

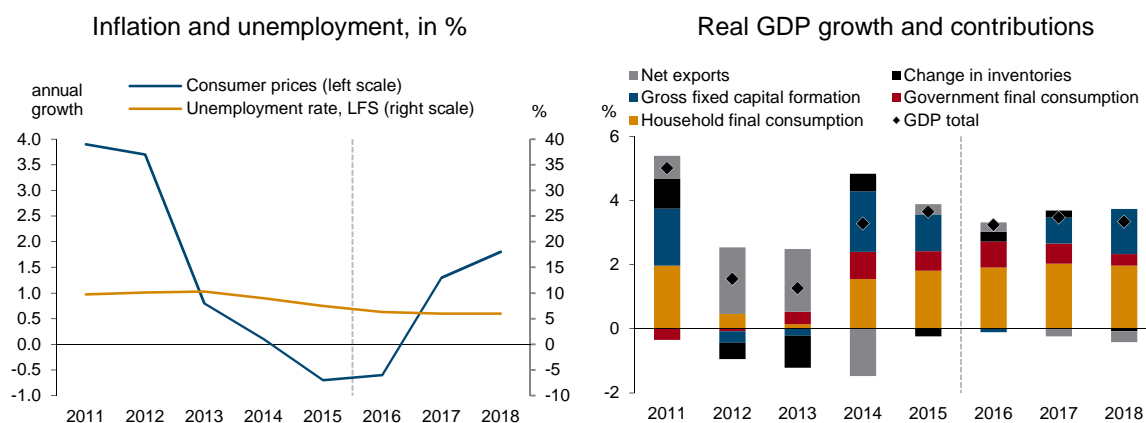


POLAND: So far so good?

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The current moderate and broad-based growth will continue throughout the biennium 2017-2018, with the GDP growth rate averaging 3.4%. The current evolution of the political system may well prove harmful – in purely economic terms as well. 2017 will prove a critical year for fiscal policy as the increase in social expenditures may call for higher taxation.

Figure 37 / Poland: Main macroeconomic indicators



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

At 3% the GDP growth in the first quarter of 2016 was perceptibly weaker than generally expected or throughout 2014-2015. In the second quarter growth did not accelerate visibly. While unfavourable foreign trade (in goods and services) developments were the main factor slowing down GDP growth in the first quarter, the strong decline in capital formation suppressed growth in the second. Overall, the contribution of foreign trade to the 3.1% GDP growth reported for the first half of the year appears to have been about zero. Gross fixed capital formation contributed negatively, by 0.6 percentage points (pp) and rising inventories contributed positively (again by 0.6 pp). Contrary to earlier expectations, growth in household and public consumption did not accelerate. The contributions of household and public consumption to GDP growth in the first half of the year were 2.0 pp and 0.8 pp respectively. Growth in household consumption remains, unexpectedly, rather subdued – and that despite some significant additional public transfers to households (promised or already implemented) and despite rising employment and real wages. Apparently, the household sector's propensity to consume must

have been depressed, most possibly temporarily (perhaps also on account of self-reinforcing deflationary expectations).

As elsewhere in the region, the decline in gross fixed capital formation has been primarily due to the completion of infrastructural projects co-financed by EU transfers under the 2007-2013 financial perspective. This fact is confirmed by information on investment outlays at the sectoral level. While the investment outlays in manufacturing still expanded by 7.6% in the first half of 2016, such outlays declined in the construction sector by over 10% and in the transport and storage sector (the main beneficiary of EU structural grants) by about 38%. The estimated value of investment projects actually started in the first half of 2016 fell by close to 2% in manufacturing, by over 20% in the construction sector and by close to 80% in land transport. The slack in investment activities will be continuing until the means available under the new perspective feed the new investment projects (whose preparation will also take some time-consuming paperwork).

The financial standing of the non-financial corporate sector is good. The sector's net profit rose by 11.4% in the first half of the year, reaching PLN 74.8 billion (equivalent to some EUR 17 billion). The commercial banks swallowed the 'banking tax' in force since February 2016 (amounting to 0.44% of banks' assets). In the first half of the year banks' net profits managed to rise by 1.2%, reaching over EUR 1.8 billion.

Despite continuing deflation (in both consumer and producer prices) the interest rates administered by the National Bank have stayed at comparatively high levels. The change at the helm of the National Bank has not (yet) changed the NBP's approach to the real economy. The prevalence of high nominal (and even higher real) interest rates on credit is, at least partly, the consequence of the official policy. It is therefore not surprising that the private non-financial sector's bank deposits rise much faster than the bank loans drawn. In the first half of 2016, private (non-financial sector) deposits rose by 11% while loans by 5.5%. In the same period, loans to households (financing mainly the satisfaction of housing needs) rose 4.5% and loans to the non-financial corporate sector by 7.4%. Banks' 'financing gap' (filled by liabilities to foreign parties) has been narrowing. Thereby banks' resilience to eventual negative shocks has been further strengthened.

Only a fraction of the new loans to firms has been declared as serving the financing of new fixed investment. The bulk of loans extended serve other purposes such as the financing of working capital or investment in real estate. A very slow decline in the shares of bad loans in total loans (currently 6.3% in the case of households and 9.6% in the case of non-financial firms) has been another consequence of the difficult deleveraging under unduly high interest rates.

The foreign trade performance has been satisfactory though a part of the credit for this must go to weak world market prices of raw materials, including oil and natural gas. Also, the contraction in gross fixed capital formation must have reduced the demand for imports. If 'normalcy' returns (with the recovery of prices of energy carriers and the takeoff of investment activities) trade may become a real worry. Real currency depreciation and falling unit labour costs may then be needed – although the latter development may be difficult to square with the faster growth of domestic consumption.

Whether the country has reached a stage where the improvements in cost competitiveness have exhausted their potential as a reliable source of balanced longer-term growth remains to be seen. But

there are good grounds to believe that Poland is entering a 'middle-income trap': the levels of spending on research and development is miserably low, the country has been specialising in medium- rather than high-tech activities. Getting out of that trap may require the institution of radically new economic and social policies, with priorities given, among other items, to the accumulation of human rather than physical capital. Under the present government led by the Law and Justice Party (in office for about a year now), no such radically new policy is to be expected. If anything, the policies imposed (or officially contemplated) are quite likely to lead the country astray. For example, the government seems determined to protect the oversized and inherently loss-making hard coal mining industry indefinitely.

At mid-year the central government budget deficit was lower than expected. To some extent this is due to one-off income accruing to the public accounts (large profit made by the National Bank and income from the LTE licences auctioned). Lower public spending on the required domestic co-financing of infrastructural projects financed from EU grants has also been a factor. All the same, the general government deficit is likely to approach 3% of GDP in 2016. In 2017 the public sector deficit will have to be much higher not only because one-off income need not be forthcoming. The transfers to households introduced in 2016 will cost much more in the future while some additional taxation proposed (e.g. on retail trade) may prove incompatible with the EU competition law. To muddle through 2017 fiscally, the government may decide to nationalise the remaining portion of the second (capital-based) pillar of the pension system – and appropriate its assets as well as the current income. Because of the expected worries about the public finances the government may shelve a number of social 'reforms' promised before the elections (e.g. on the lowering of the retirement age). Also, the announced re-Polonisation of foreign-owned banks and insurance companies will remain empty rhetoric, at least for the time being.

Domestic political developments have been highly disquieting. The ruling party, enjoying parliamentary (though not constitutional) majority, does not pay much attention to the Constitution itself. It is bent on subjugating all public institutions, including the ones in charge of controlling and balancing the powers of the government. That this undermines the rule of law is evident – also to the European Commission. No doubt the political system developing in Poland is unlikely to do any good to the country in the long run. In the short run it is also likely to do more harm than good. The wholesale purge of the managing personnel in the public sector (including state-owned corporations and official agencies in charge of negotiations over EU transfers) leaves a vacuum that is filled by loyal party apparatchiks often lacking any requisite skills or knowledge.

Summing up, Poland's corporate non-financial sector and the banking system are in good shape. Despite persistent deflation and inadequate monetary policy, the country will continue to grow at a moderate speed in 2016 and 2017-2018 (by 3.3% to 3.4%). Currently gross fixed capital formation is a drag on growth. But this will be changing due to the return of higher financing of infrastructural projects expected in the future. The ongoing evolution of the political system is likely to prove harmful, also economically.

Table 20 / Poland: Selected economic indicators

	2012	2013	2014	2015 ¹⁾	2015 January-June	2016	2016 Forecast	2017 Forecast	2018
Population, th pers., average	38,536	38,514	38,487	38,458	38,459	38,427	38,500	38,550	38,560
Gross domestic product, PLN bn, nom.	1,629.0	1,656.3	1,719.1	1,789.7	844.1	872.5	1,830	1,910	1,990
annual change in % (real)	1.6	1.3	3.3	3.6	3.4	2.7	3.2	3.5	3.3
GDP/capita (EUR at exchange rate)	10,100	10,200	10,700	11,100	.	.	11,100	11,500	12,100
GDP/capita (EUR at PPP)	17,600	17,900	18,600	19,700	.	.	.	.	.
Consumption of households, PLN bn, nom.	988.2	994.1	1,018.6	1,036.7	524.4	537.2	.	.	.
annual change in % (real)	0.8	0.2	2.6	3.1	3.6	2.9	3.3	3.5	3.4
Gross fixed capital form., PLN bn, nom.	322.5	311.7	339.4	360.4	136.0	131.6	.	.	.
annual change in % (real)	-1.8	-1.1	10.0	5.8	7.7	-3.6	-0.5	4.0	7.0
Gross industrial production (sales) ²⁾									
annual change in % (real)	1.3	2.3	3.4	4.8	4.7	4.0	4.0	4.5	5.0
Gross agricultural production									
annual change in % (real)	1.2	0.7	6.6	-2.8	.	.	.	.	.
Construction industry ²⁾									
annual change in % (real)	-5.2	-10.2	4.3	0.3	1.7	-13.2	.	.	.
Employed persons, LFS, th, average	15,591	15,568	15,862	16,084	15,911	16,097	16,230	16,260	16,280
annual change in %	0.2	-0.1	1.9	1.4	1.5	1.2	0.9	0.2	0.1
Unemployed persons, LFS, th, average	1,749	1,793	1,567	1,304	1,388	1,134	1,090	1,040	1,040
Unemployment rate, LFS, in %, average	10.1	10.3	9.0	7.5	8.0	6.6	6.3	6.0	6.0
Reg. unemployment rate, in %, end of period	13.4	13.4	11.4	9.8	10.2	8.8	.	.	.
Average monthly gross wages, PLN ³⁾	3,530	3,659	3,777	3,900	4,051	4,220	4,000	4,200	4,400
annual change in % (real, gross) ³⁾	0.1	2.8	3.2	4.2	4.8	5.1	4.0	4.0	3.5
Consumer prices (HICP), % p.a.	3.7	0.8	0.1	-0.7	-0.9	-0.4	-0.6	1.3	1.8
Producer prices in industry, % p.a.	3.3	-1.3	-1.3	-2.0	-2.2	-1.3	-1.0	-0.5	1.0
General governm.budget, EU-def., % of GDP									
Revenues	38.9	38.4	38.9	38.9	.	.	39.5	39.0	39.0
Expenditures	42.6	42.4	42.2	41.5	.	.	42.4	42.5	42.5
Net lending (+) / net borrowing (-)	-3.7	-4.0	-3.3	-2.6	.	.	-2.9	-3.5	-3.5
Public debt, EU-def., % of GDP	54.0	56.0	50.5	51.3	.	.	52.2	53.0	53.5
Central bank policy rate, % p.a., end of period ⁴⁾	4.3	2.5	2.0	1.5	1.5	1.5	1.5	1.8	2.0
Current account, EUR mn ⁵⁾	-14,458	-5,028	-8,529	-2,654	832	807	-1,300	-2,700	-4,700
Current account, % of GDP ⁵⁾	-3.7	-1.3	-2.1	-0.6	0.4	0.4	-0.3	-0.6	-1.0
Exports of goods, BOP, EUR mn ⁵⁾	141,026	149,113	158,657	172,150	85,484	87,405	179,000	188,000	197,400
annual change in %	6.5	5.7	6.4	8.5	9.7	2.2	4.0	5.0	5.0
Imports of goods, BOP, EUR mn ⁵⁾	149,156	149,448	161,911	169,937	83,596	84,995	176,700	187,300	198,500
annual change in %	2.4	0.2	8.3	5.0	5.1	1.7	4.0	6.0	6.0
Exports of services, BOP, EUR mn ⁵⁾	31,949	33,592	36,743	40,663	19,364	20,271	42,300	44,000	45,800
annual change in %	8.8	5.1	9.4	10.7	11.5	4.7	4.0	4.0	4.0
Imports of services, BOP, EUR mn ⁵⁾	25,947	25,948	27,679	29,745	13,757	13,805	30,500	31,700	33,000
annual change in %	7.2	0.0	6.7	7.5	8.7	0.3	2.5	4.0	4.0
FDI liabilities (inflow), EUR mn ⁵⁾	5,771	658	14,824	12,631	6,067	6,445	9000	.	.
FDI assets (outflow), EUR mn ⁵⁾	1,055	-2,524	5,096	3,790	3,277	2,190	3000	.	.
Gross reserves of NB excl. gold, EUR mn	78,403	74,257	79,379	83,676	89,906	95,254	.	.	.
Gross external debt, EUR mn ⁵⁾	279,739	278,948	293,509	302,063	308,289	309,221	314,900	328,700	346,500
Gross external debt, % of GDP ⁵⁾	71.9	70.7	71.4	70.6	72.1	72.7	74.0	74.0	74.0
Average exchange rate PLN/EUR	4.1847	4.1975	4.1843	4.1841	4.1397	4.3686	4.30	4.30	4.25
Purchasing power parity PLN/EUR	2.3978	2.4087	2.4060	2.3647	.	.	.	.	.

1) Preliminary. - 2) Enterprises with 10 and more employees. - 3) Half-year data refer to enterprises with 10 and more employees. - 4) Reference rate (7-day open market operation rate). - 5) Including SPE.

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