JCR

ISSUER REPORT

April 27, 2021

12061

Poland

Chief Analyst Toshihiko Naito
Analyst Haruna Saeki

Long-term Rating	A
Outlook*	Stable
Short-term Rating	-

* Long-term Rating refers to Foreign Currency Long-term Issuer Rating in principle.

1. Overview

Poland is the largest economy in Central and Eastern Europe with a nominal GDP in excess of USD 590 billion and a population of 38 million in 2020. Following the economic transition and subsequent radical economic reforms, the country experienced a significant economic deterioration in the early 1990s. Since then, it has transformed its economic structure mainly through economic and fiscal reforms and inflow of foreign direct investments (FDI) from the EU countries as well as utilization of EU funds. It joined NATO in 1999 and acceded to the EU in 2004. Even amid the economic stagnation in the EU countries during the global financial crisis and the European sovereign crisis, the Polish economy continued growing without interruption. The conservative Law and Justice (PiS) upholds a policy of inclusive economic growth with commitment to complying with both the EU and domestic fiscal rules.

2. Sociopolitical Base and Economic Policy

Since the country's first free election held in 1991, the system of parliamentary democracy has been functioning as exemplified by a multi-party system and change of administration. In the process of its EU entry negotiation, Poland had to make a major review of its political, economic and fiscal systems. The systems in conformity with the EU standards have been put in place to ensure political and social stability. PiS, then the country's largest opposition party, won both the presidential election in May 2015 and the general elections in October 2015. The party took power for the first time in eight years by winning a working majority in the upper and lower houses of parliament. The current prime minister is Mateusz Morawiecki, the former deputy prime minister and finance minister. In the latest general elections held in October 2019, PiS was re-elected on the back of high public support. Incumbent President Andrzej Duda, supported by PiS, was also re-elected in the presidential election in July 2020.

PiS is originated from the anti-communist Solidarity trade union and is a conservative Christian democratic party. The party leader is Jaroslaw Kaczynski, who is the most influential person in politics. The party puts priority on enhancement of social welfare and intervention in economic management. In foreign policy, it looks to strengthen the relationships with the EU and the United States, but currently takes a cautious stance toward introduction of the euro. Since taking office, the PiS government has pushed ahead with contentious amendments of the laws regarding the Supreme Court and public media. The European Commission (EC) found that the revision of the constitutional court law could threaten the rule of law and has been recommending the Polish government to take appropriate corrective measures. In December 2017, the EC decided to trigger Article 7 of the Lisbon Treaty. The heaviest possible sanction under Article 7 would be suspension of Poland's voting rights in EU institutions. Following the advisory made by the European Court of Justice, the government partially scrapped its judicial reforms in a bid to avoid enforcement of sanctions. Even when the EC should decide to invoke sanctions, they would be hardly practicable because they require a unanimous vote and the Hungarian government has already indicated its opposition.

In conformity with the EU's 2021-2027 Multiannual Financial Framework and its recovery fund, the EC is considering possible imposition of sanctions such as a freezing of funds from the EU budget on the countries that do not comply with its “rule of law” principle. However, concrete methods for enforcement of its new rules have not been fixed yet. Poland had already established high-level political, social and economic systems in its EU accession process. JCR holds that unless the issue leads up to a substantial reduction of EU fund allocations, its impact will be rather limited.

The government’s priorities in economic and fiscal policies had been promotion of inclusive growth with commitment to keeping the fiscal deficit below 3% of GDP. It has implemented various measures to enhance social benefits, reduce household burdens and invigorate the labor market. On the fiscal front, it has been working to contain the fiscal deficit by enhancing tax compliance and adhering to the expenditure rule. In response to the COVID-19 pandemic, it practically closed the borders and restricted the movement of people in mid-March of 2020. Such strict restrictions were eased toward the summer and more moderate measures have been put in place following a second wave of the pandemic since the autumn. The country is now facing a third wave of the pandemic but vaccination has also been gradually making progress. In order to support companies and households, the government has implemented a large-scale economic package equivalent to around 15% of GDP. The package mainly consists of fiscal measures such as waiver of social security contributions and wage compensation, financial support to companies by the Polish Development Fund (Financial Shield), and guarantees for corporate loans through the BGK (national development bank). Loans provided under the Financial Shield are converted into subsidies when companies meet certain conditions such as maintenance of employment.

3. Economic Base

Poland is a relatively advanced economy with its per capita GDP (in ppp terms) in 2020 estimated to have exceeded USD 33,000, which is slightly higher than the average of sovereigns rated in the A range by JCR. Its industrial structure is diversified, encompassing logistics hubs and outsourcing business lately in addition to the traditional manufacturing such as steel, car and electric appliances and wholesale/retail. Since the middle of the 1990s, the country has attracted FDI mainly from other European countries and deepened its economic relationship with those countries through international trade and finance. The outstanding balance of FDI on an IIP basis at the end of 2020 stood at around 50% of GDP. Poland is firmly integrated into the EU's supply chain, with above 70% of its exports bound for the EU member countries, including close to 30% bound for Germany alone. Since its accession to the EU, the country has been receiving a substantial amount of subsidies from the EU funds and the government has been upgrading the social infrastructure by effectively using them. It was entitled to receive EUR65 billion (equivalent to 21% of 2007 GDP) between 2007 and 2013 and more than EUR76 billion (equivalent to 18% of 2014 GDP) between 2014 and 2020. It is to receive EUR75 billion (equivalent to 14% of 2020 GDP) between 2021 and 2027. In addition, it has been allocated up to EUR23.9 (in current prices) billion (equivalent to around 4.5% of 2020 GDP) in subsidies from the “Recovery and Resilience Facility” of the EU recovery fund.

Meanwhile, Poland’s population began declining in the late 1990s, giving rise to concern over future supply of labor force as the economy kept expanding before the pandemic. In addition to an increased employment rate and a reduced unemployment rate, the inflow of foreign workers mainly from Ukraine has been helping to ease the labor shortage. Electricity consumed in the country is mainly generated with the coal produced at home, but the government is planning to diversify power sources through a shift to renewable energies and nuclear power. Other energy resources such as oil and natural gas are mostly imported from Russia.

4. Economic Trends

The Polish economy had kept growing uninterruptedly until 2019 led by stable domestic demand with annual growth rates averaging close to 5% between 2017 and 2019. The economic growth decelerated in 2019 but remained high at 4.5% on robust consumer spending brought by increased wages and employment and solid investment prompted by a massive inflow of EU funds. The country faced a labor shortage with the unemployment rate falling to a record low of 3.3% in 2019. However, inflation remained contained as a rise of wages had been partly offset by improved productivity.

Due to the impact of the restrictive measures taken to address the pandemic, Poland's real GDP contracted 8.4% year-on-year in the second quarter of 2020. The economic activity resumed thereafter along with the relaxation of the restrictive measures, with the contraction easing significantly to 1.5% in the third quarter of 2020. The growth rate in the fourth quarter of 2020 was affected by the second wave of the pandemic, but the decline was limited as compared to the second quarter. The economy shrank 2.7% in 2020 for the first full-year negative growth since the economic transition. Nevertheless, the deterioration was relatively modest among the EU countries as consumer spending declined only slightly and exports remained almost close to the previous year's level. On the other hand, investment recorded a huge drop. As for developments in the labor market, an increase of unemployment remains curbed. This seems to be due to the employment support measures taken by the government and companies in addition to the tightened labor market prior to the pandemic. The impact of the recent pandemic, which are continuing to weigh on the economy, is expected to subside in the second half of 2021 as vaccination progresses and the restrictive measures are relaxed. Capital inflows from the EU funds and the recovery fund are also expected to support a pickup of investment. JCR expects that a full-year economic growth will recover to around 4% in 2021 and remain in the range of 4-5% in 2022 and 2023.

5. Financial System

The country's financial system stays stable. In the process of privatization in the 1990s, many major Polish banks excluding PKO BP, the country's largest bank, became subsidiaries of major European banks. The bank lending to the private sector remained not so high at slightly above 50% of GDP at the end 2020, and it has been growing close to the nominal GDP growth rates in recent years. Banks registered solid earnings in 2020 by absorbing the higher credit costs resulting from the economic downturn. Their nonperforming loans ratio slightly rose to 6.9% at the end of 2020 from 6.5% a year earlier. A moratorium on loan repayments has been in place as part of anti-pandemic support measures. The outstanding balance of loans under moratorium fell to 1.2% of the total lending as of the end of 2020 from the peak of around 10% in mid-year. Some of these loans may become nonperforming after the end of the moratorium period, but JCR holds that banks will be able to absorb any additional credit costs with their profit. Their capital adequacy ratio stayed high at around 20% at the end of 2020.

With regard to the conversion of CHF-denominated mortgage loans into PLN at non-market exchange rates, borrowers can sue their bank if they find something wrong in their loan contract. The outstanding balance of such loans kept shrinking to account for less than 10% of the total stock of outstanding loans at the end 2020. Moreover, the credit quality of those loans stays sound as compared to that of PLN-denominated loans because borrowers are financially better off. Banks have already set aside a certain amount of provisions in preparation for litigation risks. However, they may need additional provisions if they face more lawsuits. JCR will monitor future developments of this issue.

6. External Position

Poland's current account balance ended in a surplus equivalent to 3.6% of GDP in 2020. The surplus expanded significantly from a year earlier because a trade surplus increased as imports slowed on bleak demand at home while exports stayed unabated. The country's external liquidity stayed solid as it enjoyed a net capital inflow amid an increased current account surplus and the continued inflow of EU funds. The primary income balance remains in chronic deficit as the foreign owners of Polish firms receive a large share of their profit. On the other hand, the country's transportation and business service exports have been growing markedly in recent years, with its structurally increasing service balance surplus more than offsetting a primary income balance deficit. Capital account mainly consisting of net capital inflows from the EU funds in 2020 amounted to 2.4% of GDP.

The country's net external liabilities on an IIP basis and gross external debt shrank to 44% and 60% of GDP, respectively, at the end of 2020, which were comparable to those of other sovereign governments rated in the A range by JCR. The public and private sectors respectively accounted for 36% and 64% of the external debt. Intercompany loans, a more stable source of funding, accounted for more than 40% of the debt owed by the private sector. The country's foreign exchange reserves increased to EUR 125.6 billion at the end of 2020, or equivalent to 5.9 times of its monthly goods and services imports and 2.9 times of its short-term external debt (excluding intercompany loans).

7. Fiscal Base

Prior to the outbreak of the pandemic, the country had made good progress on fiscal consolidation thanks to increased tax revenues resulting from economic expansion and intensified tax compliance and adherence to the expenditure rule. Its general government fiscal deficit (ESA 2010) had been kept below 3% of GDP since 2015 and was curbed to below 1% in 2018 and 2019. The general government debt (ESA 2010) also shrank to 45.6% of GDP at the end of 2019.

The government had initially planned to contain the fiscal deficit at 1.2% of GDP. However, the deficit is actually estimated to have widened to 7% of GDP due to a sizable increase of expenditures necessitated by the implementation of the economic package and a slower growth of tax revenues amid the economic deterioration. JCR estimates that the total size of the measures in the economic package that have an impact on the fiscal balance is around 5% of GDP. The general government debt (ESA 2010) increased to 57.5% of GDP at the end of 2020, but it was still at a level comparable to those of other sovereigns rated in the A range by JCR. The State Treasury debt (national definition) structure also improved, with the ratios of foreign currency-denominated debts and those held by nonresidents falling to 24% and 34%, respectively, at the end of 2020. Japan, Luxemburg and the Netherlands were the major nonresident creditors on the domestic Treasury Securities market with a combined share in excess of 50% (excluding omnibus accounts). Other creditors were geographically diversified. Average debt maturity was relatively longer at 4.6 years.

In the 2021 budget plan, the government set the general government deficit at 6% of GDP. Economic stimulus measures related to the pandemic are in place in 2021 such as the second phase of the Financial Shield, but they are smaller in size than those implemented in 2020, as the support has been targeted only at selected sectors of the economy, which have been affected by reintroduced sanitary restrictions due to the second and the third wave of the pandemic. Other than the economic stimulus measures, main measures include the provision of additional pension bonus. However, the government adheres to prudent fiscal management by trying to expand revenues through increased tax collections. JCR holds that the budget deficit will shrink in 2021 as the economy recovers and that the general government debt-GDP ratio will start declining within a few years.

8. Outlook and Overall Assessment

The rating on Poland mainly reflects the country's diversified and stable economic base, prudent fiscal management and solid external liquidity. Its outlook is Stable. Due to the impact of the pandemic, the Polish economy contracted, albeit relatively modestly, in 2020. The public finance deteriorated as a result of the implementation of a fiscal package aimed to support the economy. Nonetheless, the general government debt remained at a manageable level in GDP terms as the country had secured sufficient fiscal leeway as a result of the fiscal consolidation in the past years. JCR expects that the economy will recover solidly and fiscal consolidation will resume once the impact of the pandemic recedes.

The levels of the country's net external liabilities and gross external debt in GDP terms, which had been constraining the rating, have steadily improved in recent years. Meanwhile, the implementation of the economic package to mitigate the impact of the pandemic has resulted in deterioration of the country's public finance. Future improvement of the public finance will be a positive factor for the rating. On the other hand, the rating will come under downward pressure if a prolonged pandemic and a substantial reduction of EU fund allocations resulting from sanctions have material impacts on the economy and public finance.

12061 Poland

Selected economic and fiscal indicators

		2016	2017	2018	2019	2020
Nominal GDP	USD billions	472.0	587.4	585.7	595.9	594.2
Population	millions	38.4	38.4	38.4	38.4	38.0
Per capita GDP in PPP	USD	28,310	30,180	31,890	34,510	33,620
Real GDP growth rate	%	3.1	4.8	5.4	4.5	-2.7
Consumer price inflation(Eurostat)	%	-0.2	1.6	1.2	2.1	3.7
Unemployment rate(Eurostat)	%	6.2	4.9	3.9	3.3	3.2
General government revenues/GDP	%	38.7	39.8	41.3	41.1	41.7
General government expenditures/GDP	%	41.1	41.3	41.5	41.8	48.7
General government balance/GDP	%	-2.4	-1.5	-0.2	-0.7	-7.0
General government debts/GDP	%	54.3	50.6	48.8	45.6	57.5
Current account balance/GDP	%	-0.5	0.1	-1.0	0.5	3.6
External debts/GDP	%	75.2	68.4	63.6	59.3	60.3
Net international investment position	%	62.5	62.2	55.4	49.9	43.7
External debts/Export G&S	%	144.5	126.0	114.9	106.9	103.9
Foreign exchange reserves/Monthly import G&S	Times	6.0	4.6	4.5	4.6	5.3
Foreign exchange reserves/Short-term external debts	Times	2.1	2.1	2.2	2.1	2.4

(Sources)
Eurostat, Statistics Poland, Ministry of Finance, and National Bank of Poland

Ratings

	Rating	Outlook*	Amount (millions)	Currency	Rate (%)	Issue Date	Maturity Date	Release
Foreign Currency Long-term Issuer Rating	A	Stable	-	-	-	-	-	2021.03.29
Local Currency Long-term Issuer Rating	A+	Stable	-	-	-	-	-	2021.03.29
No.6 Yen Bonds	A	-	60,000	JPY	2.62	2006.11.14	2026.11.13	2021.03.29
No.13Yen Bonds	A	-	10,000	JPY	2.50	2012.11.08	2027.11.08	2021.03.29
No.7 Yen Bonds	A	-	50,000	JPY	2.81	2007.11.16	2037.11.16	2021.03.29

History of Long-term Issuer Rating (Foreign Currency Long-term Issuer Rating or its equivalent)

Date	Rating	Outlook*	Issuer
2002. 05. 31	BBB+	-	Poland
2003. 05. 08	A-	Stable	Poland
2008. 02. 26	A-	Positive	Poland
2008. 12. 16	A-	Stable	Poland
2013. 03. 01	A	Stable	Poland

*Outlook for Foreign Currency long-term issuer rating, or direction in case of Credit Monitor

Japan Credit Rating Agency, Ltd.
Jiji Press Building, 5-15-8 Ginza, Chuo-ku, Tokyo 104-0061, Japan
Tel. +81 3 3544 7013, Fax. +81 3 3544 7026