COUNCIL OPINION

of 27 February 2007

on the updated convergence programme of Poland, 2006-2009

(2007/C 72/04)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies ([1]), and in particular Article 9(3) thereof,

Having regard to the recommendation of the Commission,

After consulting the Economic and Financial Committee,

HAS DELIVERED THIS OPINION:

(1) On 27 February 2007 the Council examined the updated convergence programme of Poland, which covers the period 2006 to 2009.

(2) The macroeconomic scenario underlying the programme envisages real GDP growth to have reached 5,4 % in 2006 and to broadly stabilise (around 5¼ % on average) over the rest of the programme period. Assessed against currently available information, this scenario appears to be based on growth assumptions which are cautious in 2007 and rather favourable thereafter as the labour market may not improve as rapidly as foreseen in the programme in particular. The programme's projections for inflation appear realistic, tilted to be on the low side towards the end of the programme horizon, notably because of rising wage pressures from the tightening labour market.

(3) In the January 2006 convergence programme, the target for the general government balance in 2006 was set at – 2,6 % of GDP, the Commission services' autumn forecast points at – 2,2 % of GDP, while the November 2006 update of the convergence programme estimates the 2006 outturn at – 1,9 % of GDP. The better-than-expected outturn mainly results from an incomplete execution of expenditure plans (especially social transfers and public investment), while revenue increase resulted mainly from stronger-than-expected growth. The above-mentioned deficit figures exclude the pension reform cost, estimated at around 2 % of GDP in 2006, in line with the transition period for implementing the Eurostat decision of 2 March 2004 on the classification of funded pension schemes ([2]), which expires in spring 2007. The main goal of the budgetary strategy in the November 2006 update is to correct the excessive deficit by 2007 by qualifying for the provision of the reformed Pact which allows a part of the pension reform cost to be deducted. For the following years, the programme plans a gradual reduction of the deficit so that the 3 % of GDP reference value is reached in 2009.

(4) The deficit is planned to narrow by 0,4 percentage point of GDP annually (0,3 percentage point if the pension reform costs are included), from 1,9 % of GDP in 2006 to 0,6 % of GDP in 2009. The primary surplus is planned to improve from 0,5 % of GDP in 2006 to 1,7 % of GDP in 2009. Including the impact of the above-mentioned Eurostat decision, the deficit in the updated programme would improve from 3,9 % of GDP in 2006 to 2,9 % in 2009. The adjustment is planned to be revenue-based in 2007 (revenue ratio increase by 0,6 percentage point of GDP with a near-constant expenditure ratio) and strongly expenditure-based in 2008-2009 so as to more than offset a large

([1]) OJ L 209, 2.8.1997, p. 1. Regulation as amended by Regulation (EC) No 1055/2005 (OJ L 174, 7.7.2005, p. 1). The documents referred to in this text can be found at the following website: http://europa.eu.int/comm/economy_finance/about/activities/sgp/main_en.htm

([2]) See Eurostat News Releases No 30/2004 of 2 March 2004 and No 117/2004 of 23 September 2004.

decline in the revenue ratio (average annual expenditure ratio reduction by 1,6 percentage point, especially consumption and social transfers, with the revenue ratio declining by 1,2 percentage point on average mainly reflecting a cut in social contributions, changes in personal income tax system and other changes to the tax system, which are not always fully specified). Compared with the previous programme, the deficit targets have been revised downwards in view of much stronger growth and the better-than-expected outcome in 2006.

(5) The structural balance (i.e. the cyclically-adjusted balance net of one-off and other temporary measures) calculated according to the commonly agreed methodology is planned to improve from around – 2 % of GDP in 2006 to – ¾ % of GDP in 2009 at the end of the programme period (pension reform costs not included). As in the previous update of the convergence programme, the medium-term objective (MTO) for the budgetary position presented in the programme is a structural deficit of 1 % of GDP, which the programme does not aim to achieve within the programme period. As the MTO is more demanding than the minimum benchmark (estimated at a deficit of around 1½ % of GDP), achieving it should fulfil the aim of providing a safety margin against the occurrence of an excessive deficit. The MTO adequately reflects the debt ratio and average potential output growth in the long term.

(6) The budgetary outcomes could be worse than targeted in the programme in particular in the outer years of the programme. There are significant uncertainties about the effective implementation of planned reforms as they are not backed up by precise measures supporting the envisaged expenditure restraint. In addition, there are risks stemming from the rather favourable macroeconomic scenario for the outer years of the programme period. Consequently, the action taken so far is not sufficient and the planned measures should be strengthened to achieve that result.

(7) In view of this risk assessment, the budgetary stance in the programme does not seem consistent with a correction of the excessive deficit by 2007 as recommended by the Council. The budgetary targets do not provide a sufficient safety margin against breaching the 3 % of GDP deficit threshold with normal macroeconomic fluctuations throughout the programme period. In the years following the correction of the excessive deficit, the pace of the structural adjustment towards the MTO implied by the programme should be strengthened, taking advantage of good economic times, and should be backed up by measures.

(8) Government gross debt is estimated to have reached 42,0 % of GDP in 2006, well below the 60 % of GDP Treaty reference value. The programme projects the debt ratio to decline by 1,4 percentage point over the programme period. Including the impact of the above-mentioned Eurostat decision, the government gross debt would rise from 48,9 % in 2006 to 50,2 % in 2009.

(9) The long-term budgetary impact of ageing in Poland is the lowest in the EU, with age-related expenditure projected to fall, partly as a result of the considerable expenditure-reducing impact of the reform of the pension system — assuming that the pension reforms are fully implemented. The initial budgetary position, although improved compared to 2005, still constitutes a risk to sustainable public finances before the long-term budgetary impact of an ageing population is considered and further budgetary consolidation envisaged in the programme would contribute to contain risks to the sustainability of public finances. Overall, Poland appears to be at low risk with regard to the sustainability of public finances.

(10) The convergence programme contains a qualitative assessment of the overall impact of the reforms listed in the October 2006 implementation report of the national reform programme within the medium-term fiscal strategy. In addition, it provides some information on the direct budgetary costs or savings of the main reforms envisaged in the national reform programme and its budgetary projections seem to take into account the public finance implications of the actions outlined in the national reform programme. The measures in the area of public finances envisaged in the convergence programme seem consistent with those foreseen in the national reform programme. In particular, both programmes envisage some harmonisation of the farmers' social security system with the general national system, the gradual harmonisation of the disability benefits with the reformed pension system and the implementation of the basket of guaranteed medical services.

(11) The budgetary strategy in the programme is partly consistent with the broad economic policy guidelines included in the integrated guidelines for the period 2005-2008. In particular, action taken to correct the excessive deficit does not appear adequate.

(12) As regards the data requirements specified in the code of conduct for stability and convergence programmes, the programme provides all required and most of the optional data ([1]).

The programme envisages a correction of the excessive deficit by 2007, referring to the provision of Article 2(7) of Council Regulation (EC) No 1467/97, but the Council recalls that the action taken so far does not appear adequate and the planned measures appear insufficient to achieve that result.

While in subsequent years the programme envisages to make appropriate progress towards the MTO in a context of strong growth prospects, there are important risks to the achievement of the budgetary targets and the durability of the adjustment.

In view of the above assessment, and taking into account a new recommendation addressed to Poland to correct the excessive deficit adopted by the Council on 27 February 2007 under Article 104(7) of the Treaty, the Council invites Poland to:

(i) ensure the correction of the excessive deficit by 2007 in line with the new recommendation under Article 104(7).

(ii) taking advantage of the good economic times, using any extra revenue for deficit reduction, strengthen the pace of adjustment towards the MTO after the planned correction of the excessive deficit, by specifying and implementing the additional measures, especially on the expenditure side, that are necessary to achieve the envisaged adjustment.

(iii) safeguard the results of the pension reform.

Comparison of key macroeconomic and budgetary projections

		2005	2006	2007	2008	2009
Real GDP (% change)	**CP Nov 2006**	**3,5**	**5,4**	**5,1**	**5,1**	**5,6**
	COM Nov 2006	3,2	5,2	4,7	4,8	n.a.
	CP Jan 2006	*3,3*	*4,3*	*4,6*	*5,0*	*n.a.*
HICP inflation (%)	**CP Nov 2006**	**2,2**	**1,4**	**2,1**	**2,5**	**2,5**
	COM Nov 2006	2,2	1,4	2,5	2,8	n.a.
	CP Jan 2006	*2,2*	*1,5*	*2,2*	*2,5*	*n.a.*
Output gap (% of potential GDP)	**CP Nov 2006** ([1])	**– 0,4**	**0,5**	**0,5**	**0,3**	**0,4**
	COM Nov 2006 ([3])	– 0,3	0,4	0,3	0,1	n.a.
	CP Jan 2006 ([1])	*0,1*	*0,3*	*0,3*	*0,6*	*n.a.*
General government balance (pension reform cost excluded) (% of GDP)	**CP Nov 2006**	**– 2,5**	**– 1,9**	**– 1,4**	**– 1,0**	**– 0,6**
	COM Nov 2006	– 2,5	– 2,2	– 2,0	– 1,8	n.a.
	CP Jan 2006	*– 2,9*	*– 2,6*	*– 2,2*	*– 1,9*	*n.a.*

([1]) In particular, the data on employment in hours worked and labour productivity measured as GDP per hours worked have not been provided. Contributions to the potential growth are also missing.

		2005	2006	2007	2008	2009
General government balance (pension reform cost included) (% of GDP)	**CP Nov 2006**	**– 4,4**	**– 3,9**	**– 3,4**	**– 3,1**	**– 2,9**
	COM Nov 2006	– 4,4	– 4,2	– 4,0	– 3,9	n.a.
	CP Jan 2006	*– 4,7*	*– 4,6*	*– 4,1*	*– 3,7*	*n.a.*
Primary balance (pension reform cost excluded) (% of GDP)	**CP Nov 2006**	**0,1**	**0,5**	**1,0**	**1,4**	**1,7**
	COM Nov 2006	0,1	0,2	0,4	0,6	n.a.
	CP Jan 2006	*– 0,3*	*– 0,2*	*0,3*	*0,6*	*n.a.*
Structural balance (2) (pension reform cost excluded) (% of GDP)	**CP Nov 2006**	**– 2,4**	**– 2,1**	**– 1,6**	**– 1,1**	**– 0,7**
	COM Nov 2006	– 2,3	– 2,3	– 2,1	– 1,8	n.a.
	CP Jan 2006	*– 2,1*	*– 2,7*	*– 2,4*	*– 2,1*	*n.a.*
Structural balance (2) (pension reform cost included) (% of GDP)	**CP Nov 2006**	**– 4,3**	**– 4,1**	**– 3,6**	**– 3,2**	**– 3,0**
	COM Nov 2006	– 4,2	– 4,3	– 4,1	– 3,9	n.a.
	CP Jan 2006	*– 4,7*	*– 4,7*	*– 4,2*	*– 3,9*	*n.a.*
Government gross debt (pension reform cost excluded) (% of GDP)	**CP Nov 2006**	**41,9**	**42,0**	**42,1**	**41,4**	**40,6**
	COM Nov 2006	42,0	42,4	43,1	42,7	n.a.
	CP Jan 2006	*42,5*	*45,0*	*45,3*	*45,4*	*n.a.*
Government gross debt (pension reform cost included) (% of GDP)	**CP Nov 2006**	**47,3**	**48,9**	**50,0**	**50,3**	**50,2**
	COM Nov 2006	47,4	49,3	51,0	51,6	n.a.
	CP Jan 2006	*47,9*	*51,2*	*52,1*	*52,6*	*n.a.*

Notes

(1) Commission services calculations on the basis of the information in the programme.

(2) Cyclically-adjusted balance excluding one-off and other temporary measures. Cyclically-adjusted balance and structural balance are the same since one-off and other temporary measures taken from the programme are insignificant.

(3) Based on estimated potential growth of 4,1 %, 4,4 %, 4,8 % and 5,0 % respectively in the period 2005-2008.

Source

Convergence programme (CP); Commission services' autumn 2006 economic forecasts (COM); Commission services' calculations