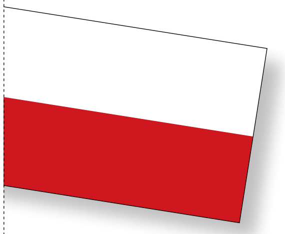


Poland

A healthy banking sector, large population and low wages are some of the strengths of this steadily rising European economy, writes Marcin Mrowiec

Poland, with more than 38 million inhabitants, is the largest nation in Central and Eastern Europe (CEE). It reinforced its image as a steadily rising economy following the global financial crisis, when it was the only country in the EU to enjoy economic growth in 2009. Even more impressively, this was not a one-off achievement. Poland has the best long-term record for cumulative growth among CEE countries since 1989. Back then, its GDP was \$62bn, but by 2011, it was over eight times that, at \$514bn. The same trend is mirrored in its per capita GDP growth, which has climbed from \$1,625 in 1990 to \$13,500 in 2011.

Poland's strong, steady growth is linked to its reputation as one of the most attractive places to invest in Europe. A survey by Ernst & Young in June ranked Poland as the second-best investment destination in Europe, behind Germany. Other rankings over the past few years have reached similar conclusions.

So what are Poland's big attractions? Firstly, there is the size of the domestic market (by far the largest in CEE), which means that it is much easier to find workers with appropriate skills in appropriate numbers (especially important for larger production sites). Secondly, Poles are still in the catch-up phase when it comes to consumption, so on the one hand they're ready to work hard, and on the other hand, pretty willing to spend – which means not only a big, but also a growing, market. Thirdly, many investors recognise that wages in Poland are significantly below EU average, but the skills they find there are very similar to those they can tap into in Western Europe. Finally, as a member of the EU since 2004, Poland gives investors access to this market while its geographical closeness means low transportation costs and an ability to respond quickly – two advantages over transportation from Asia.

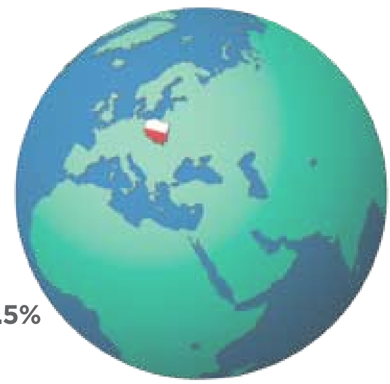
These factors mean that Poland has consistently continued to attract foreign direct investments (FDIs), with nearly €140bn invested since 1994. Importantly, Poland is also attracting more high value-added investments. This is because its main asset is not just low per-hour labour costs; it also offers a highly skilled workforce. This can be seen in the strong growth of business process outsourcing and offshoring, which has taken place in the past couple of years. The number of business service centres has jumped from less than 80 in 2004 to more than 300 in 2011. And this appears to be the beginning rather than the end – in a recent ranking by the United Nations Conference on Trade and Development, the city of Kraków in southern Poland was ranked the top emerging city for global outsourcing, which suggests further inflow of this kind of investment. What's more, it is not just business outsourcing that is taking place – an increasing number of companies are locating their R&D units to Poland, including GE, IBM, Google, Thomson Reuters and dozens of other global companies. In fact, R&D centres constitute a quarter of the number of business service centres mentioned above.

Poland's biggest export products comprise vehicles and parts (12.6% of total exports in 2011); machinery and mechanical appliances (12.3%); and electrical machinery and equipment (11.3%). Other important export groups are furniture (5.3%); mineral fuels and oils (4.9%); plastics (4.4%); and rubber and articles made from rubber (2.7%). Fuels, oils and products of their distillation constitute the biggest group of imports (12.6% of total imports in 2011), followed by machinery and mechanical appliances (12%), and electrical machinery and equipment – mainly household appliances and consumer electronics (10.1%).

One of the important stabilising factors for the economy – and an interesting

COUNTRY FILE

Population size: 38,482,919
Area: 312,685km²
% growth in 2011: 4.3
Type of govt: Republic
Official language: Polish
Capital city: Warsaw
Largest city: Warsaw
GDP (PPP): \$771,658bn
Central govt debt as a proportion of GDP: 53.5%
Currency: Polish zloty (PLN)
Currency rate against the pound: 5.068



Standing almost three metres tall, the Warsaw Mermaid Fountain sits in the Old Town Square (Rynek Stare Miasto); the mermaid 'Szawa' is said to protect the city

GETTY

TOP TIPS FOR DOING BUSINESS IN POLAND

1. Familiarise yourself with a few Polish phrases, such as *dzień dobry* ('good day', used universally throughout the day; *dobry wieczór* would be the phrase to use in the evening).

2. **Learn the basic facts of Poland's history.**

3. Although less pronounced in business contacts and among the young generation, women have certain expectations about how they are treated. For example, it is considered impolite for a man not to allow a woman to pass through a door first.

4. **Poles have a healthy attitude of criticism towards themselves and they appreciate similar self-criticism among foreigners.**

5. A practical tip for occasions when vodka is available, is not to drink vodka and other alcohols at the same time – the results would not simply add, but multiply...

destination for investment – is the banking sector. With core tier one capital ratio at 12.5% for the whole sector (and 13.5% for the top five names), Poland's domestic banking industry is one of the best capitalised in Europe. At the end of 2011, the loan to deposit ratio was at 1.11, proving that banks are mostly deposit-funded, with only 11% of loans financed abroad, mostly via loans to banks operating in Poland from their mother companies abroad. This way of financing ensures stability, as a mother company will not withdraw financing from its Polish subsidiary unless it has first secured another source of funding for it.

The banking industry remains an attractive place to invest given the growth potential of Poland's domestic market. With housing loan penetration (loans/GDP) at 19% in Poland versus the European average of about 40% and UK penetration of 70%, this means it's one of the markets with the greatest growth potential. Similarly, with 15.4% penetration in corporate loans, Poland is not only way below all Western European countries (the UK's corporate loan penetration was at 31.1% in 2011 while Germany's was 35.3%, and in many smaller countries it was above 50%), but it is also below the penetration of regional peers (Slovakia 23.4%; Hungary 24.5%). Given the huge investment needed in infrastructure (especially in the energy sector, where investment needs are estimated in the tens of billions of Polish zloty over the next decade), there is plenty of room for growth – for the banking industry as well as for the corporate bond market.

Financial markets are also one of the success stories of Poland's post-communist transformation. The Warsaw Stock Exchange (WSE), which has more than 380 companies listed on the main market, and another 130+ on the NewConnect market, has become one of Europe's most dynamic initial public offering markets, attracting many companies from the region. It entices both companies that want to be listed, as well as investors, thanks to its clear and prudent regulations.

Another important factor is the size of the market – as the biggest stock exchange in the region it attracts many companies that want to raise funds for their growth, but find their domestic stock exchanges either non-existent, or much smaller than appropriate for their size. As an example, in recent years there have been many Ukrainian food companies listed on the WSE that have raised hundreds of millions of zloty each. In addition, the WSE derivatives trading platform has grown to become the largest in CEE.

Other financial markets that attract many investors are the interbank FX and fixed income markets. The Polish zloty FX market is the deepest and most liquid in the region. And along with FX spot and forward transactions, the FX options market is pretty active. In terms of fixed income instruments, the liquid Polish treasury bonds form the core of most CEE bond portfolios and foreign investors keep adding them to their portfolios, encouraged by Poland's positive performance during the financial crisis and the government's deficit-reducing activity. The portfolio of zloty-denominated treasury bonds held by foreigners has increased in size from less than PLN 60bn in 2009 to almost PLN 180bn in August 2012. This shows how much trust there is in Polish treasury bonds – and helps to explain why Poland remains an attractive investment destination.

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