

27 August 2020

# Economic Comment

## 2020 Budget: Amendment with a lot of space

Marcin Luziński, +48 22 534 18 85, [marcin.luzinski@santander.pl](mailto:marcin.luzinski@santander.pl)

Piotr Bielski, +48 22 534 18 87, [piotr.bielski@santander.pl](mailto:piotr.bielski@santander.pl)

The government delivered the draft budget amendment act 2020 to the Sejm. The budget was based on macroeconomic assumptions which seem conservative to us. The deficit was ballooned from 0 to PLN109.3bn with PLN36.7bn as a result of lower income forecast and PLN72.7bn as a result of higher spending cap. The scale of revision in incomes is not controversial, in our view, while rise in spending is excessive and we see it as a tool to lower the 2021 deficit (a lot of budget positions from 2021 were moved into 2020 in order to improve 2021 results at the cost of 2020). The rise in spending does not have much to do with the costs of fighting the effects of the epidemic or with reviving the economy: expenditure fitting this description was pushed away from the central budget right at the start of the epidemic in Poland.

We think that a final realisation below the assumed deficit limit at PLN109.3bn is probable. In our view the risk that the general government deficit will exceed 10% of GDP fell and we are now expecting a result closer to 8-9% of GDP.

The government delivered the draft budget amendment act 2020 to the Sejm after adjusting it to the new macroeconomic environment. Macroeconomic assumptions were revised with GDP growth forecast lowered to -4.6% from +3.7%. In general, these assumptions seem conservative, at least as compared to current our and market forecasts. The central budget deficit was increased from 0 to PLN109.3bn with PLN36.7 as a result of lower income forecast and PLN72.7bn as a result of higher spending cap. We think that a final realisation below the assumed deficit limit at PLN109.3bn is probable, as the assumed investment spending seems too ambitious.

The government has pushed a big chunk of costs of fighting the epidemic away from the central budget to various funds and agencies, so these are not affecting the central budget. Still, the government failed to show its forecasts of general government debt and deficit. In our view, higher-than-expected GDP in 2Q20 and positive financial results of local governments in 1H20 decrease the risk that the general government deficit will exceed 10% of GDP and we are now expecting a result closer to 8-9% of GDP.

### Main parameters of the budget

	2019 realisation (2)	2020 act (3)	2020 amendment (2)
Revenues (PLNm)	400 535	435 340	398 672
Expenditures (PLNm)	414 273	435 340	508 019
<b>Balance (PLNm)</b>	<b>- 13 738</b>	<b>0</b>	<b>- 109 348</b>
<b>GG balance (% GDP)</b>	<b>-0,3%</b>	<b>-1,2%</b>	<b>?</b>
<b>GG balance (% GDP) without one-off revenues</b>	<b>-1,3%</b>	<b>-2,2%</b>	<b>?</b>
GG debt (% GDP)	46,3%	46,5%	?

Source: Ministry of Finance, Santander

### Budget incomes: a necessary correction

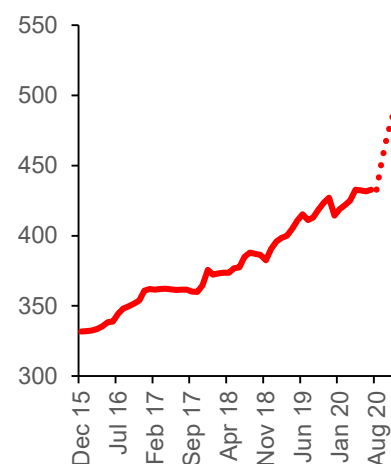
Central budget incomes were forecasted at PLN398.7bn after a downward correction by PLN36.7bn (-8.4%). All estimates of tax revenues were cut, with the most considerable being: VAT (-PLN26.5bn and -13.5%), excise duties (-PLN6.7bn, -8.9%), CIT (-PLN3.5bn, -8.3%), PIT (-PLN2.5bn, -3.7%). The government has also cancelled the planned inflows from new retail sales tax. As regards non-tax revenues: forecast of dividend incomes was cut by 2/3 to PLN0.5bn, while incomes of budget units were revised upwards by PLN4.4bn and 16.5%.

### Macroeconomic forecasts for 2020

	2020 Act	Amendment	Santander
GDP, PLNbn	2 373.3	-	2 295.0
GDP, %	3.7	-4.6	-3.0
Consumption, %	3.8	-4.2	-2.8
CPI, %	2.5	3.3	3.3
Employment, %	0.5	-2.4	-0.9
Unemployment, %	5.1	8.0	7.6
Wages, %	6.0	3.5	5.1

Source: Ministry of Finance, Santander

### Central budget spending - 12m sum



Source: Ministry of Finance, Santander

### Economic Analysis Department:

al. Jana Pawła II 17, 00-854 Warszawa  
 email: [ekonomia@santander.pl](mailto:ekonomia@santander.pl)  
 website: [santander.pl/en/economic-analysis](http://santander.pl/en/economic-analysis)  
 Piotr Bielski +48 22 534 18 87  
 Marcin Luziński +48 22 534 18 85  
 Wojciech Mazurkiewicz +48 22 534 18 86  
 Grzegorz Ogonek +48 22 534 19 23  
 Marcin Sulewski, CFA +48 22 534 18 84

Data on year-to-date realisation of tax incomes and our estimates make us believe that the government assumptions on this year's budget revenues are not controversial and the correction was necessary. Until July VAT incomes fell by about 6% y/y (amendment assumed -6% y/y for the entire year), PIT by 6.7% (-2.1% entire year in amendment), CIT rose by 2.8% y/y (-3.7% y/y), excise duties fell by 4.9% (-5.5% y/y). Thus, a major rebound in 2H20 was assumed only in case of PIT. Let us remind that it is highly probable that the Finance Ministry again did the trick of accelerating VAT returns, which could have weighed on net VAT inflows in 1H20 but benefitting the second half of the year. Moreover, deadlines for payments of other taxes were also postponed, yielding a similar effect.

### Budget revenues (PLNm)

	2019 realisation (1)	2020 act (2)	2020 amendment (3)	2020 change (3) - (2)
<b>Budget revenues</b>	<b>400 535</b>	<b>435 340</b>	<b>398 671</b>	<b>-36 669</b>
<b>1. Tax revenues</b>	<b>367 291</b>	<b>390 039</b>	<b>349 740</b>	<b>-40 299</b>
VAT	180 892	196 500	170 000	-26 500
Excise	72 396	75 083	68 400	-6 683
Gambling tax	2 337	2 660	2 300	-360
CIT	39 985	42 000	38 500	-3 500
PIT	65 445	66 555	64 100	-2 455
Mining tax	1 536	1 700	1 700	0
Bank tax	4 700	4 878	4 740	-138
Retail sales tax	0	663	0	-663
<b>2. Non-tax revenues</b>	<b>31 379</b>	<b>42 960</b>	<b>46 590</b>	<b>3 630</b>
Dividends	3 511	1 546	500	-1 046
Payment from NBP profit	0	7 163	7 437	274
Custom duties	4 409	4 680	4 680	0
Budgetary units revenues and other non-tax revenues	20 862	26 633	31 034	4 401
Payments of local governments	2 598	2 938	2 938	0
<b>3. Non-refundable funds from the EU and from other sources</b>	<b>1 866</b>	<b>2 342</b>	<b>2 342</b>	<b>0</b>

Source: Ministry of Finance, Santander

### Spending sharply up ... but why?

The spending limit has been increased to PLN508bn from PLN435.3bn initially planned (+PLN72.7bn). The whole year spending is now planned to be by PLN93.7bn higher than in 2019. It is worth to notice that until July the spending was already PLN18.6bn higher y/y. This means that in August-December period the government wants to spend PLN255.9bn vs PLN180.7bn spent in the same period in 2019. The pace of spending rise assumed for 2H20 is thus unprecedented. It is hard to justify this by the pandemic situation since it has not caused any meaningful jump of central budget spending in 1H20. Actually, it is worth to underline that little rise of spending in 1H20 was the effect of the government's decision to push pandemic-related expenses outside the central budget – spending was realized mainly by the Social Insurance Fund (FUS), Labour Fund (FP), Fund of Guaranteed Employee Benefits (FGŚP), all supplied with cash from issuance of state-owned BGK bank. Also, Polish Development Fund issued bonds to fund pandemic expenses.

The biggest item of the higher spending is a payment of PLN26.5bn to the Solidarity Fund and the budget amendment gives a dubious explanation it for "realisation of important public tasks". The second biggest item is an increase of spending of the State Insurance Institute (ZUS) by PLN12.5bn out of which PLN12bn will go to the Social Insurance Fund (FUS) to create a "cushion limiting the risk resulting from the impact of the COVID-19 pandemic and the systemic risk resulting from unfinished works on the act on the reform of open pension funds". Third, is higher spending for public investments (land transport infrastructure) by PLN12.1bn. Other more important items are, among others, increase in specific provisions by PLN6.8bn (including PLN2bn for health care), increase in

### Budget expenditures in 2020 by sections (PLNm)

	2020 act (1)	2020 amendment (2)	Change (2) - (1)
<b>Budget expenditures</b>	<b>435 340</b>	<b>508 019</b>	<b>72 679</b>
Agriculture and hunting	5 609	5 627	18
Forestry	9	12	3
Fisheries	124	124	0
Mining	695	2020	1 325
Manufacturing	818	824	6
Trade	441	442	1
Hotels/restaurants	21	21	0
Transport, Communication	13 823	25 997	12 174
Tourism	58	58	0
Housing	741	741	0
Services	499	500	1
IT	24	24	0
Higher education	24 808	25 440	632
Public administration	16 039	16 037	-2
Offices of supreme state authorities, control and protection of law and the judiciary	2 774	2 751	-23
Defence	40 957	43 957	3 000
Social security	78 486	91 922	13 436
National security and fire protection	17 038	18 674	1 636
Justice	15 088	15 088	0
Debt servicing	27 600	29 800	2 200
Various expenditures	111 847	119 157	7 310
Education	2 283	2 319	36
Health	8 496	10 499	2 003
Social aid	4 077	4 077	0
Other tasks of social policy	1 297	27 793	26 496
Educational care	141	140	-1
Family	56 803	58 557	1 754
Communal services and environment protection	1 163	1 440	277
Culture and heritage protection	3 163	3 579	416
Botanical and zoological gardens, areas and items of nature protection	114	114	0
Physical education	283	283	0

Source: Ministry of Finance, Santander

expenditure on modernisation of the Armed Forces (PLN3bn), increase in expenditure on servicing the State Treasury debt (PLN2.2bn), increase in expenditure on the Police, Border Guard, State Security Division and Firefighters (PLN1.4bn) and mining (PLN1.3bn).

In our view, the rise of spending assumed in the amendment does not have much to do with fighting the COVID-19 effects or with reviving the economy. The only bigger spending item, which seems to be directly connected to the epidemic is PLN2bn in reserve of health care, but this sum is way below PLN7.5bn announced in the first version of the so-called Anti-crisis shield. The biggest items in the amendment (payments to FS and FUS) do not generate actual spending, but only, as it seems, are 2021 expenditure booked in 2020. Payment to FS is likely to cover the 2021 payment of 13. And 14. retirement pension bonuses and payment to FUS is to cover for OFE transformation fee, which was planned initially for 2020, but is unlikely to happen. This will allow to improve the central budget balance by this sum in the incoming years. As regards road transport investment: this year end in 4 months. Big investments need a long planning period, tenders and are time-consuming. In our view it is not very probable that this sum will be actually spent in 2020.

The government's action in field of budget spending in 2020 could be summarised as pushing 2021 spending items into 2020 in order to improve fiscal metrics next year. We guess that the purpose was to take advantage of the social and market consent for much higher deficit in 2020 and reduce the burden for 2021 somehow. It does not serve well for public finance transparency, though.

The details of 2021 budget are not available yet but the most recent comment of the finance minister suggested that the deficit may reach PLN82.3bn. So, without the manoeuvre with pushing some spending to 2020 (around PLN40bn), it is possible that 2021 budget gap would be even twice as big as in 2020.

#### Budget expenditures by economic groups (PLNm)

	2019 realisation (1)	2020 act (2)	2020 amendment (3)	2020 change (3) - (2)
<b>Budget expenditures</b>	<b>414 135</b>	<b>435 340</b>	<b>508 019</b>	<b>72 679</b>
Grants and subsidies	233 329	235 894	291 348	55 454
Transfers to households	28 365	26 270	26 743	473
Current expenditure of budgetary units	78 194	87 715	88 837	1 122
Capital expenditure	18 477	24 058	33 759	9 701
Debt servicing	27 336	27 600	29 800	2 200
Contribution to the EU	21 720	23 328	25 592	2 264
Co-financing of EU funds-based projects	7 714	10 476	11 939	1 463

Source: Ministry of Finance, Santander

#### Borrowing needs practically covered

Net borrowing needs of this year's budget are to reach PLN103.3bn, almost four times more than planned in the Budget Act. Borrowing needs are planned to be financed mostly by issues of Treasury Bonds: PLN104.7bn net, including PLN176bn in gross issuance and buybacks/maturities of PLN71.2bn. Please note that this plan has been virtually accomplished already in the first year-half: after June the value of total outstanding government securities was higher by PLN112bn than in December 2019. At the same time, redemptions scheduled since end-June until end-December amounted to c.PLN10bn. As a result, any new issuances after August are likely to serve 2021 pre-financing.

We assume that new supply of government bonds in September-December (both regular and switching tenders) may amount to around PLN20bn.

At the same time, it should be remembered the Finance Ministry is still holding a large liquidity cushion (over PLN90bn after July), providing much comfort in planning bond issuances in the remaining part of the year and allowing flexibility in reacting to market conditions. Competition in form of "Covid" bonds issued by PFR and BGK is fading. Given the large excess liquidity of the commercial banking sector and the still open NBP bond-purchasing programme, this will be limiting upward potential of Polish bond yields in the months to come, in our view.

## Borrowing needs and their financing (PLNmn)

	2019 realisation (1)	2020 act (2)	2020 amendment (3)	2020 change (3) - (2)
Central budget deficit	13 738	0	109 348	109 348
EU funds deficit	-2 643	16 954	16 954	0
Loans granted	-13	1 889	1 887	-2
Pre-financing from EU	-73	-76	-75	1
Pre-financing from international institutions	196	716	769	53
Liquidity management	-15 188	4 000	-23 600	-27 600
Management of EU funds	5 183	56	-52	-108
Other	-1 379	-22	-1 889	-1 867
<b>TOTAL (net borrowing needs)</b>	<b>-180</b>	<b>23 517</b>	<b>103 340</b>	<b>79 823</b>
Of which:				
1. Domestic financing	16 381	46 386	115 022	68 636
1.1 State Treasury debt	21 648	46 210	104 718	58 508
1.2 Budget current accounts	-5 267	175	10 304	10 129
2. Foreign financing	-16 561	-22 868	-11 682	11 186
2.1 Government bonds	-16 790	-14 790	-589	14 201
2.2 Credit received	-5 057	-1 230	-2 491	-1 261
2.3 SURE credit			4 395	4 395
2.4 Cash flow linked to the fx account	5 285	-6 847	-12 997	-6 150

Source: Ministry of Finance, Santander

## POLGBs issuance in 2020 assumed in the budget amendment, PLNmn

Numbers in PLN mn	Net	Redemptions	Gross
T-bills	10 843	-	10 843
POLGBs (fixed coupon)	83 509	34 620	118 128
POLGBs (floating coupon)	-844	30 522	29 678
POLGBs (retail/savings)	11 210	6 062	17 272
<b>Total</b>	<b>104 718</b>	<b>71 203</b>	<b>175 921</b>

Source: Ministry of Finance, Santander

This publication has been prepared by Santander Bank Polska S.A. for information purposes only. It is not an offer or solicitation for the purchase or sale of any financial instrument. Information presented in the publication is not an investment advice. All reasonable care has been taken to ensure that the information contained herein is not untrue or misleading. But no representation is made as to its accuracy or completeness. No reliance should be placed on it and no liability is accepted for any loss arising from reliance on it. Forecasts or data related to the past do not guarantee future prices of financial instruments or financial results. Santander Bank Polska S.A. its affiliates and any of its or their officers may be interested in any transactions, securities or commodities referred to herein. Santander Bank Polska S.A. or its affiliates may perform services for or solicit business from any company referred to herein. This publication is not intended for the use of private investors. Clients should contact analysts at and execute transactions through a Santander Bank Polska S.A. entity in their home jurisdiction unless governing law permits otherwise. Copyright and database rights protection exists in this publication.

Additional information is available on request. Please contact Santander Bank Polska S.A. Financial Management Division, Economic Analysis Department, al. Jana Pawła II 17, 00-854 Warsaw, Poland, phone +48 22 534 18 87, email ekonomia@santander.pl, http://www.santander.pl.