

Poland



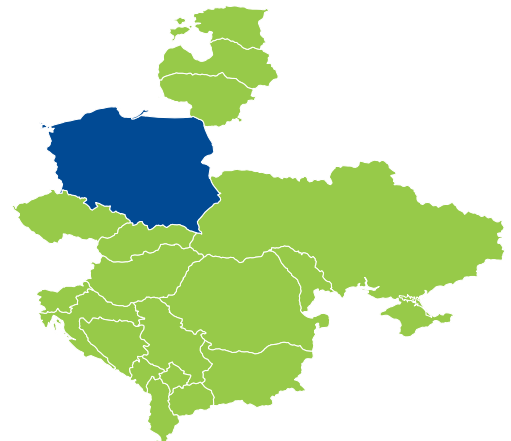
With almost 39 million inhabitants, Poland is the second most populous country (after Ukraine) in the Central European (CE) region. It is also the region's largest economy (eighth in the EU), with GDP totalling EUR 309 billion in 2008. Both its GDP and EU ranking would have been higher but for the weakening of the Polish Zloty (PLN) that took place at the end of 2008 due to foreign capital outflows from CE. However, the global economic crisis may prove to be less painful for Poland than for many other countries, with statistical support for this position emerging after the first quarter of 2009.

Economic growth across 2008 reached 4.9%, but the fourth quarter in 2008 saw this rate fall to 2.9% year-on-year. For 2008 as a whole, household consumption was the engine of GDP growth, growing by 5.4% in 2008 (5.3% year-on-year in the fourth quarter). The economic slowdown rapidly had an impact upon previously positive trends in the labour market. The unemployment rate, for example, stood at 9.5% at the end of 2008 (i.e., just 1.7 percentage points less than a year earlier) and the number of unemployed people at 1.5 million. In December, however, the number of new unemployed rose sharply (up 19% year-on-year), and the number of those deregistering continued to weaken (a trend underway since May 2007). Household incomes continued to register growth in both nominal and real terms, however, which kept consumption at around its pre-crisis level and supported GDP during the following months of 2009.

Investment growth in 2008 was 8.2%, falling to 4.6% in the fourth quarter. An important element of this growth was driven by outlay from EU funds. According to a report on the use of EU funds, expenditure on implementing investments from the cohesion funds (mainly road-building) accelerated strongly in 2008,

with combined year-on-year growth (together with structural funds) standing at 27% in the fourth quarter. Construction production data also confirmed this, showing that double-digit year-on-year growth (13%) was maintained by sales of services connected with highway, road and bridge-building.

Exports and imports were quite robust throughout 2008 (growing in real terms respectively by 7.2% and 8.2%). In the fourth quarter though, the global financial crisis started to reveal its influence with exports to the EU falling by 1%, to Italy and Hungary by about 15%, to Germany by just under 1%, to France by 0.4% and to Ukraine by 16%. The risk to Poland's balance of payments affected the Zloty, with the final quarter of 2008 marking the end of its appreciation in annual terms. In December, the average Zloty exchange rate weakened by 11.3% year-on-year against the Euro (to 4.01) and by 19.7% year-on-year against the USD (to 2.96).



The first months of 2009 brought with them record falls in the Zloty, to a level of 4.8975 against the Euro (on 17 February), the same as noted almost exactly five years earlier (20 February 2004). The Zloty's fall against both the Euro and the USD was close to the largest of all emerging countries in the Americas, Asia and Central Europe. For example, in January 2009, the Zloty lost on average 43% year-on-year against the Euro, while the Romanian Leva and the Hungarian Forint both lost 15.5% year-on-year and the Russian Rouble lost 26% year-on-year.

Given the strength of the Polish economy, the Zloty's decline appears perplexing, but there were a number of factors that can provide some context: speculative attacks on the foreign exchange market; rising cost of closing open positions on currency options by organizations; the depository policies of Western parent banks, resulting from pressure to achieve liquidity in the countries where the capital originated.

The global financial crisis arrived in Poland when the first symptoms of economic overheating appeared throughout CE. The current account deficit set a new record, reaching 6.4% of GDP in 2008. Mortgage loans, including foreign currency products, were up by over 50% year-on-year as well, while increased household debt fuelled private consumption to growth levels ahead of GDP (6.4% versus 5.4%). Enterprises became less averse to risky investment decisions, such as purely speculative transactions on the financial markets, while the valuation of financial assets, from stocks to properties, lost contact with economic fundamentals in a manner similar to the situation in developed countries.

The pro-cyclical fiscal policy of recent years has not helped reduce Poland's general government deficit that has averaged 3.2% of GDP from 2005 to 2007 and grew to 4.6% of GDP in 2008. This was irrespective of 2008's 4.9% GDP growth, down from the average 5.5% achieved from 2005 to 2007. Polish governments of recent years have been unable to launch any fiscal or structural reforms. The most recent successful self-government reforms, partially successful pension reforms, and disastrous health care reforms were implemented as long ago as 1999. On the other hand, Poland's accession to the EU in May 2005 proved to be a great political

and economic success, stabilising the situation in the country. Support for this move has not dropped below 75%, and the highest increase was recorded among farmers covered by the Common Agricultural Policy. Political parties seeking to exploit anti-EU resentment lost votes and seats in the Polish and European parliaments after the elections of October 2007 and June 2009 respectively. EU funding is a powerful growth factor, second only to household consumption, and practically all investment activities in early 2009 were related to the resources provided by the EU.

By the end of the first quarter of 2009, the Polish economy was the only EU economy registering GDP growth in both quarterly and yearly terms (0.8% year-on-year). The Polish banks were surprisingly resistant to the financial crisis, as non-performing loans barely exceeded 5%, and Polish companies remained sufficiently conservative to finance most of their investments from retained earnings. The abolition of the highest personal rate of income tax (40%) in 2009 has increased household disposable incomes, which together with continued wage growth is affecting retail sales positively. The stimulus packages of the biggest EU countries (particularly Germany) have helped maintain positive industrial production dynamics, especially in the car industry. Imports dropped significantly in the early months of 2009, as the result both of a decline in exports (most imports to Poland are related to exports) and the weakening of the Zloty. As a result, the current account deficit declined by 11% year-on-year in 2009's first quarter and by 54% year-on-year in the second, to below 3% of GDP. In this way, Poland was shown to be much less dependent on external circumstances and foreign trade than other, smaller CE economies.

The near future will show whether Poland can manage to escape recession, and if the upcoming self-government and presidential elections (in the spring and autumn of 2010) will not see the introduction of populist economic policies, which could undermine weak but still positive GDP dynamics. As in other CE countries, the issue of entry to the Eurozone appears to be on hold until parliamentary elections (due in 2011). The ambitious privatisation plan proposed by the government may prove to be more important for the future performance of the Polish Zloty and efficiency-growth at a microeconomic

level. It includes the sale of state assets in the energy and chemical sectors, as well as minority share-holdings in already privatised companies, to realise revenues of around PLN 36.7 billion (roughly EUR 9 billion) before the end of 2010. With the government's general reluctance

to raise taxes or increase the national debt, financing the deficit with privatisation revenues looks to be the next-best option (after reducing government spending), always assuming that the global crisis does not become a long-term phenomenon.

Poland	2005/2007 Average Values	2007-2008	2008
	Change (%)	Change (%)	
Population (mil.)	-0.1	0.0	38.5
Average monthly gross wage (EUR)	10.9	-6.6	752.5
EUR Exchange rate vis-à-vis	-4.0	14.3	4.1
USD Exchange rate vis-à-vis	-5.8	20.1	3.0
	Real change (%)	Real change (%)	EUR mil.
GDP	5.5	4.8	309,040
Private consumption	4.0	5.4	186,671
Public consumption	4.9	0.2	57,298
Gross fixed capital investments	12.9	7.9	67,888
Exports (goods and services)	10.6	5.8	122,906
Imports (goods and services)	12.7	6.2	134,343
	Nominal change (EUR mil.)	Nominal change (EUR mil.)	EUR mil.
Trade balance	-2,128	-1,498	-21,016
Current account balance	-2,154	-5,038	-19,647
General government balance	1,930	-8,256	-14,105
General government gross debt	13,523	-1,219	145,273
External debt	2,263	2,977	37,457
Foreign currency reserves	3,943	3,496	40,637
	Percentage point change	Percentage point change	%
Economic activity rate	-0.2	0.5	54.2
Unemployment rate	-2.6	-1.7	9.5
CPI rate (previous year = 100%)	-0.2	-0.4	3.4
Central bank interest rate	-0.5	0.0	5.0
1-year yield on Treasury Bill	-0.2	-0.5	5.3
10-year yield on Treasury Bond	0.1	-0.5	5.5

Sources used: Reuters EcoWin Pro

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