Minutes of the Monetary Policy Council decision-making meeting held on 5 October 2016

At the meeting, the members of the Monetary Policy Council discussed monetary policy against the background of macroeconomic developments in Poland and abroad.

The Council reviewed the developments abroad, which have an impact on economic conditions in Poland. It was recognised that global economic growth remained moderate, but uncertainty about its outlook continued. It was noted that economic growth in the euro area was stable despite negative impact of weak economic conditions in the non-European emerging market economies. Attention was drawn to signs of recovery in European and German industrial sector and to a rise in export orders in Germany. It was stressed that this could support growth in Polish industrial output, particularly export manufacturing. It was assessed that GDP growth in the United States might have picked up slightly in 2016 Q3, but – like in the previous quarters – had been held back by low investment growth rate. It was also pointed out that in China GDP growth was lower than in previous years, yet data on activity indicated a stabilisation of economic conditions in the previous months. At the same time, an opinion was expressed that this stabilisation had been achieved due to significant fiscal expansion and an acceleration in lending growth, which had perpetuated long-term risks for the Chinese economy. Also in Russia, recession had been alleviated, mainly by the rise in oil prices since the beginning of the year.

The Council members emphasised that prices of oil and many other commodities – despite the rise earlier in the year – were lower than in previous years. It was also indicated that at the time of the meeting the level of oil prices was close to that in previous year, which implied a near-zero annual price growth rate of oil. It was judged that low commodity prices and moderate global economic activity had a negative impact on consumer price growth in many economies, though to an increasingly lesser extent. Some Council members pointed out that a risk of a fall in oil prices stemming from still high supply of oil was a source of uncertainty for the expected price growth, both in Poland and abroad. They argued that this risk has been increased further in the recent period by a renewed rise in shale oil production in the United States.

Referring to monetary policy abroad, it was highlighted that the European Central Bank was keeping interest rates close to zero, including the deposit rate below zero, and continued financial asset purchases. At the same time, it was stressed that there were signs of a possible gradual reduction of asset purchases in the future. It was also pointed out that the Federal Reserve, despite the relatively favourable data on the US economic activity, had not increased interest rates in September and had again revised down their interest rate projections for the coming years.

When discussing developments in the domestic economy, the Council members underlined that stable economic growth continued in Poland. In particular, the data

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available at the time of the meeting indicated that GDP growth in 2016 Q3 had probably been close to that in the previous quarter. The main driver of economic growth is steadily increasing consumer demand, supported by gradual improvement in the labour market, favourable household sentiment and the child benefit payments under the ”Family 500 plus” programme. It was argued that data on economic activity in August, most notably an increase in retail sales growth, had confirmed such an assessment. It was also indicated that industrial output had risen markedly in August following a temporary decline in the previous month, and that sentiment in manufacturing had improved significantly. Attention was also drawn to the balance of payments data, which confirmed the acceleration in export growth in 2016 Q2, despite the fall in world trade volumes observed at that time. It was also highlighted that fall in construction and assembly output had deepened in August, which – like in the previous months – was most probably due to a decline in investment driven by the temporarily lower absorption of EU funds after expiration of the previous EU financial framework. Some Council members were of the opinion that the lower investment growth rate might have resulted from uncertainty about the regulatory environment of business in Poland.

During the discussion about the labour market, it was noted that employment had continued to rise steadily, accompanied by a sustained decline in the unemployment rate. It was highlighted that job vacancies were at historical highs, which indicated ongoing high demand for labour. It was underlined that the recovery in the labour market was translating into growing wage pressure in the corporate sector, and, in effect, wage growth was already higher than in previous years. An opinion was expressed that a hike in the minimum wage in early 2017 could be also conducive to faster wage growth in the coming quarters.

While discussing the economic outlook for Poland, the majority of the Council members judged that stable economic growth would most likely continue in the following quarters. In the opinion of certain Council members, GDP growth could even accelerate slightly. Growing consumption will remain the major driver of economic growth. In the further quarters, the economic activity should also be propped up by the expected recovery of investment outlays, including those financed with the EU funds. To reinforce this view, some Council members cited a significant increase in the number of new EU financial framework contracts signed in the recent quarters. Certain Council members noted that the favourable outlook for consumer demand and the recent improvement in sentiment in the industrial sector would also support the recovery in corporate investment . At the same time, in the opinion of certain Council members, over the longer run investment growth might be additionally backed by the "Housing Plus" programme. However, as certain Council members pointed out, due to a deterioration of some sentiment indicators in the previous months and the uncertainty about the regulatory environment of business, it could not be excluded that low investment growth would continue in the coming quarters.

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When analysing price developments in Poland, it was underlined that annual consumer price growth remained negative, yet deflation was gradually subsiding. It was judged that the increase in price growth resulted mainly from dissipating effects of the earlier sharp fall in global commodity prices. Another factor conducive to higher price growth cited during the meeting was the gradual acceleration in wage growth in Poland, translating into faster growth in unit labour costs. It was pointed out that the reversal of deflationary trends was also confirmed by the producer price index, in particular net of energy prices, which had been growing since early 2016. It was also pointed out that the growth rate of consumer prices sensitive to domestic economic conditions had been significantly positive for several months. The majority of the Council members judged that there were still no visible signs that deflation had affected the activity of most economic agents. Certain Council members underlined that it was still necessary to analyse the business conditions of enterprises and consumer behaviour for possible adverse effects of the negative price growth.

Referring to the outlook for price growth, the majority of the Council members judged that the scale of deflation would continue to gradually decrease in the coming months. It was stressed that, according to both NBP's and external forecasts, the annual price growth rate should be close to 1% in 2017. It was pointed out that higher price growth would be supported by stable GDP growth, amid accelerating wage growth and higher child benefits. However, certain Council members were of the opinion that, due to downside risks to oil prices in the global markets, it could not be ruled out that the period of deflation in Poland might extend. In turn, certain Council members expressed a view that the price growth rate could be higher than indicated by the forecasts available at the time of the meeting. Stronger acceleration in price growth could, in their opinion, be backed by faster closure of the output gap and higher growth in unit labour costs. At the same time, these Council members underlined that the impact of unit labour cost growth on price developments could be mitigated for some time if companies reduced their profit margins.

While discussing the level of NBP interest rates, the Council members judged that they should remain unchanged. The Council members confirmed their assessment that the stabilisation of interest rates helped to keep the Polish economy on a sustainable growth path and maintain macroeconomic stability. The majority of the Council members pointed out that in 2017 price growth should already be clearly positive. The majority of the Council members also assessed that GDP growth – though somewhat lower than in 2015 – remained close to potential output growth. An additional argument for interest rate stabilisation was elevated uncertainty regarding domestic and external conditions for monetary policy. Some Council members noted that the Council's decisions should also take into account the impact of the interest rates level on the stability of the domestic financial sector.

At the same time, some Council members pointed out that should economic growth accelerate markedly and inflationary pressure appear, creating a risk of exceeding the

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inflation target in the medium term, it could be appropriate to raise the interest rates. However, these Council members indicated that, in light of the data available at the time of the meeting, stabilisation of the interest rates in the following quarters was the most likely scenario. In turn, some Council members assessed that a further slowdown in economic growth, prolonged period of deflation and adverse effects of deflation might justify a decrease in the interest rates in the future. They emphasised that the reduction in the NBP interest rates would be conducive to higher GDP growth, most notably by boosting investment activity. Certain Council members underlined in addition that the level of real interest rates in Poland was relatively high compared to other countries in Central and Eastern Europe. Other Council members judged that the level of NBP interest rates was currently not a factor curbing investment growth in the economy, particularly taking into account high corporate savings allowing firms to finance business activity from their own funds.

The Council decided to keep the NBP interest rates unchanged: the reference rate at 1.50%, the lombard rate at 2.50%, the deposit rate at 0.50%, the rediscount rate at 1.75%.

Publication date: 20 October 2016

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