

Warsaw, 28 June 2006

INFORMATION FROM THE MEETING OF THE MONETARY POLICY COUNCIL

held on 27-28 June 2006

The Council decided to keep the NBP interest rates unchanged, i.e.:

reference rate 4.00% on an annual basis;

lombard rate 5.50 % on an annual basis;

deposit rate 2.50% on an annual basis;

rediscount rate 4.25% on an annual basis.

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Since the Council's meeting in May 2006, the forecasts of inflation in 2006 in the euro area and the United States have been slightly revised upwards, while forecasts for 2007 have remained unchanged. Forecasts of economic growth in both the euro area and the United States for 2006-2007 have not changed, either. In May, the annual growth of consumer prices increased both in the United States (from 3.5% in April to 4.2%) and in the euro area (from 2.4% to 2.5%). Since the May meeting of the Council no change has occurred in crude oil prices, either current or those forecast for 2006-2007. Still, uncertainty persists as to the effect of high oil prices on economic growth and inflation.

The May data on output, retail sales and employment in the enterprise sector in Poland proved better than expected and indicated that the high rate of economic growth recorded in Q1 will be also continued in 2006 Q2. The rise in industrial output in May 2006 was markedly higher than expected both by the NBP and external forecasters, reaching 19.1% y/y (compared with 5.7% y/y in April). In seasonally adjusted terms, the growth in industrial output in May amounted to 15.6% y/y (compared to 10.2% y/y in April). Also significantly higher than previously expected proved the surge in construction and assembly output, reaching the level of 13.4% y/y against 4.1% y/y in April, which in seasonally adjusted terms corresponds to 7.0% y/y compared to 4.9% y/y. The rise in retail sales also outstripped the expectations at 13.7% y/y in nominal terms compared with 13.2% y/y in April. Similarly, as in the case of industrial output, this rise in retail sales has been the highest since April 2004, when economic activity rose significantly before Poland's entry to the EU. The growth of household lending has continued at a robust pace: consumer loans registered an increase of 19.2% y/y in May (compared with 17.6% y/y in April), while the growth rate of housing loans stepped up to 48.2% y/y (compared with 41.1% y/y in April). The growth in corporate lending accelerated (from 3.4% y/y in April to 4.1% y/y in May), though it still remains moderate.

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The rapid economic growth increases the demand for labour. Since December 2004 the growth of corporate sector employment has been constantly accelerating. In May 2006, employment in enterprises increased by 3.1% y/y (compared to 2.8% y/y in April 2006). 2006 Q1 also brought acceleration in the number of people working in the economy as measured by the Polish Labour Force Survey (BAEL) – 3.1% y/y against 2.4% y/y in 2005 Q4. The number of persons working outside private farming is soaring rapidly (a rise of 3.8% in 2006 Q1 compared with 3.5% y/y in 2005 Q4). There was also a significant drop in unemployment figure – in 2006 Q1 the unemployment rate according to the BAEL stood at 16.0% compared with 18.9% a year before. According to labour office data in May 2006 the rate of unemployment slid to 16.5% compared with 18.2% a year before. This rapid growth in the number of working persons and the significant slump in unemployment rate was accompanied by a drop in the economically active figure, which in 2006 Q1 fell in relation to 2005 Q1 by 0.4%.

In May 2006, the growth in the corporate sector's wages rose to 5.2% y/y (compared to 4.0% y/y in April). The estimated rate of growth of unit labour costs in the economy (excluding private farming) fell from 4.3% in 2005 Q4 down to 3.3% y/y in 2006 Q1. In turn, the rise in labour productivity in industry in January-May (10.5% y/y) was still higher than wage growth, which has resulted in a decline of unit labour costs in this sector by 5.2% y/y. Since the May meeting of the Council: the Government has adopted a draft act on transferring funds to public health-care institutions to finance a 30-percent pay rise for their employees, an agreement has been reached on bonus payments for miners to be made from profits of coal-mines and further signals have arisen pointing to building wage pressure in some parts of the public sector. All this may lead to further increases in wage pressure. It should be emphasised that an indispensable condition for a sustained acceleration of economic growth which would not pose a threat to the achievement of the inflation target is that the growth in wages does not outpace the growth in labour productivity. This requires strong and productivity-oriented corporate governance in enterprises.

The annual growth of consumer prices in May rose to 0.9% (against 0.7% y/y in April). The increase in the annual rate of inflation as compared to April 2006 was driven by the rise in prices of food and non-alcoholic beverages and also in fuel prices. The majority of core inflation indicators edged up as well, even though their levels remained low (in May core inflation indicators ranged between -0.4% y/y and 1.0% y/y). This low level of all core inflation indices suggests that inflationary pressure continues to be low. June did not bring any significant modifications to the inflation expectations of households, which continued at a low level. According to GUS business tendency surveys, the expected prices of enterprises' output have been gradually increasing since the beginning of 2006.

In May 2006 the producer prices in industry (PPI) rose by 2.3% y/y as compared to 1.7% y/y in April, i.e. by 0.4% m/m against 1.5% m/m in April, which to a large extent resulted from higher prices of commodities and energy carriers. The rise in annual PPI growth rate occurred even though the effective exchange rate of the zloty proved 4.5% stronger than a year before.

The Council maintains its belief that implementing an economic strategy focused on creating conditions which ensure the introduction of the euro at the earliest possible date would be most favourable for Poland and would contribute to higher long-term economic growth.

In the Council's assessment, the balance of risks for future inflation may point to an increased probability of inflation running, in monetary policy transmission horizon, at a higher level than it was accounted for in the April projection and at the May meeting of the Monetary Policy Council. A broader assessment of the inflation outlook will be possible in July 2006 after the publication of the inflation projection.

The next meeting of the Council will be held on 18 July 2006 and will be devoted to discussing the draft *Inflation Report*. The *Report* will be finally approved at the Council's meeting scheduled for 25-26 July 2006.