

## 21. POLAND

### Public deficit to widen despite stronger GDP growth

The economy is expected to gather momentum in 2017 and 2018 as investment gradually recovers from a substantial contraction in 2016. Private consumption is set to remain the main growth driver, and the labour market is expected to tighten further. Costs from a lowering of the statutory retirement age are set to add to the widening of the budget deficit.

#### Falling investment explains the 2016 growth slowdown

Investment is estimated to have contracted by 5.5% in 2016, limiting GDP growth to 2.8%. The apparent volatility through weak investment appears to be mainly related to the slow progress of projects financed by EU structural funds under the new programming period and increased policy and regulatory uncertainty. Private consumption, by contrast, expanded strongly (by 3.6%) providing the main growth driver. Solid real wage increases and rising employment, as well as increased social transfers, explain the continued strength of private consumption.

#### Positive growth outlook

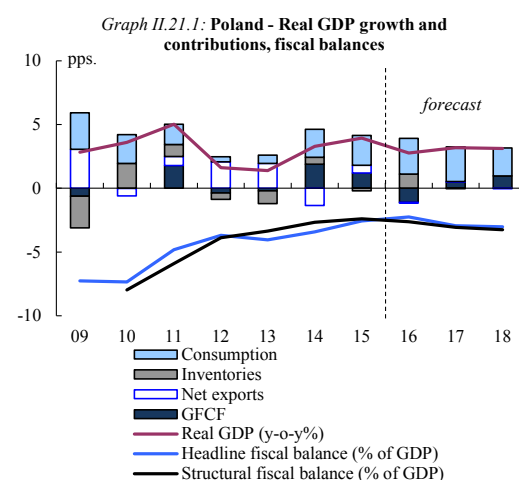
GDP growth is expected to rebound to 3.2% in 2017 and then to broadly stabilise at 3.1% in 2018. This rebound is set to be driven by domestic demand. In particular, private consumption is expected to increase strongly in 2017, before moderating somewhat in 2018, as the transitory impact of increased social transfers fades out and employment stagnates. Public investment is expected to rebound strongly in 2017 and 2018 as EU funds are put to use. Private investment is projected to recover gradually, helped by solid domestic demand and an outlook for further export growth. Relatively high capacity utilisation rates, solid corporate profits and low interest rates are expected to support investment.

Exports are expected to continue their rapid growth as labour costs remain competitive despite wage growth and external demand is projected to gradually strengthen. At the same time, rising domestic demand is set to fuel imports, so the contribution of net exports to growth is forecast to be fairly neutral in 2017 and 2018.

#### Price pressures to remain contained

After turning positive in November 2016, inflation is projected to increase to around 2% in the first months of 2017, mainly driven by rising energy

and food prices. Price pressures are expected to edge upwards in the subsequent period but inflation is expected to remain below 2.5% until the end of 2018.



#### Tightening labour market

Employment growth is expected to decline in 2017 and come to a halt in 2018 due to a combination of a falling working age population and disincentives to labour market participation stemming from certain policy measures. These include a significant lowering of the statutory retirement age from October 2017 and a universal child benefit that was introduced in April 2016. Incentives for labour force participation will weaken mainly for people with low skills. Wage growth is projected to accelerate as unemployment falls to a new record low. Temporary immigration is expected to continue to increase labour supply and the flexibility of the labour market.

#### Risks are broadly balanced

On the downside, a prolongation of policy and regulatory uncertainty may weigh on investment and eventually also private consumption more strongly than currently foreseen. Labour supply could become a growth barrier in some sectors, e.g. if the EU visa-free regime for Ukrainian citizens limits their interest in temporary work in

Poland. On the upside, public and private investment could accelerate faster than currently projected.

### Government deficit to widen in 2017 and 2018

The headline general government deficit is estimated to have narrowed to 2.3% of GDP in 2016, its lowest level since 2007. The improvement was mainly driven by a drop in public investment and one-off revenue, while tax collection was in line with budget plans.

The general government deficit is set to widen to 2.9% of GDP in 2017. This is because the impact of the lowering of the statutory retirement age starts to be felt on top of a full-year impact of the universal child benefit. In addition, public investment is projected to rise strongly. However, these measures should be partially offset by a two-year extension of higher VAT rates that were initially set to expire at the end of 2016.

Under a no-policy-change assumption, Poland's headline general government deficit is expected to widen further to 3.0% of GDP in 2018, reflecting mainly increasing costs of the lowering of the statutory retirement age. The forecast does not include the effects of ongoing efforts to enhance the collection of taxes on production and income, as their likely impact is hard to estimate with sufficient accuracy at this stage.

After having improved to 2½% of GDP in 2015, the structural deficit is estimated to have widened marginally in 2016. It is projected to continue increasing in 2017 and 2018, to reach around 3¼% of GDP at the end of the forecast horizon.

The general government debt is set to grow, from 53.6% of GDP in 2016 to below 56% of GDP in 2018. Considering the relatively high share of debt denominated in foreign currencies, the debt projection for Poland continues to be particularly uncertain.

Table II.21.1:

### Main features of country forecast - POLAND

	2015			97-12	Annual percentage change					
	bn PLN	Curr. prices	% GDP		2013	2014	2015	2016	2017	2018
GDP	1798.3		100.0	4.1	1.4	3.3	3.9	2.8	3.2	3.1
Private Consumption	1051.4	58.5		3.8	0.3	2.4	3.2	3.6	3.9	2.9
Public Consumption	323.5	18.0		3.1	2.5	4.1	2.3	3.7	2.4	2.5
Gross fixed capital formation	360.8	20.1		5.4	-1.1	10.0	6.1	-5.5	2.7	5.3
of which: equipment	136.5	7.6		5.2	4.6	11.2	5.3	-1.0	3.2	4.9
Exports (goods and services)	891.1	49.6		8.3	6.1	6.7	7.7	7.3	6.0	6.4
Imports (goods and services)	835.4	46.5		7.7	1.7	10.0	6.6	7.9	6.4	6.9
GNI (GDP deflator)	1731.8	96.3		3.9	1.8	2.9	3.9	2.7	3.1	3.0
Contribution to GDP growth:										
Domestic demand				4.1	0.4	4.1	3.5	1.7	3.2	3.2
Inventories				0.0	-1.0	0.5	-0.2	1.1	0.0	0.0
Net exports				0.0	1.9	-1.3	0.6	-0.1	0.0	0.0
Employment				0.2	-0.1	1.7	1.5	0.9	0.3	0.0
Unemployment rate (a)				13.4	10.3	9.0	7.5	6.3	5.6	4.7
Compensation of employees / head				7.1	1.7	2.2	1.1	3.9	4.7	5.3
Unit labour costs whole economy				3.0	0.2	0.6	-1.2	2.0	1.8	2.1
Real unit labour cost				-1.2	-0.1	0.1	-1.8	1.3	0.2	0.0
Saving rate of households (b)				8.2	2.5	2.1	1.8	3.1	2.3	2.1
GDP deflator				4.4	0.3	0.5	0.6	0.7	1.6	2.1
Harmonised index of consumer prices				4.9	0.8	0.1	-0.7	-0.2	2.0	2.1
Terms of trade goods				-0.2	1.7	2.2	2.9	1.5	-0.8	-0.1
Trade balance (goods) (c)				-4.3	-0.1	-0.8	0.5	0.9	0.4	0.1
Current-account balance (c)				-4.1	-0.5	-1.4	0.1	0.2	-0.4	-0.8
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-3.5	1.5	0.3	2.4	2.1	1.7	1.7
General government balance (c)				-4.4	-4.1	-3.4	-2.6	-2.3	-2.9	-3.0
Cyclically-adjusted budget balance (d)				-4.4	-3.3	-2.9	-2.4	-2.2	-3.1	-3.3
Structural budget balance (d)				-	-3.3	-2.7	-2.4	-2.6	-3.1	-3.3
General government gross debt (c)				45.1	55.7	50.2	51.1	53.6	54.5	55.8

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.