Poland Watch

EU funds likely on the way soon

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Positive EU signals should ensure c.EUR27bn for 2024

Following several constructive comments from the EU in the past week, we expect the EC to positively assess Poland's judiciary reform next Wednesday. This would formally pave the way for recovery and cohesion fund inflows soon. The first tranche of the RRP could be paid by April, amounting to EUR6.3bn. In total, Poland could get c.EUR27bn in recovery and cohesion money in 2024 (c.3.2% of GDP) and another EUR11.5bn of RRP funds likely in 1Q 2025. For 2024, this amount has been budgeted by FinMin, but it adds to the strong financing so far. FinMin expects to cover more than 50% of this year's gross borrowing requirement by end-March, before counting these EU inflows.

Recent developments confirm our view that despite the legal difficulties with President Duda's threat of veto, Poland under PM Tusk's leadership will likely gain access to EU funds sooner or later this year. This news, together with the positive developments in equity markets this week, supports our long-term constructive view on the PLN. We do not think that the (possible upcoming) government motion against NBP Governor Glapinski will materially affect the PLN's constructive fundamentals.

Judiciary reform roadmap acceptable to the EU

Justice Minister Bodnar's presentation of the judiciary reform plan in Brussels on Tuesday has been favourably received by the EU. This is key to unlocking the RRP and cohesion funding. The plan is also seen by EC Deputy Head Jourova as "the first positive step that could result in the closure of the Article 7 procedure". The plan includes profound changes to the functioning of the National Council of the Judiciary, the Supreme Court, the Constitutional Tribunal, the common courts and the public prosecutor's office. The EC has indicated that it does not expect quick enforcement given resistance from President Duda. But it welcomes and trusts the Tusk government's commitment to restoring the rule of law and is thus keen to support Poland by releasing funding.

1st RRP payment by April, four more tranches in next 12 months

Following the EC's likely positive opinion next Wednesday, the EU Council is due to vote within four weeks to approve the first RRP tranche to Poland by end-March/early April, with payment of EUR6.3bn likely in April. To catch up with the delayed absorption, the government also plans to submit four more RRP payment requests in 2024. We understand that Poland is well on track with other milestones and targets besides the judiciary ones, so this timeline looks realistic. It implies another EUR10.6bn in 2H 2024 and EUR11.5bn in 1Q 2025 of RRP funding (see scheduled tranches in Exhibit 1).

As for cohesion funds, inflows depend on the progress of investment projects, and absorption is usually low at the beginning of the effective absorption period (2023-29). We expect c.EUR5bn in 2014, before picking up to c.EUR10bn in the coming years.

Abbreviations

c.: circa

EC: European Commission

FinMin: Ministry of Finance

NBP: National Bank of Poland

PiS: Law and Justice Party

PM: Prime Minister

PO: Civic Platform party

RRP: Recovery and Resilience Plan

Exhibit 1: Poland – RRP scheduled payment tranches
Poland will get c.EUR22bn in RRP payments this year, including pre-funding and tranches 1-3

	Pre-funding	1st	2nd	3rd	4th	5th	6th	7th	8th	9th
Grant	0.6	2.7	3.0	2.0	2.4	2.2	3.0	2.9	3.0	3.4
Loans	4.5	3.6	2.8	2.7	2.8	4.2	5.5	2.9	3.2	2.4
Total	5.1	6.3	5.8	4.7	5.1	6.4	8.5	5.9	6.2	5.8

Source: European Commission, BofA Global Research

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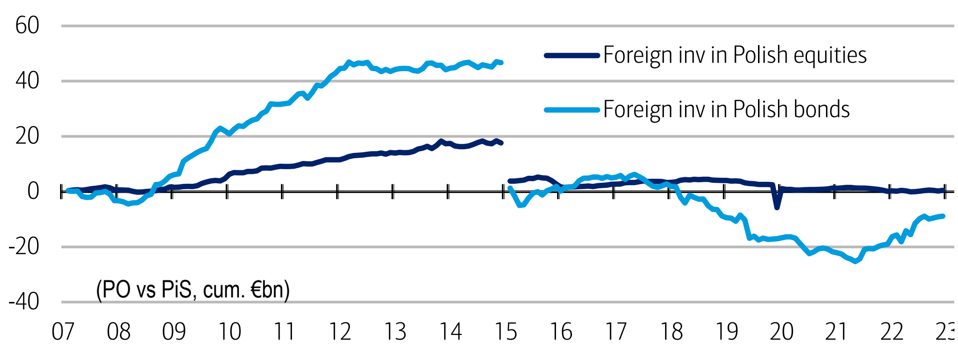
Fiscal financing well advanced

The confirmation of EU inflows reinforces FinMin's strong financing situation. FinMin Domanski notes that Poland will finance over 40% of its 2024 borrowing requirement by end-February and expects 50% to be funded by end-March. If we include all EU inflows expected this year, we estimate that financing needs would be over 60% covered by end-March, leaving FinMin in a very comfortable position.

Investors have been concerned about upside spending risks given the election calendar and possible extension of the inflation shield in 2H 2024, but FinMin still appears optimistic about the deficit target of 5.1% of GDP, citing favourable VAT trends so far. Any slippage is likely to be small, we think. In any case, we do not expect the deficit to be more than 5.5% of GDP this year. Progress on financing looks well advanced even if we include overshooting of up to 5.5% of GDP.

Exhibit 2: Portfolio inflows under past PiS versus PO governments
Past experience suggests that market-friendly PO government could attract more portfolio inflows



Source: Haver, BofA Global Research

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Good news for banks to support equity inflows, thus PLN

Another source of support for the PLN this week comes from the equity markets, which we think will outperform under the PO government versus the PiS government (). FinMin's Domanski suggested on Tuesday higher dividends from state-owned banks and expressed a wish to build a stronger Polish capital market. Polish banks have subsequently received approvals from the regulator for higher dividend pay-outs. BofA Global Research's banks analyst, Olga Veselova, expects them to keep paying good dividends as profitability is high (thanks to higher rates for longer, now that NBP is not expected to cut any time soon) with no proper loan growth. This follows years in which banks accumulated capital due to the CHF loan saga, the pandemic, and the Russia-Ukraine war. There is now much less need to keep sitting on such a large cash pile, given that they have the blessing of both the regulator and FinMin.

NBP hawkish amid trial threat to NBP governor

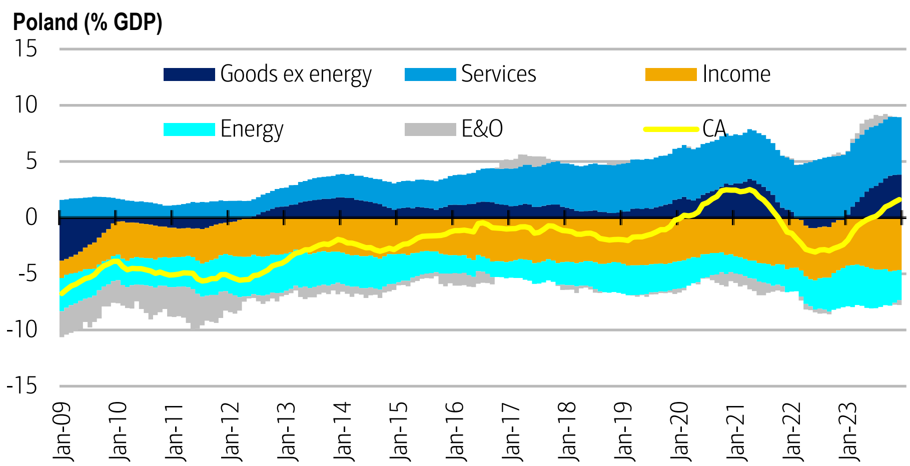
We do not think that the government proceedings against NBP Governor Glapinski will negatively affect the PLN's constructive fundamentals in any material way. On monetary policy, we expect the NBP to be in defensive mode in response to the government's motion, which means no rate cuts any time soon with rates likely steady at 5.75% this year. The legal process can be lengthy and uncertain, so it is too early to say if and when Glapinski could be suspended from his duties or how the MPC might behave subsequently. However, we still believe that the next move is likely to be a cut.

Investors may be wary of the uncertainty and the idea of the government interfering with the central bank. However, we do not think that this is a strong reason to turn bearish on the PLN, rather a short-term reaction to headlines. Market confidence is important but perhaps more relevant for countries with weaker fundamentals. Poland does not have large funding needs or vulnerabilities, given its solid current account position, strong EU inflows, and comfortable fiscal financing.

In terms of the process, if the government decides to go ahead, the motion would initiate a preliminary trial against Glapinski in the lower house (Sejm), after which he could be referred to the State Tribunal. Currently, the law requires an absolute majority to do that, which the ruling coalition has. However, the Constitutional Tribunal (dominated by PiS appointments) has challenged this and insists that a majority of 60% is needed. To make things more complicated, government officials have suggested that they would not abide by any rulings of a body they see as illegitimate.

Exhibit 3: Current account breakdown

Balances of goods ex energy and services in solid surpluses



Source: Haver, BofA Global Research

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