

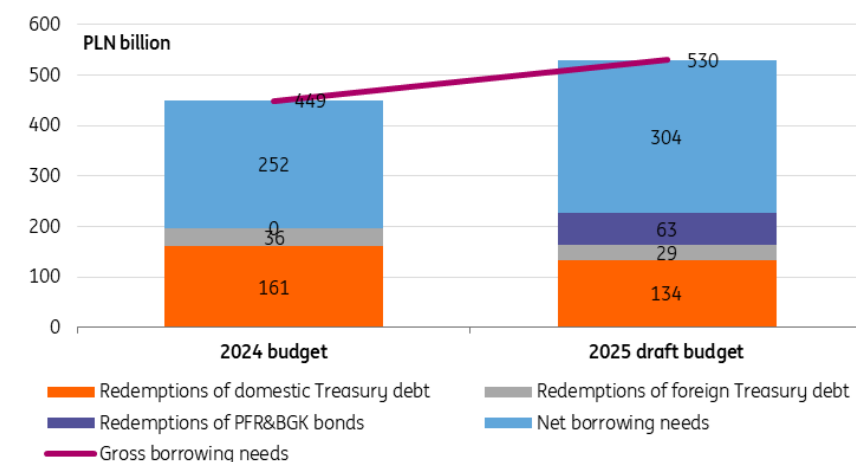
## What we learned from Poland's draft budget for 2025

Poland's draft budget 2025 is an attempt to meet defence needs and deliver (already limited) social pledges from the 2023 elections, while complying with fiscal consolidation, expected by the EC. Gross borrowing needs to hit new records, but its growth should be lower than presented by Ministry of Finance. We expect a moderate negative market reaction



Finance Minister Andrzej Domański presented the main assumptions for next year's budget at a press conference

## Significant 18% YoY increase of gross borrowing needs in draft budget 2025



Finance Minister Andrzej Domański presented the main assumptions for next year's budget at a press conference. Our main takeaways are the following:

The 2025 general government deficit (ESA2010) should reach 5.5% of GDP compared to 5.7% of GDP according to the planned implementation for 2024 (and 5.1% of GDP originally). This means probably a revision of this year's budget, but at the same time a higher deficit in the starting point for an EDP procedure.

The state budget deficit (on a cash basis) is to reach PLN289bn, but PLN63bn is spent on the rollover of maturing debt of development institutions (PFR fund and BGK bank), which was accumulated when they distributed public aid during the Covid-19 pandemic. To roll over these bonds, maturing in 2025, the Ministry of Finance will need to issue new, but cheaper Polish government bonds than bonds of the two entities. Adjusted for these items (because this is not adding to borrowing needs), the state budget deficit will amount to PLN226bn (5.7% of GDP) vs. the PLN184bn planned for 2024 – an increase of 23%, not nearly 60% as the unadjusted numbers would suggest.

In addition, PLN24.8bn should be subtracted from the state budget deficit to account for the reform of inter-governmental finances (previously, there was a larger deficit at the local government level, and now, the state budget is taking over this deficiency from local governments). Adjusted for both the PFR and BGK debt roll-over and the reform of inter-governmental relations, the state budget deficit (in comparable terms to 2024) would amount to PLN201bn (5.1% of GDP) vs. the PLN184bn planned for 2024 – an increase of just 9.2%, which is much lower the unadjusted figures presented by MinFin (60%).

The lower general government deficit, according to ESA2010 in accrual terms (5.5% of GDP) compared to the headline state budget deficit in cash terms (PLN289bn, 7.3% of GDP), is due to the fact that payments for redeeming BGK and PFR bonds is a cash expenditure of the state budget, while the ESA2010 methodology already accounted for public expenditures via PFR and BGK institutions during the pandemic. In 2025, it will be just a transfer within a broad public finance sector. The same applies for fiscal effects of inter-governmental relations. This is a transfer from

the state to the local level within a broader public sector.

Net borrowing needs are projected at PLN367bn in 2025 vs. the PLN252bn projected for 2024, but adjusted for payments for PFR and BGK bonds redemptions (which does not add new borrowing needs), the 2025 net borrowing needs should reach PLN304bn. This compares to PLN252bn budgeted in 2024, an increase of 20.5% year-on-year (and 45.5% YoY without the correction for PFR and BGK bonds). This is a significant increase, but lower than presented by the Ministry of Finance.

We assume a moderately negative market reaction to these announcements. We have known for a long time that Poland would have high borrowing needs in the coming years, and foreign investors have refrained from a large presence on the Polish market. The Ministry of Finance also has several options for financing the high borrowing needs. It still maintains a high liquidity buffer of PLN141bn in July – if it halves this buffer net needs may not change compared to 2024. In addition, the Ministry of Finance can issue foreign debt (the starting position is low, i.e. its share today is about 25% vs. over 30% a few years ago). Finally, it can still count on domestic financing due to the large inflow of savings into the banking sector.

Nonetheless, this is a budget draft of difficult policy choices, as the government has to fulfil strategic national defence needs, and meet election promises (which have been trimmed), as 2025 is a presidential election year. At the same time, it needs to comply with the European Commission recommendation, which may require some fiscal consolidation. The starting point is 5.7% of GDP fiscal gap in 2024, which offers space to deliver these fronts in a satisfactory manner.

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