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Statement by Ms. Mannathoko and Mr. Abdullahi on Republic of Poland
(Preliminary)
Executive Board Meeting
February 3, 2021

We thank staff for the informative report and Messrs. Trabinski and Piasecki for their helpful Buff statement. We commend the authorities for their recent pre-COVID track record of prudent macroeconomic policies and robust economic growth, as well as for the swift and forceful measures taken more recently to mitigate the COVID-19 impact on the economy. These measures led to lower reported cases and fatalities compared to other EU members in the first wave of the virus. However, we note that for the second wave, containment measures to control the virus were less stringent despite significant increases in both confirmed cases and fatalities since September 2020. We therefore agree with staff on the importance of vigilance and flexibility, and that the authorities should continue to utilize the fiscal space available to support the economy as needed during the pandemic, and to limit further devastating impacts on lives and livelihoods that could arise from the second wave. We agree with the thrust of the staff analysis and have the following comments and questions for clarification.

Fiscal policy: On crisis spending, while we support the governance safeguard measures taken to minimize waste and fraud, we urge the authorities to further target additional COVID-19 related spending. On the fiscal stance beyond the short term, we agree with staff that once the recovery takes hold, gradual fiscal consolidation centered on revenue mobilization and improved expenditure efficiency is needed to rebuild fiscal buffers that will help mitigate risks from future crises. Given the very sharp increase in the fiscal deficit in 2020 (from 1.2% of GDP in 2019 to 7% in 2020) alongside a rising public debt ratio, and noting that a durable recovery is delayed, *could staff clarify assumptions under the adverse scenario mentioned? What are its implications for the fiscal deficit should it materialize? We assume the sizable grant inflows from the EU in the medium term preclude the need for a contingency plan. Staff views are welcome.*

Monetary and exchange rate policies: We view the current accommodative monetary policy stance as appropriate and while we encourage a data driven policy stance, we concur with staff that in the short-term, supply-induced inflation is likely to abate and considering the negative output gap, should not warrant a response. We also encourage the use of a flexible exchange rate as a shock absorber, and to limit adjustment pressure on the fiscal balance, and urge the authorities to limit FX market interventions.

Financial sector: Notwithstanding the resilience of the financial sector so far, risks to financial stability have increased with the crisis, and we agree close monitoring is important. In particular, the crisis has increased risks of non-performing loans, suggesting that banks should defer dividend payments and use their profits to increase their capital buffers until sustained stability is assured. *Could staff indicate if there are other risks from the housing market for the sector apart from the issues with the declining stock of foreign-currency denominated mortgages and associated court disputes? Could staff also elaborate on the impact of the crisis on the sovereign-financial institution nexus and linkages? Leading up to the pandemic, the state already held around 40% of the banking sector's assets, and at the same time banks had significant holdings of sovereign bonds. What are staff views on potential negative feedback effects between the financial situation of the State and the banking sector?* Given the critical role of the supervisory function at this time, we are encouraged by reports on new legislation passed and that the recently empowered and well-resourced Polish Financial Supervisory Authority's supervisory capacity has improved and there has been increased focus on AML/CFT compliance.

Employment: The unchanged 2020 unemployment rate shown in Table 3 may understate the extent of unemployment in the wake of COVID given the labor force slack data shown in Annex III. Figure 5 of the Annex suggests a significant potential increase in unemployment between 2019 and 2020, among the working age cohort (20 – 64 years), once the stimulus ends. *Could staff comment on their expectations for unemployment once employment support policies are phased out. Should we expect a rapid enough recovery in jobs to offset the withdrawal of support to firms? We also note the more pronounced adverse impacts on youth and women. Could staff clarify how these vulnerable groups are targeted in the government support strategy?*

Medium term adjustment and demographics: In the last Article IV discussion there were concerns over a shrinking working age population and implications for pensions and long-term sustainability of public finances. *Do staff have a sense of the extent to which the COVID-19 pandemic and response has impacted the Employee Capital Plan? Could staff also comment on any discussions on adequate health insurance plans for the post COVID-19 era, in addition to measures being taken to strengthen the health system?*

Private sector role: While government is expected to increase its investment spending with EU next generation funds, Annex I (p.40) suggests no progress has been made in levelling the playing field for all investors or in reducing state ownership. *Could staff brief us on progress since the 2018 Article IV on measures taken to support the private-sector-led growth needed to increase efficiency, productivity, and innovation?*