

The Polish Economy in 2010: A Retrospective View Looking Towards 2011

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“Poland’s macroeconomic performance was strong in the decade leading up to the global crisis, supported by sound economic policies....” John Lipsky, Acting Chairman of the IMF Board

Abstract

This paper discusses the Polish economy in the period 2010 to 2011. It focuses on several positive aspects, including privatization and foreign direct investment and several negative aspects of the economy including unemployment, infrastructure deficits, and deficits in public finances.

Key Words: Poland, economy, privatization, FDI

1. Overall Indicators

Poland was the only member of the European Union in 2009 to post real growth in its GDP (Deutsche Bank, 2011). In 2009, Poland’s GDP grew by 1.7 percent. *Deutsche Bank* estimated that Poland’s GDP grew by 3.4 percent in 2010. The IMF joins *Deutsche Bank* in forecasting that GDP will rise by 3.7 percent in 2011—second only in the European Union to that of Slovakia, which is expected to grow by 4.1 percent (EU Business, 2010). The main driver behind Poland’s economic growth was an increase in domestic demand. The Ministry of Economy fully expects that growth in the economy will continue to stimulate increasing activity in the important industrial and construction sectors. Increases in output were recorded in 28 out of 34 sectors in the Polish economy. It is interesting to note that manufacturers of three products—computers, electronics, and optical products—recorded the highest rise in production, a more than a 40 percent increase. Also experiencing a high rate of growth was the sector involving motor vehicles, trailers, and semi-trailers which grew by 16 percent.

The export sector also performed well. Favorable trends were experienced in sectors that export most of their output or production. In September of 2010, on a year-to-year basis, the value of Polish merchandise exports rose by almost 17.9 percent while the value of imports rose by 24 percent. Poland’s central bank expects that exports will increase approximately 8.8 percent and imports to grow by 11 percent in 2011, with the trade deficit growing to around 2.1 percent of GDP. Ironically, Poland’s economy may have benefitted from its close proximity to Germany—which sports the region’s largest economy and the fourth largest economy in the world (World Bank, 2011).

2. Positive Indicators: Foreign Direct Investment and Privatization

Because Poland was able to avoid the more drastic consequences of the world-wide recession, Poland is now perceived as a large European country with an expanding economy rather than as an amorphous part of the larger region of Eastern and Central Europe mired in stagnation with an uncertain or negative economic future.

Foreign Direct Investment in Poland- A Synopsis (Hunter & Ryan, 2003)

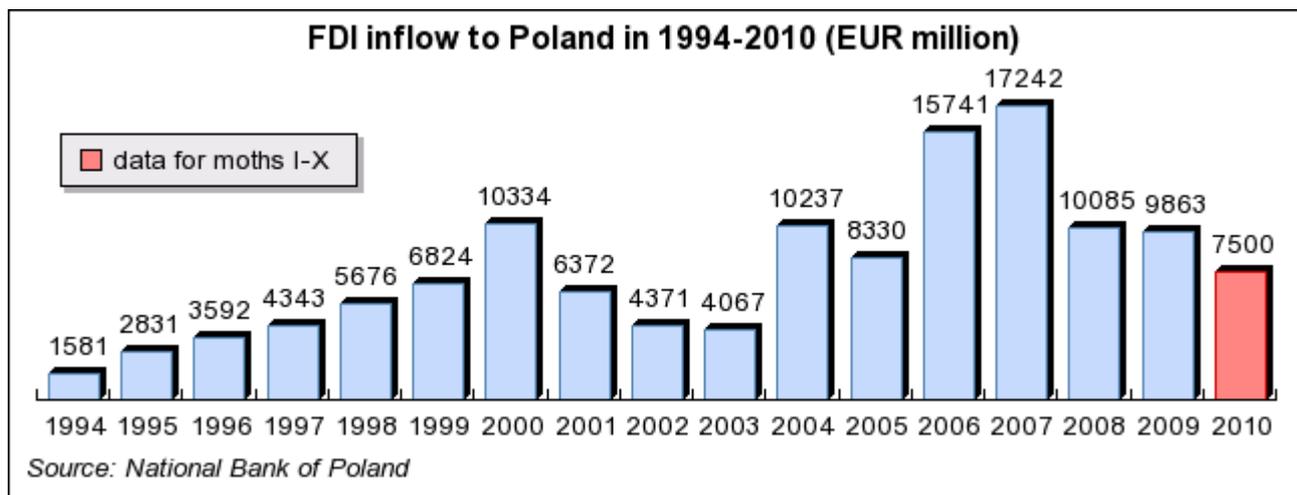
Three factors have been listed as basic preconditions to Poland’s continued success in attracting foreign direct investment [FDI]: Poland’s large potential market, relatively low labor costs, and a well-educated labor force which is able to carry out projects involving a strong advanced technology component. Andrzej Ratajczyk, who writes for the *Warsaw Voice-Business & Economy* section, notes:

“Foreign investors have welcomed the stability of the Polish economy and its prospects for further growth. The Economy Ministry estimates that foreign investment in Poland... is likely to continue at a similar level [to 2010] in 2011” (Ratajczyk, 2011)

In 2010, the total value of new foreign direct investment exceeded 5 billion Euros, representing a 75 percent increase on a year-to-year basis.

In addition, in this same period, the Polish Information and Foreign Investment Agency [PAIiIZ] completed negotiations with foreign investors for 29 new investment projects (PAIiIZ, 2011). The following chart indicates the extent of foreign investment in Poland in the period 1994-2010:

Foreign direct investment in Poland



Current data on investment indicates that FDI has moved away from traditional investments in the manufacturing sector toward investments in highly specialized services and research and development (R&D) in such areas as telecommunications, information technology, machine-building, and aviation, with EUR 9.863 billion or 92% coming from EU states. PAIiIZ reports that fully one-fourth of FDI projects are involved in what are called “intellectual businesses,” which require heightened technological training.

A listing of major investors by percentage of investments in the Polish economy includes:

Country	Value in EUR mn	Share
Germany	2,137	21.73%
France	1,375	13.98%
Luxembourg	1,250	12.71%
Sweden	940	9.56%
USA	895	9.10%
Austria	586	5.96%
Netherlands	478	4.86%
Italy	459	4.67%
Spain	393	4.00%
Other	429	13.73%

This optimistic view of Poland’s ability to attract FDI is bolstered by the latest research coming from the *2010 AT Kearney Foreign Direct Investment Confidence Index* (AT Kearney, 2011) which shows that Poland is considered as one of the world’s best investment locations. According to the Index, Poland ranks sixth in the Index in terms of global investment attractiveness behind China, the United States, India, Brazil, and Germany. Since 2007, the date of the last report, Poland has jumped 16 places, which represents the best improvement in the group of 25 most attractive countries. One concern, however, lies in the fact that software piracy continues to thrive in Poland with the value of illegal software estimated at \$506 million. The existence of piracy to this extent is a continuing impediment to attracting a variety of high-tech business interested in investing in the Polish economy (Warsaw Voice, 2011).

Privatization (Hunter & Ryan, 2004, 2007, 2009a)

The government of Donald Tusk was the first government in Poland since the transformation to prepare a privatization plan for its entire term in office and not for a limited one year period as was the common practice before. Roman Frydman and Andrzej Rapaczynski, two major researchers in the field, delineated four major requirements of the privatization process that would guide future privatization activities:

- Privatization must be accomplished quickly;
- Privatization must be socially acceptable and elicit wide-spread societal support;

- Privatization must assure effective “private” control over the management of the newly privatized enterprises; and
- Privatization must assure access to significant foreign capital and expertise (Frydman & Rapaczynski, 1994).

Key provisions of the plan, organized under the aegis of Treasury Minister Aleksander Grad, were the introduction of transparent privatization rules including information on the progress of any privatization effort, information on the adviser, the purchaser, and the price. Since its inception, the Tusk government has completed in excess of 300 projects. 2010 was an extraordinary year for privatization efforts in Poland (Warsaw Voice, 2010). In fact, some of the EU’s largest initial public offerings (IPOs) were accomplished—including those involving major state owned companies such as the PZU, Poland’s largest insurance group,¹ the Tauron energy group,² and perhaps most importantly, the Warsaw Stock Exchange [WSE] in November 2010.³ Two other large energy groups, Energa⁴ and Enea,⁵ may be privatized by the end of 2012. The value of companies listed on the WSE at the midpoint of 2010 stood at 115 billion Euros. Leading financial institutions from thirty countries—including pension and investment funds, sovereign wealth funds, mutual funds, and university endowments and investments—placed orders for shares on the WSE.

Under plans announced by Prime Minister Tusk, Poland will reap around zł.55 billion from the sales of government stakes in companies over a three year period from 2010 through 2013. The privatization effort has been led by Aleksander Grad, who serves as the Treasury Minister in the coalition government of the Civic Platform (PO) and the Polish People’s Party (PSL). Privatization generated zł.25 billion in revenue in 2010 with expected revenues of zł.15 billion in 2011. Minister Grad completed 400 privatizations in three years and plans to complete another 150 in 2011. Due largely to the privatization projects, the Warsaw Stock Exchange ranked second only after London in terms of the number of IPOs and in total IPO value. There were 25 individual IPOs on the WSE, worth a total of 3.13 billion Euros. In fact, the privatizations of PZU and Tauron had a combined value of nearly 3.02 billion Euros. These IPOs were the largest since the privatization of PKO BP bank which was carried out in 2004—which was worth almost 1.78 billion Euros.

3. Potential Negatives

Unemployment remains a persistent problem in the Polish economy. At the start of 2010, unemployment stood at 11.9 percent, which translated into 1.89 million Poles who were out of work. For the entire year, the unemployment rate stood at 9.6-9.8 percent. 2011 should see a slight reduction to the range of 9.2-9.4 percent, and 8.9 percent in 2012. Another of the potential negatives or “drags” on the Polish economy continues to be the state of *public finances*. Poland’s public debt (sometimes referred to as *sovereign debt*) is now very near to the threshold of 55 percent of GDP.

¹ The privatization of PZU insurance yielded the Treasury zł.5 billion. The auction price was 15 percent higher than the initial issue price. PZU’s debut on the Warsaw Stock Exchange involved 250,000 individual investors. The listing of PZU was the largest IPO in Europe in the three preceding years.

² More than 230,000 individual investors and 120 institutional investors participated in the Tauron privatization. The website of Tauron Group reports: “TAURON Group is one of the largest companies in Poland with share capital of approximately PLN 14 billion. The holding is the largest electricity distributor in Poland. The Group’s distribution grid covers an area of approximately 53,000 square kilometers, which represents approximately 17% of Poland’s total area, and consists of power lines measuring about 187,000 kilometers. In 2009 the Group Companies sold approximately 30.4 TWh of electricity to more than 4 million end clients. In addition, the Group controls approximately 20% of Poland’s total hard coal resources and is responsible for 5% of domestic hard coal production. The TAURON Group is the second largest electricity generator in Poland. In 2010 total capacity of Group’s power plants was about 5,448 MW and annual electricity generation reached 18.2 TWh. TAURON Group’s core business areas: hard coal mining; electricity and heat generation; electricity distribution; electricity trading; and heat distribution and sales. See www.tauron-pe.pl/sites/en/Pages/default.aspx (last visited January 29, 2011).

³ The state retained a 35 percent *controlling interest* in the WSE as its “strategic investor,” with control over strategic decisions regarding the development of the stock exchange’s development. This arrangement is also known as the state retaining a “Golden Share” in a business. ING Investment Management predicts that the WIG Index will increase by “dozen or so percent” in 2011, with small and medium-sized enterprises flourishing. The WSE has established a strategic partnership with the New York Stock Exchange.

⁴ The Energa share offering is targeted at institutional investors—most especially with investors from the power sector. “Energa is one of four great electro-energy holdings in Poland. Headquarters is placed in Gdansk. Group is energy producer, supplier and vendor for over 2.7 millions of Polish households and 300 thousand companies. Energa is national leader in production of energy from renewable sources and one of biggest employers in Poland - it employs over 12.5 thousand persons.” (Energa SA Company Profile). One “glitch” occurred early in 2011 when Poland’s anti-monopoly office [UOKiK] ruled against top utility PGE’s (PGEP.WA) takeover of 84 percent stake at rival Energa worth 7.5 billion zlotys (\$2.6 billion).

⁵ “ENE A S.A. (ENEA) is a Poland based electric energy company engaged in the electricity generation, distribution, and trading in Poland. The company generates electricity mainly from coal and hydro power plants. The company distributes electricity in the north-western part of the Poland.” See www.alacrastore.com/company-snapshot/Enea_SA-3580200 (last visited January 29, 2011). Enea shares are available to individual investors on the WSE. In 2010, 16 percent of the shares were offered on the exchange. The government was offering a 51 percent stake in the company, hoping to raise zł.25 billion.

It is recognized that if the public debt would exceed this threshold, drastic cuts in government spending would have to ensue. Leszek Balcerowicz, former deputy Prime Minister and ex-President of the National Bank (Hunter & Ryan, 2005),⁶ observed: “Budget expenditure, especially welfare spending in relation to GDP is also too high.... Large and growing budget spending hampers economic growth and means that our taxes are too high.... This is why the greatest barrier to our country’s rapid economic growth is the state of public finances....” (Warsaw Voice, Dec. 2010).

A third impediment to increasing growth may be seen in Poland’s poorly developed *transportation infrastructure*. Among the most potentially positive factors in the development and upgrading of Poland’s roads will be the choice of Poland as one of the hosts—along with Ukraine—of the 2012 UEFA [Union of European Football Associations] Euro soccer tournament. It is estimated that approximately 1,400 kilometers [8,500 miles] of national roads are now being constructed or modernized. In addition to 68 kilometers of existing roads, work is being completed on the construction of 735 kilometers of freeways, 510 kilometers of expressways, and 87 kilometers of beltways around Poland’s major cities. The value of these projects is zł.21 billion. Once the 2012 tournament is completed, these infrastructure improvements will be significant permanent improvements to Polish infrastructure. These will include:

- ... The entire A2 freeway from Warsaw to the German border will be opened to traffic in 2012;
- ... The northern section of the A1 freeway from Gdansk to Strykow near Lodz will be opened where the A1 crosses with the A2;
- ... Modernization of Polish airports and railway stations.

These improvements will be vital to increase the share of the tourism sector in Poland’s GDP, which “officially” stands at 6 percent. [By way of contrast, agriculture accounts for 4-4.5 percent of Poland’s GDP—although agriculture accounts for over 11 percent of exports.] Polish agriculture, though vastly improved and having benefitted from EU accession, continues to be somewhat problematic. Agriculture Minister Marek Sawicki reports that 90-95 percent of Polish processing plants are of a “world standard.” However, only about 30 percent of Polish farms are considered as competitive, modern farms. Most of Polish farms are less than five hectares—measuring about 12.355 acres. It is important to note the role that funding from European Union [EU] sources plays in financing needed infrastructure projects. Poland is now the largest beneficiary of EU funds. Poland has to this date absorbed into its economy more than half of the 67.3 billion Euros that had been allocated for the years 2007-2013. Andrej Ratajczyk notes that: “These favorable results are also reflected in European Commission statistics, which show that Poland is the country which absorbs EU funding most efficiently” (Ratajczyk, 2010).

4. Some Tentative Conclusions and Observations

Prime Minister Tusk had originally indicated that 2011 would be a realistic date for Poland to enter the Eurozone. As we approach the midpoint of 2011, there is no indication that Poland will be able to come up with an official schedule for adopting the single European currency that will make this possible (Hunter & Ryan, 2009b).

⁶ It should be noted that the National Bank of Poland was organized in 1945 as a state-owned bank supervised by the Treasury ministry. Under the command-and-control system, however, the NBP was made the responsible party for financial controls over the mining, steel, and textile industries, and for the direct financing of these industries. As such, the NBP was transformed into what is termed as a *monobank*, with a monopoly on the issuance of currency and the granting of loans and collecting savings. The zloty became a non-convertible currency with little or no intrinsic value in a system characterized by endemic shortages. After 1997, the NBP regained its preeminent position as a central bank in a functioning capitalist economy. Responsibility for monetary policy was assigned to the Monetary Policy Council and protecting the zloty and assuring the stability of the system became the main objectives of the NBP.

Under Article 12 of the Law on the National Bank of Poland, the Monetary Policy Council:

- Adopts annual monetary policy guidelines;
- Submits a report on the implementation of monetary policy guidelines to the Sejm;
- Sets central bank interest rates;
- Sets minimum reserve rules and the required reserve ratio;
- Sets the upper limit on obligations resulting from loans taken by the NBP from foreign banking and financial institutions;
- Approves the NBP’s financial plan and report;
- Approves the NBP’s annual financial statement; and
- Sets the rules for open market operations.

In this manner, the NBP operates much in the same fashion as the Federal Reserve in the United States. Under the Monetary Policy Guidelines for 2011, the main goal of the Monetary Policy Council will be to keep inflation at 2.5 percent. *See* www.nbp.pl/en/publikacje/o_polityce_pienieznej/zal2011a.pdf.

One reason that few in Poland seemed overly concerned that the deadline had not been met is the general feeling that Poland may have escaped the recession largely because it was *not* a member of the Eurozone! John Lipsky, the acting chairman of the Board of the International Monetary Fund noted: “Poland’s macroeconomic performance was strong in the decade leading up to the global crisis, supported by sound economic policies” (Associated Press, 2011). Joining the Eurozone is no longer seen as the prime indicator of the general health of the Polish economy. Under projection of the Tusk government, the budget bill has targeted a growth rate of 3.5 percent in 2011; an inflation rate of 2.3 percent; and an unemployment rate that will not exceed 9.9 percent. The target for government revenue is zł.273.27 billion, with public spending set below zł.313.47—leading to a public deficit not exceeding zł.52.2 billion. This figure represents a drop from the zł.40.2 billion experienced in 2010. In order to cut the expected deficit, the government indicated it wished to raise the VAT rates (yielding an additional zł.5 billion) and also to cut expenses of individual government ministries (generally, Hunter & Ryan, 2009b)

In a general business sense, optimism about the future seems to pervade the Polish business community. According to a market survey coordinated by the Polish Chamber of Commerce, 66.7 percent of Polish businesses surveyed expect to boost their sales in 2011. Almost 47 percent of businesses surveyed plan to increase investment in 2011 and 35.1 percent of the business polled planned to expand their work forces. Economists and other observers are anxious to see if the Polish experiment in free market capitalism will stay on its strong glide path in 2011 (e.g., Pienkos, 2010). Certainly, Poland has come a long way since its experiment began in the fall of 1989—then under the leadership of Minister Balcerowicz and the economic team he assembled in order to fundamentally alter the nature of the economic system in Poland. To paraphrase Professor Donald Pienkos of the University of Wisconsin, Milwaukee, in another context, “But in [economics] there is very little if any certainty, especially in times as convulsive as they are in the world today” (Pienkos, 2010, p. 336).

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