21. POLAND

Domestic demand to support growth

Private consumption is set to remain the key growth driver in 2019 and 2020 supported by a robust increase in wages. An increase in social transfers will act as additional stimulus until around mid-2020. Investment growth is projected to gradually moderate, due to slowing expansion of EU-funded projects, only partially offset by the strengthening in private investment. After hitting a multiannual low in 2018, the headline fiscal deficit is forecast to increase sharply in 2019 and to slightly decrease thereafter.

Fast GDP expansion in 2018

Buoyant domestic demand drove economic growth to 5.1% in 2018, the fastest pace in more than a decade. Favourable labour market developments and strong consumer confidence were key factors supporting private consumption. The fast increase in utilisation of the EU funds translated into a rapid expansion of public investment, while private investment also increased.

Fiscal stimulus set to support consumption in 2019 and early 2020

GDP growth is forecast to remain solid in 2019, at 4.2% to then slow to 3.6% in 2020. Private consumption growth will remain strong in the forecast horizon, on the back of further small employment gains and strongly increasing wages. In addition, the new fiscal package will support income of households in 2019 and 2020.

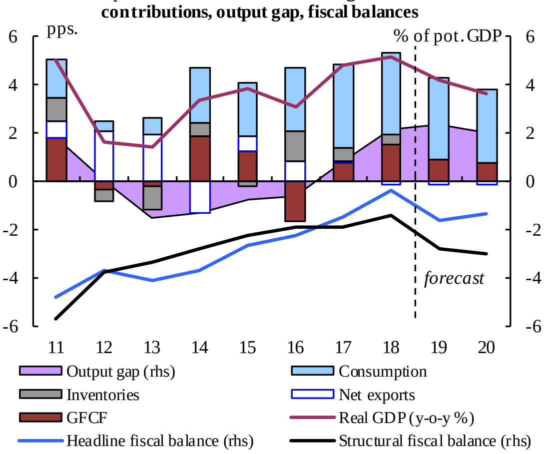
High capacity utilisation levels, low interest rates and a favourable demand outlook are projected to act as incentives for rising private investment, especially given a prolonged period of weak activity in the past. This is set to partly compensate the slowing, though still positive dynamics of public investment being supported by EU funding.

Given its strong international competitiveness, Poland is expected to continue gaining export shares in its key markets. Exports are projected to continue rising, although at a slower pace than in 2017 and 2018 given slower world trade dynamics. Robust domestic demand is projected to keep import growth strong. As a result, the contribution of net exports to GDP growth is set to remain slightly negative in 2019 and 2020.

Rising wages and record low unemployment

The demand for labour is projected to remain solid, resulting in wage growth remaining at around 8% in both 2019 and 2020. Employment gains are set to slow visibly reflecting very low unemployment and existing barriers to a faster increase in labour force participation. Following several years of rapid reduction, the unemployment rate is set to decrease only marginally during 2019 and 2020, reaching a new record-low of 3.5%.

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



Inflation to gradually increase

Oil prices staying close to 2018 levels, a cut in taxes rendering electricity prices and falling unprocessed food prices have limited inflation in the first quarter of 2019. Inflation is forecast to gradually increase in 2019 and in early 2020 and then remain broadly stable until the end of 2020. Faster wage growth is expected to be the main factor behind rising prices, especially in service sectors. The annual administrative control on electricity prices is assumed to expire in January 2020. Thus, rising electricity prices are also expected to add to inflation, both directly through electricity bills paid by households and indirectly through the prices of energy-intensive consumer goods. In turn, strong competition in the markets for consumer goods and services, the rising importance of e-commerce, and the assumed path of global oil prices, are forecast to constrain inflation growth.

Balanced risks

The uncertainty surrounding the economic outlook relates primarily to the external environment and the extent to which possible disruptions in international production chains will affect Polish producers. On the domestic demand side, there is a chance that investment could rise more than expected, if projects co-financed by the EU are rolled out more quickly or if business sentiment improves. However, there is also a risk that concerns about the institutional quality of Poland's justice system could negatively affect investment decisions sooner or more severely than assumed.

Fiscal deficit to rise in 2019

After reaching a multiannual low of 0.4% of GDP in 2018, the headline fiscal deficit is set to increase to 1.6% of GDP in 2019. The key drivers are lower dynamics of indirect taxes following measures aimed at administratively controlling electricity prices from the beginning of 2019 and a significant increase of social transfers to pensioners and middle and upper income households with children. Simultaneously, the dynamics of revenue from direct taxes and social contributions is set to remain strong, driven by economic growth and a buoyant labour market. This forecast includes the 13th pension benefit to be paid in 2019 and the extension of the universal child benefit scheme as of mid-2019. In 2020, under a no-policy-change scenario, the headline deficit is projected to fall to 1.4% of GDP. It is set to be driven by still strong macroeconomic environment, the labour market situation and a full year impact of newly legislated social transfers. The forecast for 2020 includes also announced changes to the personal income tax, and revenue from conversion of the second pension pillar assets, under a technical assumption that 50% of these assets would be transferred to the general pension system. It does not include other measures to finance the new fiscal and social package as they were not legislated or sufficiently detailed at the forecast cut-off date. This represents an upside risk for the 2020 fiscal forecast.

The structural deficit is set to have reached some 1½% of potential GDP in 2018, before increasing to 2¾% - 3% of potential GDP in 2019 and 2020.

General government debt is set to continue falling from over 50% of GDP in 2017 to around 47% of GDP in 2020, supported by relatively low nominal fiscal deficits and strong nominal GDP growth.

Table II.21.1:

Main features of country forecast - POLAND

	2017			Annual percentage change						
	bn PLN Curr. prices	% GDP	99-14	2015	2016	2017	2018	2019	2020
GDP	1989.3	100.0	3.7	3.8	3.1	4.8	**5.1**	**4.2**	**3.6**
Private Consumption	1160.2	58.3	3.2	3.0	3.9	4.9	**4.4**	**4.5**	**4.2**
Public Consumption	351.7	17.7	3.2	2.3	1.9	3.5	**4.7**	**4.3**	**3.3**
Gross fixed capital formation	348.7	17.5	3.8	6.1	-8.2	4.0	**8.7**	**4.9**	**4.1**
of which: equipment	148.9	7.5	3.8	12.1	-7.6	8.3	**9.0**	**6.8**	**5.8**
Exports (goods and services)	1081.0	54.3	7.5	7.7	8.8	9.5	**6.3**	**5.2**	**4.7**
Imports (goods and services)	997.8	50.2	6.0	6.6	7.6	10.0	**7.1**	**5.7**	**5.3**
GNI (GDP deflator)	1907.1	95.9	3.5	3.9	2.7	4.6	**5.2**	**4.3**	**3.7**
Contribution to GDP growth: Domestic demand			3.4	3.4	1.0	4.2	**4.9**	**4.3**	**3.8**
Inventories			0.0	-0.2	1.2	0.5	**0.4**	**0.0**	**0.0**
Net exports			0.3	0.6	0.8	0.1	**-0.2**	**-0.1**	**-0.1**
Employment			0.2	1.5	0.8	1.3	**0.3**	**0.2**	**0.1**
Unemployment rate (a)			13.3	7.5	6.2	4.9	**3.9**	**3.8**	**3.5**
Compensation of employees / head			5.2	1.7	4.8	5.8	**7.5**	**8.0**	**7.9**
Unit labour costs whole economy			1.6	-0.6	2.5	2.3	**2.6**	**3.9**	**4.2**
Real unit labour cost			-1.2	-1.3	2.2	0.3	**1.5**	**2.1**	**1.8**
Saving rate of households (b)			6.6	2.3	4.2	1.9	**0.7**	**1.7**	**2.0**
GDP deflator			2.9	0.8	0.3	2.0	**1.1**	**1.8**	**2.4**
Harmonised index of consumer prices			3.4	-0.7	-0.2	1.6	**1.2**	**1.8**	**2.5**
Terms of trade goods			0.1	2.9	0.6	0.3	**-1.0**	**-0.7**	**-0.5**
Trade balance (goods) (c)			-3.5	0.5	0.7	0.3	**-1.1**	**-2.0**	**-2.8**
Current-account balance (c)			-3.9	0.2	0.0	0.1	**-0.5**	**-1.0**	**-1.4**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)			-3.0	2.6	1.2	1.1	**0.5**	**0.2**	**-0.1**
General government balance (c)			-4.4	-2.7	-2.2	-1.5	**-0.4**	**-1.6**	**-1.4**
Cyclically-adjusted budget balance (d)			-3.9	-2.3	-1.9	-1.9	**-1.4**	**-2.8**	**-2.4**
Structural budget balance (d)			-	-2.3	-1.9	-1.9	**-1.4**	**-2.8**	**-3.0**
General government gross debt (c)			46.7	51.3	54.2	50.6	**48.9**	**48.2**	**47.4**

(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.