Poland: Budget on track but risks lurk beneath

VAT revenues declined by 17% year on year, but this was mostly due to statistical base effects. However, the acceleration of investments (exempt from VAT) poses some risk for budgetary revenues

Source: iStock

VAT revenues slump 17%

VAT revenues in January amounted to PLN18.2bn, which is PLN3.7bn or 17% lower than in January 2017. This figure seems alarming, but let's not jump to conclusions yet. The base of this comparison - the Jan-17 figure was significantly inflated due to an unprecedented acceleration of VAT returns in the last month of 2016. This deficit-shifting decision spared the budget PLN3.3bn in January and another PLN3.1bn in February 2017. This move was not repeated last year so it was perfectly reasonable to expect a slight (3%) decrease in VAT revenues in January 2018. We say 'slight' because economic growth and tax tightening in the past year should have added PLN2.6bn to the balance.

However, what we saw was not a 'slight' decrease of VAT revenues, but a 17% slump. How could this be explained? The lower VAT returns weren't the only reason for January 2017's high tax base. Two important tax tightening measures have been introduced at the beginning of the year as well:

- One was the inverted VAT settlement in the construction sector, which required subcontractors to pay VAT for materials first and wait for a tax return instead of clearing it with VAT paid by the investor.
- The second measure was curtailing the possibility of quarterly VAT settlement with tax authorities in favour of monthly frequency.

Both changes may have inflated the Jan-17 VAT revenues enough to explain the 17% slump in January 2018. However, we cannot be sure of that, because their exact impact is very difficult to calculate.

The risk beneath

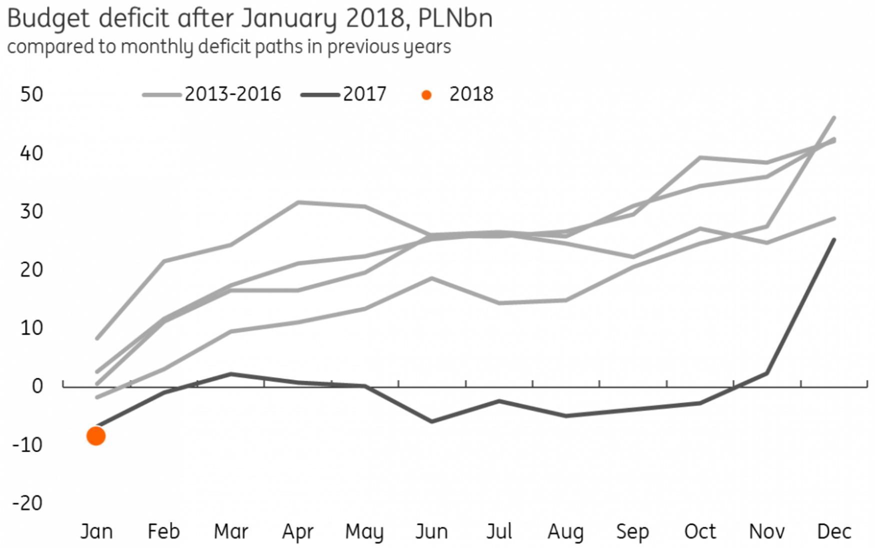
In the last quarter of 2017, we saw an acceleration of investment in Poland and we expect this to gradually become the main GDP driver (in place of consumption) in 2018 and beyond. However, this poses a risk for budget revenues. Investments are, in principle, exempt from VAT and they lower the CIT tax base (whereas consumption fuels both taxes). Therefore there is a possibility that the acceleration of investment has contributed to the 17% VAT slump in January. One-off effects from the beginning of the year will fade out from budget data but in March, we will be able to estimate the size of this effect. Until then, we expect the deficit of the general government in 2018 to reach 1.5% of GDP, which is 0.2ppt more than we expected at the beginning of 2018.

What about other taxes and budget expenditure?

Apart from VAT, tax revenues were relatively high at the beginning of the year. The proceeds from Personal Income Tax grew by 14% compared to January 2017, continuing their good performance from previous months. Corporate Income Tax and excise revenues were up by 11% each as well, which bodes well for the following months. On the other hand, budget expenditures were 11%, or PLN3,6bn, lower than in January 2017, presumably thanks to budgetary sprint at the end of last year. All in all, the budget scored a record PLN8.5bn surplus at the end of month, which fuelled a PLN57bn cash cushion. This gives the Ministry of Finance plenty of room to manage borrowing needs for this year.

Budget deficit after January, PLNbn

Negative values indicate a surplus.



Source: ING, based on Ministry of Finance data