

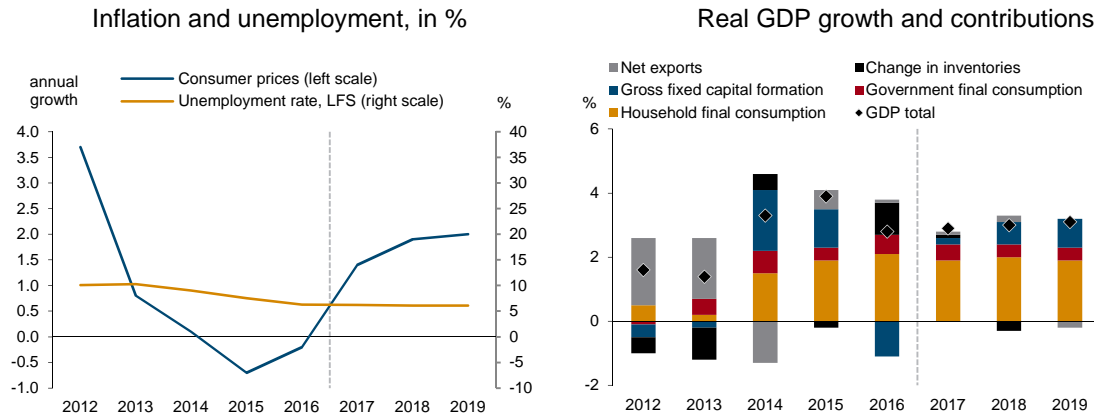


## POLAND: Not so brilliant anymore

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Under the impact of policies that seek to imbue the national economic and social life with ‘law and order’, Poland’s economy clearly underperformed in 2016. This was epitomised by a dramatic decline in gross fixed capital formation. But the economy is still in pretty good shape. It is expected to grow at a respectable pace, provided the institutional changes imposed consider more carefully the needs of the business sector and the limits to what can be achieved through administrative regulation.

Figure 47 / Poland: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

**At 2.8%, GDP growth in 2016 was perceptibly weaker than had been generally expected and then was the case throughout 2014-2015.** Rising consumption (by both the household and the public sector) was the sole item behind the GDP growth. Household consumption contributed 2.1 percentage points (pp) to the overall growth rate, and public consumption another 0.7 pp. The contributions of foreign trade in goods and non-factor services and of gross capital formation were both quantitatively insignificant (+0.1 and -0.1 pp, respectively). However, the contribution of gross fixed capital formation was large and negative (-1.1 pp), while that of rising inventories was large and positive (+1.0 pp).

**The dramatic decline in gross fixed capital formation (down 5.5% in 2016) is not entirely due to the completion of infrastructure projects co-financed by EU transfers under the financial package for 2007-2013.** As is shown by business climate surveys, the heightened levels of uncertainty

over institutional (mainly legal and tax) changes have been very detrimental to propensity to invest: close to 35% of those private firms that do not intend to invest in 2017 quote heightened institutional uncertainty as the reason (and only 13% quote problems with the availability of financial means). The politically motivated official agitation aimed at private business (and its foreign-owned branch in particular) is thus bearing fruit. The draconian penalties proposed (including confiscation of assets) for e.g. faulty corporate tax reporting may well impair private investment (or even production) activities in the future. Interestingly, publicly owned corporations also suffer from the heightened legal uncertainties: 20% of those public corporations that are not undertaking investments in 2017 quote legal uncertainty as the reason. That is not unexpected: for managers of public corporations, inactivity may be safer than activity, as the latter always carries a risk of falling from political grace. Besides, much of the public sector is actually controlled by local government. But local government, predominantly run by the opposition parties, has also become the target for increased 'auditing and surveillance'. No doubt this is also limiting its investment appetite.

**The financial standing of the corporate sector is very good.** The non-financial corporate sector's net profits rose by 22% in the first three quarters of 2016, reaching PLN 88.9 billion (equivalent to some EUR 20.7 billion). Profitability and liquidity ratios have attained levels not seen since 2010. The commercial banks swallowed the additional 'banking tax' introduced in February 2016 (amounting to 0.44% of banks' assets). In 2016, banks' net profits rose by 24.3%, to reach the equivalent of over EUR 3.2 billion. Corporations' ample financial resources tend to swell their idle bank deposits, whose stocks rose by 8.6% in 2016. (Publicly owned corporations increased the stocks of their deposits by 16.6%; private corporations by 6.9%.) Rather unexpectedly, the stocks of bank deposits of households (including firms and farms run by physical persons) also rose quite strongly, by 9.8%. At the same time, both the corporate and the household sectors have remained reluctant to place themselves in debt. The stocks of their debt to the banking sector rose by 5.4% and 5.2%, respectively. These monetary developments reflect, at least partly, the rather restrictive interest rate policy in the clearly deflationary environment that has prevailed since 2013.

**Deflationary tendencies to be overcome.** The long spell of deflation seems just to have ended. Under the impact of higher household income and consumer spending, inflation looks set to rise, returning to more normal levels. The interest rates administered by the national bank are likely to stay comparatively high in 2017 and perhaps beyond. Quite possibly, this will reduce the real interest rates on bank loans and deposits, adding more vigour to lending for consumption and investment purposes. On the other hand, the return of inflation (even if quite moderate) may carry a risk of some real appreciation of the Polish currency. As the nominal depreciation of PLN is unlikely to be pronounced, inflation may somewhat weaken foreign trade performance.

**The foreign trade performance continues to be satisfactory.** Part of the explanation for this is the relatively weak world market prices for raw materials, including oil and natural gas. Also, the contraction in gross fixed capital formation must have reduced demand for imports. If 'normality' returns (with the recovery of prices of energy carriers and the take-off of investment activities), trade may become more of a worry. However, the prospects of trouble emanating from the foreign sector are rather remote. In 2017-2018, trade is likely to be roughly balanced (primarily on account of strong performance in trade in services rather than goods).

**The central government budget deficit in 2016 was lower than expected – though higher than in 2015.** The general government deficit is likely to have approached 3% of GDP in 2016 and will probably surpass that mark in 2017 and later. Additional social spending programmes initiated in 2016 had a positive impact on consumption and GDP growth in 2016. These impacts will continue in 2017. At the same time, the fiscal costs of these programmes may become a problem for the government, which may be tempted to impose extra taxes and to finish off the still surviving chunk of the second pillar of the pension system.

**Falling unemployment and rising wages have not only strengthened the economy (via strong growth in consumption),** but they have also helped to stabilise the popularity of the ruling Law and Justice (PiS) party. Otherwise the political developments have been highly disquieting. PiS, which enjoys a parliamentary (though not a constitutional) majority, pays little heed to the Constitution. It continues to subjugate all public institutions, including those in charge of controlling and balancing the powers of the government. The independent judicial system and local government are the current targets for takeover by PiS loyalists. The political system developing in Poland is certainly unlikely to do the country any good in the long – or even the medium – term.

**Summing up, Poland's economy *qua* economy is in pretty good shape.** The expectation of stable growth in consumption is well grounded, and the maintenance of foreign accounts close to balance will not be a major problem. But politically and – to some extent – also socially, something is rotten in the state of Poland. The ongoing evolution of the political system is also likely to prove harmful economically – primarily in the field of investment, which may remain depressed. This has been demonstrated by developments in 2016. Poland clearly underperformed last year, with much of its potential lying idle amid destructive fears about the legislative whims of the nationalist and populist politics. The likely continuation of current policies does not bode too well for the near future.

Table 18 / Poland: Selected economic indicators

|   | 2012    | 2013    | 2014    | 2015    | 2016 <sup>1)</sup> | 2017     | 2018    | 2019    |
|---|---------|---------|---------|---------|--------------------|----------|---------|---------|
|   |         |         |         |         |                    | Forecast |         |         |
| Population, th pers., average                                 | 38,536  | 38,514  | 38,487  | 38,458  | 38,450             | 38,550   | 38,560  | 38,575  |
| Gross domestic product, PLN bn, nom.                          | 1,629.4 | 1,656.8 | 1,719.7 | 1,798.3 | 1,830.0            | 1,900    | 1,980   | 2,060   |
| annual change in % (real)                                     | 1.6     | 1.4     | 3.3     | 3.9     | 2.8                | 2.9      | 3.0     | 3.1     |
| GDP/capita (EUR at PPP)                                       | 17,800  | 17,900  | 18,600  | 19,800  | 20,400             | .        | .       | .       |
| Consumption of households, PLN bn, nom.                       | 988.0   | 995.3   | 1,019.4 | 1,038.2 | 1,070.0            | .        | .       | .       |
| annual change in % (real)                                     | 0.8     | 0.3     | 2.6     | 3.2     | 3.6                | 3.3      | 3.4     | 3.3     |
| Gross fixed capital form., PLN bn, nom.                       | 322.5   | 311.7   | 339.4   | 360.8   | 332.0              | .        | .       | .       |
| annual change in % (real)                                     | -1.8    | -1.1    | 10.0    | 6.1     | -5.5               | 1.0      | 3.5     | 4.5     |
| Gross industrial production (sales) <sup>2)</sup>             |         |         |         |         |                    |          |         |         |
| annual change in % (real)                                     | 1.3     | 2.3     | 3.4     | 4.8     | 2.8                | 3.6      | 4.5     | 4.3     |
| Gross agricultural production                                 |         |         |         |         |                    |          |         |         |
| annual change in % (real)                                     | 1.2     | 0.7     | 6.9     | -2.5    | 8.6                | .        | .       | .       |
| Construction industry <sup>2)</sup>                           |         |         |         |         |                    |          |         |         |
| annual change in % (real)                                     | -5.2    | -10.2   | 4.3     | 0.3     | -14.5              | .        | .       | .       |
| Employed persons, LFS, th, average                            | 15,591  | 15,568  | 15,862  | 16,084  | 16,230             | 16,260   | 16,280  | 16,280  |
| annual change in %  | 0.2     | -0.1    | 1.9     | 1.4     | 0.9                | 0.2      | 0.1     | 0.0     |
| Unemployed persons, LFS, th, average                          | 1,749   | 1,793   | 1,567   | 1,304   | 1,078              | 1,070    | 1,060   | 1,060   |
| Unemployment rate, LFS, in %, average                         | 10.1    | 10.3    | 9.0     | 7.5     | 6.3                | 6.2      | 6.1     | 6.1     |
| Reg. unemployment rate, in %, end of period                   | 13.4    | 13.4    | 11.4    | 9.7     | 8.3                | .        | .       | .       |
| Average monthly gross wages, PLN                              | 3,530   | 3,659   | 3,777   | 3,908   | 4,068              | 4,300    | 4,500   | 4,800   |
| annual change in % (real, gross)                              | 0.1     | 2.8     | 3.2     | 4.5     | 4.9                | 4.0      | 3.5     | 3.5     |
| Consumer prices (HICP), % p.a.                                | 3.7     | 0.8     | 0.1     | -0.7    | -0.2               | 1.4      | 1.9     | 2.0     |
| Producer prices in industry, % p.a.                           | 3.3     | -1.3    | -1.3    | -2.0    | -0.4               | 0.0      | 0.8     | 1.3     |
| General governm.budget, EU-def., % of GDP                     |         |         |         |         |                    |          |         |         |
| Revenues  | 39.0    | 38.4    | 38.7    | 38.9    | 39.5               | 39.0     | 39.0    | 39.5    |
| Expenditures  | 42.7    | 42.4    | 42.1    | 41.5    | 42.4               | 42.5     | 42.5    | 43.0    |
| Net lending (+) / net borrowing (-)                           | -3.7    | -4.1    | -3.4    | -2.6    | -2.9               | -3.5     | -3.5    | -3.5    |
| Public debt, EU-def., % of GDP                                | 53.7    | 55.7    | 50.2    | 51.1    | 53.1               | 53.0     | 53.5    | 55.0    |
| Stock of loans of non-fin.private sector, % p.a               | 0.6     | 3.3     | 5.8     | 7.1     | 5.3                | .        | .       | .       |
| Non-performing loans (NPL), in %, Dec                         | 8.8     | 8.5     | 8.1     | 7.5     | 7.2                | .        | .       | .       |
| Central bank policy rate, % p.a., end of period <sup>3)</sup> | 4.3     | 2.5     | 2.0     | 1.5     | 1.5                | 1.8      | 2.0     | 2.5     |
| Current account, EUR mn <sup>4)</sup>                         | -14,458 | -5,028  | -8,529  | -2,654  | -2,259             | -3,100   | -5,100  | -6,700  |
| Current account, % of GDP <sup>4)</sup>                       | -3.7    | -1.3    | -2.1    | -0.6    | -0.5               | -0.7     | -1.1    | -1.4    |
| Exports of goods, BOP, EUR mn <sup>4)</sup>                   | 141,026 | 149,113 | 158,657 | 172,150 | 176,506            | 181,400  | 191,700 | 203,400 |
| annual change in %  | 6.5     | 5.7     | 6.4     | 8.5     | 2.5                | 2.8      | 5.7     | 6.1     |
| Imports of goods, BOP, EUR mn <sup>4)</sup>                   | 149,156 | 149,448 | 161,911 | 169,937 | 174,889            | 182,800  | 195,600 | 211,200 |
| annual change in %  | 2.4     | 0.2     | 8.3     | 5.0     | 2.9                | 4.5      | 7.0     | 8.0     |
| Exports of services, BOP, EUR mn <sup>4)</sup>                | 31,949  | 33,592  | 36,743  | 40,663  | 43,935             | 46,600   | 48,900  | 51,300  |
| annual change in %  | 8.8     | 5.1     | 9.4     | 10.7    | 8.0                | 6.0      | 5.0     | 5.0     |
| Imports of services, BOP, EUR mn <sup>4)</sup>                | 25,947  | 25,948  | 27,679  | 29,745  | 30,608             | 32,100   | 33,400  | 34,700  |
| annual change in %  | 7.2     | 0.0     | 6.7     | 7.5     | 2.9                | 5.0      | 4.0     | 4.0     |
| FDI liabilities, EUR mn <sup>4)</sup>                         | 5,771   | 658     | 14,824  | 12,631  | 12,506             | .        | .       | .       |
| FDI assets, EUR mn <sup>4)</sup>                              | 1,055   | -2,524  | 5,096   | 3,790   | 7,924              | .        | .       | .       |
| Gross reserves of NB excl. gold, EUR mn                       | 78,403  | 74,257  | 79,379  | 83,676  | 104,439            | .        | .       | .       |
| Gross external debt, EUR mn <sup>4)</sup>                     | 279,739 | 278,948 | 293,509 | 302,063 | 316,660            | 332,000  | 352,300 | 368,900 |
| Gross external debt, % of GDP <sup>4)</sup>                   | 71.8    | 70.7    | 71.4    | 70.3    | 75.5               | 76.0     | 76.5    | 77.0    |
| Average exchange rate PLN/EUR                                 | 4.1847  | 4.1975  | 4.1843  | 4.1841  | 4.3632             | 4.35     | 4.30    | 4.30    |

1) Preliminary and wiiw estimates. - 2) Enterprises with 10 and more employees. - 3) Reference rate (7-day open market operation rate). - 4) Including SPE.

Source: wiiw Databases incorporating Eurostat and national statistics. Forecasts by wiiw.