21. POLAND

Positive economic conditions expected to continue

Poland's economy is expected to continue growing robustly with only limited moderation in 2019. Consumption and investment are the main growth drivers, supported by fast wage growth, strong consumer confidence and EU structural funds. Inflation is forecast to dip in 2018 and then increase on the back of rising wages. The headline fiscal deficit is projected to decrease slightly in 2018 and remain stable in 2019, while the structural fiscal balance is expected to continue deteriorating gradually.

Growth to remain strong

Poland's economy is expected to continue growing strongly. Real GDP is forecast to expand by 4.3% this year, only slightly less than the 4.6% recorded in 2017. A limited moderation is forecast for 2019, with real GDP expected to rise by 3.7%. Domestic demand is projected to remain the key growth driver.

Private consumption growth is set to slow gradually from 4.1% in 2018 to 3.4% in 2019 but will nevertheless remain high as a result of strong wage growth and record-high consumer confidence. Public investment is projected to continue its fast recovery rising quickly in 2018, as funds offered by the EU are put to work, with strong moderation in 2019. Private investment, which remained weak in 2017, is expected to gradually recover over 2018 and 2019, given high capacity utilisation rates, the solid demand outlook and low interest rates. The rising scarcity of adequately qualified workers, however, is expected to limit investment growth by discouraging some investment decisions.

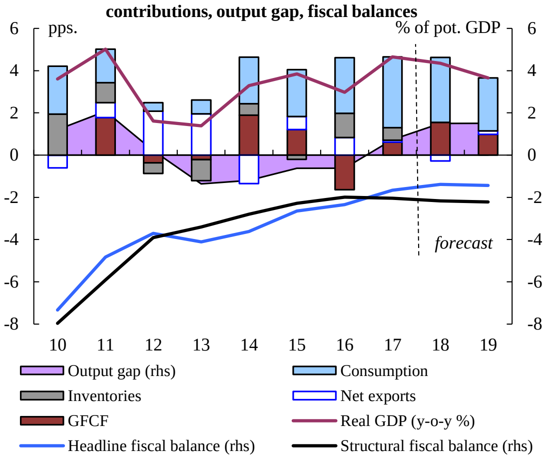
Exports are projected to continue rising in 2018 and 2019, faster than demand growth in key export markets. Strong domestic demand, in particular the investment recovery, is set to translate into higher import demand in 2018. As a result the contribution of net exports to GDP is expected to be slightly negative in 2018, before turning marginally positive in 2019.

Labour market getting tighter

Job creation was strong until late 2017 when it slowed down, partly due to a lowering of the statutory retirement age. Employment is expected to continue rising in the second half of 2018 and in 2019, but its rate of growth is set to slow given the shrinking pool of unemployed and of people who can join the labour force. There remains substantial uncertainty as to the possibility for further strong increases in employment by migrant workers, mainly from Ukraine.

Unemployment, which fell to historically low levels in 2017, is expected to continue falling. As workers become increasingly scarce, wage growth is expected to strengthen.

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



Wage hikes to gradually translate into higher inflation

Inflation dipped in early 2018 as a result of several sector-specific developments, such as lower dynamics of food and energy products and a decline in financial services charges. Going forward, inflation is forecast to increase for the rest of this year and next. Faster wage growth is expected to be the main factor behind rising prices, especially in the services sector. The assumed modest strengthening of the zloty vis-à-vis the euro in 2018, however, will dampen some prices.

Little improvement in headline deficit expected despite strong growth

The general government headline deficit contracted strongly from 2.3% of GDP in 2016 to 1.7% of GDP in 2017. This is a consequence of revenue growing faster than expenditure, in particular social contributions and taxes. The growth of social contribution revenue reflects the buoyant situation on the labour market, while the increase in revenue from taxes is driven by several factors. These include the robust macroeconomic environment and measures to increase tax collection, particularly in the area of indirect taxes.

In 2018, both revenue and expenditure are projected to increase as a share of GDP. On the revenue side, the strongest gains are again expected in indirect taxes and social contributions. On the expenditure side, the fastest increase is expected for investment. Overall, the general government headline deficit is expected to further narrow to 1.4% of GDP in 2018.

Under a no-policy-change scenario, the general government headline deficit is forecast to stabilise in 2019. Increasing tax revenue is set to counterbalance higher social spending and public investment.

In turn, the structural general government deficit is estimated to have remained broadly constant in 2017 at 2% of GDP. Considering the cyclical position of the economy marked by strong GDP growth and an increasingly positive output gap, the structural deficit is projected to widen over the forecast horizon. It is expected to reach 2¼% of GDP in 2019.

After a significant fall from above 54% of GDP in 2016 to less than 51% of GDP in 2017, the general government debt is forecast to continue declining to around 49% of GDP in 2019.

Risks to the fiscal forecast are generally balanced. On the one hand, recent policy announcements suggest that new spending measures are likely to be implemented. If so, this would increase both headline and structural deficits. On the other hand, a further extension of the application of higher VAT rates beyond 2018 could help maintain strong VAT revenues. In addition, there remains uncertainty as to the capacity to carry out public investment plans, the effectiveness of new measures to increase tax compliance, the efficiency of public expenditure management, as well as the number of retiring people who actually stop working in light of the recently reduced statutory retirement age.

Table II.21.1

Main features of country forecast - POLAND

	2016		Annual percentage change						
	bn PLN Curr. prices	% GDP	98-13	2014	2015	2016	2017	2018	2019
GDP	1858.5	100.0	3.8	3.3	3.8	3.0	**4.6**	**4.3**	**3.7**
Private Consumption	1088.4	58.6	3.4	2.4	3.0	3.9	**4.7**	**4.1**	**3.4**
Public Consumption	332.0	17.9	3.1	4.1	2.4	1.8	**3.4**	**3.7**	**3.1**
Gross fixed capital formation	335.0	18.0	4.0	10.0	6.1	-8.2	**3.4**	**8.7**	**5.3**
of which: equipment	135.8	7.3	4.1	11.2	12.1	-7.6	**4.5**	**6.9**	**5.1**
Exports (goods and services)	971.4	52.3	7.9	6.7	7.7	8.8	**8.2**	**7.3**	**6.2**
Imports (goods and services)	896.3	48.2	6.5	10.0	6.6	7.6	**8.7**	**8.4**	**6.3**
GNI (GDP deflator)	1788.8	96.3	3.6	2.9	3.9	2.9	**4.3**	**4.3**	**3.5**
Contribution to GDP growth: Domestic demand			3.6	4.1	3.4	1.0	**4.0**	**4.6**	**3.5**
Inventories			0.0	0.5	-0.2	1.1	**0.6**	**0.0**	**0.0**
Net exports			0.3	-1.3	0.6	0.8	**0.1**	**-0.3**	**0.2**
Employment			0.1	1.7	1.5	0.6	**1.4**	**0.8**	**0.3**
Unemployment rate (a)			13.3	9.0	7.5	6.2	**4.9**	**4.1**	**3.9**
Compensation of employees / head			5.9	2.2	1.7	5.1	**4.0**	**6.8**	**7.4**
Unit labour costs whole economy			2.2	0.6	-0.6	2.6	**0.7**	**3.2**	**3.9**
Real unit labour cost			-1.3	0.1	-1.3	2.3	**-1.2**	**1.5**	**1.4**
Saving rate of households (b)			7.4	2.3	2.3	4.4	**1.7**	**1.8**	**1.4**
GDP deflator			3.5	0.5	0.8	0.3	**1.9**	**1.7**	**2.4**
Harmonised index of consumer prices			4.1	0.1	-0.7	-0.2	**1.6**	**1.3**	**2.5**
Terms of trade goods			0.1	2.2	2.9	0.6	**0.4**	**0.1**	**0.0**
Trade balance (goods) (c)			-3.9	-0.8	0.5	0.7	**0.1**	**-0.4**	**-0.6**
Current-account balance (c)			-4.0	-1.4	0.2	0.9	**0.7**	**0.3**	**0.0**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)			-3.3	0.4	2.6	1.7	**1.5**	**1.5**	**1.5**
General government balance (c)			-4.4	-3.6	-2.6	-2.3	**-1.7**	**-1.4**	**-1.4**
Cyclically-adjusted budget balance (d)			-4.2	-3.0	-2.3	-2.0	**-2.0**	**-2.2**	**-2.2**
Structural budget balance (d)			-	-2.8	-2.3	-2.0	**-2.0**	**-2.2**	**-2.2**
General government gross debt (c)			45.9	50.3	51.1	54.2	**50.6**	**49.6**	**49.1**

(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.