Poland faces tougher borrowing as 2024 deficit rises

The 2024 budget amendment increases the state budget deficit by PLN56.3bn to a record high PLN240bn. The general government deficit could exceed 6% of GDP compared to 5.7% in the mid-term fiscal plan. Higher 2024 borrowing needs will be mainly financed from the liquidity cushion, which reduces 2025 pre-financing needs and could increase credit spreads

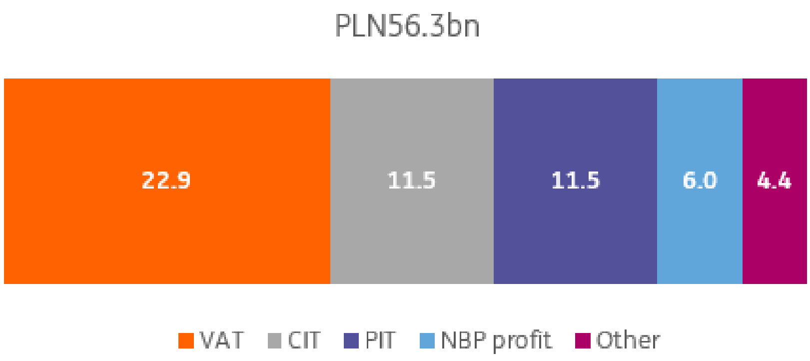
Poland's Ministry of Finance building in Warsaw

Long-awaited 2024 budget amendment amid lower revenues

Since the beginning of the year, we have been warning that the 2024 budget act was based on the overly optimistic assumptions regarding budget revenues, and the act may need to be amended before the end of the year. In particular, we saw a near- 30% year-on-year increase in VAT as unlikely. Polish authorities had been postponing the inevitable amendment, but eventually admitted that the budget is markedly short of revenues vs. plans. The biggest gaps were in VAT collections, CIT revenues and proceeds from sales of CO2 emissions allowances (see chart below). The total shortfall in budget revenues was estimated at PLN56.3bn (around 1.6% of GDP).

Shortfall in state budget revenues vs. budget act

PLN billion



Source: Ministry of Finance

Higher-than-expected increase in deficit

Surprisingly, policymakers refrained from taking any steps on the expenditure side of the budget to cushion the negative impact of lower revenues on the fiscal balance. Consequently, lower revenues increase the state budget deficit by a corresponding amount, pushing the deficit from PLN184bn to PLN240bn, up by 1.6% of GDP. However, the increase in the general government gap is expected to be smaller for two reasons. First, the 5.7% of GDP estimate for 2024 presented by the Ministry of Finance in the mid-term fiscal plan was already taking into account the need for a budget amendment, but probably on a somewhat smaller scale. Second, part of the shortfall in PIT revenues for the central budget stems from lifting the share of local governments in tax revenues. Hence, the deficit at the central government level will be offset by the improved position of the local sub-sector.

State budget borrowing needs

PLN bllion

bn PLN	**2024 budget act**	**2025 draft budget**	**2024 amendment**
Net needs	**252.3**	**215.7**	**308.6**
State budget deficit	184.0	184.0	240.3
EU funds budget	32.5	10.5	32.5
EU funds management	11.6	13.5	11.6
Loans granted	22.6	18.6	22.6
Liquidity management	0.0	-12.2	0.0
Other needs	1.6	1.2	1.6
Maturing debt	**196.8**	**209.7**	**162.8**
Gross needs	**449.0**	**425.4**	**471.4**

Source: Ministry of Finance

Liquidity cushion to cover most of the higher borrowing needs

With no action taken on the spending side of the budget, lower revenues directly increase the 2024 borrowing needs. According to the draft amendment bill, net borrowing needs will increase to PLN309bn from PLN252bn assumed in the budget act. The PLN56bn increase in borrowing needs will be mainly financed domestically (PLN55bn) with higher issuance of POLGBs (PLN11bn), but predominantly via the reduction of the liquidity cushion by PLN44bn. At the end of September it stood at PLN155bn.

Upward pressure on credit spreads

Since the majority of the current cash buffer will be utilised to finance 2024 needs, the pre-financing of record-high 2025 gross needs of PLN553bn (14% of GDP) is expected to be low. At the current stage, the pre-financing via switch auctions (buyback of T-bonds maturing in 2025) is around PLN23bn i.e. some 4% of 2025 gross borrowing needs.

The debt management team is facing a serious challenge in the coming quarters. Demand for non-FX Polish treasury debt from foreign investors remains weak, while October primary tenders showed a visible setback in demand from domestic players. A less favourable starting financing position and loose fiscal policy may put upward pressure on sovereign credit spreads in Poland in the coming months.

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