Labour Fund – also contributed to deficit reduction. In the course of the year, further plans were presented aimed at curbing the general government deficit in the coming years. Some of these measures were reflected in the 2012 Budget Act.

Bank loans to the corporate sector – following a decrease in the years 2009-2010 – increased in 2011 (Figure 2.13, Appendix 4). The rebound in corporate lending in 2011 comprised of both higher

\(^1\) Except for the third quarter of 2011. However, the hike in wage growth in that period resulted from a statistical effect.
current loans as well as higher investment and real property loans. At the same time, loans to households remained almost unchanged on its 2010 level, as a result of further relatively strong growth in housing loans combined with decline in consumer loans. In 2011, the majority of newly granted housing loans were loans in zloty.

Changes in global financial markets had a significant impact on the situation in the domestic financial market. In the first half of 2011, improved sentiment abroad and data on the strong performance of the Polish economy were conducive to rising prices of domestic financial assets and stable zloty exchange rate. In the second half of 2011, risk aversion increased considerably triggered by the intensifying debt crisis in the peripheral countries of the euro area. This led to a significant slump in share prices and strong depreciation of the zloty (Figure 2.15, Figure 2.16), as well as a slight rise in the yields on Polish bonds. The relatively small increase in the yields on Polish Treasury bonds was supported by a stable inflow of capital to the Polish treasury securities market (Appendix 3).

![Figure 2.15](image1.png)
**Figure 2.15**
Nominal effective zloty exchange rate (increase denotes appreciation).

![Figure 2.16](image2.png)
**Figure 2.16**
Main stock exchange indices in Poland.

After 2010, when inflation stood at 2.6%, in 2011 the annual consumer price index (CPI) reached 4.3%, thus exceeding the NBP inflation target set at 2.5% +/- 1 percentage point (Figure 2.17, Figure 2.18, Appendix 2). In all the months of 2011, the annual CPI inflation remained above the upper band for deviations from the target, i.e. above 3.5%. The elevated inflation was largely the effect of factors beyond the direct influence of the domestic monetary policy, i.e. surging commodity prices in the global markets, tight supply conditions in the domestic agricultural market in the first half of 2011 as well as the zloty depreciation in the second half of 2011 due to deteriorating sentiment in the global financial markets. The above factors translated, in particular, into higher than expected increase in food and energy prices, the latter fuelling a significant rise in administered and regulated prices. Another driver of inflation was the VAT rate increase in January 2011. A limited impact of demand pressure on price growth was evidenced by significantly decelerating consumer demand growth in 2011.

In 2011 it was expected that the impact of most factors increasing inflation would wane – in the case of food prices, since the beginning of a new agricultural season, and in the case of energy prices and VAT increases – over the one year horizon. Similarly, the significant zloty depreciation in the second
half of 2011, related to adverse conditions in the global financial markets could have been treated as a factor whose impact on inflation, although significant, would prove temporary.

Most of the above mentioned factors also affected price developments abroad, keeping inflation rates in a number of countries – both developed and emerging – above the target levels.

Figure 2.17
Annual price growth in the prices of consumer goods and services and contribution of main price categories to CPI.

Figure 2.18
Annual CPI and the inflation target.

2.2. Monetary policy in 2011

Similarly to the previous years, in 2011 in its monetary policy decisions the Council considered, on each occasion, the outlook for inflation in the medium term. The decisions of the Council were affected by the changing assessment of factors influencing inflationary processes over the monetary policy horizon, including, above all, the risk of inflation deviating from the NBP target in the medium term. The assessment took into account the information on current economic developments as well as macroeconomic forecasts prepared by the NBP and external institutions.

In the first half of 2011, the Council increased the NBP interest rates four times: in January, April, May and June, each time by 0.25 percentage point, in particular the reference rate was increased from 3.5% to 4.5%, i.e. by a total of 1 percentage point. Interest rate hikes reflected the Council’s assessment that the relatively strong economic growth combined with rising employment posed the risk of gradually mounting wage pressure. Moreover, in the Council’s opinion, increasing current inflation amidst surging global commodity prices, coupled with the rise in inflation expectations generated the risk of persistently elevated inflation.

In the second half of 2011, the MPC kept the NBP rates unchanged in view of the intensifying debt crisis in the euro area and the ensuing surge in uncertainty about the outlook for global business conditions. In the Council’s opinion the expected deceleration in the domestic economic growth in 2012, triggered by the anticipated global slowdown, amid fiscal tightening and interest rate increases
implemented in the first half of 2011 should enable inflation to return to the target in the medium term. At the same time, the Council stressed in its press releases that it did not rule out the possibility of further monetary policy adjustments, should the outlook for inflation returning to the target deteriorate.

Rising risk aversion in the global financial markets related to heightened concerns about the fiscal problems of some euro area countries in the second half of 2011, contributed to both depreciation and higher exchange rate volatility of the currencies of the emerging economies, including of the zloty exchange rate. At that time, the Council emphasised that the impact of developments in the global financial markets upon the zloty exchange rate may temporarily add to inflation. The NBP conducted several currency interventions selling foreign currencies in exchange for zloty, which curbed the volatility of the zloty exchange rate.

The measures taken by the NBP in 2011 were conducive to inflation returning to the target in the medium term. These measures are presented below in greater detail, along with the circumstances under which they were taken.

***

In 2011 Q1, the incoming data indicated that the recovery in the global economy had consolidated at the turn of 2010 and 2011. Growth continued in the United States and in the euro area. Favourable business conditions sustained in Germany, Poland’s main trading partner. However, economic activity in many developed countries were persistently curbed by high unemployment. In the emerging economies, especially the Asian ones, GDP continued to expand fast. Robust activity in the global economy, especially in the emerging countries, was conducive to rising demand for commodities, which drove their prices up. In turn, surging commodity prices triggered a rise in inflation across the world. In the emerging economies, fast economic growth added to inflationary pressures.

In the period under review, strong macroeconomic data supported improving sentiment in the global financial markets. Yet, the persisting uncertainty about the fiscal situation of some euro area countries, political tensions in the Middle East and Northern Africa, as well as the natural disaster in Japan enhanced risk aversion.

Major central banks continued expansionary monetary policies by maintaining their interest rates at historically low levels, while simultaneously pursuing other, non-standard monetary policy activities. At the same time, major emerging economies kept tightening their monetary policies in order to curb inflation.

In Poland, 2010 Q4 data, pointed to a stabilisation of economic growth at a relatively high level (4.7% y/y), supported by a strong increase in consumption which was driven by rising employment.Incoming monthly data, including those on retail sales, industrial and construction/assembly output indicated sustained robust economic activity in 2011 Q1. Mortgage lending to households continued to rise relatively steeply, whereas consumer loans declined. At the same time, the number of economically active persons in the labour market increased, which, in spite of the upward trend in
employment, translating into an elevated unemployment rate. Consequently, wage growth in enterprises remained moderate.

In 2011 Q1, inflation increased and exceeded the upper band for deviations from the inflation target (in this period inflation amounted to 3.8%, on average). Acceleration in inflation took place amidst moderate demand pressure and was mainly the result of higher than expected growth in food and energy prices, related to unfavourable supply conditions in the domestic food market on the one hand, and rising global commodity prices on the other. Price growth at the beginning of 2011 was additionally boosted by the increase in VAT rates. Core inflation and inflation expectations also rose.

Under these circumstances, the Council assessed that the relatively strong economic growth and rising employment might gradually drive up wage and inflationary pressures in the medium term. A surge in global commodity prices combined with economic recovery generated the risk of persistently elevated inflation expectations. To reduce the risk of heightened inflation persisting in the medium term, the Council raised the NBP rates in January and April 2011, each time by 0.25 percentage point, in particular the reference rate was increased from 3.5% to 4.0%. At the same time, in its press releases the Council emphasised that it would continue to analyse possible signs of mounting inflationary pressure. This indicated the possibility of further interest rate hikes.

Data incoming in 2011 Q2 confirmed a sustained upward trend in the global economy in 2011 Q1, despite a slowdown in the United States. The euro area saw a continued recovery in economic activity, particularly robust in Germany. In many developed countries, however, growth was still curbed by the persistently high unemployment.

In turn, data on 2011 Q2 signalled a possible slowdown abroad. In particular, global business confidence indicators in manufacturing and services deteriorated, and the volume of world trade decreased. Economic activity continued to be adversely affected by the aftermath of the natural disaster in Japan in March 2011, high commodity prices and persisting fiscal problems in some countries, all adding up to uncertainty about future business conditions. On the other hand, a gradual recovery in private consumption in the developed economies and the sustained strong domestic demand in the emerging countries were conducive to higher economic growth.

Concerns about the global economic outlook, particularly in the United States, contributed to slowing the rise in global commodity prices. Yet, commodity prices remained high, which led to rising inflation across the world. In the emerging economies, inflation continued to be additionally fuelled by robust economic growth.

In 2011 Q2, concerns about the stability of public finance in some peripheral countries of the euro area intensified as reflected in ratings downgrades and rising yields on the bonds of these countries (Greece, Portugal and Ireland). There were also mounting concerns about the situation of the public finance in the United States, which led to a lowered outlook on the long-term rating for US bonds.

Monetary policy in major developed countries remained expansionary, although became somewhat diversified. While most major central banks maintained their interest rates at historically low levels, the ECB raised its rate in April 2011 for the first time in three years (by 0.25 percentage points). Amidst fast economic growth and rising inflation, central banks in most emerging economies continued to tighten their monetary policies.
Incoming 2011 Q2 data on the Polish economy confirmed a sustained, relatively high GDP growth in 2011 Q1 (4.5% y/y), which was driven by – apart from the steadily expanding private consumption – rising investment. At the same time, LFS data for 2011 Q1 indicated an accelerated growth in the number of persons working in the economy and a reduction in the unemployment rate, while wage pressure did not rise.

Monthly 2011 Q2 data, including those on industrial and construction/assembly output and on retail sales showed sustained, relatively robust economic activity. Mortgage lending to households continued to rise relatively fast. At the same time, lending to corporates accelerated.

In 2011 Q2, inflation continued to increase (to an average of 4.6% y/y), driven mostly by further – faster than expected – food price growth related to the persistently tight supply conditions in the domestic food market. Simultaneously, the growth in the prices of the remaining goods accelerated somewhat, thus contributing to higher core inflation. Inflation expectations remained elevated.

The Council maintained its assessment that the relatively strong economic growth combined with a further rise in employment might gradually drive up wage pressure, leading to sustained heightened inflation. The elevated inflation expectations added to the risk that heightened inflation would persist. In order to curb this risk, in May and June 2011, the Council continued to tighten monetary policy by raising the NBP rates, each time by 0.25 percentage point, in particular the reference rate was increased from 4.0% to 4.5%. In June 2011 – after the interest rate increase – the Council hinted the possibility of keeping interest rates unchanged in the subsequent months, and assessed that the substantial monetary tightening implemented since the beginning of the year should enable inflation to return to the target in the medium term. At the same time, the Council did not rule out further adjustment of monetary policy, should the outlook for inflation returning to the target deteriorate.

Data on GDP in 2011 Q2, incoming in the subsequent period, signalled a deeper than expected economic slowdown in the United States and the euro area, accompanied by weaker performance of the emerging economies, including China. In 2011 Q3, the sentiment of economic agents deteriorated considerably across the world, and economic growth forecasts for many countries were revised downward. Current and future business conditions were adversely affected by mounting concerns about the fiscal stability of many countries, high (though gradually subsiding) commodity prices and slow household consumption growth in the developed countries, curbed by the persistently weak labour market. Inflation in both developed and emerging economies remained elevated.

Simultaneously, in 2011 Q3, the downgrade of long-term US treasury bond rating was accompanied by a slump in equity prices and a further decline in global commodity prices. Against the backdrop of rising risk aversion in global financial markets, emerging market currencies weakened, including considerable depreciation of the zloty.

The monetary policy of major central banks was diversified in that period: the ECB raised interest rates again in July 2011, by 0.25 percentage point, while the Fed, Bank of England and the Swiss National Bank maintained policy interest rates at historically low levels. Moreover, in September the Fed initiated the program of extending the average maturity of its portfolio (the so-called Operation
Twist), thus exerting downward pressure on long-term interest rates. At the same time, monetary policy was eased in some emerging economies.

In Poland, data on GDP in 2011 Q2 confirmed relatively strong and stable growth (4.3% y/y), fuelled by steadily rising private consumption and accelerating investment. At the same time, following a period of solid growth, employment slowed down and the unemployment rate remained at an elevated level. Wage growth temporary accelerated in 2011 Q2, driven mainly by disbursement of additional remuneration components related to very good financial performance of enterprises.

In 2011 Q3, the incoming monthly data suggested slower growth in the corporate sector employment and in industrial output amid further strong performance in construction/assembly output and retail sales. At the same time, business confidence indicators deteriorated, signalling a possible slowdown in economic activity in the subsequent quarters. Lending to corporates continued to rise and a relatively fast growth in mortgage lending was sustained.

In 2011 Q3, the CPI inflation decreased driven by slower growth in food prices. Yet, the annual CPI index - as well as inflation expectations - remained high (it amounted to 4.1% on average in 2011 Q3) and persisted markedly above the NBP’s inflation target. Energy price growth picked up again, including the prices of fuel, which rose considerably after the deep depreciation of the zloty in August and September related to strong increase in risk aversion in the global financial markets. At the same time, core inflation increased, in part as a result of rising administered prices of services relating to home maintenance.

Given the above, the Council assessed that in the medium term inflation would be curbed by the anticipated slower domestic economic growth, amidst the fiscal tightening, including reduced public investment spending, coupled with interest rate increases implemented in the first half of 2011 and the likely global economic slowdown. In the opinion of the Council, the significant monetary policy tightening implemented in the first half of 2011 should be conducive to inflation returning to the target in the medium term. Consequently, in 2011 Q3 the Council kept the NBP interest rates unchanged. However, in its press releases the Council still did not rule out the possibility of further monetary policy adjustments, should the outlook for inflation returning to the target deteriorate.

At the same time, the Council pointed out that the impact of the developments in global financial markets upon the zloty exchange rate might pose an upside risk to inflation. Strong depreciation and heightened volatility of the zloty exchange rate, triggered mostly by rising risk aversion in the global financial markets, could temporary contribute to rising inflation. At the end of 2011 Q3, the NBP intervened in the currency market by selling foreign currencies in exchange for zlotys.

Data incoming in 2011 Q4 showed that global growth in 2011 Q3 continued at a sluggish pace and economic conditions varied considerably across countries. In the United States, GDP growth accelerated, while in the euro area it remained slightly above zero. In Germany, GDP growth accelerated in 2011 Q3, supported by favourable conditions in the labour market and relatively strong economic growth in Asia; yet, incoming monthly data pointed to a weakening in this economy in the next quarter. In the major emerging economies, 2011 Q3 economic growth slowed down, in most cases largely as a result of a prior tightening of their macroeconomic policies.
A gradual decrease in commodity prices combined with deteriorating economic activity across the world in 2011 Q4 favoured lowering inflation, both in the developed and in the emerging economies. However, inflation persisted at elevated levels in most countries.

Like in the preceding quarter, in 2011 Q4 the fiscal problems of euro area countries continued to fuel uncertainty concerning future developments in global economic activity, with an adverse effect on the sentiment of economic agents, thus contributing to increasing tensions in the global financial markets.

In the period under review, major central banks were conducting expansionary monetary policy; the ECB - after increasing interest rates in April and in July - decreased them again in November and December, bringing them back to the level seen at the beginning of 2011. Moreover, in December the ECB launched additional long-term operations providing liquidity to financial institutions of the euro area and extended the range of assets eligible as collateral in open market operations, which had a mitigating effect on tensions in the international markets. Also central banks in many emerging countries eased their monetary policies at the end of 2011.

Data on the Polish economy indicated that GDP growth in 2011 Q3 remained relatively robust (4.2%), mainly due to expanding domestic demand. At the same time, the contribution of net exports to GDP growth increased markedly, driven by the zloty depreciation. Although business confidence indicators continued to signal a possible slowdown in economic activity, 2011 Q4 saw further strong growth in industrial as well as construction/assembly output and retail sales. At the same time, lending to corporates continued to increase, accompanied by a relatively fast growth in zloty-denominated mortgage loans to households, amid a further decline in consumer loans.

The number of persons working in the economy continued to rise at an increasingly sluggish pace in 2011 Q3, while the unemployment rate remained elevated. Even though wage growth picked up, this was primarily due to statistical factors. Incoming 2011 Q4 labour market data showed falling employment in the corporate sector in monthly terms and further moderate wage growth.

In the period under review, the annual CPI inflation increased again (in 2011 Q4, it averaged 4.6% y/y), remaining markedly above the NBP’s inflation target, which fuelled elevated inflation expectations. Rising inflation was largely driven by a significant zloty depreciation observed from August 2011 and related to persistently heightened risk aversion. The significant depreciation of the zloty exchange rate contributed to a rise in energy prices (including, in particular, fuel prices), food prices and the prices of the remaining imported goods. As a result, zloty depreciation also translated into higher core inflation.

In 2011 Q4, the Council upheld its opinion that medium-term inflation would be curbed by gradually decelerating domestic demand amidst fiscal tightening, including reduced public investment spending, and the NBP interest rate increases in the first half of 2011, as well as the expected global economic slowdown. Assessing that the monetary policy tightening of the first half of 2011 should enable inflation to return to the target in the medium term, and taking into account the elevated uncertainty about global economic conditions in the subsequent quarters, the Council kept the interest rates unchanged in 2011 Q4. The Council still did not rule out the possibility of further monetary policy adjustments, should the outlook for inflation returning to the target deteriorate.
At the same time the Council continued to emphasise that the potential impact of developments in global financial markets upon the zloty exchange rate posed an upside risk to domestic price growth. Amidst the persistent considerable zloty exchange rate volatility in 2011 Q4, the NBP conducted several interventions in the currency market.

***

In 2011 – as in the previous years – communication with the public was an important element in conducting monetary policy based on inflation targeting regime. It involved the Council’s presentation of its assessment of the current condition of the economy and future path of economic developments. The most important instruments of communication in 2011 continued to include the following cyclical publications: *Inflation Reports*, *Information from the meeting of the Monetary Policy Council* (with accompanying press conferences held after the Council’s meetings), *Minutes of the Monetary Policy Council decision-making meetings* (Appendix 5), as well as the annually published: *Report on Monetary Policy Implementation in 2010* and the *Monetary Policy Guidelines for 2012*\textsuperscript{2}. In the *Monetary Policy Guidelines for 2012*, the Council confirmed the main elements of the hitherto pursued monetary policy strategy of the NBP, introducing some minor amendments thereto.

From April 2011, the Council also decided to speed up the publication of the MPC voting records on the motions and resolutions concerning interest rates. This decision was made with a view to further increasing the transparency of monetary policy.

\textsuperscript{2} The *Minutes of the Monetary Policy Council decision-making meetings* (Annex 5) present a more detailed discussion of the problems and arguments which had a significant impact on the decisions taken by the Council in 2011.
In 2011, the National Bank of Poland pursued the monetary policy by influencing the level of inflation through the interest rate policy. The Monetary Policy Council set the NBP's official interest rates, which determined the yield on other monetary policy instruments.

The range of instruments applied in the implementation of monetary policy did not substantially differ from that used in 2010 and comprised the NBP interest rates, open market operations, standing facilities and the reserve requirement. The NBP's set of available monetary policy instruments to be used was aligned with the monetary policy strategy implemented by NBP as well as with the persisting liquidity surplus in the banking sector. In addition, the range of the adopted monetary policy instruments for 2011 enabled the NBP to launch additional operations at any time, should the situation in the financial markets, particularly in the domestic banking sector, deteriorate.

With the help of the monetary policy instruments, the Council was influencing the level of money market short-term interest rates. In doing so, the Council strove to attain a level of interest rates in the economy that would be conducive to achieving the adopted inflation target in the medium term.

Liquidity in the banking sector in 2011

In 2011, the NBP pursued its monetary policy amidst liquidity surplus prevailing in the banking sector\(^3\), amounting to an average of PLN 95,928 million. This represents an increase of PLN 25,021 million, i.e. 35%, on the 2010 level\(^4\). The amount of liquidity surplus in the banking sector rose steadily until July, with the trend reversing in the subsequent months of 2011.

In the course of the year 2011, changes in the level of the banking sector liquidity surplus were primarily driven by factors beyond the NBP's control (the so-called autonomous liquidity factors).

Key influences here include the purchase by the NBP of foreign currencies deriving mainly from EU funds, and the operations involving exchange of foreign-currency funds into zloty performed by the Ministry of Finance at the NBP. As the net balance of currency purchases by the NBP (i.e. one reduced by the value of currencies sold by the NBP) posted a surplus, liquidity surplus rose by an

---
\(^3\) Liquidity surplus of the banking sector is the surplus of funds retained by the banking sector in excess of the average level of banks' current accounts with the NBP, as determined by the required reserve ratio in the required reserve maintenance period. Liquidity surplus is measured by the total balance of the following operations: main operations, fine-tuning operations such a foreign exchange swaps (none were conducted in 2011) standing facilities.

\(^4\) The data on overall excess liquidity as well as the respective monetary policy operations (presented further on in this chapter) are averages for the required reserve maintenance period.
average of PLN 11,598 million. This was further boosted by the disbursement of PLN 6,203 million from the NBP profit to the Treasury and the payment of discount on the NBP bills, with the average amount standing at PLN 4,062 million.

Factors limiting the level of liquidity surplus in 2011 included increase in volume of cash in circulation (by an average of PLN 8,452 million) as well as in the level of the required reserves (by an average of PLN 6,044 million).

The Council was informed, on an on-going basis, of the amount of the banking sector liquidity surplus.

**NBP interest rates**

In 2011, the principal instrument of the NBP’s monetary policy was the short-term interest rate, i.e. the NBP’s reference rate. Changes in the level of this rate set the direction of the monetary policy pursued. The reference rate determined the yield on the main open market operations and at the same time affected the level of short-term market interest rates.

The NBP deposit rate and the Lombard rate set the corridor for overnight interest rate fluctuations in the interbank market. The rediscount rate, in turn, indirectly determined the interest on the required reserve holdings.5

In the first half of 2011, the Council raised the NBP interest rates four times, by a total of 1 percentage point. As a result of these decisions, from June 2011, the NBP reference rate stood at 4.50%, the Lombard rate at 6.00%, the deposit rate at 3.00% and the rediscount rate at 4.75%.

**Open market operations**

In 2011 the NBP strove to influence liquidity conditions in the banking sector through conducting open market operations, seeking to ensure that short-term market interest rates are kept at a level consistent with the NBP’s reference rate as set by the Council. The goal was pursued through open market operations conducted on a scale sufficient to allow the POLONIA rate to run close to the NBP’s reference rate6.

In 2011, the main open market operations were carried out on a regular weekly basis, in the form of issue of the NBP bills with a 7-day maturity. In 2011, the average issue of bills under the main operations amounted to PLN 95,217 million and exceeded the 2010 level by PLN 22,249 million (Figure 3.1)

In 2011, the Bank also issued the NBP bills as its fine-tuning operations. The maturity of these operations was shorter than that of the main operations. They were designed to curb the impact of changes in the liquidity conditions in the banking sector on short-term market interest rates. A total of 27 fine-tuning operations were carried out throughout the year. The average issue of the NBP bills

---

5 In 2011, the remuneration on the required reserve holding amounted to 0.9 of the rediscount rate.
6 POLONIA (Polish Overnight Index Average) – average overnight rate weighted with the value of transactions in the unsecured interbank deposit market. The NBP publishes the levels of this rate on the Reuters website (NBPS) every day at 5.00 p. m.
under the fine-tuning operations amounted to PLN 1,453 million and exceeded the 2010 level by PLN 1,405 million.

The volume of bills issued, rising until July 2011, was driven by growing liquidity surplus in the banking sector. Lower issues in the subsequent months of 2011 resulted from the above mentioned reversal of the trend in developing liquidity conditions within the banking sector.

As in the preceding year, in 2011 the global financial markets were marred by turmoil which intensified, in particular, in 2011 Q4. As a result, banks became more cautious in managing their own liquidity position, tending to do it on an overnight basis and to build up liquidity buffers. Interbank market participants still maintained low-level lending limits on mutual transactions.

The above patterns hampered the effectiveness of the NBP’s main open market operations. This was evidenced by episodes of underbidding during the NBP’s main operations conducted through tenders.

In spite of adverse trends persisting in the financial markets, in 2011 the POLONIA rate came closer to the NBP reference rate than in the previous years. The positive trend in this respect became particularly pronounced in the second half of 2011, when the deviation of the POLONIA rate was reduced to levels seen only before the collapse of Lehman Brothers (Figure 3.2).

The gap between the POLONIA rate and the NBP reference rate gradually narrowed over 2011, primarily as a result of short-term fine-tuning operations launched by the NBP in December 2010. Initially, the NBP resorted to fine-tuning operations on an ad-hoc basis, within the required reserve maintenance period, in order to affect the liquidity conditions prevailing in the banking sector. These were usually operations with a 2-day or 3-day maturity. As of June 2011, they were supplemented with fine-tuning operations offered at the end of the required reserve maintenance period. These enabled banks to balance their liquidity position over the entire reserve maintenance period.

---

7 A situation in which during monetary policy operations conducted in the form of tender, the banks’ total bid is lower than the supply offered by the central bank.
The NBP interest rates and the POLONIA rate in 2011

Source: NBP data.

Fine-tuning open market operations conducted by the NBP substantially reduced banks’ use of deposit facility as compared to the period after the Lehman Brothers’ collapse. This can be put down to the fact that shorter maturity of the instruments offered under fine-tuning operations, compared with the 7-day maturity of the main operations, coupled with their higher yield versus the remuneration of deposit facility (150 basis points difference) encouraged banks to invest more of their liquidity buffer in the NBP bills (under fine-tuning operations). Consequently, as compared to the previous years, the impact of the deposit facility remuneration (the NBP deposit rate), relatively largely used by banks in the previous years, on the POLONIA rate, diminished. Market participants began to expect the central bank to be able to balance the liquidity conditions in the banking sector predominantly through open market operations with yields equal to the NBP's reference rate.

The effectiveness of fine-tuning operations conducted by the NBP is also evidenced by the limited impact of adverse developments in the global financial markets, which intensified in the second half of 2011 (along with the exacerbation of the sovereign debt crisis in some euro area countries), on the POLONIA rate in that period.

The average absolute deviation of the POLONIA rate from the reference rate stood at 43 basis points in 2011 (56 basis points in the period January-May and 34 basis points in the period June-December, i.e. before and after the NBP launched fine-tuning operations at the end of the required reserve maintenance period respectively)\(^8\). Thus, it was 26 basis points lower than in 2010 and 46 basis points lower than in 2009. However, this level was still higher than that observed before the onset of the crisis in the global financial markets, due to persistence of factors contributing to banks' propensity to maintain liquidity surpluses.

At the same time, volatility of the POLONIA rate, as measured by standard deviation, also decreased in 2011. Compared to 2010, this indicator was 4 basis points lower and stood at 34 basis points. An equal decline in the volatility of the POLONIA rate on the previous year’s level was recorded in 2010.

---

\(^8\) Average deviation of the POLONIA rate was calculated according to the uniform base of 365 days in the year.
Reserve requirement

The requirement to maintain a certain amount of reserves on accounts with the NBP applied to banks, branches of credit institutions and Polish subsidiaries of foreign banks. The required reserves were maintained on an averaged basis, i.e. banks were obliged to hold the average balance of funds on accounts with the NBP in the reserve maintenance period at a level not lower than the amount of the reserve requirement.

Required reserves were calculated on the basis of banks' collected deposits and funds coming from sale of securities. Excluded from reserve calculation were funds received from another domestic bank, acquired from foreign sources for at least 2-year period and those deposited in credit and savings accounts of building societies and in individual pension accounts. Required reserves were calculated and maintained in the Polish zloty. Banks reduced the amount of the calculated reserve requirement by the PLN equivalent of EUR 500 thousand.

In 2011, the reserve requirement ratio amounted to 3.5% on all liabilities, except for funds coming from the sale of securities under repurchase agreements, in which case the reserve requirement stood at 0%.

The amount of required reserves as of 31 December 2011 amounted to PLN 28,039 million, posting an increase of PLN 2,091 million on the corresponding amount as of 31 December 2010 (increase of PLN 8.1%).

The interest earned on banks' required reserve holdings on accounts with the NBP was equivalent to 0.9% of the NBP’s rediscount rate. Given the fact that the rediscount rate was increased, by the decision of the Council, from 3.75% to 4.75% over 2011, average interest on the required reserve holdings rose from 3.38% in 2010 to 4.03% in 2011.

In all reserve maintenance periods, average balances held by banks at the NBP remained slightly in excess of the required reserve level, the surplus ranging from PLN 12.7 million in August to PLN 46.9 million in December. The average excess reserves on banks' accounts amounted to PLN 21.3 million, accounting for 0.08% of the average required reserve (Figure 3.3).

The difference between the reserve holdings and the required reserve in respective reserve maintenance periods could be minimised owing to the range of instruments facilitating the management of funds on accounts with the NBP (standing facilities and intra-day credit facility) and the fact that interest earned on reserve funds was paid only up to the amount of the required reserve.

In 2011, one instance was recorded of breach of the reserve obligation by a commercial bank. All the co-operative banks maintained the mandatory level of required reserve.
Figure 3.3
Changes in the required reserves level and deviations from the reserve requirement in 2011

Source: NBP data.

Standing facilities

Standing facilities (overnight deposit and Lombard credit) served to smooth the level of liquidity in the interbank market and the fluctuations in the overnight rates. These operations were conducted at the initiative of commercial banks, and were designed primarily to provide, on a short-term basis, more liquidity to the banking sector and enable banks to place excess available funds with the NBP for one-day period.

Remuneration of Lombard credit facility, which determines the price of money obtainable from the NBP, set ceiling on fluctuations of overnight rates in the interbank market, while the deposit rate constituted the floor.

Drawings on the Lombard credit were moderate in 2011 and totalled PLN 173.0 million as against PLN 184.2 million in 2010. The average daily use of the Lombard credit amounted to PLN 0.5 million, in similarity to the previous year.

The average daily level of deposits placed by banks at the end of the business day amounted to PLN 261.1 billion in 2011 and was 31% lower than during the previous year. The average overnight deposit amounted to PLN 711.4 million, as against PLN 1,036.1 million in 2010. The facility was most heavily used, as a rule, on the last days of reserve maintenance periods.

Intra-day credit facility helps banks manage liquidity during the business day, while, at the same time, ensuring the liquidity of interbank settlements at the NBP. It is a non-interest bearing loan secured with debt instruments, incurred and repaid on the same business day. In 2011, daily liquidity provision to the banks in the form of intra-day credit facility ranged from PLN 15.4 billion to PLN 41.1 billion. Drawings on intra-day credit facility had increased by 45.5% on its 2010 value.

Intra-day credit in the euro is an instrument ensuring liquidity of settlements in the SORBNET-EURO and TARGET2-NBP systems. The loan, collateralised with Treasury bonds previously admitted by the ECB was incurred and repaid on the same business day. In 2011, daily operational euro liquidity
provision to banks fluctuated between EUR 2.0 million and EUR 54.5 million (in 2010, from EUR 2.3 million to EUR 3.5 million, respectively).

Foreign exchange swaps

By using foreign exchange swap transactions, the NBP was able to purchase (or sell) zloty for foreign currency in the spot market with a simultaneous sale (repurchase) in a fixed-date forward transaction.

Despite the NBP’s continued readiness to offer this type of transaction, in 2011, like the previous year, there was no demand from the banking sector for foreign currency liquidity which the central bank could provide in the form of foreign exchange swap transactions.

Currency interventions

The NBP sold certain amounts of foreign currency between September and December 2011. Foreign exchange interventions were conducted amid heightened global risk aversion resulting in increased volatility of exchange rates of the emerging economy currencies, including the zloty.

The currency interventions were compliant with the monetary policy strategy pursued by the NBP in 2011.
Appendix 1
GDP AND AGGREGATE DEMAND

In 2011, relatively buoyant GDP growth was sustained (4.3% y/y as against 3.9% y/y in 2010). It was driven, amidst weakening aggregate consumption growth, by a marked acceleration in investment, which was accompanied by a positive contribution of net exports to GDP growth in the second half of 2011 (Figure Z.1.1, Figure Z.1.2, Table Z.1.1).

2011 saw a gradual decline in the growth of consumption demand, particularly pronounced in the second half of 2011. Among factors conducive to weaker private consumption growth were: low real disposable income growth, including moderate wage growth, modest increase in social benefits, continued heightened inflation and moreover, in the second half of 2011, zloty depreciation adding to households’ debt burden resulting from FX loans. Lower private consumption growth could have also resulted – albeit to a lesser extent – from a decline in consumer loans, and, in particular, deteriorating household expectations about future economic situation, in particular, amidst persistently elevated unemployment rate and decelerating growth in employment in the second half of 2011.\(^9\)

Gross fixed capital formation rose significantly in 2011, with their growth rate accelerating considerably during the year. The strong rise in investment was supported by a robust growth in

---

9 Negative household sentiment was reflected in the persistently low Current and Leading Consumer Confidence Index published by the GUS. The unemployment rate component of the latter points to concerns about unemployment mounting significantly since 2011 Q2.
public investment, in particular, infrastructural investment, which was largely fuelled by high utilization of EU funds. Growth in households’ housing investment and corporate investment was another factor conducive to higher fixed capital formation. According to the available data, corporate investment expenditure in 2011 rose markedly, which was driven by a relatively high production capacity utilization. Sound financial condition of enterprises was conducive to higher investment expenditure. On the other hand, persisting uncertainty about the overall economic situation deterred companies from significantly expanding their production potential. This was reflected in a high share of replacement investment in the new investment projects.

Changes in inventories had a positive – albeit lower than in 2010 – contribution to GDP growth in 2011. The inventory cycle, which started at the beginning of 2010, came to an end in the second half of 2011 which might have been connected with mounting concerns about economic slowdown in the euro area.

Public consumption was the only GDP component posting a negative growth in 2011. The decline in public consumption might have been connected with the curbing of current expenditure in the public finance sector caused by attempts to tighten fiscal policy.

2011 saw a continued rise in foreign trade; yet, foreign trade growth declined as compared to 2010. A significant fall in import growth was accompanied by a strong depreciation of the zloty, coupled with slightly weakened export growth in the second half of the year, translated into a positive contribution of net exports to GDP growth.

Growth in the gross value added in 2011 remained close to that recorded in 2010 (4.0% y/y and 3.9% y/y, respectively). The three main production sectors made positive contributions to the growth of gross value added, while industry was the only sector whose contribution diminished as compared to 2010. Despite this decline, industry continued to make the largest contribution to gross value added growth (of 1.3 percentage points), followed by market services and agriculture (both of 1.2 percentage points) and construction making a contribution of 0.9 percentage point (Figure Z.1.3, Figure Z.1.4).
## Table Z.1.1

### GDP and domestic demand.

<table>
<thead>
<tr>
<th>Year</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP</td>
<td>3.9</td>
<td>5.3</td>
<td>3.6</td>
<td>6.2</td>
<td>6.8</td>
<td>5.1</td>
<td>1.6</td>
<td>3.9</td>
<td>4.3</td>
</tr>
<tr>
<td>Domestic demand</td>
<td>2.8</td>
<td>6.2</td>
<td>2.5</td>
<td>7.3</td>
<td>8.7</td>
<td>5.6</td>
<td>-1.1</td>
<td>4.6</td>
<td>3.8</td>
</tr>
<tr>
<td>Consumption</td>
<td>2.7</td>
<td>4.3</td>
<td>2.7</td>
<td>5.2</td>
<td>4.6</td>
<td>6.1</td>
<td>2.0</td>
<td>3.4</td>
<td>2.2</td>
</tr>
<tr>
<td>Private consumption</td>
<td>2.1</td>
<td>4.7</td>
<td>2.1</td>
<td>5.0</td>
<td>4.9</td>
<td>5.7</td>
<td>2.1</td>
<td>3.2</td>
<td>3.1</td>
</tr>
<tr>
<td>Capital formation</td>
<td>3.3</td>
<td>14.7</td>
<td>1.4</td>
<td>16.1</td>
<td>24.3</td>
<td>4.0</td>
<td>-11.5</td>
<td>9.3</td>
<td>10.0</td>
</tr>
<tr>
<td>Gross fixed capital formation</td>
<td>-0.1</td>
<td>6.4</td>
<td>6.5</td>
<td>14.9</td>
<td>17.6</td>
<td>9.6</td>
<td>-1.2</td>
<td>-0.2</td>
<td>8.5</td>
</tr>
<tr>
<td>Exports</td>
<td>14.2</td>
<td>14.0</td>
<td>8.0</td>
<td>14.6</td>
<td>9.1</td>
<td>7.1</td>
<td>-6.8</td>
<td>12.1</td>
<td>7.3</td>
</tr>
<tr>
<td>Imports</td>
<td>9.6</td>
<td>15.8</td>
<td>4.7</td>
<td>17.3</td>
<td>13.7</td>
<td>8.0</td>
<td>-12.4</td>
<td>13.9</td>
<td>5.9</td>
</tr>
<tr>
<td>Contribution of net exports to GDP growth (percentage points)</td>
<td>1.0</td>
<td>-1.0</td>
<td>1.1</td>
<td>-1.1</td>
<td>-2.1</td>
<td>-0.6</td>
<td>2.7</td>
<td>-0.7</td>
<td>0.5</td>
</tr>
</tbody>
</table>

### Structure of GDP at current prices (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
<tr>
<td>Domestic demand</td>
<td>102.7</td>
<td>102.4</td>
<td>100.7</td>
<td>101.8</td>
<td>102.9</td>
<td>104.0</td>
<td>100.0</td>
<td>101.2</td>
<td>101.3</td>
</tr>
<tr>
<td>Consumption</td>
<td>83.9</td>
<td>82.3</td>
<td>81.5</td>
<td>80.8</td>
<td>78.4</td>
<td>80.1</td>
<td>79.6</td>
<td>80.3</td>
<td>79.5</td>
</tr>
<tr>
<td>Private consumption</td>
<td>64.8</td>
<td>63.7</td>
<td>62.5</td>
<td>61.6</td>
<td>59.6</td>
<td>60.7</td>
<td>60.3</td>
<td>60.6</td>
<td>60.5</td>
</tr>
<tr>
<td>Capital formation</td>
<td>18.7</td>
<td>20.1</td>
<td>19.3</td>
<td>21.1</td>
<td>24.4</td>
<td>23.9</td>
<td>20.4</td>
<td>21.0</td>
<td>21.8</td>
</tr>
<tr>
<td>Gross fixed capital formation</td>
<td>18.2</td>
<td>18.1</td>
<td>18.2</td>
<td>19.7</td>
<td>21.6</td>
<td>22.3</td>
<td>21.2</td>
<td>19.9</td>
<td>20.3</td>
</tr>
<tr>
<td>Exports</td>
<td>33.3</td>
<td>37.5</td>
<td>37.1</td>
<td>40.4</td>
<td>40.8</td>
<td>39.9</td>
<td>39.5</td>
<td>42.3</td>
<td>44.7</td>
</tr>
<tr>
<td>Imports</td>
<td>36.0</td>
<td>39.8</td>
<td>37.8</td>
<td>42.2</td>
<td>43.6</td>
<td>43.9</td>
<td>39.4</td>
<td>43.5</td>
<td>46.0</td>
</tr>
<tr>
<td>Net exports</td>
<td>-2.7</td>
<td>-2.4</td>
<td>-0.7</td>
<td>-1.8</td>
<td>-2.9</td>
<td>-4.0</td>
<td>0.1</td>
<td>-1.2</td>
<td>-1.3</td>
</tr>
</tbody>
</table>

**Source:** GUS data, NBP calculations.
Appendix 2

PRICES OF CONSUMER GOODS AND SERVICES

In 2011 the average annual price index of consumer goods and services (CPI) stood at q%, thus running above the NBP inflation target of 2.5%, with symmetrical band for deviations of ± 1 percentage point. Throughout 2011, the annual CPI inflation remained above the upper limit for deviations from the target, i.e. above 3.5% (Figure Z.2.1, Table Z.2.1).

Inflation running at a heightened level in 2011 was mainly caused by factors beyond the direct influence of domestic monetary policy decisions, amidst rather moderate demand pressure. Factors beyond the direct influence of domestic policy decisions, which considerably boosted inflation in 2011, included, in particular: high prices of agricultural and energy commodities, substantial depreciation of the zloty, largely related to significantly deteriorating sentiment in the global financial markets in the second half of 2011 and VAT increases¹⁰. The majority of the above mentioned factors affected also core inflation, which in 2011 – similarly to CPI inflation – was higher than a year before (Figure Z.2.2).

¹⁰At the beginning of 2011 VAT rates were changed. The basic VAT rate increased from 22% to 23%, and the 7% rate rose to 8%. At the same time, 3% VAT for unprocessed food and 7% VAT for processed food were cancelled. 5% VAT was applied to the majority of food articles, the remaining ones being subject to 8% or 23% VAT.
The consumer price index reflects price developments in four main categories: energy, food and non-alcoholic beverages, goods and services (Figure Z.2.3, Figure Z.2.4). 2011 saw the following changes in price growth in particular groups (categories are listed in the sequence corresponding to their contribution to the total CPI inflation in 2011):

- **Energy** – growth in energy prices throughout 2011 was the highest in the past 10 years. It was largely driven by high prices of energy commodities in the global markets, including, in particular, crude oil prices, which were accompanied by substantial depreciation of the zloty in the second half of the year, additionally boosting commodity prices as expressed in zloty. High commodity prices translated mainly into considerable increases in fuel prices. Energy price growth in 2011 was also supported by higher energy, heating and gas tariffs approved by the Energy Regulatory Office as well as the change in VAT rates. As a result, the average annual energy price growth in 2011 reached 9.1% as compared to 6.2% in 2010.

- **Food and non-alcoholic beverages** – growth in the prices of food and non-alcoholic beverages in 2011 was high, as compared to the previous years, yet subject to considerable fluctuations throughout the year. Food prices were mainly affected by supply changes, amidst relatively stiff demand for food. Rise in the growth of food prices in the first half of 2011 resulted mainly from poor supply conditions in the cereals, fruit and vegetables markets in the 2010/2011 agricultural season. In turn, falling growth in the prices of food and non-alcoholic beverages in the second half of 2011 was largely related to the improved supply conditions, especially in the domestic agricultural market, combined with the beginning of a new agricultural season. Changes in VAT rates were conducive to lower growth in food prices throughout 2011 (the total effect of lower tax rate on processed food and increased tax rate on unprocessed food on food prices was negative). In 2011, the annual average growth of food and non-alcoholic beverages prices amounted to 5.4% as compared to 2.7% in 2010.

- **Services** – growth in the prices of services was on a steady rise in 2011, yet remained moderate, as compared to the previous years. Growth in the prices of services was driven by both rising prices impacted by administrative decisions (e.g. higher sewerage and water supply charges, higher prices of urban transport tickets and railways tickets) and market factors (e.g. higher prices in the category of recreation and culture in mid-2011, including, in particular, higher prices of foreign organized tourism services). At the same time, increases in VAT rates were conducive to higher price growth in services. In 2011 their average annual price growth stood at 3.3% as compared to 2.2% in 2010.

- **Goods** – growth rate of goods was steadily rising throughout 2011 and remained high as compared to the previous years. Growing prices of goods since the beginning of 2011 were supported by increases in the prices of excise goods (tobacco products), which was accompanied by further reduction in decline in the prices of goods subject to competition from low production cost countries. In turn, in the second half of 2011 growth in the prices of goods was mainly driven by zloty depreciation, which was reflected in faster growth in prices of goods sensitive to zloty exchange rate fluctuations (e.g. home equipment and maintenance, goods connected with recreation and culture, in particular, electronic equipment, hygiene products). At the end of 2011 higher growth in the prices of goods was also driven by rising prices of medical articles, resulting from the implementation of new regulations on the prices of reimbursable drugs. VAT rate increases were another factor behind price growth of goods. In
2011 the average annual growth in the prices of goods stood at 1.5% as compared to 1.0% in 2010.

While analysing inflation developments in 2011, it should be noted that in January 2011, the Central Statistical Office (GUS) introduced new rules for quotations of seasonal goods, which in certain months had a relatively strong impact on CPI developments\(^\text{11}\). In particular, according to GUS estimates, changes in quotations of seasonal goods prices decreased the CPI index in February and March 2011 by 0.2 percentage point, and in June and July 2011 drove it up by 0.3 percentage point. In the remaining months of 2011 the impact of changes in seasonal goods quotations on the CPI was less pronounced.

\(^{11}\) On 1 January 2011 came into effect the EU Commission Regulation (EC) no. 330/2009 of 22 April 2009 which introduced minimum requirements for seasonal products to be included in the harmonised index of consumer prices (HICP). This Regulation did not impose the obligation to apply those requirements when computing domestic price indices, yet the GUS decided to implement them in computing the CPI index.
Table Z.2.1
Annual price growth in consumer goods and services and contribution of main price categories to CPI.

<table>
<thead>
<tr>
<th>Weights</th>
<th>Growth rate (y/y, in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2011 (%)</td>
</tr>
<tr>
<td>CPI</td>
<td>100.0</td>
</tr>
<tr>
<td>Core inflation</td>
<td>59.1</td>
</tr>
<tr>
<td>Goods</td>
<td>30.4</td>
</tr>
<tr>
<td>Services</td>
<td>28.8</td>
</tr>
<tr>
<td>Food and non-alcoholic beverages</td>
<td>24.0</td>
</tr>
<tr>
<td>Processed</td>
<td>13.2</td>
</tr>
<tr>
<td>Unprocessed</td>
<td>10.8</td>
</tr>
<tr>
<td>Energy</td>
<td>16.9</td>
</tr>
<tr>
<td>Energy carriers</td>
<td>12.3</td>
</tr>
<tr>
<td>Fuels</td>
<td>4.6</td>
</tr>
</tbody>
</table>

Weights

<table>
<thead>
<tr>
<th>Weights</th>
<th>Contribution to CPI (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2011 (%)</td>
</tr>
<tr>
<td>CPI</td>
<td>100.0</td>
</tr>
<tr>
<td>Core inflation</td>
<td>59.1</td>
</tr>
<tr>
<td>Foods</td>
<td>30.4</td>
</tr>
<tr>
<td>Services</td>
<td>28.8</td>
</tr>
<tr>
<td>Food and non-alcoholic beverages</td>
<td>24.0</td>
</tr>
<tr>
<td>Processed</td>
<td>13.2</td>
</tr>
<tr>
<td>Unprocessed</td>
<td>10.8</td>
</tr>
<tr>
<td>Energy</td>
<td>16.9</td>
</tr>
<tr>
<td>Energy carriers</td>
<td>12.3</td>
</tr>
<tr>
<td>Fuels</td>
<td>4.6</td>
</tr>
</tbody>
</table>

As broken down to 12 COICOP categories

<table>
<thead>
<tr>
<th>Weights</th>
<th>Contribution to CPI (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2011 (%)</td>
</tr>
<tr>
<td>CPI</td>
<td>100.0</td>
</tr>
<tr>
<td>Core inflation</td>
<td>59.1</td>
</tr>
<tr>
<td>Food and non-alcoholic beverages</td>
<td>24.0</td>
</tr>
<tr>
<td>Alcoholic beverages and tobacco products</td>
<td>5.7</td>
</tr>
<tr>
<td>Clothes and footwear</td>
<td>5.2</td>
</tr>
<tr>
<td>Home maintenance and energy</td>
<td>20.7</td>
</tr>
<tr>
<td>Home equipment and household maintenance</td>
<td>4.9</td>
</tr>
<tr>
<td>Health</td>
<td>4.8</td>
</tr>
<tr>
<td>Transportation</td>
<td>9.1</td>
</tr>
<tr>
<td>Recreation and culture</td>
<td>7.8</td>
</tr>
<tr>
<td>Education</td>
<td>1.2</td>
</tr>
<tr>
<td>Restaurants and hotels</td>
<td>6.8</td>
</tr>
<tr>
<td>Other goods and services</td>
<td>5.2</td>
</tr>
</tbody>
</table>

Source: GUS data and NBP calculations based on GUS data.
In 2011, the current account deficit narrowed from 4.7% of GDP recorded in 2010 to 4.3% of GDP. The reduction in the current account deficit – despite increases in the deficits in both goods and income – was due to increases in the surpluses in services and in current transfers (Figure Z.3.1, Figure Z.3.2, Table Z.3.1).

Following a steep rise in foreign trade in 2010, export and import growth declined gradually over 2011. While the first half of the year saw imports rise faster than exports, enhancing the imbalance on the trade account, this trend reversed in the latter half of the year, enabling trade deficit to narrow down\(^\text{12}\). Trends in exports reflected mainly changes in demand from Poland’s main trading partners. In the early 2011, this demand was on a substantial rise – as Germany enjoyed continued robust economic activity – but it embarked on a gradual decline in tact with the economic slowdown in the euro area (Germany included) and its environment. In the second half of 2011, decline in export growth was mitigated by substantial zloty depreciation. Imports, in turn, were largely determined by the size of demand for intermediate goods from the domestic export sector, the scale of inventory rebuilding and the level of private consumption. As the above import drivers lost momentum, particularly in the second half of the year (slower export activity, lower private consumption growth and the completion of the inventory rebuilding cycle), amid substantial zloty depreciation, growth in imports decelerated considerably.

\(^{12}\) Appendix 3 analyses balance of payments data expressed in the euro, referring to trade in goods. Both the total amount of imports and exports and their trends differ from those from the national accounts.
In 2011, the rising deficit in goods was driven by deteriorating terms of trade. The increase in relative import prices vis-a-vis export prices was related to a hike in energy commodity prices in the global markets, which, in the second half of 2011, was accompanied by zloty depreciation.

The 2011 increase in the current account deficit was also triggered by a deepening deficit in income. The latter was related to sound financial performance of Polish companies, resulting in high dividend payments and high amount of reinvested profits by foreign direct investors as well as considerable income paid on portfolio and other investment (comprising, in particular, trade credits).

The improvement in the current account balance was, on the other hand, supported by growing surpluses in services and current transfers. Higher surplus in services was the result of a simultaneous improvement in foreign travel and transportation services. The rising surplus in current transfers was, in turn, related to higher surplus in government transfers, involving mainly net inflow of funds from the European Union, amidst slightly decreased surplus in private transfers, related to lower remittances of income from abroad.

Table 2.3.1
Main items of the balance of payments (EUR million).

<table>
<thead>
<tr>
<th>Balance of payments</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current account</td>
<td>-5 856</td>
<td>-10 425</td>
<td>-19 245</td>
<td>-23 799</td>
<td>-12 152</td>
<td>-16 493</td>
<td>-15 917</td>
</tr>
<tr>
<td>Balance on trade in goods</td>
<td>-2 508</td>
<td>-5 829</td>
<td>-13 827</td>
<td>-20 928</td>
<td>-5 427</td>
<td>-8 893</td>
<td>-10 112</td>
</tr>
<tr>
<td>Balance on trade in services</td>
<td>585</td>
<td>582</td>
<td>3 441</td>
<td>3 475</td>
<td>3 427</td>
<td>2 334</td>
<td>4 341</td>
</tr>
<tr>
<td>Balance on income</td>
<td>-5 490</td>
<td>-7 728</td>
<td>-11 928</td>
<td>-8 685</td>
<td>-11 828</td>
<td>-12 779</td>
<td>-14 443</td>
</tr>
<tr>
<td>Balance on current transfers</td>
<td>1 557</td>
<td>2 550</td>
<td>3 069</td>
<td>2 339</td>
<td>1 676</td>
<td>2 845</td>
<td>4 297</td>
</tr>
<tr>
<td>Capital account</td>
<td>786</td>
<td>1 666</td>
<td>3 418</td>
<td>4 068</td>
<td>5 080</td>
<td>6 453</td>
<td>8 063</td>
</tr>
<tr>
<td>Financial account</td>
<td>12 151</td>
<td>10 586</td>
<td>27 621</td>
<td>25 924</td>
<td>24 597</td>
<td>28 529</td>
<td>19 800</td>
</tr>
<tr>
<td>Polish direct investment abroad</td>
<td>-2 792</td>
<td>-7 137</td>
<td>-4 020</td>
<td>-3 072</td>
<td>-3 335</td>
<td>-4 149</td>
<td>-3 722</td>
</tr>
<tr>
<td>Foreign direct investment in Poland</td>
<td>8 330</td>
<td>15 741</td>
<td>17 242</td>
<td>10 128</td>
<td>9 343</td>
<td>6 996</td>
<td>10 340</td>
</tr>
<tr>
<td>Portfolio investment - assets</td>
<td>-2 008</td>
<td>-3 685</td>
<td>-4 606</td>
<td>1 701</td>
<td>-1 009</td>
<td>-786</td>
<td>477</td>
</tr>
<tr>
<td>Portfolio investment - liabilities</td>
<td>11 797</td>
<td>1 485</td>
<td>-20</td>
<td>-3 655</td>
<td>11 303</td>
<td>20 041</td>
<td>10 890</td>
</tr>
<tr>
<td>Other investment - assets</td>
<td>-2 181</td>
<td>-3 137</td>
<td>-3 321</td>
<td>4 039</td>
<td>3 911</td>
<td>-2 994</td>
<td>-2 099</td>
</tr>
<tr>
<td>Other investment - liabilities</td>
<td>-1 132</td>
<td>7 868</td>
<td>21 804</td>
<td>17 527</td>
<td>5 681</td>
<td>10 048</td>
<td>4 351</td>
</tr>
<tr>
<td>Derivative financial instruments</td>
<td>137</td>
<td>-549</td>
<td>-1 458</td>
<td>-744</td>
<td>-1 297</td>
<td>-327</td>
<td>-437</td>
</tr>
<tr>
<td>Errors and omissions</td>
<td>-627</td>
<td>204</td>
<td>-2 414</td>
<td>-8 621</td>
<td>-7 111</td>
<td>-6 995</td>
<td>-7 252</td>
</tr>
<tr>
<td>Official reserve assets</td>
<td>-6 454</td>
<td>-2 031</td>
<td>-9 380</td>
<td>2 428</td>
<td>-10 414</td>
<td>-11 494</td>
<td>-4 694</td>
</tr>
</tbody>
</table>

Source: NBP data.

Rising investment expenditure on projects co-financed by the European Union was reflected in higher inflows on capital account and resulted in the surplus on this account of 2.2% of GDP in 2011 as against 1.8% of GDP in 2010.

According to the data on the financial account of the balance of payments, the amount of Polish direct investment abroad remained close to its 2010 level. In turn, the value of foreign direct investment (FDI) in Poland had risen as compared to 2010, thus providing higher financing of the deficit on the combined current and capital accounts with FDI inflow. In spite of rising FDI inflow, the surplus on the capital account had shrunk to 5.4% of GDP from the 8.0% of GDP recorded in 2010. This was due to declines in both portfolio investment and other investment balances.
In 2011, the zloty exchange rate depreciated in relation to the major currencies (by 12.0% against the euro, by 12.5% against the US dollar and by 17.5% against the Swiss franc (Figure Z.3.3)\textsuperscript{13}). Consequently, the nominal effective exchange rate of the zloty (NEER) weakened by 11.4% in 2011\textsuperscript{14}. Amidst heightened inflation both globally and domestically (in terms of consumer and producer prices), changes in the real effective exchange rate (REER) in 2011 were mainly accounted for by changes in the nominal exchange rate. Consequently, CPI-deflated REER depreciated by 9.1% and PPI-deflated REER by 11.5% (Figure Z.3.4).

In 2011, the zloty – like many other emerging market currencies – was primarily affected by global factors, most specifically changes in risk aversion in the global financial markets. In 2011 Q1, the zloty exchange rate remained relatively stable, notwithstanding its slight depreciation in March related to heightened uncertainty in the global financial markets in the aftermath of the natural disaster in Japan. In the subsequent months, mounting global risk aversion fuelled by growing concerns about the solvency of certain euro area countries, translated into weaker zloty. At the same time, the exchange rate was supported by the NBP’s subsequent interest rate increases and the launch, by the Ministry of Finance, of exchange of some EU funds in the FX market. In the second half of 2011, a rebound in risk aversion due to the mounting fears about consequences of the sovereign debt crisis in Europe was reflected in a sharp depreciation of the zloty. Apart from the impact of global factors, depreciation of the zloty could also be related to Poland’s relatively close economic and financial relations with the euro area. Impacted by the above factors, the zloty exchange rate experienced considerable volatility, in particular in the second half of 2011. In order to contain its fluctuations, the NBP occasionally intervened in the currency market in the period of September-December 2011.

The year 2011 saw most indicators of the Poland’s external imbalance improve. In particular, apart from the narrowing GDP-related deficits on current and capital accounts, as well as substantial rise in the deficit financing by FDI inflow, Poland’s net external investment position strengthened. There was also a slight improvement in the short-term foreign debt financing to official reserve assets ratio (Table Z.3.2).

\textsuperscript{13} Change calculated as difference between the average rates in December 2011 and December 2010.

\textsuperscript{14} Exchange rate in December 2011 as against December 2010.
Table Z.3. 2
Selected indicators of external imbalances.

<table>
<thead>
<tr>
<th>External imbalances indicators</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current account balance/GDP(%)</td>
<td>-2.4</td>
<td>-3.8</td>
<td>-6.2</td>
<td>-6.6</td>
<td>-3.9</td>
<td>-4.7</td>
<td>-4.3</td>
</tr>
<tr>
<td>Current and capital account balance/GDP (%)</td>
<td>-2.1</td>
<td>-3.2</td>
<td>-5.1</td>
<td>-5.4</td>
<td>-2.3</td>
<td>-2.8</td>
<td>-2.1</td>
</tr>
<tr>
<td>Balance on trade in goods/GDP (%)</td>
<td>-1.1</td>
<td>-2.1</td>
<td>-4.4</td>
<td>-5.8</td>
<td>-1.7</td>
<td>-2.5</td>
<td>-2.7</td>
</tr>
<tr>
<td>Current account balance/current account inflows (%)</td>
<td>-5.8</td>
<td>-8.4</td>
<td>-13.6</td>
<td>-14.9</td>
<td>-9.0</td>
<td>-10.1</td>
<td>-8.8</td>
</tr>
<tr>
<td>Gross foreign direct investment /current account balance (%)</td>
<td>142.2</td>
<td>151.0</td>
<td>89.6</td>
<td>42.6</td>
<td>76.9</td>
<td>40.6</td>
<td>65.0</td>
</tr>
<tr>
<td>Gross foreign direct investment /current and capital account balance (%)</td>
<td>164.3</td>
<td>179.7</td>
<td>108.9</td>
<td>51.3</td>
<td>132.1</td>
<td>66.7</td>
<td>131.7</td>
</tr>
<tr>
<td>Foreign debt/GDP (%)</td>
<td>45.9</td>
<td>47.4</td>
<td>50.9</td>
<td>47.9</td>
<td>62.5</td>
<td>66.6</td>
<td>67.5</td>
</tr>
<tr>
<td>Official reserve assets in terms of monthly imports of goods and services</td>
<td>4.7</td>
<td>3.8</td>
<td>3.9</td>
<td>3.3</td>
<td>5.3</td>
<td>5.4</td>
<td>5.3</td>
</tr>
<tr>
<td>Short-term foreign debt/total foreign debt (%)</td>
<td>20.4</td>
<td>20.4</td>
<td>26.1</td>
<td>26.9</td>
<td>25.0</td>
<td>24.3</td>
<td>22.4</td>
</tr>
<tr>
<td>Short-term foreign debt/official reserve assets (%)</td>
<td>63.6</td>
<td>71.3</td>
<td>92.6</td>
<td>106.0</td>
<td>88.0</td>
<td>81.8</td>
<td>73.7</td>
</tr>
<tr>
<td>Net international investment position/GDP (%)</td>
<td>-44.2</td>
<td>-46.4</td>
<td>-52.8</td>
<td>-47.6</td>
<td>-61.9</td>
<td>-64.5</td>
<td>-59.4</td>
</tr>
</tbody>
</table>

*Source:* NBP calculations based on GUS and NBP data.
In 2011 lending to enterprises and households increased. The total of corporate loans rose substantially after the decline observed in 2009 and 2010, while lending to households increased roughly as much as in 2010.

Rise in corporate loans in 2011 was driven by the increases in current as well as in investment and real property lending, which could be attributed to a rebound in corporate investment activity, particularly pronounced in the second half of the year (Figure Z.4.1, Figure Z.4.2). Throughout the entire 2011, debt of small and medium-sized enterprises grew faster than that of large corporations, which are less reliant on external financing.

Pick-up in corporate lending in 2011 took place despite some rise in interest charged on corporate loans (by 0.7 percentage point). This rise reflected increases in the official NBP interest rates, whose impact on lending rates was though partially offset by banks cutting their margins as compared to the 2010 level. As a result, corporate lending rates increased slightly less than the total NBP rates increase in 2011.

In the first three quarters of 2011, according to banks declarations, corporate lending criteria were changed only slightly. At the same time, banks eased their lending conditions, which – apart from reduction of margins – was reflected in higher loan ceilings and longer maximum loan maturities. In

---

15 Interest rate increase refers to changes in interest on new agreements in December 2011 as compared to December 2010.
2011 Q4, banks somewhat tightened their lending policy with regard to enterprises, on the grounds of heightened risk related to future economic developments.

Housing loans to households rose at a relatively fast, if gradually decelerating pace over the year 2011 (Figure Z.4.3 and Figure Z.4.4). Most of the newly granted loans in 2011 were extended in zloty, which translated into a steadily rising share of zloty loans in total housing loans, thus increasing the effectiveness of the monetary policy transmission mechanism.

In 2011, interest on housing loans, like in the case of corporate loans, increased slightly less than the total of NBP interest rate increases (by 0.8 percentage point). This was the result of lower bank margins as well.

In spite of reduction in margins, throughout 2011, banks – according to their declarations – kept tightening their credit policy in the housing loan segment with regard to both lending criteria and lending conditions. In 2011, in particular, collateral requirements were heightened and creditworthiness assessment procedures were made more rigorous, which was related to the so-called Recommendation T coming into force, along with new provisions of Recommendation S being implemented\(^\text{16}\). Tighter lending policy in the housing loans sector was also driven by the risk related to the economic outlook and unfavourable forecasts for the housing market.

Throughout 2011, household debt resulting from consumer loans decreased steadily. This was driven by tightening lending criteria in this segment in 2010, largely as a result of banks implementing

---

\(^{16}\) Recommendation T regarding best practice in managing retail loan exposure was adopted on 23 February 2010. Its provisions were gradually implemented by the banking sector. It came into full effect ten months following its adoption.

Recommendation S regarding best practice in managing real estate and mortgage loan exposure, which replaced Recommendation S (II), was adopted on 25 January 2011. Its provisions were gradually implemented by the banking sector, coming into full effect on 1 January 2012.
Appendix 4. Money and credit

Recommendation T, coupled with deteriorating quality of the portfolio of these loans in 2009-2010. Household debt resulting from consumer loans dropped in spite of banks declaring easing most of the lending conditions in 2011, including a substantial reduction in margins. Due to lower margins, interest on consumer loans rose by a mere 0.3 percentage point over the entire year 2011, i.e. by markedly less than the total increase in the NBP rates.

In the first half of 2011, the growth of broad money (M3) remained close to that of the nominal GDP, to pick up in the second half of 2011 and subsequently exceed the nominal GDP growth at the of the year. Following the period of relatively steep rise, from July 2011 more liquid components of M3, classified as M1 aggregate, rose at a slower pace than broad money (Figure Z.4.5).

Corporate deposits increased considerably in 2011 and their growth accelerated markedly towards the end of the year (Figure Z.4.6). Rapid rise in corporate deposits in 2011 was supported by strong financial performance of companies and increase in interest rates on corporate deposits (by 1.3 percentage points during the year), which exceeded the NBP policy rates increases. At the same time, robust investment activity of enterprises curbed their deposit growth.

Household deposits also rose significantly in 2011. Their growth gradually accelerated (Figure Z.4.6), driven by both higher interest rate on new zloty deposits (by 1.2 percentage points) and sinking prices of financial assets, including those of shares (falling particularly sharply in August 2011), which encouraged households to redirect part of their savings from riskier financial assets to bank deposits.

**Figure Z.4.5**
Annual M1 and M3 growth rates.

**Figure Z.4.6**
Corporate and household bank deposit growth.

**Source:** NBP data.
Minutes of the Monetary Policy Council decision-making meeting held on 19 January 2011

At the meeting, the Monetary Policy Council discussed issues related to the external environment of the Polish economy, including developments in commodity prices and the situation in the financial markets, as well as the outlook for economic growth and inflation in Poland.

While addressing the external developments it was pointed out that although many countries reported a considerable rise in CPI inflation, global economic growth was still accompanied by low core inflation. It was emphasized that despite the persisting risk of further turmoil in the global economy, the hitherto observed recovery in major developed economies – although not very strong – seems relatively sustainable. At the same time, in the opinion of some Council members previously formulated concerns about a considerable GDP slowdown in major emerging economies are diminishing.

While analysing the situation in the euro area, some members of the Council indicated that recovery in this economy was rather weak and proceeded amidst persistently high unemployment. According to those Council members, in the short term, the announced reduction of the fiscal imbalance may be conducive to lowering GDP growth in the euro area countries. Those Council members emphasized that strong dependence of the Polish economy on the economic developments in Germany might imply that an expected slight deceleration of GDP growth in Germany could be followed by a reduction of GDP growth in Poland. Other members of the Council argued that the economic developments in Great Britain, where significant fiscal tightening might be observed, confirm the limited scale of negative – in the short term – effects of fiscal consolidation on economic growth. Moreover, in the opinion of those Council members, favourable economic developments expected in Poland’s major trading partners, including Germany, where GDP is supposed to run above its long-term average, and further economic recovery in the Central and Eastern European countries, will support the growth of Polish exports, and consequently, of GDP.

While discussing the outlook for inflation, attention was paid to the further rise in the prices of energy and agricultural commodities in the global markets. Members of the Council emphasized that this trend was driven, to a large extent, by long-term factors, i.e. growing demand, especially from emerging countries amidst limited supply growth over the next few years. Factors conducive to
growing prices of certain commodities include also unfavourable weather conditions in some countries and growing production of biofuels. At the same time, some Council members argued that expansionary monetary policy of major central banks combined with improved sentiment in financial markets supported intensified speculation in the commodity markets. Some members of the Council pointed to the attempts undertaken by American supervisory institutions to limit the scale of this activity.

While discussing the issue of appropriate response of the monetary policy to price hikes in the global commodity markets, some members of the Council made reference to the experience of the 1970s oil crises. They emphasized that countries which at that time decided to conduct a relatively restrictive macroeconomic policy managed to keep inflation at a fairly low level. In the opinion of those Council members, although commodity shocks are external in nature, they should be taken into consideration when determining domestic monetary policy in order to prevent inflation from remaining at a heightened level. In this context, those Council members pointed out that currently the increase in global commodity prices translated into a rise in inflation in majority of countries.

Some Council members pointed to the unprecedented scale of fiscal expansion in major developed economies which, amidst a limited possibility of its reduction, would be another factor likely to boost inflation in the external environment of the Polish economy in the longer term.

While addressing the outlook for domestic economic growth, members of the Council pointed out that data on GDP in 2010 Q3, monthly data on economic activity in 2010 Q4 and indicators of economic conditions in January 2011 confirm that economic growth in Poland was continuing at a relatively high level. It was emphasized that in the subsequent quarters GDP growth might translate into gradual intensification of the domestic inflationary pressure, though GDP growth will probably not exceed its long-term average.

Some members of the Council pointed to a relatively fast growth in private consumption whose further rise might be supported by growing employment. In the opinion of those Council members, consumption growth might also be supported by fast growth in housing loans to households exceeding disposable income growth considered neutral with respect to the risk of rising inflation. Those Council members also pointed out that a relatively high and still growing production capacity utilization and very good financial results of companies, especially large ones using capital-intensive technologies, should contribute to a recovery in investment. Favourable outlook for demand of the private sector, combined with favourable economic developments abroad should – in the opinion of those Council members – support relatively fast GDP growth.

Other members of the Council emphasized that persistently high unemployment, which had been growing in the last months of 2010 and which is likely to limit the growth of individual consumption, constituted an uncertainty factor with respect to the scale of further recovery. According to those Council members, the absence of a revival in lending to the corporate sector and a possible tightening of banks’ lending policies due to the deterioration of their loan portfolio might be conducive to the reduction of corporate investment, especially of small and medium-sized enterprises. Moreover, it was pointed out that the risk of a slowdown in domestic economic growth should be reckoned with in the case of strong turmoil connected particularly with the strong fiscal imbalance in certain euro area countries.
Some members of the Council pointed out that the possible crowding out by household lending of other types of bank activity, including the financing of corporate investment, and the relatively weak exchange rate of the zloty, which, among other things, boosts the costs of imports of capital goods, might be conducive to the reduction of the potential output growth of the Polish economy. Those Council members argued that the reduction of the capital part of the pension system might also have a negative impact on potential output growth. Other members of the Council assessed that changes in the allocation of contributions to the pension system would not adversely affect either GDP growth or potential output growth.

While addressing inflation it was pointed out that – in line with expectations – CPI inflation in December 2010 had risen to 3.1%, remaining above the NBP’s inflation target of 2.5%. Some members of the Council emphasized that although the coming months were likely to bring a further rise in CPI inflation due to factors independent of domestic monetary policy such as increases in most VAT rates, inflation might be expected to fall in the second half of 2011. Other members of the Council pointed out that a rise in inflation in December 2010 was partly connected with a rise in core inflation and that available forecasts suggested that over the horizon of monetary policy’s strongest transmission CPI inflation would remain above the inflation target. Those Council members emphasized that the rise in global commodity prices was a risk to price stability. This rise translates into increasing costs of production, which manifests itself in fast PPI growth. Continued economic recovery in Poland, combined with rising inflation abroad will, in the opinion of those members of the Council, make it easier for enterprises to shift growing costs onto consumers. Members of the Council agreed that the risk of inflation consolidating at a heightened level was enhanced by a considerable rise of inflation expectations of individuals and enterprises at the end of 2010, accompanied with upward revisions of inflation forecasts by financial sector analysts.

While analyzing the impact of increases in VAT rates on inflation developments, some members of the Council assessed that it would be insignificant and temporary since in the case of certain goods increases in VAT rates would be offset by reduced markups. Other members of the Council indicated that if, in line with preliminary estimates, the increase in VAT rates had the strongest impact on the costs of road transport, its secondary inflation effect might prove stronger than earlier assessed. Some members of the Council also argued that a stronger translation of the increase in VAT rates into inflation might also be due to a psychological effect resulting in a rise in inflation expectations.

While discussing the situation in the labour market, some members of the Council pointed to the persistent relatively high unemployment rate and a fall in unit labour costs in 2010 Q3 which limit the rise in wage pressure. However, other Council members argued that further recovery in the economy would boost wage demands of employees and reduce enterprises’ ability to resist to those demands. The scale of wage demands may be additionally enhanced by persistently heightened inflation. On the other hand, in addition to increased staff turnover, enterprises' resistance to wage demands may be diminished by very good financial results of companies, especially commodity companies with relatively powerful trade unions.

While discussing the level of interest rates in the Polish economy, members of the Council assessed that the consolidation of the economic recovery abroad and the acceleration of economic growth in Poland, combined with further strong increases in global commodity prices and heightened inflation expectations, increased the risk of inflation running above the NBP’s inflation target in the medium
term. In the Council opinion this warranted a tightening of the monetary policy which, considering a certain improvement in the financial markets' sentiment, should take place at the current meeting. At the same time some members of the Council emphasized that the lower than in the past zloty exchange rate sensitivity to the interest rate differential raises the costs of a possible too late a reaction of the central bank to the inflationary pressure.

The majority of the Council members acknowledged that the raising of interest rates at the January meeting was the beginning of a gradual tightening of the monetary policy, the scale and pace of which would depend on incoming macroeconomic data. Yet, certain members of the Council assessed that at that moment it was difficult to decide whether a further tightening of the monetary policy would be necessary. According to those Council members, in its decisions the Council should take into account, among other things, the monetary policy of the European Central Bank which might start increasing interest rates only in the second half of 2011.

A motion to raise the NBP interest rates by 25 basis points was put forward at the meeting. The motion was passed. The Council decided to raise the interest rates to the following levels: the reference rate to 3.75%, the lombard rate to 5.25%, the deposit rate to 2.25% and the rediscount rate to 4.00%.

Minutes of the Monetary Policy Council decision-making meeting held on 2 March 2011

At the meeting, the Monetary Policy Council discussed the outlook for growth and inflation in Poland, the situation in the domestic labour market and in the external environment of the Polish economy.

With regard to the developments in Poland’s real economy, it was pointed out that GDP growth was likely to remain close to the previous year’s level. Some Council Members drew attention to the fact that there were still no signs of a visible recovery in corporate investment. They emphasised that at the current rate of economic growth there was a limited risk of deep macroeconomic imbalances building up. At the same time, those Council members pointed out that recent data increased the uncertainty about the short-term outlook for output growth. In particular, a further rise in (seasonally adjusted) unemployment rate was mentioned, along with a relatively slow growth of construction and assembly, a slowdown in retail sales growth in January 2011, a deterioration in some economic climate indicators and a markedly slower expansion in lending than in the corresponding periods of previous years.

At the same time, it was pointed out that much of the December 2010 and January 2011 data could have been influenced, to a significant degree, by one-off factors (economic and statistical), which made their assessment more difficult. In this context, some Council members assessed that slow growth in construction and assembly was primarily due to unfavourable weather conditions and thus did not constitute a negative signal for recovery in corporate investment. Equally, in the opinion of these Council members, the weaker retail sales growth did not reflect a strong decrease in individual consumption, as it resulted mainly from the slump in car sales, affected largely by the abolition, as of 2011, of VAT rebates for cars with goods vehicle approval certificates. At the same time, they pointed out that while advance purchases of cars in 2010 increased the growth of domestic demand they simultaneously deepened the negative contribution of net exports to GDP.
With regard to GDP growth in 2012 and 2013, it was pointed out that the March NBP projection expected it to slow down, and individual consumption and gross fixed capital formation growth were weaker than in the previous projection. It was emphasised that the slower rise in investment resulted from the envisaged postponement of the absorption of some EU funds from 2012 till subsequent years as well as the adverse impact of commodity price rises on enterprises’ investment activity. However, some members drew the Council’s attention to the significant uncertainty regarding the developments of investment projects co-financed from EU funds. In addition, some members were of the opinion that the developments in the labour market would act against a deceleration in individual consumption. In those members’ opinion, investment might also rise faster than in the projection. Factors pointing to such a scenario include the rising production capacity utilisation and enterprises’ good financial results, enabling them to self-finance investment projects as well as facilitating access to external financing.

While discussing inflationary pressures in the economy, it was emphasised that the pronounced rise in CPI was driven mainly by the rise in agricultural and energy commodity prices in the world markets, increases in VAT rates and administered prices, i.e. primarily factors unrelated to domestic monetary policy. It was pointed out that the increase in headline inflation feeds into higher inflation expectations of households and enterprises as well as expectations implied by yields on long-term Treasury securities. At the same time, it was indicated that while the available forecasts point to a possible further rise in inflation in the coming months, the impact of the factors contributing to its elevated level will dissipate in the second half of 2011 and – according to some Council members – inflation will subside. Notwithstanding that, it was pointed out that over almost the whole horizon of the March projection – assuming no change in the NBP policy rates – inflation remains above the inflation target. According to the assessment of some Council members, the risk of inflation running above the central path of the March projection was higher than the risk that it would be running below this path.

While addressing wage pressures in the economy, some Council members stressed the fact that the current situation in the labour market did not indicate that these pressures should escalate. They pointed out that the marked acceleration in wage growth in Q4 2010 was probably temporary, as it had been driven by a sharp rise in government sector wages preceding a wage freeze in 2011. Those Council members stated that wage growth in enterprises remained moderate, especially against the background of labour productivity growth, and was consistent with inflation stabilising at the inflation target. However, other Council members pointed to the fact that the acceleration in wage growth at the turn of 2010 and 2011 was indicative of uncertainty as to whether that growth would continue to be moderate and thus might signal the risk of mounting wage pressures within the monetary policy transmission horizon. Those members also expected a gradual deterioration in the relationship between wage and labour productivity growth, stronger than the one signalled by the March projection of inflation and GDP.

Amongst the factors pointing to a limited risk of intensifying wage pressure – including a limited risk of elevated inflation and inflation expectations feeding into wage growth – some Council members listed the rising unemployment rate and the fall in the number of jobs offered, resulting in a significant decrease in the labour market tensions index. Those members highlighted the fact that the weaker labour demand, while resulting mainly from the reduction in the number of subsidised jobs, should mitigate wage growth demands. However, other Council members assessed that while
subsidised jobs had fallen, surveys suggest rising reservation wage. This reduces the likelihood that rising unemployment will significantly weaken wage pressures. These Council members also pointed to the March projection, according to which unemployment rate will gradually decrease and in the second half of 2011 will go below the steadily rising NAWRU unemployment rate. In the opinion of these Council members, good financial results of enterprises were another factor conducive to a possible fast build-up of wage pressures.

While discussing the developments in the external environment of the Polish economy, the Council pointed to the continued moderate GDP growth in major advanced economies and the accompanying rise in headline inflation, driven by rising global commodity prices. Some Council members pointed out that major central banks kept interest rates low, despite some signals pointing to the possibility that some of them will tighten monetary policy. Those members added that the quickly rising government debt in the advanced economies remains an important uncertainty factor for economic growth, including the situation in the global financial markets. At the same time, continued good business climate in Germany was emphasised, along with the strong synchronisation of business cycles in Germany and Poland. Some Council members were of the opinion that the tightening of monetary policy in China may adversely affect the outlook for German, and consequently also Polish exports. According to those members, other factors with a potentially weakening effect on Polish exports include the fiscal consolidation in the EU countries and a possible tightening of monetary policy in some of these economies.

While discussing the rapid growth of commodity prices, some Council members expressed the opinion that the current commodity shocks were temporary supply shocks. However, it was pointed out that the ample liquidity in the financial markets, coupled with low short-term elasticity of commodity supply may result in a stronger than expected rise in these prices. Furthermore, other Council members expressed the view that a sharp rise in demand for commodities on the part of emerging economies may also have been conducive to commodity price increases and therefore these increases may be more lasting. Those Council members believed that rising commodity prices may also reflect mounting inflation concerns amongst the financial markets participants. It was simultaneously pointed out that the elevated commodity prices could act towards a weakening of global economic activity.

While analysing developments in loan aggregates, some Council members highlighted the continuing fall in consumer loans, along with a deceleration in the expansion of housing loans at the beginning of 2011. At the same time other Council members stated that growth of housing loans remained strong compared to the growth in disposable income achievable in the low inflation environment. Some Council members expressed the view that the sluggish expansion in corporate loans might have a curbing effect on investment growth. They also pointed out that a rise in the number of entities without creditworthiness in Q4 2010 did not bode well for a possible recovery in lending. However, other Council members pointed out that the rise in the number of entities without creditworthiness was accompanied by a drop in the share of liabilities of these entities in the total liabilities to the banking sector.

With regard to public sector demand, some Council members assessed that a significant fiscal tightening was unlikely in the years 2011-2012 given the date of the parliamentary election. Other Council members, however, argued that the need to comply with the requirements relating to the
public finance sector deficit resulting from the Excessive Deficit Procedure will translate into a more pronounced fiscal tightening in 2012. In this context, the European Commission decision was invoked, concerning the maintenance of the current approach to accounting for the costs of pension reform in the calculation of the deficit and debt of the sector. Simultaneously, these Council members held the view that a fiscal policy tightening would not curb the build-up of demand pressures in the economy. It was pointed out that a more comprehensive evaluation of the outlook for public finance sector demand would be possible only after the government had presented measures to limit the sector’s deficit in its Convergence Programme update.

While discussing the level of NBP interest rates it was emphasised that their increase in January 2011 initiated the process of a gradual tightening of monetary policy, the scale and pace of which would depend on the incoming data on macroeconomic developments. In the opinion of some Council members, a further interest rate increase at the current meeting was justified, considering the sustained risk that wage and inflation pressure would intensify in the medium term. Such a decision would also limit the risk that the elevated inflation expectations persist. These Council members argued that prompt interest rate increases would reduce the overall scale of increases necessary to stabilise inflation at the inflation target in the medium term. In these members’ opinion, the reduced sensitivity of the zloty exchange rate to the interest rate differential was another argument in favour of prompt interest rate increases.

The majority of Council members represented the view that recent data increased the uncertainty regarding economic growth, including a recovery in investment and sustainability of the acceleration in consumption and thereby substantiated the decision not to change interest rates at the current meeting. Further arguments in favour of this decision included the persistently high unemployment rate and modest wage pressures in the enterprise sector, both reducing the risk that heightened inflation, which up to now has resulted from factors beyond the direct influence of monetary policy, should persist. Furthermore, in the opinion of some Council members, NBP decisions on interest rates should take into account the monetary policy pursued by major central banks, in particular the European Central Bank.

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: reference rate at 3.75%, the lombard rate at 5.25%, the deposit rate at 2.25%, the rediscount rate at 4.00%.

**Minutes of the Monetary Policy Council decision-making meeting held on 5 April 2011**

At the meeting, the Monetary Policy Council discussed the situation in the external environment of the Polish economy, the outlook for economic growth and inflation in Poland as well as the situation in the domestic labour market, including the risk of second round effects.

While assessing the external environment of the Polish economy, it was pointed out that activity growth in the global economy was stable. Yet, it was emphasized that uncertainty about its outlook remained high, and in the recent period was further exacerbated by the events in Japan, North Africa and the Middle East. Some members of the Council also indicated that recovery in many developed economies continued to be sluggish, and activity growth in the United States might not be maintained at the current, relatively high, level as it was largely supported by significant monetary
stimulation. At the same time, attention was paid to a rapid GDP growth in emerging economies and in Germany, and emphasis was given to the strong business cycle synchronization between the Polish and German economies.

Some members of the Council also indicated that inflation remaining at a heightened level in emerging economies was accompanied by signs of growing inflationary pressures in developed economies. Those members pointed out that the central banks in many emerging economies and in some small open developed economies increased their interest rates considerably, and that the European Central Bank was likely to embark on monetary policy tightening in the coming period. Yet, other members of the Council emphasized that even after an increase the ECB's interest rates, similarly to other major central banks' interest rates, would remain at a low level. At the same time, some members of the Council assessed that likely continuation of the accommodative monetary policy in some major developed economies would act towards sustained high global liquidity, and, consequently, increased global inflationary pressure.

While discussing commodity prices in the world markets it was assessed that intensified activity of short-term investors in these markets contributed to the growth of these prices. In the opinion of some members of the Council this was indicative of a temporary character of commodity price increases and the coming months might be expected to bring a fall of these prices. According to those members of the Council, such an assessment is supported also by forecasts of improved supply conditions in the agricultural commodity markets in 2011. Other members of the Council assessed, however, that the rise in commodity prices was to a large extent driven also by growing demand from emerging economies, which indicates that despite possible temporary fluctuations in those prices due to the changing level of short-term investor activity in commodity markets the upward trend of these prices would continue.

With regard to the outlook for economic growth in Poland, some members of the Council pointed out that GDP growth in 2011 and in subsequent years was most likely to be close to, or slightly higher than, that recorded in 2010. It was assessed that GDP growth would be supported by growing external demand and a rise in domestic demand would mainly be driven by rising household consumption, supported by growing employment. Other members of the Council emphasized, on the other hand, that in the absence of recovery in corporate investment and in view of the likely weakening of infrastructure investments co-financed with EU funds, as well as in the face of the anticipated fiscal policy tightening, economic growth might be expected to slow down in subsequent years. It was also pointed out that growing commodity prices in the global markets might also be conducive to lower growth in investment and consumption.

With regard to the prospects for recovery in investment, some members of the Council assessed that corporate investment growth might be faster than currently expected, as suggested by: the growth in gross fixed capital formation in large enterprises in 2010 Q4, very good financial, including liquidity, situation of enterprises and steadily growing production capacity utilization, now exceeding the long-term average. Yet, some members of the Council emphasized that the degree of production capacity utilization in Poland continued to be moderate compared to other EU countries. Members of the Council also pointed at the continuing downward trend in construction and assembly production at the beginning of 2011 and the decline in the indicator of new investment in the enterprises survey. It
was pointed out that continuing uncertainty about the future economic situation was a factor behind enterprises’ lower propensity to invest.

While addressing the developments in individual consumption, some members of the Council assessed that its acceleration at the end of 2010 was not only due to advance purchases of certain goods in response to the expected changes in taxation starting from January 2011. In the opinion of those members of the Council this conclusion was suggested by the data on retail sales at the beginning of 2011. Yet, some members of the Council highlighted that monthly data on retail sales were highly volatile whereas high growth in retail sales in February 2011 resulted partly from a statistical base effect.

While discussing the situation in the labour market, some members of the Council assessed that the data released recently mitigate the risk of rapid build-up of wage and inflationary pressure. In particular, those members pointed at wage growth in enterprises slowing down at the beginning of 2011 and high unemployment level persisting as a result of a relatively rapid rise in the number of the economically active. At the same time, however, the uncertainty regarding the impact of the opening up of the labour market in Germany on labour supply in Poland was emphasized. Those members also pointed out that amidst the falling number of job offers, the labour market tensions indicator (number of job offers per one unemployed) was now at its lowest level in five years. Other members of the Council emphasized, however, that the decline in the number of job offers was driven mainly by the falling number of subsidized job offers which was not a good indicator of labour demand developments in the economy. Those members also pointed at the continuing relatively high employment growth in enterprises.

While discussing the developments in CPI inflation and its outlook, it was emphasized that its heightened level was mainly related to the growing prices of agricultural and energy commodities in the global markets, which had not been offset by changes in the zloty exchange rate, and – to a markedly lesser degree – by a rise in VAT rates. Some members of the Council pointed at a risk of inflation continuing to run above the upper limit for deviations from the NBP inflation target in 2011. Some members of the Council, on the other hand, assessed that following its temporary rise, inflation would fall markedly in the second half of 2011. At the same time, in the opinion of the majority of members of the Council, the risk of intensifying inflationary pressure resulting from the excessive demand growth was currently limited. Yet, some members of the Council pointed at the uncertainty regarding the potential output estimates and indicated at the risk of positive output gap being higher than in the March projection of inflation and GDP.

Some members of the Council emphasized that also a possible increase in wage pressure, driven by heightened inflation expectations could be conducive to a rise in inflation. In the opinion of those members of the Council, a marked rise in inflation expectations of both individuals and enterprises in the recent period was indicative of a higher risk of intensifying wage demands and their translation into wage growth, especially in view of a very good financial condition of enterprises. They pointed that the share of enterprises planning to increase wages in 2011Q2 was the highest in ten quarters. At the same time, some members of the Council emphasized that amidst heightened inflation expectations enterprises might show more propensity to shift higher costs to product prices. Other members of the Council, on the other hand, pointed out that the risk of second round effects in a
situation of high unemployment was uncertain. They emphasized that this risk was also reduced by the limited role of labour unions in the Polish economy.

With regard to the developments in loan aggregates, some members of the Council assessed that a rise in lending to the private sector was moderate and was not a factor behind higher demand pressure in the economy. Those members paid particular attention to the fact that the growth in housing loans weakened at the beginning of 2011 and investment loans to enterprises showed a low growth rate. A slump in consumer loans was also pointed out, yet it was emphasized that this was due to the banks’ tightening their lending policies in response to worsening credit quality and regulatory changes. Other members of the Council assessed, on the other hand, that the growth in housing loans remained strong as compared to the growth in disposable income achievable under price stability. They also stressed that the low growth of corporate lending was connected with very good liquidity situation of enterprises and low level of investment activity.

While discussing the situation in the public finance sector, some members of the Council emphasized that in 2011 the expansionary fiscal policy would be continued which, in their opinion, required a tighter monetary policy. Other members of the Council assessed, however, that in the face of the anticipated tightening of fiscal policy in 2011 it was not a factor justifying interest rate hikes. At the same time, the uncertainty about the scale and structure of fiscal tightening in the coming years was emphasized.

While addressing the zloty exchange rate developments, some members of the Council assessed that a rise in the interest rate differential would support the appreciation of the zloty. Other members of the Council emphasized, however, that the impact of a higher differential on the exchange rate might be limited by the risk of revision of the current account deficit estimates, the uncertainty related to parliamentary elections and the continuing fiscal risk in some euro area countries.

The Council discussed the scale and pace of monetary policy tightening. Some members of the Council assessed that fast interest rate increases would constitute a more effective measure of curbing inflation expectations than gradual tightening of monetary policy. They also emphasized that a quicker ending of the cycle of interest rate increases would mitigate the uncertainty in the financial markets and could support the appreciation of the exchange rate of the zloty. Other members of the Council argued, however, that amidst persisting heightened uncertainty about the outlook for economic growth and inflation in the domestic and global economy, continuation of the gradual tightening of monetary policy was justified.

While analyzing the decision about changing the interest rates at the current meeting, some members of the Council represented the view that persisting uncertainty about the prospects of activity growth in the Polish economy and its environment justified keeping the interest rates unchanged. Yet, the majority of the Council members argued that a marked rise in inflation expectations combined with a strong growth in commodity prices in the global markets created, in a situation of continuing economic recovery, a risk of persisting heightened inflation. In order to contain the risk of inflation running above the inflation target in the medium term, it is justified to continue the cycle of monetary policy tightening and increase interest rates at the present meeting of the Council. Some members of the Council also indicated that the low level of real interest rates
connected with inflation and, as a result, inflation expectations running at a heightened level was another argument in favour of interest rate increases.

A motion to raise the NBP interest rates by 25 basis points was put forward at the meeting. The motion passed. The Council decided to increase the interest rates to the following levels: reference rate to 4.00%, lombard rate to 5.50%, deposit rate to 2.50% and rediscount rate to 4.25%.

Minutes of the Monetary Policy Council decision-making meeting held on 11 May 2011

At the meeting, the Monetary Policy Council discussed the outlook for economic growth and inflation, including the risk of inflation persisting at a heightened level, as well as the pace and possible overall scale of interest rate increases.

While discussing the outlook for domestic economic growth, some members of the Council pointed out that the annual growth rate – after reaching a high level in 2011 Q1 - was likely to decline gradually in the coming quarters, which should reduce the overall scale of interest rate increases necessary to stabilize inflation at the inflation target in the medium term. It was pointed out that GDP growth would be constrained by – somewhat slower than in the first phase of the recovery – growth in external demand, adverse impact of high inflation on private consumption and corporate investment growth, as well as tightening of domestic fiscal policy. Some members of the Council pointed at the persisting risk to GDP growth stemming from the developments in the external environment of the Polish economy, including concerns over the sustainability of economic recovery in the major developed economies associated with an elevated level of unemployment and reduction of high fiscal imbalances.

Other members of the Council, however, assessed that Poland’s economic growth might be faster than currently forecast. Good outlook for growth in Polish exports associated with continued rapid growth in exports in Germany and signs of recovery in corporate investment were, in their opinion, indicative of such a possibility. Those members of the Council pointed out that in view of improving expectations of enterprises about demand and future economic performance, sustained growth in production capacity utilization and good liquidity position, corporate investment could be growing faster than currently anticipated, despite increases in the NBP’s interest rates. According to these members of the Council, acceleration of investments was likely to be accompanied by continued rapid growth in employment, which would support a rise in private consumption. Growing prices of commodities and materials, which the enterprises started to quote as the main barrier to their development, was seen by these members as the main threat to investment growth. At the same time - in their opinion - good liquidity situation of enterprises reduced the risk of potential interest rate increases curbing investment growth.

While discussing the risk of intensifying wage pressure, including second round effects, some members of the Council assessed that this risk was limited at the moment. They pointed to the continuing moderate wage growth in enterprises, and argued that the risk of second round effects was reduced by increased level of unemployment, freezing of aggregate wages in the public finance sector in 2011 and limited role of trade unions in wage-setting in the Polish economy. Those members also pointed out that until now there were no signs that the opening of the labor market in Germany and Austria had resulted in a growing scale of migration to these countries. Other members
of the Council emphasized that the continuing rapid growth of employment in enterprises was indicative of the mounting risk of intensifying wage pressure. They also pointed out that wage demands had soared recently in industries with high trade union density, pointing out that wage growth in enterprises in these industries might put an upward pressure on wages in other enterprises. Those members of the Council pointed out that the risk of accelerating wage growth was boosted by high inflation expectations of households and businesses. They also underlined that starting from 2012, wage growth in the economy would be heightened by the minimum wage increase.

While addressing the situation in the credit market, some members of the Council emphasized that lending to households and businesses continued at a relatively low level. Other members of the Council, however, assessed that a certain upturn in corporate lending could be observed. In particular, they pointed to some signs of recovery in demand for corporate loans, which was an important factor limiting the growth of bank lending to this sector. They also paid attention to the announced easing of lending policy for enterprises in 2011 Q2.

While discussing the NBP interest rate policy, members of the Council agreed that the current assessment of the outlook for economic growth and inflation justified the continuation of monetary policy tightening in a previously assumed scale. The discussion focused on the timing of further tightening of the policy.

According to some members of the Council it was justified to continue with tightening monetary policy by raising interest rates at several month intervals. They pointed out that the recently released data had not fundamentally changed the assessment of the outlook for economic growth and inflation, and emphasized that most participants in the financial markets expected that the current pace of monetary policy tightening would continue. In the opinion of some participants of the meeting, factors speaking in favour of such pace of monetary policy tightening included: supply-side character of an inflation increase reflected in core inflation net of food and energy prices running well below the CPI, absence of signs of second-round effects, forecasts pointing to a slowdown in annual economic growth later in 2011 as well as in commodity prices growth in the world markets and the related projected decline in inflation around the inflation target in 2012. These meeting participants also assessed that the acceleration of interest rate increases might not reduce inflation expectations of households, which are highly adaptive in nature.

Moreover, some members of the Council paid attention to the decision of the Ministry of Finance to exchange some of the European Union funds in the foreign exchange market. They emphasized that a more comprehensive assessment of the impact of this decision on macroeconomic conditions of monetary policy would be possible in the coming months, which – in their view – spoke in favour of keeping interest rates unchanged at the current meeting.

The majority of the Council members decided that acceleration of interest rate increases would be a more effective way to reduce the risk of persisting heightened inflation than interest rate increases implemented at the current pace. According to these members of the Council, the rationale behind more rapid interest rate increases was the need of a pre-emptive response to the growing risk of higher costs of enterprises and heightened inflation expectations translating into price and wage increases. In this context, those members pointed out the data on CPI inflation in March 2011,
indicating an acceleration in price growth not only in food and energy but also in most of other categories of consumer goods and services. Those members also stressed that, considering strong shocks in the agricultural and energy commodity markets, core inflation net of food and energy prices might not correctly reflect permanent changes in inflationary pressures. Those members also pointed out that the projected decline in inflation around the inflation target at the beginning of 2012 was connected with base effects and assumed that rapid increases in commodity prices in the global markets would slow down. It was pointed out that this assumption was subject to uncertainty due to persisting political risk in some oil-exporting countries and growing demand for commodities from emerging economies. Some members of the Council also argued that, in view of the likelihood of inflation and inflation expectations continuing at an elevated level in the coming months, factors speaking in favour of accelerating NBP interest rate hikes included also the risk of real interest rates running at very low levels. It was also emphasized that acceleration of interest rate increases would reduce the need for any strong interest rate adjustments in the future.

While arguing in favour of accelerating interest rate hikes, some members of the Council justified it through uncertainty about the developments of the zloty exchange rate.

A motion to raise the NBP interest rates by 25 basis points was put forward at the meeting. The motion passed. The Council decided to increase the interest rates to the following levels: reference rate to 4.25%, lombard rate to 5.75%, deposit rate to 2.75% and rediscount rate to 4.50%.

Minutes of the Monetary Policy Council decision-making meeting held on 8 June 2011

At the meeting, the Monetary Policy Council analyzed the current and anticipated economic growth and inflation, including the prospects for inflation returning to the target, and discussed future decisions on the NBP interest rates.

While addressing external conditions of economic growth and inflation in Poland, some members of the Council pointed out that although the global economy was recovering, there were signs of a possible weakening of economic conditions abroad in the coming quarters. In particular, attention was paid to the negative effects of the large fiscal imbalance in some euro area countries, including worsening consumer sentiment in the peripheral countries of the euro area and the risk of increasing financial market turmoil related to the fiscal problems of Greece. At the same time, some members of the Council pointed to the limited impact of the so-called quantitative easing of monetary policy on economic activity in the United States. They also emphasized that given the risk of a further weakening of economic conditions in the United States, the Fed might undertake additional measures supporting economic growth in the United States despite rising inflation.

Other members of the Council argued that from the perspective of business conditions in Poland, it was particularly important to take into account the economic situation in Germany, whose prospects remained good, as indicated, among other things, by a favourable structure of GDP growth. The growing role of domestic demand, including investment and private consumption, in Germany’s economic growth means lower sensitivity of this economy to fluctuations in external demand. Moreover, some members of the Council emphasized that economic activity in Poland might increase relatively fast even in the case of moderate GDP growth abroad.
While addressing the situation in the commodity markets, it was pointed out that the worsening of investor sentiment due to concerns about economic growth in the United States translated into a halt of commodity price growth in the world markets. Members of the Council emphasized, however, that considering the prospects for growing demand for commodities amidst limited supply growth, the observed slowdown in price growth might be temporary. Moreover, some members of the Council indicated that unfavourable agro-meteorological conditions in certain regions key to global food supply (i.e. protracted drought in China) might contribute to a further rise in the prices of agricultural commodities. At the same time, members of the Council argued that the anticipated good crop in Russia would limit the growth in food prices.

While discussing the outlook for economic growth in Poland, some members of the Council argued that subsequent quarters might see GDP growth decline as compared to 2011 Q1, which was signalled, among other things, by a halt in the upward trend in industry and construction. In the opinion of these members of the Council the growth inhibiting factors will include weaker growth of public investment which, most likely, will not be accompanied by a proportionally strong acceleration in corporate investment growth, and a slowdown in private consumption growth. In their opinion, the slowdown in private consumption growth will be connected with a weak – amidst heightened inflation - growth of real disposable income. Those members also pointed out that the acceleration in annual retail sales growth in April was largely due to a statistical base effect.

Other members of the Council assessed, however, that economic growth might continue at a relatively high level due to a favourable outlook for growth of both external and domestic demand. In the opinion of those members of the Council, export growth was supported by good conditions in the German economy, investment growth was supported by good financial results of enterprises and growing productive capacity utilization, and the rise in consumption was driven by increasing employment which might continue as a result of growing investment. While referring to the factors that may weaken consumption growth, those members pointed out that maintaining private consumption growth in 2011 Q1 at a level close to that recorded in 2010 Q4 – despite the already heightened inflation at that time, a simultaneous decline in consumer loans and the bringing forward of purchases to the end of 2010 due to changes in VAT rates scheduled to take effect in 2011 – might attest to the fact that the impact of these factors was limited, and improvement in the labour market was crucial for consumption prospects.

While addressing the impact of growing economic activity on inflation, members of the Council were of the opinion that the implemented fiscal tightening combined with the more restrictive monetary policy would limit the risk of too rapid growth of aggregate demand and of intensifying inflationary pressure. Furthermore, the rebound in corporate investment should boost potential output growth, which is a factor supporting the return of inflation to the target in the medium term. At the same time, some members of the Council emphasized that, in their view, the potential growth rate was now lower than before the financial crisis, which should be taken into consideration in the analysis of the output gap and inflationary pressure. Other members of the Council assessed that the impact of the global financial crisis on potential output growth in Poland was not significant.

While assessing wage growth developments, it was emphasized that the acceleration in wage growth in the enterprise sector in April could largely have resulted from the postponement of the payment of bonuses and awards in the mining and energy sectors, and therefore it was difficult to assess the
Appendix 5. Minutes of MPC decision-making meetings held in 2011

sustainability of this phenomenon. At the same time, some members of the Council pointed out that factors such as rising current inflation, elevated inflation expectations, weaker than in previous years growth in the number of the economically active, good financial condition of enterprises, particularly in industries with a strong presence of labour unions where wage demands intensified in the recent period, as well as an increase in the minimum wage, could put an upward pressure on wages. Those members also stressed that although growth in unit labour costs in the economy declined in 2011 Q1, the service sector – constituting the largest share of value added in the economy – saw labour productivity growth significantly below wage growth. They also pointed to lags between wage bargaining and real wage growth. Other members of the Council argued, however, that the still high unemployment rate reduced the risk of a mounting wage pressure. This risk, according to members of the Council, is also limited by the already implemented substantial tightening of the monetary policy of the NBP.

While analyzing the developments in lending to the corporate sector, some members of the Council pointed out that the already observed monetary policy tightening did not hamper growth in loans to businesses, although it translated into rising credit costs, which might be indicative of a favorable outlook for lending to this sector. Other members of the Council assessed that rising credit costs could have a dampening effect on growth in corporate lending.

While addressing the outlook for inflation it was pointed out that the acceleration in price growth was observed in most categories of goods and services, and hence affected core inflation. It was also emphasized that an important change as compared to previous years was the fading of the anti-inflationary effect of falling prices of goods imported from countries with low production costs. Some members of the Council assessed, at the same time, that the downward trend in prices of these goods coming to a halt might be a lasting phenomenon, resulting from changes in the labour markets of the largest emerging economies. It was also stressed that the rapid growth in prices was accompanied by heightened inflation expectations.

While assessing the prospects for inflation returning to the target, some members of the Council pointed out that by the end of 2011 inflation was likely to remain above the upper limit for deviations from the inflation target, as suggested by the short-term forecasts prepared at the NBP. It was argued, at the same time, that in line with these forecasts, inflation was soon to start declining gradually and to come close to the inflation target of 2.5% in 2012.

While discussing the NBP interest rates, the majority of Council members agreed that a fast growth in prices in most groups of goods and services and a high level of inflation expectations combined with the risk of rising wage demands justified raising the NBP interest rates further at the current meeting. In their opinion, the low level of the real interest rate was another factor speaking in favour of an interest rate increase.

Some members of the Council assessed, however, that it was not necessary to increase the NBP interest rates at the current meeting, particularly in view of the expectations of ECB interest rates being kept unchanged in June 2011 as well as considering the external nature of the shocks driving up current inflation in Poland.

At the same time, the majority of Council members indicated that the substantial tightening of monetary policy implemented since the beginning of 2011 should enable inflation to return to the
target in the medium term, and further tightening of monetary policy would be justified should the prospects of inflation returning to the target deteriorate. An assessment of these prospects will be possible after data released in subsequent months have been analysed. Some members of the Council assessed that in subsequent months further tightening of monetary policy was more likely than monetary policy easing. Yet, other members of the Council argued that from the perspective of stabilizing inflation at the target, the current level of the NBP interest rates might be appropriate in the longer term.

The issue of the POLONIA rate running below the NBP reference rate was also addressed at the meeting. In the opinion of some members of the Council, it would be justified to symmetrically narrow the corridor between the NBP deposit rate and the NBP lombard rate which would lead to a lowering of the deviation of the POLONIA rate from the NBP reference rate.

A motion to raise the NBP interest rates by 25 basis points was put forward at the meeting. The motion passed. The Council decided to increase the interest rates to the following levels: reference rate to 4.50%, lombard rate to 6.00%, deposit rate to 3.00% and rediscount rate to 4.75%.

At the meeting a motion to symmetrically narrow the corridor between the NBP deposit rate and the NBP lombard rate by a total of 50 basis points was put forward. The motion did not pass.

Minutes of the Monetary Policy Council decision-making meeting held on 6 July 2011

At the meeting, the Monetary Policy Council analysed the situation in the external environment of the Polish economy, the outlook for economic growth and inflation in Poland, including the prospects for inflation returning to the target, and discussed the current and future decisions on the NBP interest rates.

While addressing the external conditions of economic growth and inflation in Poland, the Council pointed to heightened uncertainty surrounding the outlook for the global economy, including the recent signs of a weakening economic growth in the United States and the prolonged public finance crisis in some euro area countries. In particular, attention was paid to mounting concerns about the stability of the economic situation in Greece and the related rise in risk aversion in the international financial markets.

It was emphasized that the debt crisis might – by increasing uncertainty in the euro area – lead to a decline in economic growth in this region, which would translate into slower GDP growth in Poland. However, some members of the Council argued that activity growth in Poland might be relatively fast even in the case of a moderate GDP growth abroad. In turn, other Council members were of the opinion that increased risk aversion in the international financial markets related to the fiscal problems of Greece was more likely to affect Polish economy through a depreciation in the zloty exchange rate, which would support a heightened inflation in the country.

While discussing the economic growth in Poland in the coming quarters, it was emphasized that GDP growth would most probably weaken gradually, which was also in line with the NBP’s July projection. In this context, a slight weakening of the upward trend in industrial output in the past few months and a decline in the PMI anticipating a slowdown in the manufacturing sector in 2011 Q3 were
pointed to. The expected decline in GDP growth would be – in the opinion of members of the Council – partly connected with fiscal tightening. Some members of the Council emphasized that a rise in current inflation, through its curbing effect on the growth of households’ real disposable income, might also lead to a slowdown in economic growth. Other members of the Council, however, pointed to a drop in households’ deposits last month, which might be indicative of a lower propensity to save. At the same time, it was indicated that it was difficult to assess, on the basis of one month’s data, whether this situation would be a lasting phenomenon. Moreover, it was pointed out that interest rate increases implemented earlier this year might also act towards slower economic growth, albeit with a lag. Some members of the Council remarked, in turn, that interest rate increases had not so far hindered the growth in corporate loans and a rapid increase in housing loans.

While addressing the outlook for maintaining the current rate of GDP growth in Poland in subsequent years, members of the Council emphasized the related high uncertainty, mainly with respect to investment. More specifically, it was unclear, in their opinion, to what extent the decline in public investment might be offset by rising corporate investment. Some members of the Council pointed out that the expected decline in public investment would reduce the crowding out effect on private investment by mitigating the upward pressure on cost of materials and construction works. It was also added that the rise in corporate investment would be fuelled by a relatively high capacity utilization at present. At the same time, other members of the Council indicated that reduced public investment, resulting in lower demand growth in the economy, might stem private investment. While addressing the developments in demand in subsequent years, it was pointed out that the heightened current inflation would boost public expenditure in 2012 as a consequence of indexation of old-age and disability pensions and social benefits.

While discussing inflation, it was indicated that price growth in Poland was largely affected by external factors. In this context, some members of the Council pointed to a high risk of external factors continuing to push up inflation in Poland. Some members of the Council emphasized that the recently observed halting in commodity price growth in the global markets might be temporary, considering the prospects of persistently high global demand for commodities amidst limited possibilities of increasing their supply and a considerable liquidity surplus in the financial markets. In their opinion, commodity prices might, in the longer run, continue on an upward trend. Some members of the Council pointed to the possibility of other countries, including in particular the United States, further easing their monetary and fiscal policy with a view to stimulate economic growth, despite rising inflation. Among other potential external sources of inflation, the announced tax reduction in Germany was mentioned, which would boost demand pressure in this economy, and persistently high inflation in China.

While addressing current inflation in Poland, in particular the fact that it is presently running above the target, some members of the Council were of the opinion that this was due not only to the external supply shocks but also to the heightened domestic inflationary pressure. This followed, in their opinion, from the fact that both the level and the rate of growth of inflation in Poland exceeded those observed in many other countries which had also experienced external supply shocks.

While discussing the outlook for inflation in Poland in 2011, it was emphasized that although May 2011 saw a marked rise in CPI inflation (partly as a result of a change in GUS quotation of seasonal goods prices), and inflation expectations of individuals remained at a heightened level, the available
forecasts suggested that the coming months should see a gradual fall in inflation. Yet, some members of the Council pointed out that, notwithstanding the above, inflation would remain – according to the same forecasts – significantly above the target.

It was emphasized that due to lags in the monetary policy transmission mechanism, the medium-term outlook for inflation was of key importance. It was pointed out that, in line with the July projection based on the NECMOD model, the years 2012-2013 would see inflation lowering close to the target. This would be driven by a weaker GDP growth, a slow-down in the growth of global commodity prices and the statistical base effect. At the same time, some members of the Council indicated the risk of persistence of external sources of inflation and the possibility of a faster GDP growth in Poland than suggested by the projection, which would translate into higher price growth. Some members of the Council emphasized that the persistence of a relatively high core inflation within the projection horizon constituted a risk to CPI inflation subsiding close to the target. According to those members of the Council, a strong deceleration in the growth of food and energy prices expected within the projection horizon is very unlikely.

While discussing the NBP interest rates, the majority of Council members agreed that the interest rates should be kept unchanged at the current meeting. Some members of the Council assessed that the NBP interest rate increases implemented since the beginning of 2011 should enable inflation to return to the target in the medium term as indicated by the July projection of inflation and GDP. It was emphasized that all the available inflation forecasts anticipate its decline within one year. At the same time, the majority of Council members did not rule out the possibility of further interest rate increases in the future, should the prospects of inflation returning to the target deteriorate, and the risk of the so-called second round effects rise.

Some members of the Council indicated, however, that the May 2011 inflation, significantly exceeding expectations, and the fact that it is anticipated to decline only slightly by the end of 2011, coupled with the deepening of the negative real interest rate in Poland amidst a relatively fast economic growth, justified increasing the NBP interest rates at the current meeting.

A motion to raise the NBP interest rates by 25 basis points was put forward at the meeting. The motion was rejected. The Council kept the interest rates unchanged: reference rate at 4.50%, lombard rate at 6.00%, deposit rate at 3.00% and rediscount rate at 4.75%.

Minutes of the Monetary Policy Council decision-making meeting held on 7 September 2011

At its meeting, the Monetary Policy Council addressed the situation in the external environment of the Polish economy and the outlook for domestic economic growth and inflation. It also discussed future decisions concerning the NBP interest rates.

Members of the Council emphasized the recent considerable deterioration of the situation in the external environment of the Polish economy, including a stronger than expected slowdown in the United States and in the euro area, and weaker GDP growth in emerging economies, notably in China, as well as the mounting turmoil in international financial markets. It was pointed out that the flagging business sentiment was also, to a considerable extent, the effect of uncertainty about the effectiveness of political measures undertaken to resolve the fiscal crisis in the euro area. Moreover,
Appendix 5. Minutes of MPC decision-making meetings held in 2011

the Council emphasised the significant downgrades of global growth forecasts by financial market participants, and the end of the cycle of interest rate increases by central banks in a number of small open developed economies and some developing ones.

In the opinion of some Council members, the risk of a global recession recurring has increased in recent weeks. However, according to other Council members, the current slowdown in key developed economies does not presage a forthcoming recession; it is rather a reflection of the reduced growth potential of those economies in the aftermath of the global financial crisis. In this context, these members emphasised particularly the adverse impact of the steep rise in public expenditure following the financial crisis on the private sector's propensity to invest and to consume. They also pointed to the constrained potential for funding private spending with more debt, since the level of that debt is already high. It was stressed that although it is difficult to assess the depth of the global economic slowdown, the risk of a sudden collapse in global business activity remains limited.

While discussing the impact of deteriorating external conditions on the prospects for the Polish economy, some Council members underlined the relative resilience of this economy to external shocks. They assessed that even in the face of slow economic growth in Poland's external environment, domestic GDP growth may remain steady, in particular - in the opinion of some Council members - exports growth may be sustained at a fairly high level. At the same time, the Council pointed to the risk of Polish exports weakening more markedly, should growth in China decelerate considerably, resulting in smaller exports from Germany to that country.

With regard to the economic situation in Poland it was emphasised that while GDP data indicate sustained relatively robust growth in 2011 Q2, incoming information implies it might lose momentum over the subsequent quarters. However, some Council members pointed out that the scale of the slowdown may be mitigated by a rise in private investment, which could be stronger than in the July NBP projection. In support of their position, those members cited higher than anticipated growth in gross fixed capital formation and a marked acceleration in investment outlays by large enterprises in 2011 Q2, as well as very good financial performance of enterprises. At the same time, it was pointed out, however, that the recently observed heightened uncertainty surrounding the outlook for demand may lower enterprises' propensity to invest, as also indicated by survey results. A year-on-year decline in the estimated costs of new investment started by large companies in 2011 Q2 was also emphasized as a possible sign of corporate investment weakening in the coming quarters.

With respect to inflationary processes in Poland, it was highlighted that in spite of a fall in recent months, partially due to seasonal factors, CPI and core inflation persist at an elevated level. Sustained fast growth in producers' prices was also pointed out. In addition, the Council paid attention to the fact that while inflation expectations of market participants have fallen, households' inflation expectations continue to run relatively high. It was emphasised, however, that given the adaptive nature of these expectations, they are bound to decrease with a decline in current inflation.

The Council members argued that in light of available forecasts, it was reasonable to expect elevated inflation levels until the end of 2011, with a subsequent return to the NBP inflation target in mid-2012. It was emphasised that the monetary tightening implemented this year will be conducive to a fall in inflation. At the same time, it was pointed out that the return of CPI inflation to the target may be jeopardised by exchange rate developments, particularly amid the turmoil persisting in
international financial markets. It was also noted that in the event of an economic collapse abroad, weak domestic GDP growth would probably coincide with a zloty depreciation, which would hinder the disinflation process. Among the threats to lower inflation, a possible new increase in commodity prices was also pointed out, along with stronger than currently expected rises in fuel, food and administered prices.

As regards the conditions in the credit market, some Council members assessed that lending growth at the current rate does not, as for now, fuel inflationary pressures in the economy. They pointed, in particular, to a decline in consumer loans and a stabilization of growth in housing loans. However, other Council members highlighted the relatively high ratio of total consumer loans to GDP in Poland in comparison to other countries, adding that a reduction of this kind of debt would be welcome since it would be conducive to greater macroeconomic stability. Moreover, they assessed that given robust growth in housing loans and a continuing expansion in lending to corporations, the conditions in the credit market were conducive to higher aggregate demand in the economy.

When discussing the situation in the domestic labour market, the Council underscored weaker employment growth in the enterprise sector in the recent months, following a period of robust expansion, as well as the stabilisation of the unemployment rate at a relatively high level. Some Council members assessed that given the deteriorating outlook for demand, employment levels in enterprises may be expected to stabilise, or even fall slightly. It was also pointed out that given the circumstances, the wage pressure will probably remain limited.

With regard to monetary policy pursued amid mounting adverse trends in the external environment of the Polish economy, the Council members emphasised that monetary policy should foster sustained macroeconomic equilibrium. They pointed out that a monetary policy which takes macroeconomic stability into account will be conducive to maintaining price stability.

While discussing the NBP interest rates, the Council members agreed that these should remain unchanged at the current meeting. Arguments in support of this stance included the anticipated disinflation in Poland and a weaker outlook for growth in the global economy, and, in consequence, also in Poland.

The Council assessed that recently the balance of risks for inflation has become more balanced, adding that the current evaluation of the inflation and growth outlook for Poland did not imply a need to cut the NBP interest rates. At the same time, some Council members emphasized that the current level of the NBP interest rates was low against the background of their historical levels and vis-a-vis estimates of Poland’s natural interest rate. Moreover, it was pointed out that the potential impact of the developments in global financial markets on the zloty exchange rate will constitute an upside risk factor to domestic inflation.

In the opinion of the Council, the significant monetary policy tightening implemented since the beginning of 2011 should facilitate inflation’s return to the target in the medium term. Given the above, the Council decided to keep the NBP interest rates at the current level. The Council does not rule out the possibility of further monetary policy adjustment, should the outlook for inflation returning to the target deteriorate.
The Council kept the 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%.

Minutes of the Monetary Policy Council decision-making meeting held on 5 October 2011

At its meeting, the Monetary Policy Council discussed the impact of external developments on the situation in the Polish economy, the present and future trends in domestic economic activity, the likely shape of fiscal policy in the coming year as well as the outlook for inflation’s return to the target. In this context, the Council discussed the current and possible future monetary policy decisions.

While addressing conditions in the external environment of the Polish economy, Council members highlighted the recent signs of a further weakening of economic activity in the United States, the euro area and in some emerging market economies, particularly in China. It was pointed out that the deteriorating outlook for global economic growth was reflected in the fact that international financial institutions considerably downgraded GDP growth forecasts for major advanced and developing economies. The weaker outlook for global economic activity combined with the fiscal problems of some euro area countries resulted in higher risk aversion in the international financial markets, leading, as a consequence, to a depreciation in the exchange rates of emerging market currencies, including the zloty.

While discussing the longer-term outlook for the global economy, some Council members highlighted the fact that the reduction of private sector debt is a significant challenge currently facing economic policy in the United States, while in the euro area the challenge is to solve the sovereign debt crisis. These Council members maintained that given the above one may expect a protracted economic slowdown in both economies. Some Council members pointed out, however, that due to the structural differences between these economies the United States will see a recovery sooner than the euro area. In the opinion of some Council members, in the longer term weaker economic activity can also be expected in China, where the limited possibilities of further export growth mean that domestic demand’s role will have to increase, which, considering demographic factors and the absence of a social security system, will be difficult. All in all, according to those Council members, the debt crisis, and, in the longer term, the structural factors (mainly of demographic nature), may result in a prolonged period of slower growth of the global economy. Growth may also be less stable, especially given the limited options to stabilize the economy. Moreover, in this context some members of the Council highlighted the strongly expansionary monetary policy conducted by the major central banks as an additional drag on economic growth in the developed countries in the longer term. In the opinion of those members, such a policy delays the restructuring of these economies by hampering an effective re-allocation of resources.

While assessing the situation in the Polish economy, some Council members underlined the fact that despite its relatively sound fundamentals, the expected deterioration of external economic conditions – mainly in the euro area, including, in particular, in Germany – increases the risk of slower growth of Polish exports, and, hence, of slower GDP growth in the coming quarters. In the opinion of these Council members, despite a larger resilience of the Polish financial system in comparison to the other countries of the region, the links between financial systems in Europe may amplify the negative impact of external developments on economic activity in Poland. However,
other members of the Council argued that despite markedly slower economic growth in the euro area, Polish exports have been rising relatively fast. Therefore, it may be expected that domestic GDP growth will not slow down significantly amidst an expected deterioration in the external environment of the Polish economy. While discussing economic activity in Poland, some Council members pointed to August 2011 data showing a marked increase in corporate deposits and somewhat slower lending to this sector, which may signal that enterprises’ propensity to invest is decreasing in a situation of a deteriorated outlook for domestic growth.

With regard to the impact of developments in the public finance sector on economic growth in Poland, some Council members pointed to the likely significant reduction of the sector’s deficit in 2011 and to the announcements of continued fiscal tightening in 2012. In this context, it was pointed out that although a further reduction of fiscal imbalances will hamper GDP growth in the short term, abandoning it would be viewed negatively by financial markets, which would increase both the cost of public debt servicing and the risk of macroeconomic destabilization. Some Council members emphasized that the way in which fiscal imbalances are contained is important. If it is to be achieved by limiting expenditure, it may contribute to increasing the propensity of enterprises to invest by reducing concerns about a future rise in the tax burden and by easing the wage pressure. According to other Council members, fiscal tightening in 2012 may be significantly smaller than this year and smaller than that assumed by the government in the state’s Multi-year financial plan.

While discussing current data on inflationary processes in Poland, Council members pointed to the rise in both CPI and core inflation in August 2011. Some Council members also emphasized the concurrent acceleration in producer prices and faster-than-expected wage growth in the enterprise sector as factors that may signal higher-than-anticipated inflation in the future. On the other hand, the persistently elevated unemployment rate and the weaker growth of household disposable income were mentioned as factors conducive to curbing inflationary pressure. In the opinion of some Council members, the somewhat slower growth of lending to the private sector in August 2011 may also point to the absence of mounting inflationary pressure.

The Council members argued that in light of the NBP’s internal short-term forecasts one may expect heightened inflation till the end of the year, followed by inflation’s return close the NBP inflation target in the first half of 2012. This will be facilitated by the subsiding effects of earlier rises in food and energy prices as well as the VAT increase at the beginning of 2011, despite the forecasted concurrent sustained fast growth in administered prices. It was emphasized that the easing of inflationary pressure in the coming quarters will be fostered by an expected decrease in GDP growth amidst monetary policy tightening implemented in the first half of 2011 and the ongoing tightening of fiscal policy, as well as the expected weakening of economic activity in the external environment of the Polish economy. In the context of the inflation outlook, it was also pointed out that the latest results of business activity surveys show that the number of enterprises intending to reduce employment is larger than that of enterprises that intend to increase it, and that the percentage of enterprises planning to increase wages has fallen, which suggests that that wage pressure in the economy remains limited.

At the same time, Council members indicated that considering the persisting tensions in international financial markets the weakening of the zloty exchange rate may be an important risk factor for the fall of CPI inflation to the inflation target. Some Council members emphasized that if there was a
slump in economic activity abroad, the zloty might depreciate further, which would keep inflation at an elevated level, despite a slowdown of domestic GDP growth. Some Council members also indicated that high inflation expectations of individuals may jeopardise the decline in inflation. Although in the past these expectations were strongly adaptive and they decreased in August 2011, they have remained above the inflation target most of the time since the end of 2007.

While discussing the NBP interest rates, the Council members agreed that these should remain unchanged. Arguments in support of this stance included the expected decline in inflation in Poland, particularly in the context of a weakening outlook for growth in the global economy, and, as a consequence, also in Poland. It was also indicated that currently the main risk factor for price stability in Poland is the impact of the unstable situation in international financial markets on the zloty exchange rate. Some Council members emphasized that the NBP interest rates may now be maintained at a lower level than would be justified before the global financial crisis. In their opinion, this is the effect of, on the one hand, the existing financial market frictions increased by the crisis, and, on the other hand, the probable decline in factor productivity growth leading to a decline in the natural rate of interest.

While discussing future monetary policy the Council was of the opinion that given the currently expected macroeconomic scenario which assumes some economic slowdown and a concurrent gradual decline in inflation, the interest rates could remain at the present level in subsequent quarters. It was indicated that the stabilisation of monetary policy parameters is conducive, particularly given increased uncertainty, to maintaining macroeconomic stability. At the same time some Council members argued, however, that in subsequent quarters the likelihood of interest rate increases is larger than that of interest rate cuts, especially if inflation – due to the depreciation of the zloty triggered by the turmoil in the international financial markets – remains above the target for a period longer than currently anticipated. Some Council members indicated that a potentially significant slowdown of GDP growth in Poland in response to significantly weaker economic activity abroad may, given the expected decline in inflation, justify a reduction of the NBP interest rates at some point in the future.

The Council also discussed the long-term challenges to economic policy. The Council members pointed to the need to take measures aimed at enhancing macroprudential policy, including the development by the central bank and other institutions responsible for the financial system of new instruments mitigating systemic risk in the financial sector. The need to coordinate regulatory and macroeconomic policies in order to maintain macroeconomic stability, including the stability of the financial system, was also emphasized.

The Council kept the interest rates unchanged at the following levels: reference rate at 4.50%, Lombard rate at 6.00%, deposit rate at 3.00%, rediscount rate at 4.75%.

Minutes of the Monetary Policy Council decision-making meeting held on 9 November 2011

At its meeting, the Monetary Policy Council discussed the external environment of the Polish economy and the outlook for economic growth and inflation in Poland. In this context, the Council discussed the current and future monetary policy decisions.
While discussing the external environment of the Polish economy, the Council pointed to weak GDP growth in the euro area in 2011 Q3 and high probability of recession affecting the euro area economy in the subsequent quarters, which might be driven by the problems connected with the sovereign debt crisis. In the United States, in turn, GDP growth in 2011 Q3 accelerated slightly. In the opinion of some members of the Council, the US economy could be gradually returning to equilibrium, albeit at higher unemployment rate and weaker output growth. At the same time it was emphasized that despite relatively sound economic conditions, the probable recession in the euro area could also translate into a slowdown in economic activity in the United States.

With regard to the euro area sovereign debt crisis, members of the Council pointed out that mere announcements of economic reforms including, in particular, the tightening and coordination of fiscal discipline in the euro area, if not supported with rapid adjustments, might be insufficient to improve financial market sentiment.

It was highlighted that worsening sentiment in the global economy, largely triggered by the euro area crisis and the accompanying tensions in the financial markets, had been translating into the zloty depreciation observed in recent months. Some members of the Council assessed that the resulting higher price competitiveness of domestic output would contain the deceleration in the growth of Polish exports stemming from the anticipated global economic slowdown, particularly in the euro area. The weaker zloty coupled with worsening price competitiveness of imports would be conducive to higher growth of domestic output and improvement in Poland’s current account balance.

At the same time, members of the Council indicated that, since a large share of Polish corporate debt was foreign held, depreciation of the zloty would deteriorate the financial account of the balance of payments. Depreciation of the zloty would also result in higher value of domestic debt denominated in foreign currencies which, especially in the case of households, might exacerbate difficulties with debt repayment. This would, in consequence, lead to deteriorating banking sector conditions and curb credit supply. Some members of the Council also highlighted the risk of Poland facing elevated capital outflows, driven by the euro area crisis and unfavourable capital position of European banks, and, as a result, limited credit supply to Polish entities. Other members of the Council argued, however, that weaker economic growth would lead to lower credit demand.

Some members of the Council pointed out that in the case of improving sentiment in the global financial markets gradual appreciation of the zloty was possible, given “undervaluation” of the zloty and the expected reduction of both external imbalance (i.e. improving current account balance) and domestic imbalance (i.e. narrowing public finance deficit) of the Polish economy. It was noted, however, that amid shocks abroad and growing risk aversion that would increase risk premium, volatility of the zloty might remain elevated.

While analysing current situation in Poland, it was pointed out that GDP data for 2011 Q1 confirmed that relatively high growth had been sustained in that period. Some members of the Council also assessed that the anticipated deceleration in economic growth in Poland would be largely due to growing uncertainty triggered by external factors. In their opinion, it was supported by business condition surveys that pointed to a relatively high capacity utilization. Against this background, some members of the Council noted that concerns about the impact of the current crisis on domestic
economic developments in the coming quarters affected considerably stronger business activity than consumers’ behaviour, as could be concluded from persistent high growth of retail sales.

As regards the outlook for economic growth in Poland, the members of the Council assessed that despite slight slowdown in GDP growth anticipated for 2012, the growth rate would remain relatively high, especially against significant slowdown in the global economy. Some members of the Council also indicated that GDP growth in 2012 might exceed 3% in year-on-year terms, with private consumption being an important factor supporting it. In the opinion of some members of the Council, the key risk to GDP growth would be private investment growth, with the scope of public investment co-financed with the EU funds likely to diminish.

While discussing inflation developments in Poland, it was pointed out that the currently observed heightened inflation was mainly driven by factors beyond the direct impact of domestic monetary policy decisions, i.e. high commodity prices in the global markets, depreciation of the zloty stemming from growing risk aversion in the global financial markets and a rise in administered prices. The first two of these factors were reflected in high PPI growth. Some members of the Council also indicated that inflation remaining markedly above the target for a longer time was not conductive to anchoring inflation expectations. This, in turn, was reflected in both the worsening perception of inflation and response structure of individuals to the surveys questions on inflation expectations. Factors behind increasing inflation, albeit to a lesser extent, also included demand pressure, stemming mostly from continued relatively high growth of private consumption, translating into rising core inflation. At the same time, some members of the Council pointed to the labour market conditions, in particular to persistently high unemployment rate, declining employment in the corporate sector and moderate wage growth, which contained cost pressure, and, consequently, inflationary pressure. Some members of the Council were of the opinion that inflation was likely to return to the target in the second half of 2012. Among other factors contributing to lower inflation some members of the Council indicated a rise in saving rate in the enterprise sector.

In the opinion of the Council, the key factor containing inflationary pressure in the coming quarters would be a weaker GDP growth, stemming from slower global economic growth. The members of the Council were also of the opinion that lower domestic activity would additionally result from further fiscal tightening. Yet, as regards the impact of fiscal tightening on inflation, some members of the Council assessed that its structure might boost inflation in the short term, as it would largely consist of rises in tax burdens.

At the same time, further pass-through of the zloty depreciation observed over the past few months into domestic prices, coupled with inflationary expectations unanchored at the target level, posed, in the opinion of some members of the Council, the risk of inflation persisting at a heightened level. The Council also pointed to the expected rise in administered prices, excise tax and charges imposed by local governments in 2012, as factors prolonging the return of inflation to the target.

While discussing the NBP interest rates, the Council agreed they should remain unchanged. When justifying the decision, the Council pointed to the currently high uncertainty regarding economic activity and inflation developments both in global and domestic markets. This made it difficult to explicitly assess the probability of inflation remaining above or below the target over the period of the strongest impact of monetary policy on the economy. Moreover, some members of the Council
argued that stabilization of monetary policy parameters is conducive, particularly given increased uncertainty, to maintaining macroeconomic stability.

In the opinion of some members of the Council, current inflation persisting at a heightened level and a relatively long period of its expected return to the target might be supportive of an increase in the NBP interest rates. On the other hand, however, the likely global and domestic economic slowdown, should be easing inflationary pressure in the medium term. In these circumstances, in the opinion of some members of the Council, the tightening of monetary policy might additionally weaken domestic economic growth and increase the risk of inflation remaining below the target in the long run.

While discussing future monetary policy, some members of the Council upheld their assessment that the persisting relatively balanced risks to the future inflation justify stabilization of interest rates at present level in the following quarters. The macroeconomic scenario they expected assumed smooth slowdown in economic growth along with a gradual decline in inflation. Yet, according to some members of the Council, it might be justified to tighten monetary policy in the future. In their opinion, this would be due to a high probability of inflation remaining at a heightened level in the coming quarters despite the expected slowdown in economic growth, as supported by lower responsiveness of inflation to the negative output gap, stronger exchange rate pass-through on inflation amidst large and one-directional exchange rate fluctuations and a relatively strong rise in money supply.

Some members of the Council, however, highlighted macroeconomic scenarios justifying future reduction in the interest rates. In their opinion, this would be advisable amidst strong slowdown in economic growth combined with inflation declining to the target.

The Council kept the NBP interest rates unchanged at the following levels: reference rate at 4.50%, lombard rate at 6.00%, deposit rate at 3.00%, rediscount rate at 4.75%.

**Minutes of the Monetary Policy Council decision-making meeting held on 7 December 2011**

At its meeting, the Monetary Policy Council discussed the external environment of the Polish economy and the outlook for economic growth and inflation in Poland. In this context, the Council discussed the current and future monetary policy decisions.

While discussing the external environment of the Polish economy, the Council pointed to weak GDP growth in the euro area in 2011 Q3 and high probability of recession affecting the euro area economy in the subsequent quarters, which might be driven by the problems connected with the sovereign debt crisis. In the United States, in turn, GDP growth in 2011 Q3 accelerated slightly. In the opinion of some members of the Council, the US economy could be gradually returning to equilibrium, albeit at higher unemployment rate and weaker potential output growth. At the same time it was emphasized that despite relatively sound economic conditions, the probable recession in the euro area could also translate into a slowdown in economic activity in the United States.

With regard to the euro area sovereign debt crisis, members of the Council pointed out that mere announcements of economic reforms including, in particular, the tightening and coordination of
fiscal discipline in the euro area, if not supported with rapid adjustments, might be insufficient to improve financial market sentiment.

It was highlighted that worsening sentiment in the global economy, largely triggered by the euro area crisis and the accompanying tensions in the financial markets, had been translating into the zloty depreciation observed in recent months. Some members of the Council assessed that the resulting higher price competitiveness of domestic output would contain the deceleration in the growth of Polish exports stemming from the anticipated global economic slowdown, particularly in the euro area. The weaker zloty coupled with worsening price competitiveness of imports would be conducive to higher growth of domestic output and improvement in Poland’s current account balance.

At the same time, members of the Council indicated that, since a large share of Polish corporate debt was foreign held, depreciation of the zloty would deteriorate the financial account of the balance of payments. Depreciation of the zloty would also result in higher value of domestic debt denominated in foreign currencies which, especially in the case of households, might exacerbate difficulties with debt repayment. This would, in consequence, lead to deteriorating banking sector conditions and curb credit supply. Some members of the Council also highlighted the risk of Poland facing elevated capital outflows, driven by the euro area crisis and unfavourable capital position of European banks, and, as a result, limited credit supply to Polish entities. Other members of the Council argued, however, that weaker economic growth would lead to lower credit demand.

Some members of the Council pointed out that in the case of improving sentiment in the global financial markets gradual appreciation of the zloty was possible, given “undervaluation” of the zloty and the expected reduction of both external imbalance (i.e. improving current account balance) and domestic imbalance (i.e. narrowing public finance deficit) of the Polish economy. It was noted, however, that amid shocks abroad and growing risk aversion that would increase risk premium, volatility of the zloty might remain elevated.

While analysing current situation in Poland, it was pointed out that GDP data for 2011 Q1 confirmed that relatively high growth had been sustained in that period. Some members of the Council also assessed that the anticipated deceleration in economic growth in Poland would be largely due to growing uncertainty triggered by external factors. In their opinion, it was supported by business condition surveys that pointed to a relatively high capacity utilization. Against this background, some members of the Council noted that concerns about the impact of the current crisis on domestic economic developments in the coming quarters affected considerably stronger business activity than consumers’ behaviour, as could be concluded from persistent high growth of retail sales.

As regards the outlook for economic growth in Poland, the members of the Council assessed that despite slight slowdown in GDP growth anticipated for 2012, the growth rate would remain relatively high, especially against significant slowdown in the global economy. Some members of the Council also indicated that GDP growth in 2012 might exceed 3% in year-on-year terms, with private consumption being an important factor supporting it. In the opinion of some members of the Council, the key risk to GDP growth would be private investment growth, with the scope of public investment co-financed with the EU funds likely to diminish.

While discussing inflation developments in Poland, it was pointed out that the currently observed heightened inflation was mainly driven by factors beyond the direct impact of domestic monetary
policy decisions, i.e. high commodity prices in the global markets, depreciation of the zloty stemming from growing risk aversion in the global financial markets and a rise in administered prices. The first two of these factors were reflected in high PPI growth. Some members of the Council also indicated that inflation remaining markedly above the target for a longer time was not conductive to anchoring inflation expectations. This, in turn, was reflected in both the worsening perception of inflation and response structure of individuals to the surveys questions on inflation expectations. Factors behind increasing inflation, albeit to a lesser extent, also included demand pressure, stemming mostly from continued relatively high growth of private consumption, translating into rising core inflation. At the same time, some members of the Council pointed to the labour market conditions, in particular to persistently high unemployment rate, declining employment in the corporate sector and moderate wage growth, which contained cost pressure, and, consequently, inflationary pressure. Some members of the Council were of the opinion that inflation was likely to return to the target in the second half of 2012. Among other factors contributing to lower inflation some members of the Council indicated a rise in saving rate in the enterprise sector.

In the opinion of the Council, the key factor containing inflationary pressure in the coming quarters would be a weaker GDP growth, stemming from slower global economic growth. The members of the Council were also of the opinion that lower domestic activity would additionally result from further fiscal tightening. Yet, as regards the impact of fiscal tightening on inflation, some members of the Council assessed that its structure might boost inflation in the short term, as it would largely consist of rises in tax burdens.

At the same time, further pass-through of the zloty depreciation observed over the past few months into domestic prices, coupled with inflationary expectations unanchored at the target level, posed, in the opinion of some members of the Council, the risk of inflation persisting at a heightened level. The Council also pointed to the expected rise in administered prices, excise tax and charges imposed by local governments in 2012, as factors prolonging the return of inflation to the target.

While discussing the NBP interest rates, the Council agreed they should remain unchanged. When justifying the decision, the Council pointed to the currently high uncertainty regarding economic activity and inflation developments both in global and domestic markets. This made it difficult to explicitly assess the probability of inflation remaining above or below the target over the period of the strongest impact of monetary policy on the economy. Moreover, some members of the Council argued that stabilization of monetary policy parameters is conducive, particularly given increased uncertainty, to maintaining macroeconomic stability.

In the opinion of some members of the Council, current inflation persisting at a heightened level and a relatively long period of its expected return to the target might be supportive of an increase in the NBP interest rates. On the other hand, however, the likely global and domestic economic slowdown, should be easing inflationary pressure in the medium term. In these circumstances, in the opinion of some members of the Council, the tightening of monetary policy might additionally weaken domestic economic growth and increase the risk of inflation remaining below the target in the long run.

While discussing future monetary policy, some members of the Council upheld their assessment that the persisting relatively balanced risks to the future inflation justify stabilization of interest rates at
present level in the following quarters. The macroeconomic scenario they expected assumed smooth slowdown in economic growth along with a gradual decline in inflation. Yet, according to some members of the Council, it might be justified to tighten monetary policy in the future. In their opinion, this would be due to a high probability of inflation remaining at a heightened level in the coming quarters despite the expected slowdown in economic growth, as supported by lower responsiveness of inflation to the negative output gap, stronger exchange rate pass-through on inflation amidst large and one-directional exchange rate fluctuations and a relatively strong rise in money supply.

Some members of the Council, however, highlighted macroeconomic scenarios justifying future reduction in the interest rates. In their opinion, this would be advisable amidst strong slowdown in economic growth combined with inflation declining to the target.

The Council kept the NBP interest rates unchanged at the following levels: reference rate at 4.50%, lombard rate at 6.00%, deposit rate at 3.00%, rediscount rate at 4.75%.
Appendix 6

VOTING RECORDS OF MPC MEMBERS ON MOTIONS AND RESOLUTIONS IN 2011

Voting records of Monetary Policy Council Members on motions and resolutions in 2011 are presented below:

- **Date:** 19 January 2011

**Subject matter of motion or resolution:**
Resolution No. 1/2011 on the level of the reference rate, lombard rate, deposit rate and rediscount rate of the National Bank of Poland.

**MPC decision:**
The MPC increased the level of all interest rates by 0.25 percentage points.

**Voting of the MPC members:**

For:  M. Belka
     A. Bratkowski
     E. Chojna-Duch
     Z. Gilowska
     A. Glapiński
     J. Hausner
     A. Kaźmierczak
     A. Rzońca
     J. Winiecki
     A. Zielińska-Głębocka

Against:
Date: 15 February 2011

Subject matter of motion or resolution:
Resolution no. 2/2011 on the regulations governing the Monetary Policy Council.

Voting of the MPC members:
For:  M. Belka
      A. Bratkowski
      E. Chojna-Duch
      Z. Gilowska
      A. Glapiński
      J. Hausner
      A. Kaźmierczak
      A. Rzońca
      A. Zielińska-Głębocka

Against:  J. Winiecki

Date: 2 March 2011

Subject matter of motion or resolution:
Motion to raise the NBP interest rates by 0.25 percentage points.

MPC decision:
Motion did not pass.

Voting of the MPC members:
For:  A. Bratkowski
      J. Hausner
      A. Rzońca

Against:  M. Belka
         E. Chojna-Duch
         Z. Gilowska
         A. Glapiński
         A. Kaźmierczak
         A. Zielińska-Głębocka

J. Winiecki was absent.

Date: 4 April 2011

Subject matter of motion or resolution:
Voting of the MPC members:
For:  M. Belka
     A. Bratkowski
     E. Chojna-Duch
     Z. Gilowska
     A. Glapinski
     J. Hausner
     A. Kazmierczak
     A. Rzonca
     J. Winiecki
     A. Zienicka-Glebocka
Against:  A. Bratkowski
         E. Chojna-Duch
         Z. Gilowska
         A. Glapinski
         J. Hausner
         A. Kazmierczak
         A. Rzonca
         J. Winiecki
         A. Zienicka-Glebocka

Date: 5 April 2011

Subject matter of motion or resolution:
Resolution No. 4/2011 on the level of the reference rate, lombard rate, deposit rate and rediscount rate of the National Bank of Poland.

MPC decision:
The MPC increased the level of all interest rates by 0.25 percentage points.

Voting of the MPC members:
For:  M. Belka
     A. Bratkowski
     Z. Gilowska
     A. Glapinski
     J. Hausner
     A. Kazmierczak
     A. Rzonca
     J. Winiecki
     A. Zienicka-Glebocka
Against:  E. Chojna-Duch

Date: 10 May 2011

Subject matter of motion or resolution:
Resolution No. 5/2011 on approving the report on monetary policy implementation in 2010.
Voting of the MPC members:
For: M. Belka
     A. Bratkowski
     E. Chojna-Duch
     Z. Gilowska
     A. Glapiński
     J. Hausner
     A. Kaźmierczak
     A. Rzońca
     J. Winiecki
     A. Zielińska-Głębocka

Against: A. Bratkowski

Date: 10 May 2011

Subject matter of motion or resolution:
Resolution No. 6/2011 on the evaluation of the activities of the NBP Management Board as regards the implementation of the monetary policy guidelines for the year 2010.

Voting of the MPC members:
For: M. Belka
     E. Chojna-Duch
     Z. Gilowska
     A. Glapiński
     J. Hausner
     A. Kaźmierczak
     A. Rzońca
     J. Winiecki
     A. Zielińska-Głębocka

Against: A. Bratkowski

Date: 11 May 2011

Subject matter of motion or resolution:
Resolution No. 7/2011 on the level of the reference rate, lombard rate, deposit rate and rediscount rate of the National Bank of Poland.

MPC decision:
The MPC increased the level of all interest rates by 0.25 percentage points.
Voting of the MPC members:
For: M. Belka
     A. Bratkowski
     Z. Gilowska
     J. Hausner
     A. Kaźmierczak
     A. Rzońca
     J. Winiecki
     A. Zielińska-Głębocka
Against: E. Chojna-Duch
         A. Glapiński

Date: 17 May 2011

Subject matter of motion or resolution:
Resolution No. 8/2011 on approving the report on the operations of the National Bank of Poland in 2010.

Voting of the MPC members:
For: M. Belka
     A. Bratkowski
     E. Chojna-Duch
     Z. Gilowska
     A. Glapiński
     J. Hausner
     A. Kaźmierczak
     A. Rzońca
     J. Winiecki
Against: A. Zielińska-Głębocka was absent.

Date: 8 June 2011

Subject matter of motion or resolution:
Motion to symmetrically narrow the corridor between the NBP deposit and lombard rates by 0.5 percentage points.

MPC decision:
Motion did not pass.
Voting of the MPC members:
For:  A. Bratkowski  A. Rzońca  A. Zielińska-Głębocka
Against:  M. Belka  E. Chojna-Duch  Z. Gilowska  A. Glapiński  J. Hausner  A. Kaźmierczak  J. Winiecki

Date: 8 June 2011

Subject matter of motion or resolution:
Resolution no. 9/2011 on the level of the reference rate, lombard rate, deposit rate and rediscount rate of the National Bank of Poland.

MPC decision:
The MPC increased the level of all NBP interest rates by 0.25 percentage points.

Voting of the MPC members:
For:  M. Belka
Against:  E. Chojna-Duch  A. Bratkowski  Z. Gilowska  A. Glapiński  J. Hausner  A. Kaźmierczak  A. Rzońca  J. Winiecki  A. Zielińska-Głębocka

Date: 6 July 2011

Subject matter of motion or resolution:
Motion to raise the NBP interest rates by 0.25 percentage points.

MPC decision:
Motion did not pass.
Voting of the MPC members:
For:  A. Kaźmierczak  
Against: M. Belka  
A. Bratkowski  
E. Chojna-Duch  
Z. Gilowska  
A. Gliapiński  
J. Hausner  
A. Rzońca  
J. Winiecki  
A. Zielińska-Głębocka

Date: 23 August 2011

Subject matter of motion or resolution:

Voting of the MPC members:
For:  M. Belka  
    A. Bratkowski  
    E. Chojna-Duch  
    Z. Gilowska  
    A. Gliapiński  
    J. Hausner  
    A. Kaźmierczak  
    A. Rzońca  
    J. Winiecki  
    A. Zielińska-Głębocka

Against:  

Date: 20 September 2011

Subject matter of motion or resolution:
Resolution No. 11/2011 on setting the ceiling for liabilities arising from loans and credits drawn by the NBP at foreign banking and financial institutions.

Voting of the MPC members:
For: M. Belka
Against: A. Bratkowski, E. Chojna-Duch, A. Glapiński, J. Hausner, A. Kaźmierczak, J. Winiecki, A. Zielińska-Głębocka

Z. Gilowska and A. Rzońca were absent.

Date: 8 November 2011

Subject matter of motion or resolution:
Resolution No. 12/2011 amending the resolution on the required reserve rates and the remuneration of required reserves.

Voting of the MPC members:
For: M. Belka
Against: A. Bratkowski, E. Chojna-Duch, J. Hausner, Z. Gilowska, A. Glapiński, A. Kaźmierczak, J. Winiecki, A. Zielińska-Głębocka

A. Rzońca was absent.
Appendix 6. Voting records of MPC members on motions and resolutions in 2011

Date: 6 December 2011

Subject matter of motion or resolution:
Resolution No. 13/2011 on approving the Financial Plan of the National Bank of Poland for 2012.

Voting of the MPC members:
For: M. Belka
Against: A. Bratkowski

       E. Chojna-Duch
       J. Hausner
       Z. Gilowska
       A. Glapiński
       A. Kaźmierczak
       A. Rzońca
       J. Winiecki
       A. Zielińska-Głębocka