POLAND

Highlights

- **There has been a steady increase in economic activity in the first half of 2021.** The 2.5 per cent drop in gross domestic product (GDP) in 2020 was significantly lower than the European Union (EU) average and, since the beginning of 2021, investment growth and rising consumption have been driving a robust recovery.
- **Potentially one of the EU's largest Recovery and Resilience Facility (RRF) packages envisages major investment in energy transition and broad-based digitalisation.** The national plan is based on €23.9 billion in grants and €12.1 billion in loans and, in addition to the green and digital transition, it foresees strengthening health sector capacity and supporting businesses in their post-Covid-19 pandemic recovery. A legal dispute on rule-of-law reforms could postpone the roll-out of the RRF, however.
- **The energy policy strategy up to 2040 has been approved.** With an emphasis on renewable energy, it is projected that by 2040, coal's share of energy generation will be between 11 and 28 per cent, while larger cities should introduce zero-emission public transport by 2030.

Key priorities for 2022

- **High energy prices should be addressed in a market-friendly way.** While rising energy prices could provide greater incentives for energy efficiency investments, they directly affect households, especially those at risk of energy poverty. Instead of subsidising energy prices, cash transfers should be provided to the most vulnerable households.
- **The transparency of public finances needs to be improved.** While the Covid-19 pandemic triggered higher and more targeted government expenditure, including through off-balance-sheet special-purpose funds, such as those of Polish development bank BGK, budgetary transparency deteriorated sharply. Greater harmonisation of definitions with Eurostat, the EU's statistical office, would be a step forward.
- **Policies that address skills shortages and improve inclusivity would strengthen and make better use of the labour supply.** In regions dependent on the coal industry, increasing skills and targeted training would enable job transitions to the renewable energy projects announced in the national RRF plan. Policies that embrace diversity and inclusion practices, including for the LGBT+ community, and better migrant job matching could attract and retain talent, such as in the tech and creative industries.

Main macroeconomic indicators %

	2017	2018	2019	2020	2021 proj.
GDP growth	4.8	5.4	4.7	-2.5	4.9
Inflation (average)	1.6	1.2	2.1	3.7	4.7
Government balance/GDP	-1.5	-0.2	-0.7	-7.1	-4.2
Current account balance/GDP	-0.4	-1.3	0.5	2.9	2.3
Net FDI/GDP [neg. sign = inflows]	-1.4	-2.6	-2.0	-2.2	-1.1
External debt/GDP	67.0	64.2	58.8	60.6	n.a.
Gross reserves/GDP	21.4	19.9	21.5	25.8	n.a.
Credit to private sector/GDP	52.0	50.9	50.2	48.0	n.a.

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Covid-19: macroeconomic implications

The economy is growing robustly after the downturn in 2020. The Covid-19 pandemic had a relatively mild impact on the Polish economy, causing GDP to decline 2.5 per cent in 2020. Some recovery had already begun in the third quarter of 2020, but a moderate tightening of restrictive measures at the end of the year constrained GDP growth in the first quarter of 2021. After a pick-up in the second quarter, economic output increased by 4.6 per cent year-on-year in the first half of 2021, largely due to greater activity in the manufacturing sector. Restrictive measures did not significantly affect household consumption, which, along with imports of goods and services, registered a positive trend in the first half of 2021. Economic sentiment started to recover from February 2021. Industrial production so far in 2021 has exceeded pre-pandemic levels, with particularly strong activity in the automotive industry.

The labour market fallout from the pandemic was limited and wage pressures persist. The unemployment rate increased only slightly, to just 3.7 per cent, in the second quarter of 2021, with job losses limited by anti-pandemic measures. Wages are growing at a brisker clip once again, with nominal wage growth of 9.6 per cent year-on-year in the second quarter of 2021. The rise of economic activity and substantially higher energy and other utility prices has resulted in a rise in HICP inflation, to 5.6 per cent year-on-year in September 2021. In October 2021, to limit the risk of inflation staying above the central bank's target of 2.5 per cent (plus/minus 1 percentage point band) in the medium term, the Narodowy Bank Polski (NBP), the Polish central bank, increased interest rates and withdrew the bill discount credit.

Fiscal expenditure is increasing to support the economy. As a consequence of the government's comprehensive stimulus package, the general government deficit in 2020 reached 7.1 per cent of GDP, slightly above the EU average. Public debt increased to 57.4 per cent of GDP as of the end of 2020. A gradual decline in these numbers is projected in the coming years, supported by high nominal GDP growth.

Real interest rates remain negative amid persistently low financing costs and improving business sentiment, which should lead to further investment and GDP growth. Overall, GDP growth is forecast at 4.9 per cent and 4.8 per cent in 2021 and 2022, respectively. However, the delayed disbursement of the EU's RRF funds constitutes a negative risk to that scenario, especially for public-sector investment. According to the Finance Ministry, the RRF funds could add 0.4 percentage point to annual GDP growth. Another downside risk to the generally positive outlook is the population's relative reluctance to vaccinate against Covid-19, with only 53 per cent of people vaccinated as of mid-October 2021. This could lead to sporadic lockdowns this winter, aggravated by potential new variants of the virus.

Policy response to Covid-19

Crisis-response measures in 2020 alleviated the effects of the Covid-19 pandemic. The government responded to Covid-19 with fiscal measures to support the economy through the BGK and with discretionary measures. These included a job protection scheme, with co-financing of wages in the affected sectors and compensation to entrepreneurs, moratoria on loans and solidarity allowances. Total government support through various programmes is estimated at 15 per cent of GDP. Monetary policy followed economic developments, with the NBP reducing the policy interest rate three times in 2020, from 1.5 per cent to 0.1 per cent in May 2021. Some of the Polish central bank's other supportive measures have included purchasing government and government-guaranteed securities on the secondary market and offering bill discount credits with a view to refinancing bank loans to companies.

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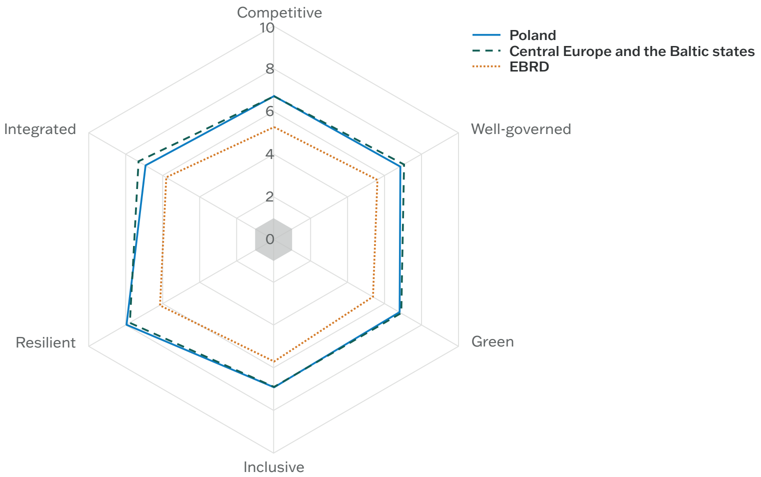
The 2021 budget envisages selective but continuous support to the economy. As the impact of the crisis is still visible in some sectors in 2021, most of the job support measures have been extended. Small and medium-sized enterprises (SMEs) in sectors heavily affected by the restrictions, such as the services sector, can receive financial support of up to 70 per cent of fixed costs. Liquidity guarantees for large companies and exemptions from social security contributions for specific industries are in place. Within the increase in expenditure, the 2021 budget envisages an increase in healthcare spending, bringing it to 5.3 per cent of GDP.

Assessment of transition qualities (1-10)



Structural reform developments

Large RRF funds, if cleared by the European Commission and Council, could further target key sectors, including the green and digital transitions. The Polish national plan is based on €23.9 billion in grants and €12.1 billion in loans. It consists of five pillars: economic resilience, green energy, digital transformation, sustainable transport and the health system. Investment in renewable energy sources such as wind farms, however, has received little emphasis to date and it remains to be seen how hydrogen and natural gas will be used in line with the EU's energy strategy. With the European Commission not having endorsed the plan as of late October 2021, Poland has expressed concerns about the timeliness of its response. The European Commission, meanwhile, has requested that the European Court of Justice (ECJ) impose financial penalties on Poland to ensure its compliance with the Court's interim measures order on the functioning of the Disciplinary Chamber of the Polish Supreme Court.

Disagreements between Poland and the EU institutions over judicial reform have escalated to new levels. In October 2021, the Polish Constitutional Tribunal ruled that some articles of the EU treaties were incompatible with the national constitution. Earlier – and further to requesting the financial penalties in relation to the functioning of the Disciplinary Chamber – the European Commission had sent a letter of formal notice to Poland for not taking the necessary measures to comply fully with the judgement of the ECJ (of 15 July 2021), which found Polish disciplinary legislation against judges incompatible with EU law.

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The government approved a new energy policy strategy to 2040. Adopted in February 2021, the strategy presents a vision for transforming the economy into a low-carbon one. Although it shows a slower energy transition plan than EU climate targets, coal's share of energy generation is projected to drop from about 70 per cent in 2020 to between 11 and 28 per cent by 2040, depending on emission prices. The strategy emphasises the need to further expand the capacity of wind farms and solar power plants. It also says that greenhouse gas emissions should fall by 30 per cent by 2030 and larger cities should introduce zero-emission public transport by 2030.

The government has presented a tax reform and economic support package. The new package, presented in May 2021, includes an increase in the tax-free income allowance and other measures leading to more progressive income tax. The health-insurance contributions of the self-employed will increase in proportion to their income, in line with the rules that apply to employees. The government also plans to introduce relief for taxpayers settling in Poland, as well as state guarantees for mortgage loans on social housing or for families with four children or more. These changes in taxation are expected to come into force from January 2022.

Uncertainty remains high with regard to the possible outcome of legal disputes over foreign-currency mortgages. In September 2021 the Supreme Court again postponed a decision on how to deal with cases involving foreign-currency loans – specifically, a large number of mortgages in Swiss francs, which may result in high costs for banks due to exchange-rate changes since the loan origination dates. The court has decided to seek the opinion of the ECJ on the composition of judicial benches. At the same time, several commercial banks have taken measures to facilitate the conclusion of voluntary settlements with their customers.

The roll-out of a high-speed internet network is focused on lower-population-density areas. Following the introduction of the National Broadband Plan to connect all households to high-speed internet by 2025, a project to develop fibre-to-the-home infrastructure in five less-populated regions was contracted in August 2021. The value of the project is approximately €227 million. It is planned that, by 2023, more than 500,000 households and 1,400 schools will get a high-speed internet connection.