20. POLAND

Flying on one engine

Economic activity hampered by weak domestic demand

After some deceleration of economic activity in the first half of 2012 (2.9%), real GDP growth continued sliding down in the second half of 2012, reaching 2% over the whole year. External trade was a strong support for economic activity as exports were relatively robust while import growth was limited due to sluggish domestic demand. Private consumption growth (0.5%) disappointed strongly as labour market prospects worsened, real wages declined and consumer sentiment deteriorated. Against this backdrop, investment growth was limited (0.6%) and also hampered by worsening financing conditions and a slowdown in public investments triggered by EU-funds cycle and fiscal consolidation.

Difficult 2013 and moderate recovery in 2014

Weak economic outlook of the main trading partners is expected to hamper domestic confidence and worsen the situation of exporters, resulting in constrained domestic demand growth in 2013. Some rebound in domestic demand is projected only towards the end of the year. Real GDP is forecast to increase by 1.2% in 2013 and 2.2% in 2014.

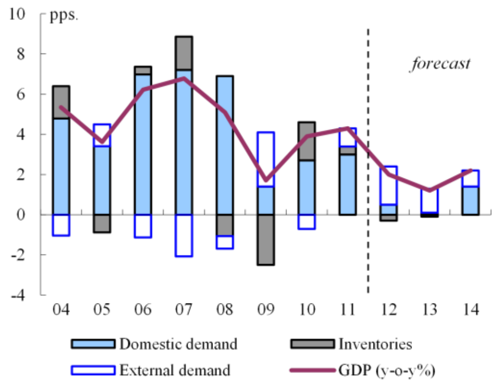
Public investment growth is projected to be strongly negative, as public spending is expected to be curbed further due to fiscal consolidation needs and lower EU-funds inflow. Private investment is forecast to moderate in 2013 as a result of uncertain demand prospects and weak global sentiment. However, the expected improvement in external demand at the end of 2013 is likely to revive confidence and improve prospects for exporters. This in turn is set to fuel private investment as companies have sufficient cash at their disposal and credit supply is set to accelerate.

The unemployment rate is forecast to increase from 10.2% in 2012 to 10.9% in 2014 due to the sluggish economic activity. It is likely to weaken disposable income, but rising real wages thanks to contained inflationary pressures are projected to offset somewhat this effect. Moreover, household savings are set to increase on the back of waning consumer confidence, constraining domestic demand as well. Only towards the end of the forecast horizon the improving labour market conditions, recovering confidence and cuts in VAT rates are likely to accelerate private consumption.

The contribution of external trade to growth is forecast to be positive, though declining, over the forecast horizon. Weak external outlook is set to hamper exports, yet limited domestic demand will result in an even stronger import compression in 2013. In 2014 rebounding external demand and improving cost competitiveness are likely to fuel exports. Since in parallel imports are expected to grow as well due to the accelerating domestic demand, the overall effect on real GDP growth is projected to moderate. Against this backdrop, the current-account deficit is set to continue improving from 3.6% of GDP in 2012 to 2.4% of GDP in 2014.

This forecast is subject to broadly balanced risks. On the upside, a stronger-than-expected depreciation would further boost exports and enhance import substitution. On the downside, more profound deterioration in confidence could hamper private investment and consumption.

Graph II.20.1: **Poland - GDP growth and contributions**



Inflation decelerates amid weak domestic demand

The zloty depreciation, high commodity prices and an increase in administered prices drove up HICP inflation to 3.7% in 2012. It is set to reverse to 1.8% in 2013, mainly on account of moderating commodity prices, weak domestic demand and declining gas prices. A moderate pick-up to 2.3%

is expected in 2014, reflecting base effects and some improvement in domestic demand.

Fiscal consolidation slows down

The general government deficit is projected to continue falling, albeit at a slow pace due to the deteriorating macroeconomic outlook. In 2012 the deficit is expected to decrease to slightly below 3.5% of GDP thanks to the previously enacted consolidation measures.

In 2013, the deficit is projected to fall slightly to 3.4% as further consolidation measures are set to be offset by slow economic growth. On the revenue side, the main deficit-reducing measures include CO2 emission rights auctions, a continued freeze in PIT thresholds and fines from the new speed-camera system. On the other hand, the share of pension contributions retained in the public pillar will start to fall (i.e. the share of the contributions transferred to the private pension funds will start increasing as their previous reduction will be partially reversed). The main structural measures decreasing expenditure are the freeze of wages of central government employees and the start of a gradual increase in retirement age. Moreover, the government is set to further lower public investment.

In 2014, the deficit is expected to further fall to 3.3%, thanks to a rebound in economic activity, which is projected to offset the developments on the revenue side. The revenue-to-GDP ratio is set to fall due to the combined effect of the end of the temporary increase in VAT rates, a reinstatement of VAT reimbursement for company cars and fuel and a further decrease in pension contributions retained in the public pillar. On the other hand, the gradual raise in the retirement age will have a consolidating effect on expenditure.

The structural deficit is set to fall from 5.2% in 2011 to 1.7% in 2014. General government debt-to-GDP ratio is forecast to increase from 56.4% in 2011 to 57.5% in 2014. The projected debt figures are, however, subject to considerable uncertainty due to high exchange-rate volatility affecting the debt valuation.

Table II.20.1:

Main features of country forecast - POLAND

	2011		Annual percentage change						
	bn PLN Curr. prices	% GDP	92-08	2009	2010	2011	2012	2013	2014
GDP	1523.2	100.0	4.6	1.6	3.9	4.3	**2.0**	**1.2**	**2.2**
Private consumption	932.8	61.2	4.4	2.0	3.1	2.5	**0.5**	**0.7**	**1.5**
Public consumption	274.8	18.0	3.5	2.1	4.1	-1.7	**0.1**	**1.6**	**2.2**
Gross fixed capital formation	309.7	20.3	7.6	-1.2	-0.4	9.0	**0.6**	**-2.8**	**0.6**
of which : equipment	106.5	7.0	-	-10.8	-3.3	9.7	**3.8**	**1.7**	**7.0**
Exports (goods and services)	688.7	45.2	10.6	-6.8	12.1	7.7	**3.2**	**3.8**	**6.4**
Imports (goods and services)	706.3	46.4	11.5	-12.4	13.9	5.5	**-0.9**	**1.2**	**4.8**
GNI (GDP deflator)	1453.9	95.4	4.7	0.1	3.5	4.0	**2.1**	**1.1**	**2.1**
Contribution to GDP growth : Domestic demand			4.9	1.4	2.6	3.0	**0.5**	**0.1**	**1.4**
Inventories			0.1	-2.5	2.0	0.4	**-0.3**	**-0.1**	**0.0**
Net exports			-0.4	2.7	-0.7	0.9	**1.9**	**1.2**	**0.8**
Employment			-	0.4	0.5	1.0	**0.1**	**-0.1**	**0.2**
Unemployment rate (a)			14.3	8.1	9.6	9.6	**10.2**	**10.8**	**10.9**
Compensation of employees/head			15.7	3.5	4.7	4.0	**3.5**	**2.5**	**3.1**
Unit labour costs whole economy			-	2.2	1.3	0.7	**1.6**	**1.2**	**1.0**
Real unit labour costs			-	-1.4	-0.1	-2.3	**-0.7**	**-0.3**	**-0.8**
Saving rate of households (b)			-	9.0	8.2	2.1	**1.9**	**3.5**	**3.8**
GDP deflator			11.8	3.7	1.4	3.1	**2.3**	**1.5**	**1.9**
Harmonised index of consumer prices			-	4.0	2.7	3.9	**3.7**	**1.8**	**2.3**
Terms of trade of goods			0.2	4.4	-1.4	-1.9	**-2.1**	**-0.6**	**-0.6**
Merchandise trade balance (c)			-3.1	-1.0	-1.8	-2.1	**-1.5**	**-0.7**	**-0.3**
Current-account balance (c)			-2.4	-3.1	-4.3	-4.5	**-3.6**	**-2.7**	**-2.4**
Net lending(+) or borrowing(-) vis-à-vis ROW (c)			-1.6	-1.9	-2.7	-2.7	**-1.2**	**-0.9**	**-0.9**
General government balance (c)			-	-7.4	-7.9	-5.0	**-3.5**	**-3.4**	**-3.3**
Cyclically-adjusted budget balance (c)			-	-7.9	-8.3	-5.2	**-2.9**	**-2.1**	**-1.7**
Structural budget balance (c)			-	-8.2	-8.3	-5.2	**-3.0**	**-2.2**	**-1.7**
General government gross debt (c)			-	50.9	54.8	56.4	**55.8**	**57.0**	**57.5**

(a) Eurostat definition. (b) gross saving divided by gross disposable income. (c) as a percentage of GDP.