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Poland

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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 EUR 466 billion and a population of 38.4 million in 2017. Following the economic transition and subsequent radical economic reforms, the country experienced 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) 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) took power in the general election in October 2015. Backed by its stable political base, it has been putting priority on promotion of inclusive growth with commitment to keep 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. New systems in conformity with the EU standards have been put in place to ensure political and social stability. The then largest opposition party PiS won both the presidential election in May 2015 and the general election 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. In December 2017 PiS decided to reshuffle the cabinet after consultation between the then prime minister Beata Szydlo and Jaroslaw Kaczynski, the leader of PiS and the most influential person in politics. Mateusz Morawiecki, the former deputy prime minister and finance minister, was appointed as new prime minister. New prime minister intends to seek softer stance with the EU relationship. Meanwhile, the recent opinion poll suggests that PiS maintains high popularity and is likely to be reelected in the next election in the fall of 2019

PiS is originated from the anti-communist Solidarity trade union and is a conservative Christian democratic party. It puts priority on enhancement of social welfare and intervention in national economy. In foreign policy, it looks to strengthen the relationships with the EU and the U.S., 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 constitutional court and public media. The constitutional court was reorganized to require resolutions to be voted by a two-third majority instead of a majority. The amended public media law empowered the government to dismiss or replace the management of public TV and radio.

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 measures since July 2016. In December 2017, the EC made a decision to trigger Article 7 of the Lisbon Treaty. The most serious sanction possible under Article 7 would be suspension of Poland's voting rights in EU institutions. However, such sanctions would be hardly practicable because they require a unanimous vote and the Hungarian government has already indicated its opposition. As such, this issue has so far had a limited impact on the Polish economy.

Under its economic and fiscal policies, the government puts priority on promotion of inclusive growth with commitment to keep the fiscal deficit below 3% of GDP. It has implemented its major election promises such as a child benefit program and a lower retirement age, but has managed to keep the fiscal deficit below 3% of GDP since 2015. The government has substantially scaled down its initial plan to convert CHF mortgage loans to PLN in light of its serious impact on the financial system. It has yet to take effective measures to stem the country's negative demographic trends and ensure the independence of the constitutional court. It is likely that the government will proceed to implement its policy more carefully by assessing possible fiscal and economic impacts.

3. Economic Base

Poland is a relatively advanced economy with its per capita GDP (ppp) standing close to USD 30,000, which is comparable to 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 introduced FDI mainly from other European countries and deepened its economic relationship with those countries through international trade and finance. The outstanding balance of FDI at the end of 2016 was equivalent to approximately 50% of GDP. Poland is firmly integrated into the EU's supply chain, with 80% 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 transfers from the EU funds and the government has been upgrading the social infrastructure by effectively using them. It was entitled to receive EUR65 billion or 21% of GDP (in 2007) between 2007 and 2013 and more than EUR76 billion or 18% of GDP (in 2014) between 2014 and 2020. Meanwhile, Poland's population began declining in the late 1990s, giving rise to concern over future supply of labor force. Currently, more than one million Ukrainians are estimated to stay in Poland as migrant workers, helping to ease the labor shortage. Electricity consumed in the country is mainly generated with the coal produced at home. Other energy resources such as oil and natural gas are mainly imported from Russia.

4. Economic Trends

The economy has been growing uninterruptedly since 1992 mainly led by domestic demand. Annual growth rates averaged higher than 3% in the past five years. The economic growth accelerated to 4.6% (preliminary) in 2017 from 2.9% in 2016, due primarily to robust consumer spending brought by increased wages and employment and child benefit program, and solid investment prompted by a massive inflow of EU funds allocated for 2014-2020. The country faces a labor shortage as the unemployment rate fell below 5% to a record low in 2017. However, the continued inflow of migrant workers may ease the problem at least in the short term. The central bank adopts inflation targeting (2.5% plus and minus 1 percent point). Consumer price inflation turned upward in late 2016 on the recovery of food and energy prices and currently is below 2%. The central bank has been keeping its policy rate unchanged since March 2015. Domestic demand continues to remain strong, but it may moderately slow down in 2018 and 2019. Barring abrupt deterioration of the external environment, however, the economy is likely to grow faster than 3% in 2018 and 2019 amid moderate price inflation.

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. A major change occurred in June 2017 when Bank Pekao, the country's second largest bank and a subsidiary of Italian UniCredit bank, was acquired jointly by PZU, Poland's largest insurance company, and the state-owned Poland Investment Fund. Bank lending to the private sector remained moderate at around 50% of GDP at the end 2017, with lending growth mirroring the nominal GDP growth in recent years . The banks continued to register solid earnings in 2017 despite additional cost burdens such as a bank tax. They have been building up their capital position amid a falling nonperforming loan ratio. Their capital adequacy ratio rose to 19.0% at the end of 2017 from 17.7% a year earlier as the nonperforming loan ratio dropped to 6.8% from 7.1%.

In January 2016, President Andrzej Duda launched a plan to convert CHF mortgage loans to PLN at non-market exchange rates, which had been one of his election promises. However, the president had to make a major revision of his initial proposal in light of its significant impact on the financial system. The latest proposal unveiled in August 2017 gave banks incentives to promote the voluntary conversion. The newly created sub-fund within the already existing Borrowers Support Fund, financed with the mandatory quarterly contributions by banks, would compensate them for the cost of the conversion. Annual contributions by the banks could maximally reach around PLN 3 billion, which can be sufficiently covered by their annual pre-prevision profit, however the draft law only settles maximum value of contributions. Their final, actual value would be made by the board of the Fund taking into account opinion of the Financial Stability Committee (acting as a macroprudential supervisor in Poland). Strict financial supervision has contained the growth of foreign currency-denominated mortgage loans and the outstanding balance of CHF loans as of end 2017 remained less than 10% of total bank loans. Moreover, the credit quality of those loans stays sound as the financial standing of FX borrowers is on average better than zloty ones. Given the situation, the government may implement the revised proposal ahead of the next general election, but not many borrowers are expected to apply for the conversion.

6. External Position

Poland's external liquidity has been improving thanks to a modest current account surplus in 2017 and the continued inflow of EU funds. While the trade surplus narrowed on increased goods imports amid strong domestic demand, a service balance surplus kept on growing, almost offsetting a chronic primary income deficit. The country's transportation and business service exports have been growing markedly in recent years. The primary income balance keeps deficit as the foreign owners of Polish firms receive a large share of the profits. While a net capital balance inflow mainly originated from the EU funds reduced to 1.3% of GDP in 2017, the annual inflows averaged almost 2% in the past five years.

The country's external debt shrank to less than 70% of GDP at the end of 2017, which was still relatively higher as compared to those of other sovereign governments rated in the A range. The public and private sectors respectively accounted for 42% and 58% of the debt. As for the debt owed by the private sector, intercompany loans made by more stable financing sources accounted for more than 40% of its total. The country's foreign exchange reserves exceeded EUR 90 billion at the end of 2017, or equivalent to 4.7 times of its monthly goods and services imports and 2.2 times of its short-term external debt (excluding intercompany lending) as of the end of 2017. The government ended in November 2017 (initial expiry date was January 2019) the IMF Flexible Credit Line, to which Poland had an access in the form of a two-year precautionary mean of SDR 6.5 billion (about EUR 8.2 billion) reduced from SDR 15.5 billion in January 2017.

7. Fiscal Base

Poland was relieved of the EU's excessive deficit procedure in June 2015 for the first time since 2009. It has since been keeping its fiscal deficit below 3% of GDP. The general government fiscal deficit (ESA 2010) in 2017 fell to 1.5% of GDP (2.9% under the budget plan). Increased tax revenues resulting from the economic expansion and intensified tax compliance more than offset the additional fiscal burdens, such as full-year contributions to the child benefit program implemented in April 2016 and expenses related to the lower retirement age introduced in October 2017. The general government debt (ESA 2010) at the end of 2017 contracted to 50.6% of GDP from 54.2% a year earlier. The debt structure also improved, with the ratios of foreign currency-denominated debts (owed by the central government) and those held by nonresidents falling to 31% and 51%, respectively, at the end of 2017 from 35% and 58% at the end of 2015. Japan, Luxemburg and the U.S. were the major nonresident creditors with a combined share in excess of 50%. Other creditors were geographically diversified. Average debt maturity is relatively longer with over five years.

With Poland's local elections and general elections expected to take place in the fall of 2018 and 2019, respectively, the government envisages keeping the fiscal deficit at 2.7% of GDP in 2018 (according to the Budget Act for 2018) and cutting the deficit further in 2019 and 2020. In order to meet the annual extra burdens necessitated by the lower retirement age in 2018, the government is counting on a spending curb based on the expenditure rule, a wage freeze for public workers and a higher tax revenue. JCR holds that the targeted fiscal deficit will be achievable in view of the stable economic expansion in the past and the government's continued tax compliance efforts. Nonetheless, some additional expenditure cuts will be needed to ensure a sustainable reduction of the fiscal deficit.

8. Outlook and Overall Assessment

The ratings are primarily supported by the country's diversified and stable economic base, containment of the fiscal deficit and government debt, and improving external liquidity. On the other hand, the ratings remain constrained by its relatively large external debt. The outlook of the ratings is Stable. The ruling PiS, backed by its stable political base, continues to put priority on promotion of inclusive growth with commitment to keep the fiscal deficit below 3% of GDP. While the government has implemented a package of measures to lower household fiscal burdens, it has so far succeeded in containing the fiscal deficit thanks to increased tax revenues brought by the economic expansion and enhanced tax compliance. The country's financial system has added to stability and the current account has begun generating a modest surplus. It is likely that Poland will keep its stable economic growth mainly led by domestic demand.

On the other hand, the ratings will be negatively affected if the followings factors have material impacts on economy and public finance; deterioration of the external environments mainly economic condition of the EU; intensification of labor shortage: and imposition of EU sanctions including suspension of the voting rights or disbursement of the EU fund.

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Selected economic and fiscal indicators

		2013	2014	2015	2016	2017E
Nominal GDP	EUR billions	395	411	430	426	471
Population	millions	39	39	38	38	38
Per capita GDP in PPP	USD	24,412	25,382	26,567	27,632	29,500
Real GDP growth rate	%	1.4	3.3	3.8	2.9	4.6
Consumer price inflation	%	0.8	0.1	-0.7	-0.6	2.0
Unemployment rate	%	10.3	9.0	7.5	6.2	4.9
General government revenues/GDP	%	38.5	38.7	38.9	38.7	39.0
General government expenditures/GDP	%	42.6	42.3	41.6	41.2	41.0
General government balance/GDP	%	-4.1	-3.6	-2.6	-2.3	-1.5
General government debts/GDP	%	55.7	50.3	51.1	54.2	50.6
Current account balance/GDP	%	-1.3	-2.2	-0.5	-0.3	0.3
External debts/GDP	%	70.7	71.4	70.5	74.9	66.5
External debts/Export G&S	%	152.7	150.2	142.5	143.3	125.7
International reserves/Monthly import G&S	Times	4.9	4.9	4.9	6.0	4.7
International reserves/Short-term external debts	Times	2.1	2.5	2.4	2.1	2.2

* Figures for the most recent period could be indicators based on preliminary figures.

(Notes)
1 Figures for general government balance and debt are preliminary release made by the government
2 Other figures for 2017 are actual result or estimation made by JCR
(Sources)
Statistics Poland, Ministry of Finance, and National Bank of Poland

Ratings

(billions of yen)

	Rating	Outlook*	Amount	Rate (%)	Issue Date	Maturity Date	Release
No. 14 Yen Bonds	A	-	50	0.67	2013.11.15	2018.11.15	2018.03.29
No. 15 Yen Bonds	A	-	10	0.91	2013.11.15	2020.11.13	2018.03.29
No. 4 Yen Bonds	A	-	50	2.24	2005.11.18	2021.02.18	2018.03.29
No. 6 Yen Bonds	A	-	60	2.62	2006.11.14	2026.11.13	2018.03.29
No. 13 Yen Bonds	A	-	10	2.50	2012.11.08	2027.11.08	2018.03.29
No. 7 Yen Bonds	A	-	50	2.81	2007.11.16	2037.11.16	2018.03.29
Foreign Currency Long-term Issuer Rating	A	Stable	-	-	-	-	2018.03.29
Local Currency Long-term Issuer Rating	A+	Stable	-	-	-	-	2018.03.29

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

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