Poland's 2022 budget brings high fiscal expansion

The government passed a 2022 budget, now to be debated in the Parliament. The moderate deficit of the central government and the entire public sector (2.8% of GDP) masks a high structural gap widening to 5.2-5.5% of GDP from around 4.5% this year

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In 2022 budget revenues are assumed at PLN481.4bn and expenditures at PLN512.4bn. This yields a central government budget deficit of PLN30.9bn, very close to the August proposal. The general government deficit is projected to fall to 2.8% from 5.3% of GDP this year. The expenditures are some PLN7bn higher than expected in August, but should be compensated by improved revenues, reflecting their outperformance this year.

Despite no tangible changes in macro assumptions and projected deficits (both the central government budget and the general government sector), the new bill assumes the general government debt at 56.6% of GDP next year, up from 55.5% expected in the August proposal. Also the public debt under the local methodology is higher, which suggests that the government plans to fund spending outside the central government. They should be covered without raising the central and sector deficit. The funding should be covered by sending Polish government bonds

(POLGBs) to public institutions outside the central government. That is presumably why government debt grew in the last version of its projections.

In order to estimate what would be total size of fiscal expansion affecting the economy, we estimate the overall structural balance. In our view it should reach 5.2-5.5% of GDP, increasing from around 4.5% this year. This consists of: (1) the general government deficit at 2.8% of GDP, (2) we add at least 0.5% correction for a cyclical improvement on the revenue side, (3) we add non-returnable Recovery Fund aid from the EU (we expect an equivalent of 1% of GDP to be spent next year) and (4) 1.1% of spending in projects outside of the central government budget.

The above suggests that the government aims to deliver another strong fiscal impulse in 2022 and it should be 0.7-1.0% of GDP higher than in 2021. The structural gap in 2022 is expected to widen to 5.2-5.5% of GDP from c.4.5% this year.

That high level of fiscal expansion comes at a time when GDP has already fully recovered from the pandemic, and the positive output gap in 2022 is already expected. Hence it should result in inflation remaining persistently high next year, though with a bit different structure compared to 2021. Core inflation should remain very high, while YoY inflation of energy, especially fuels should subside bringing headline CPI lower in 2H22, but this is only a base effect.

The budget proposal suggests that currently the government aims to rely more on government debt issuance, rather than agency debt next year. This may reflect the lacklustre demand for BGK bonds seen this quarter, especially since the National Bank of Poland may phase out its QE programme relatively soon. Some Monetary Policy Council members, including the chairman, said that QE may not continue alongside rate hikes. This supports our scenario of higher POLGBs' yields in the remainder of 2021 and in 2022.

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