

Service sector

Zofia Bolkowska, Marek Misiak

2008-12-30

In November the general climate in the service sector was less optimistic than in previous months

In November the general climate in the service sector was less optimistic than in previous months. Companies providing financial services were the most optimistic but still their outlook was worse than in October. The hotel and restaurant sector was much less optimistic than in previous months.

In November 42% of the surveyed financial companies reported an improvement, down by 5%. Only 4.2% of the surveyed companies reported no barriers to their operations. Competition from Polish and foreign companies was indicated as the most important barrier respectively by 80% and 55% of the surveyed companies. Competition was stronger than a month before.

In the transport, warehousing and communications sector, 19% of the surveyed businesses signalled an improvement and 14% a deterioration in business conditions. Managers signalled a deterioration in their financial situation. In November, 4.6% of the surveyed companies reported no barriers to their business operations. Competition from Polish companies and labour costs are the most serious barriers – indicated respectively by 57% and 55% of the surveyed companies.

Companies in the real estate, rental, education and business services sector were less optimistic in November than in October. They expected a drop in current demand and a deterioration in their companies' financial situation. 19% of the surveyed businesses signalled an improvement and 10% a deterioration in business conditions. 11.8% reported no barriers to their operations. The largest percentage of companies, 52%, pointed to labour costs as the most serious barrier.

The outlook in the hotel and restaurant sector was worse than in October. Expectations for current and future demand and sales and the companies' financial situation worsened. 18% of the surveyed businesses signalled an improvement and 17% a deterioration in business conditions. Only 2.7% of the

surveyed companies reported no barriers to their business activity. The most serious barriers were labour costs (indicated by 69% of the companies), competition from Polish companies (52%) and fiscal burdens (51%).

In November consumer confidence continued to weaken, which was reflected in both consumer confidence indices – the current index, which describes current trends in individual consumption, and the forward-looking index, which describes trends expected in the next months. The readings of the two indices in the past two months indicate that growth in individual consumption may slow as early as the fourth quarter of this year and the first months of next year.

The readings of the two indices dropped due to a deterioration in the households' outlook on the country's general economic situation in the past 12 months and especially job prospects for the next 12 months. There was a slight improvement in the outlook on the households' financial situation in the past 12 months and the next 12 months, the general economic situation in the next 12 months, the current potential to buy and the potential to save in the next 12 months. It is noteworthy that the outlook on job prospects worsened sharply in November, reaching a level recorded three years ago.

In October 2008, CPI inflation fell from 4.5% in September to 4.2%. The price index increased slightly in the industrial sector but fell in construction.

In October consumer prices were mainly driven by household services (including energy). CPI inflation was still above the inflation target set by the Monetary Policy Council. Inflation stayed 1.3 pct points above the upper limit of deviation from the NBP inflation target of 2.5%+- 1 percentage point in August, 1.0 pct point above the limit in September and 0.7 pct points above the limit in October. Compared to October last year, the highest increase was recorded in prices of household services and energy (10.7%) and prices of food (4%). Prices of health care were higher by 3.4% than a year before, prices of education were higher by 4.2%, restaurant and hotel prices were higher by 6.7%, prices of recreation and culture were higher by 1.6%, transport prices were higher by 1.6%, and prices of communications were higher by 0.7%. Prices of clothing and footwear were lower by 6.2% compared to October 2007.

In October 2008 the annual producer price index (PPI) was 2.4% against 2.3% in September. A major increase in prices, though not as high as in September, was

recorded in the mining sector (8.4%), and electricity generation, gas and water supply (9.8%). In October the average increase in producer prices in the manufacturing sector was 1.1%, with producer prices of oil products and chemicals having increased the fastest, while prices of most other products were lower than in October last year.

In the past two years construction prices were very volatile. In the first half of 2007 construction prices were increasing at a fast pace due to growing demand (companies had more orders than they were able to carry out) and upward pressure on wages in the building sector. In the third quarter of 2007 growth in prices slowed and this trend continued in 2008. Despite the increase in construction wages, which has been the highest of all sectors of the economy, construction prices have been falling due to a drop in prices of building materials. The construction price index amounted to 9% in mid-2007, 8.4% in December 2007 and 3.2% in October 2008. Average prices of mineral construction materials rose by 12% year on year in June 2007, 1.2% in June 2008 and in the third quarter were lower than a year before. Prices of metallurgical and wood products have been falling gradually for several months now.

Monetary Policy Council cuts interest rates.

At a meeting on November 25 and 26, the Monetary Policy Council reduced central bank interest rates by 25 basis points (by 0.25 pct points).

NBP (Monetary Policy Council): In October CPI inflation decreased in Poland again (to 4.2%), although it was still above the NBP inflation target of 2.5% and above the upper limit of deviation from the target of 3.5%. Inflation remained at a heightened level due to a further increase in energy prices and prices of many services, especially household services. The Council maintains its assessment that inflation will remain above the upper limit of deviation from the target in coming months, which will be largely due to a rise in regulated prices. But in the medium term inflationary pressure may be pushed down in Poland by the sharper than expected global economic slowdown, especially recession in countries which are Poland's main trading partners, and the resulting slowdown of the Polish economy. The falling GDP growth rate coupled with reduced demand for labour and deteriorating financial situation of companies will ease pressure on wages and consequently inflationary pressure. Stricter borrowing criteria imposed by banks will be working in the same direction. Apart from a high annual increase in regulated prices, growing prices of some services may be a factor delaying the fall

in inflation. This may result partly from a rise in energy prices. The Council assessed that in the medium term the probability of inflation running below the inflation target was higher than the probability of its running above the target and decided to cut interest rates. The Council's decisions in coming months will depend on prospects for economic growth and inflation in Poland and the world. Discipline in public finances may be a factor contributing to relaxing monetary policy. The Council will be analysing the impact of developments on the Polish interbank market on the transmission of monetary policy in Poland. The Council is sticking to its opinion that Poland should enter the ERM II and the euro zone as early as possible (...). ("Minutes of the Monetary Policy Council Meeting on November 25-26, 2008"; www.nbp.pl)