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Economic Comment

“Polish Deal” focused on redistribution

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The new economic agenda of Law and Justice party (PiS) called “Polish Deal” includes proposals for the tax system, support of housing demand, increase of outlays on healthcare and an investment programme.

According to the Finance Ministry, the fiscal impact of tax changes on the public finance is about PLN5-7bn annually (negative). The expected impact of the whole agenda on general government balance is unknown. The document includes a passage declaring “a delay of more profound consolidation of public finances” which suggests that the programme will cause (ceteris paribus) a rise of the deficit. No details about other parts makes it impossible to estimate the total impact.

According to our estimates, the tax changes will add about 0.5pp to private consumption in 2022. The proposed solutions for the housing market are mostly supporting the demand side, which will result in higher demand for real estate, resulting in higher demand for mortgage loans and higher house prices. Other parts of the programme look to us like a repetition of ideas that were already presented in National Recovery Plan (investment programme), were highlighted way earlier (central communication hub, high-speed rail) or are a set of generic slogans with hard to assess probability of materialisation (healthcare).

We get the impression that “Polish Deal” will matter more politically (in terms of impact on Poles’ political preferences) and from microeconomic angle (financial situation of certain groups of taxpayers and income groups) than macroeconomically (impact on economic growth and public finances seems minor).

Changes in PIT

The plan assumes a hike of tax-free sum to PLN30k (currently it ranges from zero to PLN8k, based on wage), hike of the higher tax threshold to PLN120k from PLN85.5k and cancellation of health contribution deductibility (9% basis of assessment, rate unchanged). Changes are planned to come into force in January 2022 and will apply to incomes coming from labour contracts, civil contracts, pensions and sole proprietorships taxed with a regular tax scale.

Employees with labour contracts earning between PLN68.6k and PLN133.6k annually are to be granted an additional tax relief, offsetting the negative impact of the changes on their incomes. Eventually, tax changes for labour contracts will be favourable or neutral for earnings up to cPLN13k per month, and unfavourable for higher earnings.

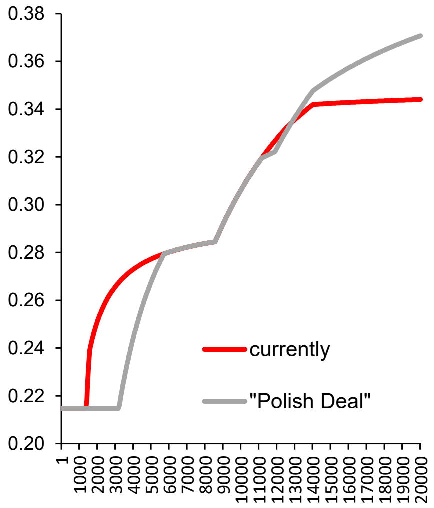
Sole proprietorships will be taxed with healthcare contribution in a similar manner as labour contracts, i.e. 9% of incomes after deducting social contributions (currently the healthcare contribution is a lump sum). Changes in sole proprietorships taxation will be favourable for earnings below cPLN6k per month, negative for higher earnings.

According to the Finance Ministry, the fiscal impact of changes described above on the public finance is about PLN5-7bn annually (negative), with PIT incomes down by PLN20-22bn and healthcare contribution (income of the National Health Fund) rising by PLN14-15bn. About half of PIT incomes is streamed to local governments, so they are likely to lose. Lower PIT revenues will be also negative for the central budget, but we think that higher incomes of the National Health Fund will lower the central budget’s subsidy. Gap in the local government’s revenues is to be offset by “investment subsidy”, but so far no details of this instrument are known.

Decreased tax burden on low-earners will be positive for consumption, as the propensity to consume is falling with rising earning. According to our estimates, the changes described above will add about 0.5pp to private consumption in 2022 and about 0.1pp to GDP growth. Effects of the fiscal stimulus will not be thus strong.

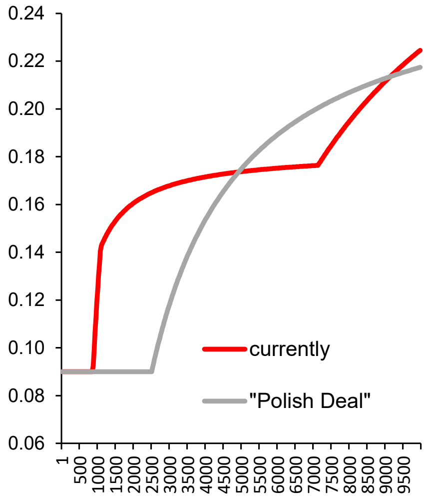
Other proposed ideas include: workers above retirement age, who are not on retirement yet, will be taxed with 0% PIT rate (in our view this could support activity in

Average tax rate and monthly earnings (labour contract)



Source: PiS, Santander

Average tax rate and monthly earnings (pension)



Source: PiS, Santander

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higher age cohorts), PIT relief for people returning from emigration: they would be eligible to deduct PLN50k from taxed incomes in 2022 and 2023, civil contracts will be taxed will all social contributions.

In our view, lower tax burden on low-earners could be positive for economic activity of the less qualified and encourage to leave the informal sector. We also think that higher taxation of civil contracts and sole proprietorships is positive in the sense that these are often used to avoid labour contract taxes. At the same time, however, this all comes at cost of higher taxation of high earners, often representing more effective workplaces and more prospective jobs. It seems that such a change in the tax system is in discord with the earlier narrative of the government and PM Morawiecki, stating that the policies should be aiming at allowing Poland to abandon the economic growth model based on low wage costs ("cheap assembly plant") and move towards higher value added and higher wages. Meanwhile, the proposed changes are positive for activation of the cheapest workforce and penalising jobs with higher potential, productivity and wages like engineers, IT specialists, lawyers, doctors.

Investment

Investment programme is also an element of the „Polish Deal". However, in our view it is based on projects already included in the KPO (National Recovery Plan) financed from the new EU framework. KPO is a direct source of ideas included in the "Polish Deal" document like digitalisation of automation relief. The plan includes a declaration that the state-owned BGK bank will finance new projects with issuance of "development bonds", but this does not encourage us to change our expectations about economic growth or investments. Higher tax rate on sole proprietorships could even discourage investment in micro companies.

Housing market

The programme includes solutions pertaining to the housing market: introduction of public guarantees of up to PLN100k for mortgage loans' own contribution for debtors aged 20-40, housing subsidy up to PLN160k (families with multiple children, families using social housing). A maximum price per square meter qualifying for the programme will be set (no details so far). There is also an announcement of deregulation in building houses up to 70 square meters (no building permit, no site manager, no construction log required).

Poland is actually struggling with low supply of housing and its low quality, but in our view the proposed solutions are mostly supporting the demand side, which will result in higher demand for loans, and further quick growth of housing and land prices. Deregulation of construction of small houses could increase demand for buying land outside of big cities in recreational purposes. We think that barriers for the housing market development stem mostly from the supply side and the programme does not propose significant changes in this respect.

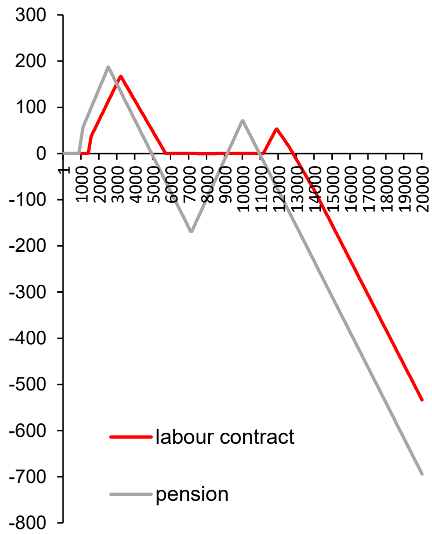
It is worth noting that the idea that the state will guarantee debtors' own contribution may have side effects for macroprudential policy. The minimal share of own contribution was increased over the last years in response to the KNF (banking sector supervising authority) recommendations and was aimed at lowering the credit market risk. From the point of view of banks' loan portfolios the proposed changes are neutral, however they limit the effectiveness of own contribution as a tool to curb potential credit and house price bubbles, if needed.

Other proposals

The document summarising the „Polish Deal" strategy covers a wide range of issues, we would only mention additional support for agriculture, for small companies, free medicines for 70+ people (currently 75+), free HPV vaccinations, payment of PLN12k for the second child aged 1-3 (we are estimating annual cost at PLN1.5bn, given that in 2019 second births made up 35% of total births) and a programme of luring foreign specialists from deficit jobs to Poland (yet at the same time higher taxes in higher earning groups could act in the opposite direction).

The plan also assumes a rise in healthcare spending to 7% of GDP in 2027, a launch of prophylactic examinations agenda, abolition of limit of visits at specialised doctors, support of doctors and nurses employment, launch of hospital modernisation fund. Over the last years the domestic healthcare spending was markedly below the EU average and in our view this sector needs more financing. So far we have no information whether these actions will increase the public deficit. We also do not know whether the healthcare quality will improve in Poland, given the lack of specialised personnel and the need to stop

Monthly change in net earnings after tax changes proposed in „Polish Deal", PLN



Source: PiS, Santander

of its outflow from Poland. Meanwhile, the proposed tax changes seem to be unfavourable for high-qualified healthcare workers.

Summary

The „Polish Deal" programme covers a change of tax system, which will decrease the tax burden on low earners and will somewhat decrease the imbalance between taxation of labour contracts and sole proprietorships. On the other hand, however, these changes will hit higher productivity workplaces and potentially more prospective jobs. In our view the plan lacks concrete ideas responding to main challenges for the Polish economy, even though general declarations point mostly in the right direction. The document covers many issues, but most are only slogans. There is not much information about issues connected to climate, environment, energy system transformation.

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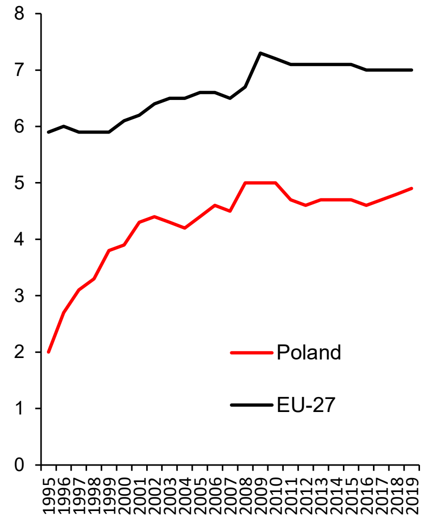
Public expenditures on healthcare, % GDP



Source: Eurostat, Santander

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