

Poland announces new anti-inflation measures

Poland's government has declared VAT cuts on food and gas as part of its 'anti-inflation shield 2.0'



Poland is cutting the VAT on gas and diesel to 8%

Poland has announced new inflation-busting measures including cutting the value-added tax (VAT) on petrol and diesel to 8%, and the VAT on food, gas and fertilisers to 0%. The base VAT rate in Poland is 23%, while food is typically taxed at a lower 5% rate.

Prime Minister Mateusz Morawiecki made the announcement at a press conference on Tuesday and said the temporary rate reduction will be in force for six months starting from February. The Premier expressed hopes that the Polish zloty will continue to strengthen, curbing inflation pressure. According to Morawiecki, the annual average Consumer Price Index (CPI) in 2022 may reach 6-7% or more.

We estimate that the VAT rate cut on gas from 8% to 0% will have a moderate impact on average inflation in 2022 (0.2 percentage points). The reduction of VAT on gasoline from 23% to 8% is more potent as a way to ease inflationary pressure. It may lower 2022 inflation by some 0.3 percentage points. The biggest potential in hammering inflation is in the VAT rate reduction on food from ~5% to 0%, as it may knock off 0.4-0.8 percentage points from the average CPI. However, the final impact is highly uncertain. We are not convinced that retailers will be eager to pass lower VAT to

customers given rising costs and buoyant demand.

As a result of these measures, the CPI increase in the first half of 2022 will be lower than previously projected, but the local peak will be pushed forward to August when lower VAT rates expire. In mid-2022 annual inflation may approach double-digit levels. Will the government announce "Anti-Inflation Shield" 3.0, 5.0, 10.0 in order to push the inflation peak further ahead?

Proposed cuts in indirect taxes are like a painkiller rather than a permanent cure

Proposed cuts in indirect taxes are like a painkiller rather than a permanent cure for inflation. They temporarily ease the negative impact of high inflationary pressure, but do not reduce price growth over the long term. We expect inflation to remain higher for longer, even after supply-side shocks recede, as elevated inflation in Poland is also fueled by domestic factors. External price shock is amplified by the inflationary structure of GDP, i.e. consumption boom. The surge in consumer prices is also driven by demand pressure as well as a wage-price spiral that will become more pronounced in 2022. High inflation cannot be contained without some form of demand cooling policies.

It looks like Poland will become increasingly dependent on temporary solutions targeted at an "artificial" reduction in inflation accompanied by policies targeted at stimulating consumer demand. Such an approach is unsustainable and sooner or later some inflation curbing policies will need to be implemented, even if they lead to a temporary economic slowdown. Interest rate hikes serve such a purpose.

The disadvantage of the current anti-inflation policy is in its broad-based approach. The International Monetary Fund (IMF) recommends more focused and targeted actions, such as aid for households that are pushed into poverty, rather than to all consumers. An anti-inflation shield prolongs the surge of demand accompanying a consumption boom.

The government estimates that all planned VAT reductions will cost the budget some 15-20 billion zloty and grants households and public utilities suffering from elevated gas prices another 10 billion zloty. Proposed measures are becoming increasingly costly for public finances, but do not change the mid-term inflationary patch. It could only be justified if the surge in food and energy prices is temporary, but we do not think this will be the case.

Author

Rafal Benecki

Chief Economist, Poland

rafal.benecki@ing.pl

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information

purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.