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Analysis by the Commission services of the budgetary situation in Poland following the adoption of the COUNCIL RECOMMENDATION to Poland of 2 December 2009 with a view to bringing an end to the situation of an excessive government deficit

Accompanying the document

Recommendation for a

COUNCIL RECOMMENDATION

with a view to bringing an end to the situation of an excessive government deficit in Poland

{COM(2013) 393 final}

1. INTRODUCTION

On 7 July 2009, the Council decided, in accordance with Article 104(6) of the Treaty establishing the European Community (TEC), that an excessive deficit existed in Poland and issued a recommendation to correct the excessive deficit by 2012 at the latest[1], in accordance with Article 104(7) TEC and Article 3 of Council Regulation (EC) No 1467/97 of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure[2]. In order to bring the general government deficit below 3% of GDP in a credible and sustainable manner, the Polish authorities were recommended to implement the fiscal stimulus measures in 2009 as planned, ensure an average annual structural budgetary adjustment of at least 1¼% percentage points of GDP starting in 2010, spell out detailed measures that are necessary to bring the deficit below the reference value by 2012 and introduce reforms to contain primary current expenditure over the following years. The Council established a deadline of 7 January 2010 for effective action to be taken.

On 3 February 2010, the Commission concluded that based on the Commission services' 2009 autumn forecast, Poland had taken necessary action in compliance with the Council recommendation of 7 July 2009 to bring its government deficit below the 3% of GDP reference value and considered that no additional step in the excessive deficit procedure was therefore necessary. On the basis of its 2011 autumn forecast, the Commission considered that Poland was not on track and asked for additional measures, which Poland provided. Thus, on 11 January 2012 the Commission confirmed that the Polish authorities had taken effective action towards a timely and sustainable correction of the excessive deficit and no further steps in the excessive deficit procedure of Poland were needed at the time[3].

This document provides an assessment of whether Poland has undertaken effective action towards the correction of its excessive general government deficit, and suggests a new adjustment path that would durably bring the general government deficit below the 3% of GDP threshold. In particular, the document examines the budgetary developments since the Commission Communication to the Council on action taken as of 3 February 2010.

2. RECENT MACRO-ECONOMIC AND BUDGETARY DEVELOPMENTS AND OUTLOOK FOR 2014

Poland has seen relatively resilient economic activity in 2009-2012, albeit with real GDP growth below potential, as a result of the global economic and financial crisis. The real GDP increase of 1.6% in 2009 was mainly driven by fiscal and monetary policy easing, inflows of EU funds financing infrastructure investments and a currency depreciation. The pick-up in exports and the rebound of domestic demand led to a recovery in 2010 and 2011, when real GDP grew by 3.9% and 4.5%, respectively. GDP growth in 2010 was well above the 0.8% expected in the Commission services' 2009 spring forecast (see Table 1), which was

1 All documents related to the excessive deficit procedure of Poland can be found at: http://ec.europa.eu/economy_finance/economic_governance/sgp/deficit/countries/poland_en.htm

2 OJ L 209, 2.8.1997, p. 6.

3 Communication from the Commission to the Council on assessment of budgetary implementation in the context of the ongoing Excessive Deficit Procedures after the Commission services' 2011 autumn forecast - COM(2012) 4 final, 11.1.2012.

underlying the EDP recommendation. The Commission services' 2009 spring forecast expected the closure of the output gap beyond the forecast horizon and implicitly assumed a growth rate of the Polish economy around its potential one in outer years.

In reality, the Polish economy slowed down sharply in 2012 with real GDP growth of 1.9%. Investment, especially construction, was held back by government consolidation, subdued credit growth and households refraining from real estate purchases. As a result of only moderately increasing real disposable income and faltering confidence private consumption grew by 0.8%, the lowest ever, in 2012. A positive contribution to growth from net external demand was a result of modest export growth by 2.8%, particularly services growing by 6.5%, and import falling by -1.8% due to weak domestic demand.

Table 1: Comparison of macroeconomic developments and forecasts

	2009	2010		2011		2012		2013			2014		
	outturn	outturn	COM SF 2009	outturn	COM SF 2009	outturn	COM SF 2009	COM SF 2009	COM SF 2013	CP 2013	COM SF 2009	COM SF 2013	CP 2013
Real GDP (% change)	1.6	3.9	0.8	4.5	n.a	1.9	n.a.	n.a.	1.1	1.5	n.a.	2.2	2.5
Contributions to real GDP growth													
Final domestic demand	1.3	2.6	0.1	3.0	n.a	0.3	n.a.	n.a.	0.2	0.8	n.a.	1.6	2.7
Changes in inventories	-2.4	2.0	0.0	0.6	n.a	-0.5	n.a.	n.a.	0.0	0.0	n.a.	0.0	0.5
Net exports	2.7	-0.7	0.7	0.9	n.a	2.1	n.a.	n.a.	0.9	0.8	n.a.	0.6	-0.1
Employment (% change)	0.4	0.5	-1.4	1.0	n.a	0.2	n.a.	n.a.	-0.4	-0.3	n.a.	-0.2	0.0
GDP deflator (% change)	3.7	1.4	1.6	3.1	n.a	2.7	n.a.	n.a.	1.4	1.5	n.a.	1.7	2.2
Output gap	1.0	1.1	-3.8	0.8	n.a	-0.7	n.a.	n.a.	-2.4	-3.1	n.a.	-2.8	-3.7
Potential output growth	3.7	3.9	3.2	4.5	n.a	3.6	n.a.	n.a.	2.9	3.3	n.a.	2.7	3.1

Source: COM SF 2009 - Commission services' 2009 spring forecast; COM SF 2013 - Commission services' 2013 spring forecast; CP 2013 - 2013 update of the Convergence Programme

The Commission services' 2013 spring forecast projects an increase in real GDP of only 1.1% in 2013 and significantly more negative output gap of -2.4%. Private consumption is forecast to grow by 0.8% due to falling employment, subdued wage growth and households rebuilding their savings. The trend in gross fixed capital formation, particularly in infrastructural construction, is set to remain negative with a decline of 2.6%, reflecting further fiscal consolidation, weak external demand and subdued credit growth. Due to the expected slow recovery of the global economy, export volumes are forecast to increase by only 2.6%. Meanwhile, imports are expected to increase by 0.6% in line with final demand growth. In total, these trends are projected to result in a limited contribution of net external demand to growth, amounting to 0.9 pps. In 2014, some pick up of the economy with real GDP growth of 2.2% is expected, although this is subject to risks in both directions depending on the speed of global recovery. Moreover, on the upside, a weaker currency would further boost exports and enhance import substitution. On the downside, a further deterioration in consumer and business confidence might lead to an even more risk-adverse behaviour of consumers and companies, delaying the pick-up in investment and consumption.

The general government deficit had jumped to 7.4% of GDP in 2009 (from 3.7% of GDP in 2008) due to a sizeable fiscal stimulus and strong, in-built expenditure dynamics predicated on high growth. After the excessive deficit procedure was launched, consolidation measures in 2010 targeted the public sector wage bill, current spending and increased excise duties. Despite these consolidation measures of 0.6% of GDP the headline deficit increased to 7.9% of GDP in 2010, driven by a sizeable increase in public investment (0.4% of GDP) and intermediate consumption (0.5% of GDP). Since 2011, the headline deficits have been influenced by continued consolidation effort, including cuts in social contributions transferred to open pension funds, increases in VAT rates and revenue-increasing changes in other taxes, the introduction of a temporary expenditure rule and cuts in spending on active labour market policies. Thus, the headline deficit decreased to 5% of GDP in 2011.

The general government deficit, as validated by Eurostat, reached 3.9% of GDP in 2012. The 2012 deficit outturn is higher than the 3.5% of GDP publicly announced by the Polish authorities in September 2012. In particular, interest expenditure and social transfers were higher than projected. On the revenue side, indirect taxes, VAT in particular, were substantially lower than forecast. An even worse outcome was prevented by lower execution of public investments, partly counterbalanced by lower capital transfers received.

The Commission services' 2013 spring forecast projects the general government deficit at 3.9% of GDP in 2013 (against Poland's deficit target for 2013 of 3.5% of GDP) and, under a no-policy-change assumption, at 4.1% of GDP in 2014. Taking into account additional measures contained in the 2013 update of the Polish Convergence Programme (CP), which was published after the cut-off date of the Commission services' 2013 spring forecast hardly change the assessment. For 2013 the CP does not incorporate new discretionary measures for 2013. Although the CP update envisages keeping VAT rates at their current level instead of lowering them, the inclusion of this measure would according to Commission estimates reduce the 2014 deficit to 3.7% of GDP. The baseline scenario (see Table 4) used in this staff working document takes this measure into account when discussing the new adjustment path.

The main downside risk to budgetary targets in 2013 and beyond is – based on past evidence – strong procyclicality of indirect and direct tax revenues, below standard revenue elasticities used in the forecast. In particular, it was experienced in 2012 when, despite an increase in the tax base, indirect tax revenues fell driven by an increase in VAT refunds and VAT arrears.

Public debt declined to 55.6% of GDP in 2012 from 56.2% of GDP in 2011. The Commission services' 2013 spring forecast projects its increase to 57½% of GDP in 2013 and, based on a no-policy-change assumption, to almost 59% of GDP in 2014. Stock-flow adjustments contributed to the debt decrease in 2012.

3. EFFECTIVE ACTION

3.1. Background information

The current assessment of the effective action is based on the Commission services' 2013 spring forecast. It takes into account the economic and budgetary developments since the last Council recommendation under Article 104(7) TEC was issued in July 2009. The assessment starts by comparing the recommended fiscal effort in the Council recommendation, the apparent fiscal effort, measured by the change in structural budget balance, and the adjusted structural effort. The adjustment of the structural balance takes into account (i) the impact of revisions in potential output growth compared to that underlying the growth scenario in the Council recommendation, and (ii) the impact on revenue of revisions of the tax content of economic activity (composition of economic growth or of other windfalls/shortfalls) relative to what is implied by long-term standard elasticities. This top-down approach in the assessment is complemented by a careful analysis, including a bottom-up assessment of consolidation measures undertaken by the Polish government.

3.2. Assessment of effective action 2010-2012 - overview

The structural deficit decreased from 8.3% of GDP in 2010 to 5.4% of GDP in 2011 and 3.8% of GDP in 2012. The Commission services' 2013 spring forecast projects its decline to 3.3%

of GDP in 2013. The average annual apparent fiscal effort over the period 2010-2012 is estimated at 1.5% of GDP. When adjusted for the significant upward revision in potential output growth since the time when the recommendation was issued (-0.3 pp.) and for unexpectedly low (compared to that implied by the standard elasticities) growth rate of revenues (+0.4 pp.), the average annual adjusted structural effort (1.6% of GDP) exceeds the recommended average annual fiscal effort (1¼% of GDP) over 2010-2012 (see Table 2).

Table 2: Change in the structural balance corrected for revisions in potential output gap and revenue windfalls/shortfalls

Un-corrected average effort up (dS)			Corrected average effort			Required fiscal effort in the latest 2009 Council recomendation	Deadline for correction
2010	up until 2011	up until 2012	2010	up until 2011	up until 2012	2010 - 2012	
-0.1	1.4	1.5	-0.3	1.3	1.6	1 1/4	2012
Source: Commission services' 2013 spring forecast and Commission services' calculations							

Table 3: Composition of the budgetary adjustment

	2009	2010		2011		2012		2013			2014		
	outturn	COM SF 2009	outturn	COM SF 2009	outturn	COM SF 2009	outturn	COM SF 2009	COM SF 2013	CP 2013	COM SF 2009	COM SF 2013	CP 2013
	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
Revenue	37.2	39.7	37.5	n.a.	38.4	n.a.	38.4	n.a.	37.6	37.8	n.a.	36.9	37.2
of which:													
- Taxes on production and imports	12.8	14.5	13.6	n.a.	13.8	n.a.	12.9	n.a.	12.7	12.8	n.a.	12.2	12.8
- Current taxes on imcome, wealth, etc.	7.4	8.2	6.9	n.a.	7.0	n.a.	7.2	n.a.	6.9	6.9	n.a.	7.1	6.9
- Social contributions	11.3	11.4	11.1	n.a.	11.4	n.a.	12.3	n.a.	12.2	12.2	n.a.	12.1	12.0
- Other (residual)	5.6	5.5	5.9	n.a.	6.2	n.a.	6.0	n.a.	5.8	5.9	n.a.	5.5	5.5
Expenditure	44.5	46.3	45.4	n.a.	43.4	n.a.	42.3	n.a.	41.6	41.3	n.a.	41.0	40.5
of which:													
- Primary expenditure	41.9	43.4	42.7	n.a.	40.7	n.a.	39.5	n.a.	38.9	38.6	n.a.	38.4	38.1
of which:													
- Compensation of employees	10.3	10.4	10.2	n.a.	9.7	n.a.	9.7	n.a.	9.6	9.7	n.a.	9.5	9.5
- Intermediate consumption	5.7	6.1	6.2	n.a.	0.6	n.a.	5.6	n.a.	5.5	5.5	n.a.	5.5	5.3
- Social payments	16.9	17.5	17.0	n.a.	16.2	n.a.	16.4	n.a.	16.7	16.4	n.a.	16.7	16.2
- Subsidies	0.5	0.8	0.5	n.a.	0.5	n.a.	0.4	n.a.	0.4	0.3	n.a.	0.4	0.4
- Gross fixed capital formation	5.2	5.5	5.6	n.a.	5.7	n.a.	4.6	n.a.	3.8	3.8	n.a.	3.6	3.5
- Other (residual)	3.3	3.1	3.2	n.a.	8.0	n.a.	2.9	n.a.	2.9	2.9	n.a.	2.8	3.2
- Interest expenditure	2.6	2.9	2.7	n.a.	2.7	n.a.	2.8	n.a.	2.7	2.7	n.a.	2.5	2.4
General government balance (GGB)	-7.4	-7.3	-7.9	n.a.	-5.0	n.a.	-3.9	n.a.	-3.9	-3.5	n.a.	-4.1	-3.3
Primary balance	-4.7	-4.4	-5.2	n.a.	-2.3	n.a.	-1.1	n.a.	-1.3	-0.8	n.a.	-1.5	-0.9
One-off and other temporary measures	0.3	-0.2	0.0	n.a.	0.0	n.a.	0.1	n.a.	0.2	0.1	n.a.	0.0	0.0
(Recalculated) structural balance	-8.2	-5.6	-8.3	n.a.	-5.4	n.a.	-3.8	n.a.	-3.3	-2.7	n.a.	-2.9	-2.2
Change in structural balance		0.4	-0.1	n.a.	3.0	n.a.	1.6	n.a.	0.5	1.0	n.a.	0.4	0.5
Real GDP growth	1.6	0.8	3.9	n.a.	4.5	n.a.	1.9	n.a.	1.1	1.5	n.a.	2.2	2.5
GDP deflator	3.7	1.6	1.4	n.a.	3.2	n.a.	2.5	n.a.	1.4	1.5	n.a.	1.7	2.2
Nominal GDP	5.4	2.4	5.4	n.a.	7.9	n.a.	4.4	n.a.	2..5	3.0	n.a.	3.9	4.8
Source: COM SF 2009 - Commission services' 2009 spring forecast; COM SF 2013 - Commission services' 2013 spring forecast; CP2013 - Convergence Programme 2013													

The cumulative size of discretionary consolidation measures over 2010-2012 is estimated at some 4.3% of GDP using the bottom-up approach (see Box 1 for the list of the main measures). These measures have targeted in particular indirect taxes, disability contributions, contributions to open pension funds, public sector (excluding local government) wage bill and intermediate consumption (see Table 4).

3.3. Budgetary implementation in 2010

Despite the launch of the excessive deficit procedure, the general government deficit continued to increase in 2010, which was due to a sizeable stimulus package conducted within the European Economic Recovery Plan (EERP) to counteract the financial and economic crisis consequences. As a result, the general government deficit deteriorated from 7.4% of GDP in 2009 to 7.9% of GDP in 2010, which was also reinforced by the fact that the authorities planned to back-load the consolidation to the following years. Overall, the structural consolidation measures applied were rather limited and amounted to roughly 0.6% of GDP in 2010. At the same time, the structural deficit increased by 0.1% of GDP. Accounting for the upward revision of potential output growth since the time of the Council recommendation would decrease the annual apparent fiscal effort in 2010 by around 0.3 pp. On the other hand, the revenue grew at a lower rate than what would have been implied by the GDP increase based on standard elasticity for Poland (in particular due to lower than expected corporate income tax revenues) which increased the annual apparent fiscal effort in 2010 by around 0.1 pp. Accordingly, the annual adjusted structural effort amounted to -0.3% of GDP in 2010.

3.4. Budgetary implementation in 2011

In 2011 the general government deficit fell sharply to 5.0% of GDP as a result of continued economic growth and ambitious consolidation efforts by the government. On the revenue side a number of measures were introduced that led to a noticeable increase in revenues expressed as a share of GDP (from 37.5% to 38.4%). These included: a change to the pension system consisting of the retention of part of the pension contribution previously earmarked to the private schemes in the first public pillar, a temporary (for three years) increase in the VAT rate (of 1 pp.) and in excise duty on tobacco, the abolition of some VAT and excise duty exemptions and a freeze in Personal Income Tax (PIT) thresholds. On the expenditure side the structural measures included: introducing a temporary expenditure rule limiting growth in all newly enacted and existing discretionary expenditure items to 1 pp. over the inflation rate, a further freeze in the wage fund of public sector employees, introducing the rule obliging the local governments to balance the current spending and some minor cuts in social spending. These measures have been complemented by a decrease in complementary direct payments to farmers in the framework of the Common Agricultural Policy. Overall, the total discretionary measures introduced in 2011 amounted to 2.1% of GDP.

At the same time, the structural deficit decreased by 2.9% of GDP in 2011. Accounting for the upward revision of potential output growth since the time of the Council recommendation would decrease the annual apparent fiscal effort in 2011 by around 0.3 pp. On the other hand, the revenue grew at a lower rate than what would have been implied by the GDP increase based on standard elasticity for Poland which increased the annual apparent fiscal effort in 2011 by around 0.3 pp. The effect of these two corrections cancelled out, and thus the annual adjusted structural effort amounted to 2.9% of GDP in 2011.

Box 1. Main budgetary measures	
Revenue	**Expenditure**
2010	
Changes in excise duties (+0.18%)	Freeze of public wages (-0.4%)
2011	
Amendment of the pension reform (+0.6%) Increase in VAT rates by 1 pp (+0.4%) Nominal freeze of PIT thresholds (+0.1%) Abolition of VAT reimbursement for company cars and fuel (+0.1%) Changes in excise duty regulations (+0.1%)	Expenditure rule (including nominal freeze in wage fund, except for teachers) (-0.5%) Cuts in spending on active labour market policies (-0.3%)
2012	
Amendment of the pension reform (+0.5%) Changes in excise duty regulations (+0.15%) Increase in disability contribution rate (+0.5%) Tax on copper and silver extraction (+0.13%) Increase in dividends from state-owned companies due to exceptionally high profits (+0.1%) (one-off)	Expenditure rule (including nominal freeze in wage fund) (-0.1%) Decrease in complementary payments to farmers (-0.1%)
Note: A positive sign implies that revenue / expenditure increases as a consequence of this measure. Annual budgetary impacts are estimated by the Commission services and expressed as a % of GDP. Measures with a budget impact of at least 0.1% of GDP are listed.	

3.5. Budgetary implementation in 2012

According to the actual data reported in the EDP notification of April 2013, the general government deficit for 2012 amounted to 3.9% of GDP in nominal terms.

On the revenue side, the main consolidation measures enacted in 2011 continued to remain in force in 2012, i.e. retention of additional part of the pension contribution previously earmarked to the private schemes in the first public pillar, a further raise in excise duty on tobacco, the full year effect of the abolition of some VAT and excise duty exemptions in the course of 2011 and a further freeze in PIT thresholds. In addition, the 2012 budget included new measures, namely a 2 pp. increase in the disability contribution rate, an introduction of a tax on copper and silver extraction and further changes in excise duty regulations. Moreover, the government received one-off revenues from dividends of state-owned companies. On the expenditure side, structural measures which have remained in force from 2011 included: an expenditure rule limiting growth in all newly enacted and existing discretionary expenditure items to 1 pp. over the inflation rate, a further freeze in the wage fund of public sector employees and some minor cuts in social spending. These measures were complemented by a decrease in complementary direct payments to farmers in the framework of the Common Agricultural Policy. Moreover, after the peak in first quarter of 2012, the government sharply cut public investment expenditure. Overall, total discretionary measures of some 1.6% of GDP were taken, most of them (almost 1.4% of GDP) on the revenue side.

The structural balance also improved by 1.6% of GDP in 2012. Accounting for the upward revision of potential output growth since the time of the Council recommendation would decrease the annual apparent fiscal effort in 2012 by almost 0.3 pp.. On the other hand, the revenue grew at a lower rate than what would have been implied by the GDP increase based on standard elasticity for Poland. This was largely due to indirect taxes. This revenue shortfall increased the annual apparent fiscal effort in 2012 by almost 0.7 pp.. Accordingly, the annual adjusted structural effort amounted to 2% of GDP in 2012.

4. PROPOSED NEW ADJUSTMENT PATH

Based on the final 2012 data confirmed by Eurostat, Poland did not correct its excessive deficit by the 2012 deadline established in the Council Recommendation of 7 July 2009. However, the average annual adjusted structural effort (1.6% of GDP) taking account of the impact of revisions in potential output growth and of revisions of the revenue content of economic activity relative to what is implied by the standard long-term elasticities was above the level recommended by the Council (1¼ % of GDP). It therefore appears justified to issue a revised EDP recommendation and to extend the deadline for correction of the excessive deficit.

In order to reduce the deficit below the 3% of GDP threshold by 2013, thus extending the deadline by one year, the required structural effort would amount to at least 1.4% of GDP. Such a yearly effort would be higher than requested in the Council Recommendation of 7 July 2009 (1¼ % of GDP), despite the fact that fiscal risk has fallen since 2009 as the headline deficit is at a much lower level and debt remains below the 60% threshold. As a consequence, a more gradual pace of consolidation is affordable as it would also reduce output costs, which would be sizeable if a correction had to be done in 2013. Finally, the introduction of additional measurers of about 1% of GDP in the second half of 2013 would practically not be feasible due to the required legislative process. In view of the above and in line with the flexibility foreseen in the Stability and Growth Pact, an extension of the deadline to correct the excessive deficit by two years is warranted.

Correcting the excessive deficit by 2014 would be commensurate with intermediate headline deficit targets of 3.6% of GDP for 2013 and 3% of GDP for 2014 (see Table 4 and Table 5).

Improvements in the structural budget balance implied by these targets are at 0.8% of GDP in 2013 and 1.3% of GDP in 2014, resulting in 1.1% of GDP on average. Although the required average annual fiscal effort is slightly lower than the one specified for the period 2010-2012 in the last Council recommendation, it takes into account that Poland has only limited time left in 2013 to adopt and implement required measures.

The baseline scenario (see Table 4) is an updated version of the Commission services' 2013 spring forecast taking into account measures publically announced in the Polish convergence programme after its cut-off date, in particular keeping the VAT rate at its current level in 2014 instead of lowering it. A strict implementation of adopted savings measures (including the nominal freeze in the wage fund), adoption and implementation of announced and budgeted savings measures, as well as additional measures of about 0.4% of GDP in 2013 and 0.4% of GDP in 2014 are needed to cut the excessive deficit by 2014.

At the current juncture of the economic cycle with growth significantly decreasing, it is important to minimise negative impact of consolidation measures on growth. Moreover, uncertainty surrounding the impact of the measures taken requires close monitoring and further corrective action. Furthermore, (i) improving the quality of public finances, in particular through minimising cuts in growth-enhancing investments, a careful review of expenditures and their efficiency; (ii) better tax compliance and an increase in the efficiency of tax administration and (iii) making the framework of public finances more binding and transparent, including through a permanent expenditure rule (consistent with ESA) on the general government budget could underpin the consolidation efforts further.

Table 4 – Forecast of key macroeconomic and budgetary variables under the baseline scenario

% of GDP	2012	2013	2014
Revenues	38.4	37.6	37.3
Current revenues	37.0	36.3	36.2
Discretionary measures with impact on current revenue*	1.4	0.2	-0.2
Expenditure	42.3	41.6	41.0
Real GDP growth (%)	1.9	1.1	1.8
Nominal GDP growth (%)	4.4	2.5	3.8
Potential GDP growth (%)	3.6	2.8	2.8
Structural balance	-3.8	-3.3	-2.4
General government balance	-3.9	-3.9	-3.7
General government debt	55.6	57.5	58.5
p.m CAB methodology revenue elasticity	0.8	0.8	0.8
p.m Apparent revenue elasticity	1.2	0.3	0.5
p.m Output gap (% of potential output)	-0.7	-2.3	-3.2

*Measures clearly specified and committed to by governments ahead of the recommendation

Table 5 - Forecast of key macroeconomic and budgetary variables under the EDP scenario

% of GDP	2012	2013	2014
Real GDP growth (%)	1.9	0.8	1.6
Potential GDP growth (%)	3.6	2.7	2.6
Structural balance	-3.8	-3.0	-1.7
General government balance	-3.9	-3.6	-3.0
General government debt	55.6	57.2	57.5
p.m Output gap (% of pot. output)	-0.7	-2.3	-3.3

5. CONCLUSIONS

Poland did not manage to sustainably correct her excessive deficit by 2012 as recommended by the Council. In 2012 the deficit was, at 3.9% of GDP, well above the 3% benchmark of the Treaty. For 2013, the Polish authorities have adopted the 2013 budget which contains additional measures, but these are – according to the Commission services' 2013 spring forecast – only sufficient to keep the general government deficit constant at 3.9% of GDP. Absent a budget for 2014, the 2013 spring forecast projects, under a no-policy-change assumption, a slight increase in the nominal deficit to 4.1% of GDP in 2014. Taking into account of the measures contained in the CP would lower the deficit to 3.7% of GDP in 2014.

However, during the period 2010-2012, the average annual fiscal effort after correction for the effects of revised potential output growth and revenue developments amounted to 1.6% of GDP, above the annual average fiscal effort of 1¼% of GDP, recommended by the Council. The bottom-up approach estimates the cumulative size of consolidation measures at some 4.3% of GDP over 2010-2012 compared to 4.5% improvement in structural balance (uncorrected for the effects of revised potential output growth and revenue developments). It therefore appears justified to issue a revised EDP recommendation and to extend the deadline for correction of the excessive deficit.

Granting two more years for the correction of the excessive deficit implies the headline deficit targets of 3.6% of GDP for 2013 and 3% of GDP for 2014. The underlying improvements in the structural budget balance implied by these targets are 0.8% of GDP in 2013 and 1.3% of GDP in 2014. This implies a need of additional measures of 0.4% of GDP in 2013 and 0.4% of GDP in 2014, on top of those already included in the spring forecast and in the update of the Convergence Programme.

Table 6: Comparison of key macroeconomic and budgetary projections

		2009	2010	2011	2012	2013	2014
Real GDP (% change)	COM SF 13	1.6	3.9	4.5	1.9	1.1	2.2
	COM SF 09	-1.4	0.8				
	CP 13					1.5	2.5
Output gap[1] (% of potential GDP)	COM SF 13	-1.1	-1.1	-1.1	-0.7	-3.1	-3.7
	COM SF 09	-1.5	-3.8				
	CP 13					-2.2	-2.7
General government balance (% of GDP)	COM SF 13	-7.4	-7.9	-5.0	-3.9	-3.9	-4.1
	COM SF 09	-6.6	-7.4				
	CP 13					-3.5	-3.3
Primary balance (% of GDP)	COM SF 13	-4.8	-5.2	-2.3	-1.1	-1.3	-1.5
	COM SF 09	-3.7	-4.4				
	CP 13	-4.8	-5.2	-2.3	-1.1	-0.8	-0.9
Cyclically-adjusted balance[1] (% of GDP)	COM SF 13	-7.9	-8.3	-5.4	-3.7	-3.0	-2.9
	COM SF 09	-6.0	-5.8				
	CP 13					-2.6	-2.2
Structural balance[2] (% of GDP)	COM SF 13	-8.2	-8.3	-5.4	-3.8	-3.3	-2.9
	COM SF 09	-6.0	-5.6				
	CP 13					-2.7	-2.2
Government gross debt (% of GDP)	COM SF 13	50.9	54.8	56.2	55.6	57.5	58.9
	COM SF 09	53.9	60.0				
	CP 13					55.8	55.7

Note:

[1] Output gaps and cyclically-adjusted balances according to the programmes as recalculated by Commission services on the bass of the information in the programmes.

[2] Cyclically-adjusted balance excluding one-off and other temporary meaures

Source: *Commission services' 2013 spring forecast, Commission services' 2009 spring forecast, 2013 update of the Convergence Programme*

Annex

Table A1: Adjustment of apparent structural effort for the revision in potential growth – details of calculation

Average potential growth assumptions underlying July 2009 Council recommendation (%)	Average potential growth (COM 2013 SF) (%)	Forecast error (%)	Structural expenditure (% of potential GDP) (COM 2013 SF)	Correction coefficient α (% of nominal potential GDP)
(1)	(2)	(3) = (1) - (2)	(4)	(5) = (3) * (4) / 100
2.7	3.3	-0.6	45.8	-0.3

Table A2: Adjustment of apparent structural effort for the revenue shortfalls/windfalls as compared to standard elasticities – details of calculation

CAB methodology revenue elasticity (ε* = 0.78)	Change in current revenues (yoy) (PLN mln)	Discretionary current revenue measures (PLN mln)	Nominal growth assumptions (%)	Current revenues in t-1 (PLN mln)	Revenues gap (PLN bn)	Correction coefficient β
2013 SF	(1)	(2)	(3)	(4)	(5) = (1) - (2)- ε*x(3)x(4)	(5) in % of nominal potential GDP
2010	21 333	2 500	5.4	492 357	-1.7	-0.1
2011	46 285	20 100	7.9	513 690	-5.2	-0.3
2012	34 581	22 000	4.4	559 975	-10.6	-0.7
Average						-0.4