25. POLAND

Poland's economy has begun to bounce back from the recession triggered by the COVID-19 pandemic, but the recent rise in infections could temporarily stall the recovery. Real GDP is forecast to decline by 3½% in 2020 and to remain below 2019 levels until the end of 2021. The general government deficit is set to deteriorate strongly in 2020 due to the economic downturn and the support measures adopted to mitigate the economic fallout of the pandemic.

After signs of strong growth in the third quarter, the recovery could stall in the fourth…

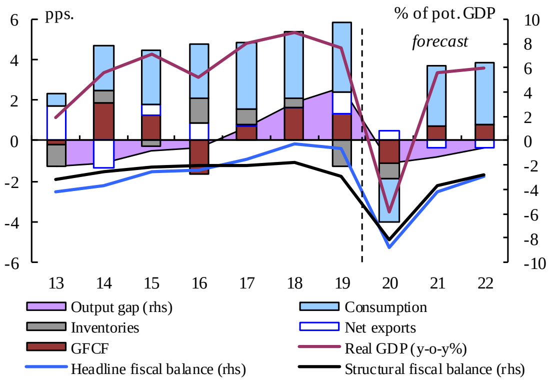
The first wave of the pandemic and the restrictions imposed to combat the virus resulted in a marked fall in economic activity in the first half of the year. Real GDP contracted by 8.9% quarter-on-quarter in the second quarter of 2020, with all components except government consumption significantly affected. Private consumption, the backbone of Poland's growth in recent years, posted a double-digit drop, as social distancing measures and low confidence took their toll.

The drop in economic activity is expected to be followed by a sharp rebound in the third quarter as the stringency of containment measures eased and supply chains were restored. The build-up of savings during the lockdown period and strong fiscal support led to a marked increase in retail sales, particularly in durable goods, while high-frequency indicators suggested a return to pre-crisis levels in recreational and hospitality activities already in July. Industrial production and exports also recovered swiftly with output and new orders recording positive year-on-year growth at the beginning of the third quarter. As a result, the third quarter of 2020 is expected to show a strong expansion in GDP of around 6¼% in quarter-on-quarter terms. Yet, a surge in new infections and decreased confidence is set to bring this recovery to a temporary halt in the last quarter of 2020, taking the annual rate of GDP growth to -3½%.

…before gradually recovering over 2021-2022

Economic growth is expected to resume in 2021 and 2022 in line with the assumed easing of containment measures and increased foreign demand, although the fading away of policy support could weigh on growth in early 2021. An expected deterioration in the labour market and a resulting sluggish confidence may lead consumers to withhold spending in the first half of 2021, leaving private consumption below pre-crisis levels until 2022. Foreign trade is expected to recover strongly in 2021 and 2022, but the higher technical rebound for imports should negatively impact the trade balance. Investment is also projected to recover in tandem with reduced uncertainty and increased domestic and foreign demand. However, this recovery is set to be partly constrained by the construction sector, which may continue suffering from a decrease in orders, particularly in the first half of 2021. All in all, GDP growth is projected to rebound by 3¼% in 2021 and strengthen slightly in 2022 to 3½% as economic activity slowly returns to potential.

Graph II.25.1: **Poland - Real GDP growth and contributions, output gap, fiscal balances**



Inflation is expected to decelerate amid worsening labour market conditions

Increased operational costs due to COVID-19 containment measures led to a hike in service price inflation in the second and third quarters of 2020, reaching 8.8% in September. Coupled with a sustained increase in food price inflation due to poor harvests, HICP inflation is thus set to reach 3.6% in 2020, despite a fall in energy prices. However, as government measures fade away, contributing to a deterioration in the labour market, service price inflation is expected to decelerate significantly in 2021. Food prices are also expected to moderate, bringing HICP inflation down to 2.0% in 2021. In 2022 inflation is forecast to rise as a result of a further increase in domestic and external demand and economic activity returning to potential.

The risks to this forecast mainly relate to how the labour market and firms will be affected by the gradual phasing out of policy support measures. Permanent changes to consumer behaviour and an increase in structural unemployment for certain population groups represent a downside risk.

2020 fiscal deficit to be close to 9% of GDP

The COVID-19 pandemic, together with measures to contain its effects, is set to have a big impact on public finances in 2020. The general government headline deficit is expected to reach some 8¾% of GDP. While tax revenues are forecast to decrease as compared to 2019, expenditures are expected to increase strongly. The evolution of the tax revenue will be driven by the economic slowdown, worsening labour market conditions and cyclical factors. On top of this, revenue from direct taxes will be negatively affected by the incremental effect of changes to the personal income tax implemented in 2019. The cost of measures to cushion the impact of the crisis is expected to amount to around 5¼% of GDP. The biggest expenditure in this area is likely to come from loans granted to firms by the Polish Development Fund. According to the authorities' estimates, around two thirds of these loans will eventually be converted into grants, with an estimated deficit-increasing impact of some 2 pps. of GDP in 2020. At the same time, several spending policies implemented in recent years remain in force.

In 2021, the headline deficit is forecast to diminish to some 4¼% of GDP, mainly on the back of the recovering economy and the phasing out of anti-crisis measures. While the authorities plan to collect additional revenues from new taxes, this will be counterbalanced by increased social spending, including a one-off additional pension bonus (so called 14th pension benefit). In 2022, under a no-policy-change assumption, the deficit is set to improve to around 3% of GDP, driven mostly by the macroeconomic developments. This forecast does not include any measures funded by the Recovery and Resilience Facility grants.

The general government debt-to-GDP ratio is expected to surge to around 56½% in 2020 from 45¾% in 2019, and to remain at the level of some 56½% - 57¼% over 2021-2022.

Table II.25.1:

Main features of country forecast - POLAND

	2019			Annual percentage change						
	bn PLN Curr. prices	**% GDP**	**01-16**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**
GDP	2287.7	100.0	3.6	4.8	5.4	4.5	**-3.6**	**3.3**	**3.5**
Private Consumption	1316.4	57.5	3.1	4.7	4.5	3.9	**-5.5**	**4.3**	**4.0**
Public Consumption	411.8	18.0	2.8	2.7	3.5	6.2	**5.7**	**2.7**	**3.9**
Gross fixed capital formation	423.6	18.5	3.1	4.0	9.4	7.2	**-6.2**	**4.2**	**4.7**
of which: equipment	176.6	7.7	3.5	8.3	1.6	9.1	**-9.8**	**8.4**	**5.6**
Exports (goods and services)	1270.5	55.5	7.2	9.6	6.9	5.1	**-9.0**	**5.3**	**4.8**
Imports (goods and services)	1162.8	50.8	5.9	10.2	7.4	3.3	**-10.8**	**6.7**	**6.0**
GNI (GDP deflator)	2196.9	96.0	3.3	4.6	5.3	4.8	**-3.5**	**3.4**	**3.5**
Contribution to GDP growth: Domestic demand			3.1	4.0	4.9	4.7	**-3.3**	**3.7**	**3.9**
Inventories			0.1	0.8	0.4	-1.3	**-0.7**	**0.0**	**0.0**
Net exports			0.4	0.1	0.0	1.1	**0.5**	**-0.3**	**-0.3**
Employment			0.6	1.3	0.5	-0.2	**-1.7**	**-2.0**	**1.3**
Unemployment rate (a)			12.3	4.9	3.9	3.3	**4.0**	**5.3**	**4.1**
Compensation of employees / head			4.1	5.8	8.1	8.5	**3.4**	**4.3**	**4.7**
Unit labour costs whole economy			1.2	2.3	3.2	3.5	**5.3**	**-1.1**	**2.5**
Real unit labour cost			-1.0	0.4	1.9	0.4	**1.7**	**-2.8**	**-0.5**
Saving rate of households (b)			5.3	2.8	1.5	2.4	**9.4**	**6.5**	**4.1**
GDP deflator			2.2	1.9	1.2	3.1	**3.5**	**1.7**	**2.9**
Harmonised index of consumer prices			2.2	1.6	1.2	2.1	**3.6**	**2.0**	**3.1**
Terms of trade goods			0.6	0.2	-1.2	1.7	**0.9**	**0.2**	**0.4**
Trade balance (goods) (c)			-2.9	-0.1	-1.2	0.2	**1.6**	**1.1**	**0.8**
Current-account balance (c)			-3.2	0.1	-0.7	1.4	**1.8**	**1.5**	**1.1**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)			-2.1	1.0	0.8	3.0	**3.6**	**3.7**	**4.0**
General government balance (c)			-4.4	-1.5	-0.2	-0.7	**-8.8**	**-4.2**	**-3.0**
Cyclically-adjusted budget balance (d)			-4.0	-2.0	-1.8	-2.9	**-7.9**	**-3.5**	**-2.7**
Structural budget balance (d)			-	-2.0	-1.8	-2.9	**-8.2**	**-3.7**	**-2.8**
General government gross debt (c)			48.8	50.6	48.8	45.7	**56.6**	**57.3**	**56.4**

(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.