21. POLAND

Robust growth amid expansionary fiscal policy

Private consumption is set to remain the main growth driver, supported by accelerating wage growth and fiscal transfers. Investment activity is expected to contract in 2016, but should gradually recover as utilisation of EU funds picks up. Price pressures are set to remain subdued. The headline general government deficit is projected to decrease slightly in 2016, but to widen in 2017 and 2018.

Falling investment in the first half of 2016

Falling investment was the main factor behind the 0.1% (q-o-q) decline in GDP in the first quarter of this year. Investment continued to fall in the second quarter but strong exports lifted GDP growth to 0.9% (q-o-q). The weakness of investment appears to be mainly related to the slow start of projects financed by EU structural funds under the new programming period and lower investment activity by state-owned and state-influenced enterprises after the change of government in late 2015. Private consumption, by contrast, continued to rise steadily in the first half of 2016, helped by solid increases in wages and employment.

Growth outlook positive, price pressures subdued

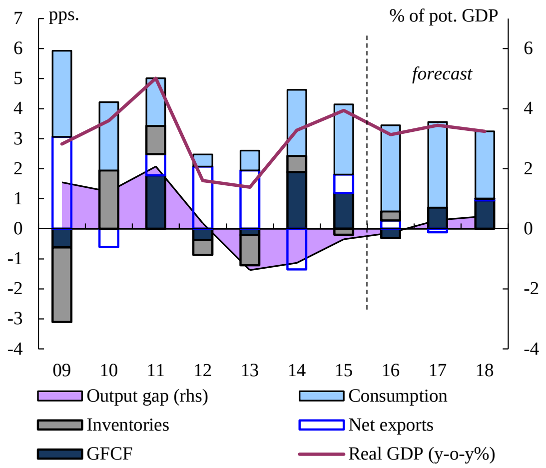
The outlook remains favourable with real GDP growth projected to reach 3.1% in 2016, 3.4% in 2017 and 3.2% in 2018, resulting in the estimated output gap turning positive. Private consumption is set to remain the dominant growth driver, with particularly strong contributions in 2016 and 2017. Further improvements in the labour market and an increase in government transfers, notably a new child benefit, are expected to boost disposable income and improve consumer confidence. Private consumption is projected to slow down towards the end of the forecast period as the temporary effects of new social transfers fade off.

Investment activity is expected to gradually recover starting from late 2016 as more projects co-financed with EU structural funds under the new programming period enter the implementation phase. Several factors point to sizeable investment potential, including, on the one hand, strong domestic demand and an outlook for further export gains and, on the other hand, a relatively high degree of capacity utilisation, still solid corporate profits and low interest rates. However, investment decisions are likely to be affected by uncertainty over the future direction of economic policies.

Polish exports are expected to continue growing robustly as labour costs remain low and the exchange rate supports cost competitiveness. In addition, external demand is projected to gradually strengthen. At the same time, accelerating domestic demand is set to fuel imports so that the growth contribution of net exports is forecast to be close to zero in 2017 and 2018.

Inflation is projected to turn positive at the end of 2016 but price pressures should remain subdued. Consumer prices are forecast to fall by 0.2% on average in 2016 and to grow by 1.3% in 2017 and 1.8% in 2018.

Graph II.21.1: **Poland - Real GDP growth and contributions, output gap**



Tightening labour market

Wage growth is forecast to accelerate in an environment of record-low and still falling unemployment. Employment growth is expected to decelerate in 2017 and come to a halt in 2018 as a result of combined effects of a decreasing working age population and policy measures discouraging labour participation, particularly among the less skilled. These measures include the new universal child benefit and the lowering of the retirement age.

Balanced risks

Risks to the macroeconomic forecast are broadly balanced. On the downside, a prolongation of uncertainty related to the future course of economic policies (e.g. changes to taxation and benefits as well as the role of state-owned enterprises) and questions concerning the rule of law, including the effective constitutional oversight of legislative acts, could affect economic activity more negatively than currently foreseen. On the upside, public and private investment could accelerate faster than currently projected.

Government deficit to widen in 2017

The headline general government deficit is expected to narrow to 2.4% of GDP in 2016, its lowest level since 2007. The improvement is mainly driven by one-off revenue of 0.5% of GDP from the sale of mobile internet frequencies.

Poland's 2017 deficit is projected to widen to 3.0% of GDP due to the increasing costs of the child benefit (in force since the second quarter of 2016) and planned lowering of the statutory retirement age (to be applied from the fourth quarter of 2017). This is expected to be partially offset by increasing revenues from taxes and social contributions due to improved macroeconomic fundamentals. In turn, additional revenues due to continued efforts to improve tax collection are not included in this forecast, as their estimated impact is difficult to assess ex ante and very much conditional on their concrete implementation.

Under a no-policy-change assumption, the general government deficit is set to reach 3.1% of GDP in 2018. This reflects, amongst other things, the full-year effect of the planned lowering of the statutory retirement age. There is, however, uncertainty as to the 2018 fiscal outlook, as some policy proposals (such as the planned reform of the personal income tax) are not yet known in sufficient detail so as to be included in the forecast.

After increasing from 2¼% of GDP in 2015 to 2¾% of GDP in 2016, Poland's structural deficit is projected to widen significantly again in 2017 and to a lesser extent in 2018, reaching 3¼% of GDP.

The general government debt-to-GDP ratio is set to increase from around 51% in 2015 to around 56% in 2018. The debt projections for Poland are, however, uncertain due to the high share of sovereign debt denominated in foreign currencies.

Table II.21.1:

Main features of country forecast - POLAND

	2015		Annual percentage change						
bn PLN	Curr. prices	% GDP	97-12	2013	2014	2015	2016	2017	2018
GDP	1798.3	100.0	4.1	1.4	3.3	3.9	3.1	3.4	3.2
Private Consumption	1051.4	58.5	3.8	0.3	2.4	3.2	3.7	3.9	2.9
Public Consumption	323.5	18.0	3.1	2.5	4.1	2.3	4.0	3.3	3.1
Gross fixed capital formation	360.8	20.1	5.4	-1.1	10.0	6.1	-1.5	3.7	4.9
of which: equipment	136.5	7.6	5.2	4.6	11.2	5.3	2.4	3.9	5.0
Exports (goods and services)	891.1	49.6	8.3	6.1	6.7	7.7	8.3	6.3	6.5
Imports (goods and services)	835.4	46.5	7.7	1.7	10.0	6.6	8.2	7.0	6.8
GNI (GDP deflator)	1744.3	97.0	3.9	1.8	3.1	4.5	2.8	3.4	3.1
Contribution to GDP growth: Domestic demand			4.1	0.4	4.1	3.5	2.6	3.6	3.2
Inventories			0.0	-1.0	0.5	-0.2	0.3	0.0	0.0
Net exports			0.0	1.9	-1.3	0.6	0.3	-0.1	0.1
Employment			0.2	-0.1	1.7	1.4	1.1	0.3	0.0
Unemployment rate (a)			13.4	10.3	9.0	7.5	6.2	5.6	4.7
Compensation of employees / head			7.1	1.7	2.2	1.2	2.7	4.3	5.2
Unit labour costs whole economy			3.0	0.2	0.6	-1.2	0.6	1.2	1.8
Real unit labour cost			-1.2	-0.1	0.1	-1.8	0.3	0.0	0.1
Saving rate of households (b)			8.3	2.5	1.9	2.1	2.8	2.4	2.5
GDP deflator			4.4	0.3	0.5	0.6	0.3	1.2	1.7
Harmonised index of consumer prices			4.9	0.8	0.1	-0.7	-0.2	1.3	1.8
Terms of trade goods			-0.2	1.7	2.2	2.9	0.6	-0.3	-0.3
Trade balance (goods) (c)			-4.3	-0.1	-0.8	0.5	0.8	0.4	0.0
Current-account balance (c)			-4.1	-0.5	-1.1	0.9	0.8	0.2	-0.1
Net lending (+) or borrowing (-) vis-a-vis ROW (c)			-3.5	1.5	0.5	2.8	2.3	2.1	2.1
General government balance (c)			-4.4	-4.1	-3.4	-2.6	-2.4	-3.0	-3.1
Cyclically-adjusted budget balance (d)			-4.4	-3.3	-2.8	-2.4	-2.4	-3.1	-3.3
Structural budget balance (d)			-	-3.3	-2.6	-2.3	-2.8	-3.1	-3.3
General government gross debt (c)			45.1	55.7	50.2	51.1	53.4	55.0	55.5

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