Warsaw, June 17, 2015

REPUBLIC OF POLAND
MINISTER OF FINANCE
Mateusz Szczurek

OFFICIAL DOCUMENTS

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Mr. Jim Yong Kim
President
World Bank

1818 H Street NW
Washington D.C. 20433
United States of America

Dear Mr. President,

Allow me first to express my gratitude for the World Bank's continued support over the past few years to the reform process in Poland. Budgetary support operations, technical assistance projects and knowledge activities continue to play a significant role in supporting the economic and social reforms undertaken by the Polish Government amidst what remains a turbulent and uncertain external environment.

With that in mind, I am writing to request your approval for the second in the series of the programmatic Resilience and Growth Development Policy Loan (DPL2) in the amount of EUR 912.7 million. The loan is aimed at strengthening macroeconomic resilience and promoting economic growth. The loan, prepared in close collaboration with the World Bank, builds on the Government's strategic priorities of reinvigorating economic growth, consolidating public finances, promoting jobs and innovation in Poland.

Macroeconomic Framework

In the past few years, and in spite of the uncertain external environment, Poland's economic fundamentals have remained strong, underpinned by sound macroeconomic policies. Poland has enjoyed one of the highest economic growth rates among EU countries. This strong performance can be credited to the considerable diversification of Poland's economy, the reduction in external imbalances prior to the crisis and prudent macroeconomic policies. Counter-cyclical policies have also helped to lessen the impact of the economic slowdown.

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The fiscal deficit narrowed to 3.2 percent of GDP in 2014, from 4 percent in 2013. Revenue collection was stronger than expected, as domestic demand pushed up VAT receipts, while expenditures continued to be closely controlled, for example through the maintenance of the ongoing wage bill freeze. Recognizing the success of the government's efforts and taking into account the cost of systemic pension reform, of 0.4 percent of GDP, the European Commission has recommended that the European Council abrogate the excessive deficit procedure (EDP) in 2015, one year ahead of schedule.

Strong macroeconomic fundamentals and sound policies have helped Poland withstand several bouts of global market turbulence and paved the way for economic recovery. Nonetheless, while benefiting from the continued transformation into a more open and dynamic economy, substantial trade and financial linkages with global markets, combined with still-large financing needs and geopolitical tensions in the region, expose the economy to external shocks and necessitate the need to further strengthen macroeconomic resilience and support growth.

Government Program

The Government remains committed to strengthening public finances, boosting private sector led economic growth, and innovation to facilitate job creation and shared prosperity. Across all these issues, the Government is concerned to address the short-term challenges, which are the legacy of the global financial crisis and current economic uncertainties, as well as medium- to long-term structural rigidities. Short-term actions are aimed at rebuilding fiscal buffers and bolstering macroeconomic resilience, while medium and long-term structural reforms are targeted at lifting productivity and potential growth. These measures are designed to help to ensure that prosperity continues to be shared across society.

In order to **strengthen public finances**, the Budget for 2015 assumes continued consolidation with a view to eventually reducing the deficit to the Medium Term Objective of a structural deficit of one percent of GDP. Implementation of the fiscal expenditure rule, supported by the DPL program, is key to achieving such reductions in the fiscal deficit. Growth and fiscal consolidation have also created fiscal space for spending on well targeted social programs that protect poor and vulnerable groups. Programs include the extension of maternity leave, more generous pension indexation and the expansion of child tax credits. On the revenue side, the main adjustment comes from reducing transfers to the second pillar pension funds, freezing PIT thresholds, and abolishing various tax reliefs, as well as measures to increase tax compliance and the effectiveness of tax administration.

The Government remains committed to enhancing **labor market flexibility and facilitating job creation.** While Poland has witnessed significant recent improvements in labor markets, with the unemployment rate falling to levels not seen since 2007, continuing to increase professional activity and employment remain amongst the main challenges. The Government has introduced measures to enhance the flexibility to adjust working hours, introduced a part-time work subsidy scheme and increased support to active labor market programs for disadvantaged groups — such as training and wage subsidies, and apprenticeship schemes. Measures have also been put in place to improve the effectiveness of public employment offices to provide better services for the unemployed, through profiling and increased focus on the hard-to-place. The Government is also promoting the expansion of childcare facilities for the re-integration of women into the labor market after child-birth. In parallel, the deregulation of professions will enhance access to over 200 professions, many of which provide greater opportunities for youth and women. The Government remains committed to the third tranche of the professions deregulation, and expects the legislation to be fully enacted by parliament in August and signed by the President by September 2015. Steps to reduce labor market duality include the introduction of social security contributions on selected civil law employment contracts, while the expansion of the child tax credit will reduce the tax wedge for low income families.

Boosting **private sector growth and innovation** continues to be one of the main pillars of the Government's reform agenda. Innovation and knowledge-based development represent an opportunity for ensuring dynamic growth of the Polish economy, especially in light of the diminishing impact of traditional sources of economic growth. In order to increase the innovativeness of enterprises, measures in numerous fields are necessary—removing barriers for conducting business activity, improving the quality of education to provide competent personnel, expanding access to finance, promoting knowledge transfer, developing business environment institutions, and stimulating cooperation between science and business. With the support of the World Bank, the Government has made significant progress in creating one-stop shops for easing business startups, has streamlined the process for obtaining construction permits for SMEs and is improving the insolvency law to promote the restructuring of viable enterprises and expedite the resolution of others. The Government also remains committed to promoting R&D, with advice from the World Bank and support from European funds under the Smart Growth Operational Program that will support the innovative activities of enterprises.

In light of the above, I strongly believe that the World Bank can continue to provide valuable support to the Polish Government's reform program. The Bank's financial assistance and expertise will serve as a crucial impetus towards the fulfillment of the program's objectives.

With kind regards,