POLAND: Consumption-driven expansion

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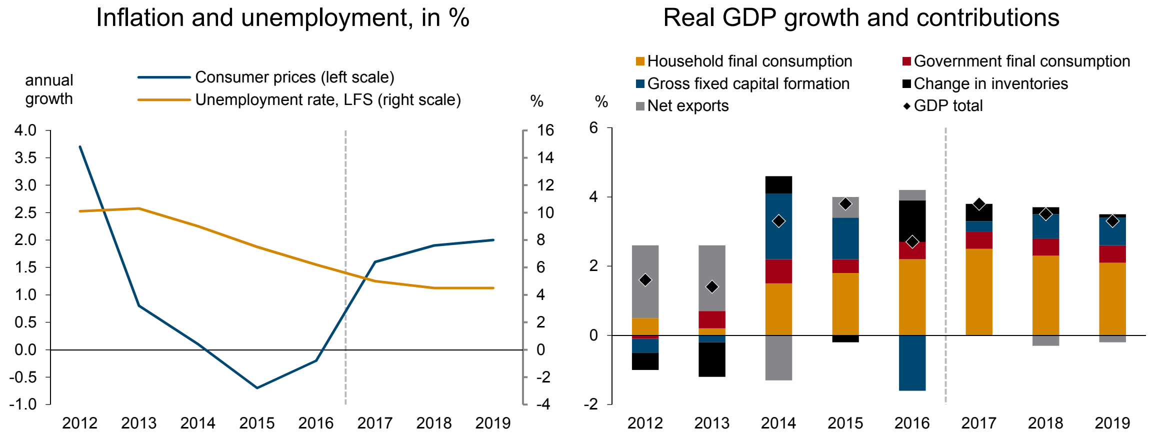
Strong consumption-driven growth has been propelled by rising wages and employment. Economic conditions are conducive to a recovery in investment activities, which has yet to materialise. The positive growth prospects may be endangered by the unwelcome effects of the ongoing evolution of the political system – including the country's progressive alienation from its EU partners.

Figure 44 / Poland: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

GDP growth in the first quarter of 2017 turned out to be stronger than generally expected: 4% year on year. At 3.9% the GDP growth was steady in the second quarter. Growth of household consumption remained strong throughout the first half of the year and growth of public consumption accelerated. Consumption has been the main factor behind GDP growth, contributing 3.3 percentage points to the 4% growth in the first half of 2017.

Gross fixed capital formation (GFCF), which virtually stagnated in the first quarter of 2017, was reported to have increased, rather symbolically, in the second quarter (by 0.8%, year on year). The contribution of GFCF to GDP growth in the first half of 2017 remains negligible. However, the contributions of changes in inventories were large and rising (0.7 percentage points in the first quarter of 2017 and 1.9 percentage points in the second). It seems rather improbable that inventories could expand strongly much longer (as they already had expanded rather strongly throughout 2016). On the other hand, the strong increase in output of the construction sector observed so far in 2017 may suggest a part of rising inventories represents construction works in progress.

The performance of foreign trade has been robust, yet weakening throughout 2017. Foreign trade developments did not affect the GDP growth rate in the first quarter of 2017 (both exports and imports of goods and non-factor services rose, by 8.3% and 8.7% respectively in real terms). But in the second quarter of the year imports rose over 6% while exports by only 2.8%. Consequently, in the second quarter foreign trade contributed negatively to the GDP growth rate (by -1.5 percentage points).

Household consumption is set to continue to grow quite strongly in the rest of 2017 (as well as in 2018-2019). Primarily this is due to a relatively strong rise in employment which has been leading to a rising wage bill. Government policy measures supporting household incomes and growing private consumption include quite generous transfers to families with children, increasing official minimum wage rates and higher tax-free personal income thresholds. On the other hand, the government tries to ‘economise’ on retirement expenditure (growth of average pensions of retirees lag behind average wages and inflation).

Rising demand for (primarily skilled) labour is one aspect of the labour market situation, which is gradually shifting in favour of the employees. Average wages are growing under the impact of tightening labour markets. The wage hikes are still quite moderate though, roughly in line with rising productivity. The presence of a large ‘shadow labour army’ consisting of potentially employable migrants (primarily from Ukraine) seems to be restricting the wage pressures. Also, the introduction of sizeable social transfers may have reduced, at least temporarily, the wage-earners income aspirations. Labour costs are not expected to activate stronger cost-push inflation anytime soon, although they may prevent further growth in the corporate sector’s profitability indicators.

Wage developments have also much to do with the demography-related weakening of the labour supply. The lowering of the retirement age (from 67 years for both sexes to 65 for men and 60 for women), effective as of October 2017, will be reducing the labour supply additionally – and as such should be conducive to further growth in wages.

The financial standing of the non-financial corporate sector has been quite strong. Net profits of the sector rose again, by 8.8% in the first half of 2017, reaching an equivalent of about EUR 15.7 billion (over 7% of the period’s GDP). Profitability of the sector is high and its financial standing very strong – though firms generally expect some deterioration of these indicators in the future (on account of possibly rising costs and more intense competition). Financial sector corporations have also been faring relatively well. Although commercial banks’ net profits declined by 17% (on account of higher personal costs, much higher obligatory contributions to the (centralised) banking system reserve fund and a higher tax burden) they reached an equivalent of over EUR 1.6 billion in the first half of 2017.

Indebtedness of the non-financial private sector remains relatively low. Borrowing by firms and households is not expensive and the interest rates on loans are quite stable. Despite this, loans to the non-financial corporate and household sectors have grown rather moderately (the stocks of such loans rose within one year by less than 6% and 3% respectively). Stronger growth in loans is observed in the segment of small and medium-sized enterprises, the larger firms ‘sit’ on cash reserves. The borrowing by households predominantly supports the satisfaction of housing needs. Overall, the levels of private sector indebtedness are comparatively low and the shares of non-performing loans are low and falling.

Purely economic factors would suggest that fixed investment by the private sector could be expanding strongly. The basic reason why corporate investment remains sluggish seems to have much to do with the political climate that set in after the electoral victory of the Law and Justice (PiS) party. The PiS government, in power since late 2015, blatantly disrespects the constitution. Actually it is now subordinating the judiciary system to its own will. That cannot but evoke anxieties among the private (domestic) businessmen who rightly fear the advent of legally unrestrained arbitrary administrative harassment and interference into their activities. These fears have been strengthened as the government has legislated draconian penalties for breaches (or apparent breaches) of tax obligations. It may be added that the prospect of such penalties (but also newly introduced administrative measures aimed at closing some VAT tax loopholes) are proving effective. The indirect tax (including VAT) revenue to be collected in 2017 will exceed all earlier expectations.

Faster growth of public investment (co-financed out of EU funds) expected in the second half of 2017 is likely to add more vigour to private sector investment. Eventually the stagnation of GFCF may be overcome in 2017 – though faster growth may only be expected in 2018-2019 when larger-scale infrastructure project are started.

The macroeconomic policies continue to be relaxed. Although the deflationary tendencies observed since 2013 are being overcome now, the National Bank of Poland (NBP) is very likely to leave its policy rates unchanged. This is not a bad position because, despite a vigorous rise in wages and consumer demand, the risk of any disquieting inflationary acceleration seems still rather remote. Nor is there any need to pre-empt a build-up of investment bubbles. But in the first place the NBP policy follows from the fact that it is now dominated by 'doves' unconditionally loyal to the ruling party. Their priority is to avoid decisions that could slow down real growth. The Finance Ministry seems to share much the same orientation. In effect, despite relatively high growth the financial deficit of the general government must be expected to exceed 3% of GDP. That is not necessarily a bad development – at least as long as the public debt is low, inflation is insignificant and the foreign trade balances remain positive.

The failure to respect the 3% budget deficit limit is still a relatively minor offence against the EU rules (especially given the fact that the authorities do not intend to access the eurozone anytime soon). Domestic political developments have been more disquieting. The ruling party, enjoying a parliamentary (though not constitutional) majority, violates the constitution. It is bent on subjugating all public institutions, including the ones in charge of controlling and balancing the powers of the government. The political system currently developing in Poland is unlikely to do any good to the country in the longer run.

The sustained assault on the basic principles and institutions of a law-abiding democratic system, conducted by the PiS authorities, constitutes a truly grave problem – both to the Polish society and the rest of the EU. For the time being it is difficult to see how that assault could be contained. On the other hand, it may be also hard to square Poland's continued EU membership with its becoming another 'sovereign democracy' of an Central European rather than Western persuasion.

Summing up, at present Poland's economy is in a good shape. Driven primarily by consumption, its GDP is likely to rise by over (or close to) 3.5% in 2017-2019. Investment is likely to add to growth also due to higher financing of infrastructure projects while trade is likely to gradually become a drag on growth. However, the positive growth prospects may be endangered by the unwelcome effects of the ongoing evolution of the political system – including the country's alienation from its major EU partners.

Table 19 / Poland: Selected economic indicators

	2013	2014	2015	2016 1)	2016 January-June	2017 January-June	2017 Forecast	2018 Forecast	2019 Forecast
Population, th pers., average	38,514	38,487	38,458	38,435	38,427	38,422	38,400	38,400	38,400
Gross domestic product, PLN bn, nom.	1,657	1,720	1,799	1,851	877	928	1,940	2,050	2,170
annual change in % (real)	1.4	3.3	3.8	2.7	2.7	4.3	3.8	3.5	3.3
GDP/capita (EUR at PPP)	17,900	18,600	19,800	20,100	.	.	.	.	.
Consumption of households, PLN bn, nom.	995	1,019	1,038	1,072	539	577	.	.	.
annual change in % (real)	0.3	2.6	3.0	3.8	3.0	4.9	4.3	4.0	3.6
Gross fixed capital form., PLN bn, nom.	312	339	361	334	128	130			
annual change in % (real)	-1.1	10.0	6.1	-7.9	-6.9	0.4	1.5	4.0	4.5
Gross industrial production (sales) 2)									
annual change in % (real)	2.3	3.4	4.8	2.8	4.0	5.7	6.0	5.5	4.5
Gross agricultural production									
annual change in % (real)	0.5	6.9	-2.6	7.2	.	.	.	.	.
Construction industry 2)									
annual change in % (real)	-10.2	4.3	0.3	-14.5	-13.2	7.2	.	.	.
Employed persons, LFS, th, average	15,568	15,862	16,084	16,197	16,097	16,388	16,360	16,440	16,440
annual change in %	-0.1	1.9	1.4	0.7	1.2	1.8	1.0	0.5	0.0
Unemployed persons, LFS, th, average	1,793	1,567	1,304	1,063	1,134	895	860	770	770
Unemployment rate, LFS, in %, average	10.3	9.0	7.5	6.2	6.6	5.2	5.0	4.5	4.5
Reg. unemployment rate, in %, eop	13.4	11.4	9.7	8.3	8.7	7.1	.	.	.
Average monthly gross wages, PLN 3)	3,659	3,777	3,908	4,047	4,224	4,434	4,240	4,440	4,680
annual change in % (real, gross)	2.8	3.2	4.5	4.2	5.1	3.0	3.2	2.7	3.3
Consumer prices (HICP), % p.a.	0.8	0.1	-0.7	-0.2	-0.4	1.6	1.6	1.9	2.0
Producer prices in industry, % p.a.	-1.3	-1.3	-2.0	-0.3	-1.3	3.4	1.0	0.8	1.3
General governm.budget, EU-def., % of GDP									
Revenues	38.5	38.8	39.0	38.8	.	.	39.0	39.0	39.5
Expenditures	42.6	42.3	41.6	41.3	.	.	42.0	42.0	42.5
Net lending (+) / net borrowing (-)	-4.1	-3.5	-2.6	-2.4	.	.	-3.0	-3.0	-3.0
Public debt, EU-def., % of GDP	55.7	50.2	51.1	54.4	.	.	55.4	55.2	55.3
Stock of loans of non-fin.private sector, % p.a	3.3	5.8	7.1	5.3	6.7	6.1	.	.	.
Non-performing loans (NPL), in %, eop	8.5	8.1	7.5	7.0	7.3	6.9	.	.	.
Central bank policy rate, % p.a., eop 4)	2.5	2.0	1.5	1.5	1.50	1.50	1.75	2.0	2.5
Current account, EUR mn 5)	-5,028	-8,529	-2,409	-1,250	1,575	712	900	-420	-1,010
Current account, % of GDP 5)	-1.3	-2.1	-0.6	-0.3	0.8	0.3	0.2	-0.1	-0.2
Exports of goods, BOP, EUR mn 5)	149,113	158,656	172,150	177,412	87,944	98,011	189,800	201,200	214,300
annual change in %	5.7	6.4	8.5	3.1	2.9	11.4	7.0	6.0	6.5
Imports of goods, BOP, EUR mn 5)	149,448	161,911	169,937	174,479	85,050	96,959	188,400	201,600	217,700
annual change in %	0.2	8.3	5.0	2.7	1.7	14.0	8.0	7.0	8.0
Exports of services, BOP, EUR mn 5)	33,592	36,743	40,663	45,018	21,147	23,605	49,100	52,000	55,100
annual change in %	5.1	9.4	10.7	10.7	9.2	11.6	9.0	6.0	6.0
Imports of services, BOP, EUR mn 5)	25,948	27,679	29,749	30,941	14,222	15,310	33,300	35,000	36,800
annual change in %	0.0	6.7	7.5	4.0	3.3	7.7	7.5	5.0	5.0
FDI liabilities, EUR mn 5)	658	14,824	13,534	15,213	8,421	-373	6000	.	.
FDI assets, EUR mn 5)	-2,524	5,096	4,385	10,233	2,636	981	4000	.	.
Gross reserves of NB excl. gold, EUR mn	74,257	79,379	83,676	104,439	95,254	94,360	.	.	.
Gross external debt, EUR mn 5)	278,948	293,510	303,120	318,956	311,437	318,891	346,900	369,000	393,200
Gross external debt, % of GDP 5)	70.7	71.4	70.5	75.2	73.4	69.9	76.0	76.5	77.0
Average exchange rate PLN/EUR	4.1975	4.1843	4.1841	4.3632	4.3686	4.2685	4.25	4.25	4.25

1) Preliminary. - 2) Enterprises with 10 and more employees. - 3) Half-year data refer to enterprises with 10 and more employees. -
4) Reference rate (7-day open market operation rate). - 5) Including SPE.

Source: wiiw Databases incorporating Eurostat and national statistics. Forecasts by wiiw.