Poland improves its public finances

In June 2015, the European Union’s Economic and Financial Affairs Council (EcoFin), which brings together finance ministers from EU member states, lifted the excessive deficit procedure imposed on Poland in 2009. The decision means improved international credibility for the country and better prospects for economic growth.

Under the EU Treaty, member states are expected to avoid excessive budget deficits. The excessive deficit procedure is designed to discipline member state governments that fail to follow sufficiently rigorous fiscal policies. The EU, at the request of the European Commission, may impose the procedure if a country’s deficit exceeds 3 percent of GDP or if its debt is higher than 60 percent of GDP. The member state must then take corrective action.

The procedure was imposed on Poland in 2009, when its general government deficit stood at 7.4 percent of GDP. A year later this rose to 7.9 percent. In recent years, however, the Polish government has gradually reduced the general government deficit. In 2013, it was brought down to 4 percent of GDP and last year it shrank further to 3.2 percent. This year’s deficit /2015/ is expected to fall below 3 percent. Public sector debt reached 50.1 percent of GDP last year, well below the reference value of 60 percent of GDP. At the same time, European Commission forecasts indicate that Poland has secured a lasting reduction in the deficit, which is expected to decrease to 2.8 percent of GDP in 2015 and 2.6 percent of GDP in 2016. Public sector debt, in turn, is expected to remain significantly below 60 percent of GDP.

The European Commission recommended that Poland make further budget savings of 0.5 percent of GDP in 2015 and 2016, in addition to establishing an “independent fiscal council” and limiting the use of reduced VAT rates. “We will continue to monitor the fiscal and budgetary situation in Poland to make sure that the necessary margins are maintained and there is a sustained reduction in the deficit,” said the European Commissioner for Economic and Financial Affairs, Pierre Moscovici. The European Commission noted that in some areas there are still structural challenges where there is room for improvement. These are public spending, uniformly applied tax rules, tax system efficiency, pension programs in some sectors of the economy, measures to promote employment, and investment in rail transportation.

Polish government officials have said that the lifting of the procedure enables Poland to shape its fiscal policy in a way more adapted to the economic situation. They have also announced measures to further reduce the public finance imbalance. The Polish government says its spending policy will be pursued within the constraints of the national and EU law, which includes a Stabilizing Expenditure Rule and the requirements of the path to the Medium-Term Budgetary Objective (MTO).

Proponents of increased spending point out that the decision to lift the excessive deficit procedure paves the way for a reduction in VAT rates and wage growth in the government sector as well as for the allocation of greater amounts of money for purposes such as research and development.

The European Commission predicts that Poland’s GDP will grow 3.3 percent this year and 3.4 percent in 2016. Others suggest that growth may be slightly faster than that, which would increase government revenue (above the forecast level) and would also mean a higher reference level for calculating the fiscal imbalance.

Economists from Narodowy Bank Polski have recently updated their assessment of macroeconomic imbalances in EU countries in line with the methodology used by the European Commission. In an Inflation Report released in September 2015, they said that their “updated scoreboard … indicates that, at present, Poland is among the most balanced European economies … There is no sign of imbalance in the real estate market, the private and public sector debts are among the lowest in Europe and the trade surplus in 2013-14 helped to reduce the current account deficit to the lowest level since 2004.”

There is no doubt that now that Poland has been freed from the excessive deficit procedure it will see an improvement in terms of its image on international financial markets and its attractiveness in the eyes of investors. But economists caution that this should not be seen as a green light for lack of responsibility in public finances.

Source: The Warsaw Voice