Poland

Highlights

- **The post-pandemic recovery has decelerated in 2022.** The slowdown is due in part to increased commodity and energy prices and uncertainty associated with the country's proximity to the war in Ukraine, accompanied by market pressure and more difficult financing conditions.
- **Crisis support measures include loan holidays for mortgage borrowers and heating subsidies.** Between 85 per cent and 95 per cent of those eligible are expected to apply for eight months' worth of credit holidays on zloty mortgages in 2022 and 2023, while one-off heating subsidies will cover up to 40 per cent of energy price hikes between October 2022 and April 2023.
- **Consolidation of the fuel and energy sectors has gained momentum.** In July 2022 the government approved the final merger of state-controlled fuel giants PKN Orlen and Lotos, as part of the consolidation of the fuel and energy sector with state-owned gas giant Polskie Górnictwo Naftowe i Gazownictwo (PGNiG).

Key priorities for 2023

- **Unlocking Recovery and Resilience Facility (RRF) fund disbursements would speed up critical investment, while keeping fiscal stresses in check.** An added benefit would be a stronger currency, which would help to fight inflation. Efforts must, therefore, be intensified to resolve current disagreements between the government and the European Commission on judicial reform.
- **The replacement of the benchmark WIBOR rate needs to be done in a consistent and careful way and communication with market participants needs to be ensured.** A working group, consisting of key stakeholders, started to work in July 2022. According to the roadmap prepared by the working group, the plan is to replace the main benchmark WIBOR rate with a new O/N risk-free rate – WIRON from January 2025. The roadmap indicates that the market should be ready for a cessation of the WIBOR reference rates at the beginning of 2025.
- **Energy crisis-shielding measures and grid and capacity investment should be consistent not only with short-term price stability, but also with long-term energy security and climate mitigation.** Means-tested support measures for the most vulnerable groups, especially households at risk of energy poverty, will require greater administrative capacity. They could prevent excessive energy use and encourage green investments.

TABLE Main macroeconomic indicators %

	2018	2019	2020	2021	2022 proj.
GDP growth	5.4	4.7	-2.2	5.9	4.0
Inflation (average)	1.2	2.1	3.6	5.2	14.0
Government balance/GDP	-0.2	-0.7	-6.9	-1.8	-4.1
Current account balance/GDP	-1.9	-0.2	2.4	1.4	-4.0
Net FDI/GDP [neg. sign = inflows]	-2.8	-2.0	-2.4	-4.1	-4.7
External debt/GDP	64.3	58.8	60.7	56.6	n.a.
Gross reserves/GDP	19.9	21.5	25.6	24.5	n.a.
Credit to private sector/GDP	50.9	50.2	47.7	45.4	n.a.

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Macroeconomic developments and policy response

The post-pandemic recovery is decelerating in the second half of 2022. Following strong gross domestic product (GDP) growth of 6.8 per cent in 2021, the Polish economy grew 6.9 per cent year on year in the first half of 2022, mostly boosted by a large increase in inventories and still very strong household consumption. While direct exposure to trade with Russia and Ukraine is modest, the war is affecting the Polish economy, mainly through higher commodity and energy prices and by uncertainty associated with the country's proximity to the war, with the accompanying market pressure and more difficult financing conditions. The pessimistic outlook is confirmed in the central bank's corporate survey of July 2022, which points to a sharp slowdown in the next 12 months. At the same time, Ukrainian refugees are filling some of the vacancies in the labour market. As of mid-2022 about 210,000 refugees had taken up work in Poland – more than a third of all working-age (18-65) refugees who applied for Polish identity cards since 24 February 2022. Overall, there are an estimated 2.5-2.8 million Ukrainians in Poland, including those who migrated to Poland before the war, according to estimates by the central bank. Refugees find employment mostly in retail trade and home-care facilities, whereas pre-war, the immigrants were mostly men working in heavy industry or construction.

External developments and domestic factors are fuelling high inflation. In September 2022 the consumer inflation rate reached 17.2 per cent, its highest level for 25 years. Rising commodity and energy prices and disrupted supply chains were already significant drivers of inflation prior to Russia's invasion of Ukraine, but the war has magnified these effects. In response, the central bank has been gradually increasing interest rates, to 6.75 per cent as of September 2022, which, together with tighter liquidity conditions and banking sector regulatory measures, led to a drop in lending in most market segments. In parallel, the government approved two anti-inflation shield bills in November 2021 and January 2022, including indirect tax cuts on fuel, food, heating energy, gas and electricity. A further extension into 2023 is likely. As of the end of June 2022, the two shields had cost the state some PLN 30 billion (€6.4 billion).

The stabilising expenditure rule has been modified again. In June 2022 the government adopted a bill that ties the future expenditure ceiling to the substantially higher actual inflation rate, rather than to the previous benchmark tied to the central bank's target of 2.5 per cent. The bill also introduced an investment clause that allows for the special treatment of public investment in green measures, digital transformation and energy security, effectively allowing for higher investments in those areas. Poland committed to increasing its military spending to 3 per cent of GDP in 2023, above the North Atlantic Treaty Organization (NATO) requirement of 2 per cent. The general government deficit is expected to widen from 1.9 per cent of GDP in 2021 to 4.7 per cent in 2022, according to the draft 2023 budget law, driven by higher public spending related to the anti-inflation shields and the extension of Polish Deal tax cuts (see below), as well as increased defence spending and cost of hosting refugees from Ukraine, estimated to cost 0.5 per cent of GDP in 2022. So far, public debt remains moderate, at an estimated 52 per cent of GDP in 2022.

The short-term outlook is highly uncertain. Although the economy grew strongly in the first half of 2022, it has lost momentum in the second half of the year, as historically high inflation has negatively affected households' disposable income, weighing on consumption and confidence. We, therefore, forecast economic growth to reach 4.0 per cent in 2022, dropping to 1.5 per cent in 2023, on the assumption of continued war in Ukraine, further monetary tightening and a deteriorating external environment. On the positive side, the inflow of Ukrainian refugees and loose fiscal policy will continue to stimulate private consumption.

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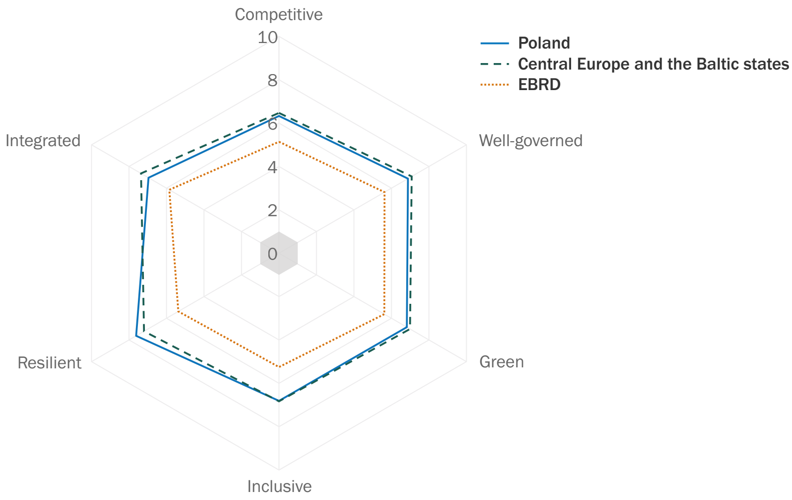
CHART Assessment of transition qualities (1-10)



Structural reform developments

Mortgage borrowers can seek loan holidays amid increased interest rates. In response to the sharp rise in inflation, in July 2022 the Polish president signed into law a borrower support package that allows for eight months' worth of credit holidays (four months in 2022 and four in 2023) for all zloty mortgage borrowers using a property for their own purposes. The Polish Bank Association (ZBP) expects between 85 and 95 per cent of those eligible, out of 2.1 million outstanding loans, to apply for the package, which is designed to have no impact on the evaluation of a borrower's creditworthiness. According to the central bank, the aggregate cost to banks will be some PLN 20 billion (€4.2 billion) in 2022-23, assuming a 100 per cent participation rate. Up to October 2022 the actual participation rate was 65 per cent.

Households can seek one-off heating subsidies, including for coal, and the tariff liberalisation of natural gas has been postponed. The president signed into law two heating subsidy bills in August 2022 amid energy price hikes. The first subsidy package is a one-off payment of PLN 3,000 (€635) for those who use coal for heating, while the other package ranges between PLN 500 (€105) and PLN 3,000 (€635) for sources of heating other than coal. It is hoped that the subsidies will cover about 40 per cent of expected energy price hikes. The PLN 11.5 billion (€2.4 billion) coal subsidy will be financed off budget from the Covid-19 countermeasure fund, which will be supplemented by some PLN 9.6 billion (€2 billion) of NBP profit in 2021. The non-coal subsidy is expected to cost PLN 9.5 billion (€2 billion) from October 2022 to April 2023. Also, the government currently envisages introducing special electricity price measures for households as well as small and medium-sized enterprises, which will freeze energy prices for a given consumption level and put a cap on them once this level is surpassed. Since Russia cut off the natural gas supply to Poland in April 2022, the country has been diversifying its energy sources. In August 2022 all gas storage facilities were filled to almost 100 per cent (about 3.2 billion cubic meter (bcm)). Poland consumes 20-21 bcm of natural gas annually, with domestic production at some 4 bcm, while 16 bcm can be imported through the newly opened Baltic Pipe (from Norway) and the liquefied natural gas (LNG) terminal in Swinoujscie. Natural gas tariff liberalisation has been postponed from 2024 to no earlier than 2027.

Consolidation of the fuel and energy sectors has gained momentum. In July 2022 the government approved the final merger of state-controlled fuel giants PKN Orlen and Lotos, as part of the consolidation of the fuel and energy sector with state-owned gas giant PGNiG. According to the government, the mergers are expected to improve energy security and improve operational efficiency in areas such as drilling and refining. Furthermore, according to the authorities, such a national champion would be in a better position to compete on the market, as the new concern would become one of the biggest integrated petrochemical producers in Europe by 2030.

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The ongoing disagreements between the government and the European Commission over judicial reform in Poland have caused the withholding of fund disbursements under the RRF. In September 2022 the government signed a financing agreement for the RRF funds with the European Commission. However, the unlocking of funds is conditional on Poland's prior and satisfactory fulfilment of the established milestones and targets, notably, those related to judicial reform. In the Commission's view, the legislative actions implementing the established milestones and targets into the Polish legal order by Poland have not gone far enough to enable the disbursement of funds. The national plan is based on €23.9 billion in grants and €11.5 billion in loans and, in addition to the green and digital transition, foresees strengthening health-sector capacity and supporting businesses in their post-Covid-19 pandemic recovery.

The Polish Deal tax reform was further revised. In June 2022 the president signed into law a modified and extended version of the Polish Deal tax bill. The altered law sees the personal income tax rate being cut from 17 per cent to 12 per cent, effective July 2022, and makes further modifications to tax thresholds, so that no group loses out (as was the case with the bill's first iteration, which entered into force in January 2022). Other solutions have also been introduced, including a division of the tax-reducing amount between up to three payers. Some 13 million taxpayers are expected to benefit from the programme, which is estimated to cost PLN 15 billion (€3.2 billion) over two years.