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LONG-TERM COMPARATIVE ANALYSIS OF PUBLIC FINANCES IN POLAND AND SLOVAKIA IN 2000 – 2018

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ABSTRACT

The subject of the paper is an analysis of the situation in public finances in Poland and Slovakia in 2000-2018. The authors formulated three research questions: 1) What was the budgetary situation and the level of public debt in both countries in the pre-accession period, in particular in the years of economic slowdown 2001-2003; 2) What were the results of public finance consolidation after the EU accession, in the period of economic prosperity 2004-2007; 3) What was the scale of the deterioration in public finances in Poland and Slovakia caused by the financial and economic crisis of 2008-2009 and the effects of post-crisis consolidation.

The analysis shows that the initial situation (pre-accession period) in public finances was better in Poland. In the period of economic prosperity 2004-2007, Poland had relaxed budgetary discipline. The 2008-2009 crisis contributed more to the increase in the budget deficit and public debt in Slovakia. The process of post-crisis consolidation is faster in Slovakia.

Keywords: GDP growth, public finances, consequences of crises, effects of consolidation

INTRODUCTION

A long-term analysis of the state of public finances in Poland and Slovakia is interesting for at least several reasons. First, the initial situation in the pre-accession period, in particular including the years of slowdown in economic growth (2001-2003), was important from the point of view of the budgetary consequences of the crisis. Secondly, the state of public finances in 2004-2007, after both countries became members of the European Union, was an important condition for the consolidation of public finances in the period of economic prosperity and the possibility of supporting GDP growth during the crisis of 2008-2009. Thirdly, the scale of deterioration in budgetary balance and the increase in public debt was significant in both countries, one of which introduced the common currency (Slovakia) and the other (Poland) maintained the national currency. Fourthly, it is worth comparing the paths of public finance consolidation of both countries and the euro area.

The aim of the paper is to answer research questions on the basis of presented statistical data illustrating the budget balance and public debt in relation to GDP in Poland, Slovakia and the euro area. The authors assume (theoretically and empirically confirmed) that the main factors influencing the budgetary situation, and thus the public debt, are: GDP growth and discipline in maintaining a safe relationship between budget revenues and expenditures. Changes in economic activity reflected in the rate of GDP growth or decline automatically lead to an adjustment in the budget balance. Decreases in output and GDP result in an increase in the budget deficit, as most taxes are proportional to the level of production while expenditures increase almost automatically during the recession [3]. Empirical studies reveal that a more sustainable improvement in the budgetary balance is the result of a reduction in budgetary expenditure than of measures leading to an increase in budget revenue [1], [4], [8]. Therefore, the data interpretation is based on the GDP growth rates (annual and average in selected periods) and on the ratios of expenditures to budget revenues.

LONG-TERM ANALYSIS OF THE STATE OF PUBLIC FINANCES IN POLAND, SLOVAKIA AND THE EURO AREA (2000-2018)

In order to achieve the research goals we first assess the state of public finances in Poland and Slovakia in the pre-accession period of 2000-2003. Both countries had high budget deficits and Slovakia exceeded the deficit level set for the countries of the common currency area by more than twice. The average deficit in the years 2000-2003 in the euro area was 2.10% of GDP, in Poland 4.67% of GDP and in Slovakia 7.30% of GDP. Detailed data presented in table 4 show a deterioration of budgetary balance during the economic slowdown (2001-2003) in Poland and in the euro area. Whereas in Slovakia the high average deficit in the pre-accession period was due to a large disturbance to the budgetary balance in 2000. Assessing the effects of the economic slowdown, it should be emphasized that the decline in the GDP growth rate took place in Slovakia at the earliest, and in the years 2001-2003 GDP growth rates ranged from 3.3% to 5.4%. For the longest period, the low economic growth rate was remaining in the euro area (2001-2003), and in Poland in 2001-2002. The economic recovery in Slovakia was stronger than in Poland, but both countries significantly reduced the economic gap to the euro area (tab. 1).

Poland's public debt in the pre-accession period was low and amounted to 36.5% of GDP, while in Slovakia it was much higher: 49.6% of GDP (2000). However, the situation began to change with an increase in the budget deficit in Poland and a decrease in the deficit in Slovakia, which in 2003 increased to 6.1% of GDP in Poland and decreased to 2.7% of GDP in Slovakia (tab. 4). As a result, in 2003 Poland's public debt increased by 10.1 percentage points to 46.6% of GDP, while in Slovakia it decreased by 8.0 percentage points to 41.6% of GDP (tab. 3). Public debt in the euro area (average for all member states) was much higher due to large differences between countries and exceeded its Treaty threshold (60% of GDP). In 2000 it amounted to 68.1% of GDP, and the lowest level (65.0% of GDP) reached in 2007.

Another research question refers to the results of the public finance consolidation in Slovakia and Poland in the early years of EU membership, when high GDP growth rates were recorded (2004-2007). The euro area’s average economic growth rate ranged from 1.8% to 2.4%. Against this background, Poland and Slovakia performed exceptionally well, but especially Slovakia, which achieved GDP growth rates ranging from 5.3% (2004) to 10.8% (2007). The GDP growth rate in Poland was lower, but high in comparison with other EU countries and ensuring a satisfactory pace of reducing the economic gap in relation to the more developed member states, especially the southern ones. The average annual GDP growth rate in Slovakia in the years 2004-2007 was at the level of 7.85%, and in Poland it amounted to 5.45% (tab. 1).

High economic growth in both countries supported the reduction of budget deficit and public debt. The public finance consolidation at that time created more opportunities to counteract the fall in GDP in 2008-2009 and the economic recovery from the recession of 2009, without the risk of a sharp deterioration in the public finance situation. Consolidation results were significantly better in Slovakia. The average annual budget deficit between 2004 and 2007 was 2.67% of GDP (the European Monetary Union - EMU criterion was fulfilled), while in Poland it was almost 1 percentage point higher and amounted to 3.62% of GDP. In the euro area, the average deficit decreased slightly from 2.10% of GDP to 1.95% of GDP. Budgetary balance has improved in all three analysed economies, but only Slovakia achieved an impressive result. Its average annual deficit fell from 7.30% of GDP to 2.67% of GDP in 2000-2003. Whereas, Poland did not use the period of high economic activity to strengthen its budgetary balance. The deficit was high in 2004-2005 and amounted to 5% and 4% of GDP respectively, despite a relatively high GDP growth rate. The improvement in the budget balance in relation to 2000-2003 amounted 1 percentage point (from 4.67% of GDP to 3.62% of GDP). Although, it should be noted that in 2007 the budget deficit in Poland decreased to 1.9% of GDP. This was due to higher-than-expected tax revenues and lower cyclical expenditure. However, already in 2008, the deficit rose to 3.6% of GDP, because taxes were reduced and wages in the public sector were raised. In fact, there was an increase in expenditure and a decrease in government revenue, which was overestimated [7]. The average deficit in the euro area, reduced to less than 2% of GDP between 2004 and 2007, should be considered positive, as it was inflated by countries that did not respect budgetary discipline, such as Portugal, Greece and Italy. Turning to the assessment of the state of public finances in Poland and Slovakia, the success of Slovakia in reducing public debt from 49.6% of GDP in 2000 to 30.1% of GDP in 2007 cannot be overlooked. In Poland, public debt increased from 36.5% of GDP to 44.2% of GDP (tab. 3).

The following third research question is the most important from the point of view of reconciling two fundamental objectives of budgetary policy: supporting the stabilisation of economic growth and maintaining a safe limit of public deficit and debt. This concerns the budgetary effects and increase in public debt during the 2008-2009 crisis and the consequences of public finance consolidation in the post-crisis years in Poland and Slovakia. The recession in Slovakia was deeper by 0.9 percentage points than the average decrease in the GDP growth rate in the euro area. Poland was the only EU country where there was no recession, but only an economic slowdown. The average annual GDP growth rate in 2009-2017 was higher in Poland (3.22%) than in Slovakia (2.47%), because of relatively high rate of GDP growth in Poland in 2009 (2,8%) and recession in Slovakia (5.4% drop of GDP). The deeper recession in Slovakia than in the euro area (average) was strongly driven by a decline in exports concentrated on the EU market caused by the appreciation of the real exchange rate [6]. Forecasts from 2019 to 2023 are more favourable for Slovakia (tab. 1).

Table 1. Growth of GDP in Poland, Slovakia and the euro area in 2000 – 2023 (constant prices, in %)

Year	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**
Poland	4.3	1.2	1.4	3.6	5.1	3.5	6.2	7.0	4.3	2.8	3.6	5.0
Slovakia	1.2	3.3	4.5	5.4	5.3	6.8	8.5	10.8	5.6	-5.4	5.0	2.8

Euro area	3.8	2.1	1.0	0.7	2.3	1.7	3.2	3.0	0.4	-4.5	2.1	1.6
Year	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**
Poland	1.6	1.4	3.3	3.8	2.9	4.6	4.1	3.5	3.0	2.8	2.8	2.8
Slovakia	1.7	1.5	2.8	3.9	3.3	3.4	4.0	4.2	3.8	3.7	3.5	3.4
Euro area	-0.9	-0.2	1.3	2.1	1.8	2.3	2.4	2.0	1.7	1.5	1.5	1.4

Source: [5]

Table 2. Total revenue and total expenditure (general government) in Poland, Slovakia and the euro area in 2000 – 2019 (% GDP)

Year	Poland		Slovakia		Euro area	
	Revenue	Expenditure	Revenue	Expenditure	Revenue	Expenditure
2000	39.1	42.1	40.0	52.0	45.5	45.9
2001	40.3	45.0	38.0	44.4	44.7	46.7
2002	40.6	45.4	37.1	45.1	44.3	47.0
2003	39.7	45.8	37.2	39.9	44.2	47.4
2004	38.5	43.6	35.5	37.8	43.9	46.8
2005	40.4	44.4	36.9	39.8	44.1	46.7
2006	41.1	44.7	35.2	38.8	44.6	46.1
2007	41.4	43.2	34.4	36.3	44.7	45.4
2008	40.7	44.3	34.5	36.9	44.4	46.6
2009	37.8	45.0	36.3	44.1	44.5	50.7
2010	38.5	45.8	34.7	42.1	44.4	50.6
2011	39.1	43.9	36.5	40.8	45.0	49.2
2012	39.1	42.9	36.3	40.6	46.1	49.8
2013	38.5	42.6	38.7	41.4	46.8	49.8
2014	38.6	42.3	39.3	42.0	46.7	49.2
2015	38.9	41.6	42.5	45.2	46.3	48.3
2016	38.8	41.1	39.3	41.5	46.1	47.6
2017	39.6	41.2	39.4	40.4	46.2	47.1
2018	40.3	41.7	38.6	39.5	46.0	46.6
2019	40.5	41.9	38.0	38.3	45.5	46.1

Source: [2]

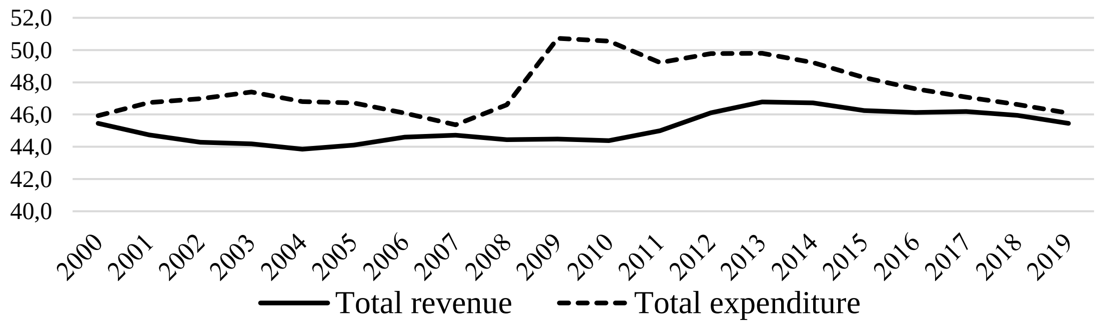


Figure 1. Total revenue and total expenditure (general government) in the euro area in 2000 – 2019 (% GDP)

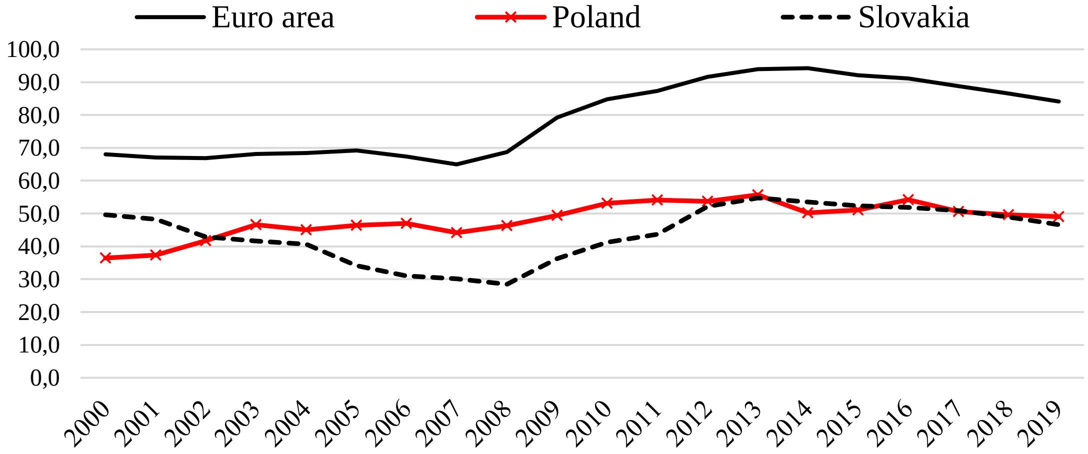
Source: [2]

Table 3. General government consolidated gross debt in Poland, Slovakia and the euro area in 2000 – 2019 (% GDP)

Year	Poland	Slovakia	Euro area
2000	36.5	49.6	68.1
2001	37.3	48.3	67.0
2002	41.8	42.9	66.9
2003	46.6	41.6	68.1
2004	45.0	40.6	68.4
2005	46.4	34.1	69.2
2006	46.9	31.0	67.4
2007	44.2	30.1	65.0
2008	46.3	28.5	68.7
2009	49.4	36.3	79.2
2010	53.1	41.2	84.8
2011	54.1	43.7	87.3
2012	53.7	52.2	91.7
2013	55.7	54.7	93.9
2014	50.3	53.5	94.2
2015	51.1	52.3	92.1
2016	54.2	51.8	91.1
2017	50.6	50.9	88.8
2018	49.6	49.0	86.5
2019	49.1	46.6	84.1

Source: [2]

Figure 2. General government consolidated gross debt in Poland, Slovakia and the euro area in 2000 – 2019 (% GDP)



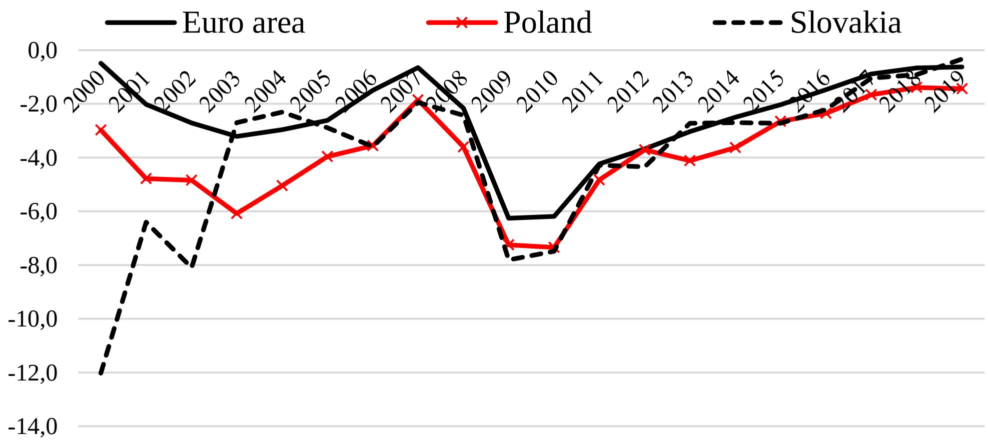
Source: [2]

Table 4. Net lending (+) or net borrowing (-) in Poland, Slovakia and the euro area in 2000 – 2019 (% GDP)

Country	Poland	Slovakia	Euro area
2000	-3.0	-12.0	-0.5
2001	-4.8	-6.4	-2.0
2002	-4.8	-8.1	-2.7
2003	-6.1	-2.7	-3.2
2004	-5.0	-2.3	-3.0
2005	-4.0	-2.9	-2.6
2006	-3.6	-3.6	-1.5
2007	-1.9	-1.9	-0.7
2008	-3.6	-2.4	-2.2
2009	-7.3	-7.8	-6.3
2010	-7.3	-7.5	-6.2
2011	-4.8	-4.3	-4.2
2012	-3.7	-4.3	-3.7
2013	-4.1	-2.7	-3.0
2014	-3.6	-2.7	-2.5
2015	-2.6	-2.7	-2.0
2016	-2.3	-2.2	-1.5
2017	-1.7	-1.0	-0.9
2018	-1.4	-0.9	-0.7
2019	-1.4	-0.3	-0.6

Source: [2]

Figure 3. Net lending (+) or net borrowing (-)in Poland, Slovakia and the euro area in 2000 – 2019 (% GDP)



Source: [2]

The achieved results of GDP growth should create greater opportunities for public finance stabilisation in Poland. However, the situation was different. The budget deficit in Poland in 2009 rised to 7.3% of GDP and remained at this level in the following year. The slowdown in GDP growth resulted in a decrease in budget revenues, in particular from the tax on goods and services (VAT). At the same time, expenditure increased (tab. 2), mainly due to the necessary own contribution to the realized public investments financed from the EU funds. The budget deficit fell below 3% of GDP in 2015 and according to forecasts, the downward trend will continue up to 2018. In Slovakia, the deficit in 2009-2010 was slightly higher (by 0.5 and 0.2 percentage points), but the downward trend was stronger than in Poland. Already in 2013, the budget deficit decreased to 2.7% of GDP and remained at this level until 2015. In 2016 the deficits in Poland and Slovakia were similar. However, the process of deficit reduction as well as forecasts are more favourable for Slovakia (tab. 4). Slovakia's budget balance improvement path is close to the euro area, while Poland's path has been slower since 2017.

Public debt was a significant consequence of the financial and economic crisis in the euro area. Already in 2009, averaged public debt increased by 10 percentage points compared to the previous year. It grew until 2014, as the possibility of improving budget balance and the rate of public debt reduction was limited by the second wave of recession in 2012-2013. Since 2014, economic growth in the euro area has remained between 1.3% and 2.3%, but forecasts predict a reduction of about 1 percentage point compared to 2017-2018. Public debt in the euro area was the highest in 2014 and amounted to 94.2% of GDP. It has been declining since 2015, but very slowly - to 88.8% of GDP in 2017, and is expected to fall to 86.5% of GDP in 2018 (tab. 3). The euro area's average debt does not reflect the real debt situation in the member states, as the average value is strongly influenced by the countries with a high debt level: Greece 178.6% of GDP, Italy 131.8% of GDP, Portugal 125.7% of GDP and Belgium 103.1% of GDP [2].

Compared to the euro area, Slovakia and Poland have low public debts, in both countries they did not exceed 51% of GDP in 2017. The forecasts for their decline are more favourable for Slovakia, which is due to the faster path of achieving budget balance and the projected higher GDP growth rate in Slovakia.

CONCLUSION

Concluding, a long-term analysis of the state of public finances in Poland and Slovakia showed that in the pre-accession period Poland's budget deficit and public debt were lower than in Slovakia. The deterioration of the budgetary balance in Poland and the increase in public debt had occurred since 2003, as shown in figures 2 and 3, which refers to the years 2003-2008. The crisis of 2008-2009 contributed more to the increase in the budget deficit and public debt in Slovakia. Public debt increased from 28.5% of GDP in 2008 to 54.7% of GDP in 2013. In Poland it increased from 44.2% of GDP in 2007 to 55.7% of GDP in 2013.

The process of post-crisis consolidation is faster in Slovakia in terms of reducing the budget deficit and comparable to Poland in terms of reducing public debt. Taking into account the deep recession in Slovakia in 2009, but the absence of a second wave of recession in 2012-2013, as well as the fulfilment of the Treaty criterion of budget deficit from 2013 and the reduction of the deficit to 1% of GDP in 2017, as well as high economic growth rate, Slovakia is an example of a country that confirms the possibility of achieving the benefits of market and currency integration.

The budgetary discipline in Slovakia after the accession to the EU was and remains stronger than in Poland. Slovakia abandoned its national currency at a very early stage (2009) and introduced the euro. In order to meet the EMU criteria, Slovakia focused on priority objectives in its budgetary policy.

The analysis reveals that the long-term GDP growth rate in Slovakia was higher than in Poland. In 2000-2017, the average annual GDP growth rate reached 3.91% in Slovakia and 3.64% in Poland. The rate of narrowing the economic gap in Slovakia was higher than in Poland. By abandoning the national currency, Slovakia did not limit its opportunities for economic development. Otherwise, the euro made it easier for foreign investors to do business in Slovakia and for Slovak investors - abroad.

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